

**SUBMISSION TO THE COMPETITION POLICY REVIEW
DRAFT REPORT**

MISUSE OF MARKET POWER and MERGERS

6 November 2014

Introduction

1. This submission responds to the Review's Draft Report, September 2014. The focus of this submission is misuse of market power and the implications for review of mergers.
2. The submission is a personal submission by Dr George Raitt, Partner, Piper Alderman, Lawyers. The views expressed are those of the author and do not represent the views of Piper Alderman. The author has no pecuniary interests, or obligations to any current or former clients, that would affect the views expressed in this submission.

Summary of recommendations

3. There is, as the Review's Issues Paper dated 14 April 2014 notes, a disturbing lack of clarity, and consequential controversy, in Australia and around the world about misuse of market power. The Review's Draft Report does not engage in any meaningful way with the international controversy or the differences between Australia's current law and major trading partners. Perhaps the report seeks to be accessible to a general audience. However, the controversy will not go away simply by not mentioning it. It is suggested that, to be credible in the international context, it is desirable that the final report critically analyse the problem, the policy issues and consequences of any change in the law. It is submitted that sensible law reform is unlikely to occur in the context of the current "popular" debate, and should not be undertaken, without verifiable data concerning the "mischief" to be addressed and solid comparative analysis to address the consequences of changing the law.
4. This submission addresses:
 - 4.1 the underlying controversy about policy goals concerning dominant firm conduct;
 - 4.2 "purpose" and "effect" in Australian competition law;
 - 4.3 disharmony around the world regarding an "effects" test for dominant firm conduct;
 - 4.4 critical analysis of the Review's proposed composite "effects" test;
 - 4.5 "road testing" the Review's proposal on leading s 46 cases;

- 4.6 the consequential effects of the controversy about policy goals for merger review.
5. It is submitted that a new s 46 along the lines advocated by the ACCC and proposed by the Review would create further divergence in international competition laws applying to dominant firm conduct, and will cause us to repeat the years of testing of a new law in the courts that the current provisions have undergone. There is nevertheless merit in introducing a “rational business decision” defence or “competition on the merits” defence similar to the US.
 6. It is submitted that the merger clearance process should not be changed to exclude the Australian Competition Tribunal from hearing first instance applications, because the ACCC is unlikely on a formal review to change an adverse view formed under the informal clearance process. Further, given the views of the ACCC which differ from those of the Tribunal on substantive and policy issues (not least of which is the “national champions” debate), a change in process would result in a *de facto* change in the merger review criteria and therefore ought to be resisted. The “national champions” debate needs to take into account experience of Australia’s innovative technology start-up sector (which this submission addresses) rather than merely the traditional traded good sector.

The nature of market power and the “mischief” to be addressed

7. The concept of market power and the regulation of it by competition laws in Australia and around the world is deeply flawed and suffers from indeterminacy and conflicting policy objectives to a greater degree than would be tolerated with any other law.¹ The longstanding debate between economists about the conflicting objectives of “total welfare” versus “consumer welfare” is not an idle debate but raises key issues for the Review’s proposed s 46 test and for the Review’s proposed changes to the merger clearance process.²
8. Some argue that the objective of competition law is to ensure an equitable distribution of surplus between producers and consumers.³ The Tribunal in *Qantas/Air New Zealand* appears to reject re-distribution as an objective of

¹ See George Raitt, ‘Misuse of Market Power: Why Policy Objectives Matter’ (2014) 22 *Competition and Consumer Law Journal* 1.

² See Herbert Hovenkamp, ‘Coase, Institutionalism, and the origins of Law and Economics’ (2011) 86 *Indiana Law Journal* 499, 514; Joshua Wright, ‘The Antitrust/Consumer Protection Paradox: Two policies at war with each other’ (2012) 121 *Yale Law Journal* 2216; Maurice Stucke, ‘Reconsidering Antitrust’s Goals’ (2012) 53 *Boston College Law Review* 551; Robert Bork, *The Antitrust Paradox: A Policy at War with Itself* (Perseus Books, 1978), in Daniel Crane and Herbert Hovenkamp (eds), *The Making of Competition Policy: Legal and Economic Sources* (Oxford University Press, 2013) 408.

³ See John Kirkwood, ‘The Essence of Antitrust: Protecting Consumers and Small Suppliers from Anticompetitive Conduct’ (2013) 81 *Fordham Law Review* 2425, 2434; to the contrary see Joseph Farrell and Michael Katz, ‘The Economics of Welfare Standards in Antitrust’ (2006) *Competition Policy International*, available at <<http://escholarship.org/uc/item/1tw2d426>>.

competition law,⁴ however, the debate continues. It can be seen that distributional equity is an objective that underpins notions of ‘consumer harm’ and ‘market power’ derived from the neoclassical economic model of monopoly. As David Gerber notes, it is not universally accepted that the nature and role of competition is to constrain excessive prices, and thus advance consumer welfare, or that this is the appropriate objective of antitrust law.⁵ According to Gerber, Michael Porter considers that the nature and role of competition is economic productivity, i.e. efficiency in the sense of maximising production from the use of limited resources.⁶

9. The Tribunal’s comments in the *Qantas/Air New Zealand* decision endorse the goal of economic efficiency (total welfare).⁷ However, the Tribunal was considering the meaning of ‘public benefit’ for the purpose of a merger authorisation, and cited only one author in support.⁸ The ACCC opposed that interpretation,⁹ and still does, submitting in its report to the Tribunal in the recent *AGL/MacGen* case that efficiency gains that may be made by AGL are not a public benefit but a private benefit.¹⁰ The contrary reasoning accepted by the Tribunal in *Qantas* is that efficiency gains contribute to GDP and should be given appropriate weight in the Tribunal’s deliberations. The Tribunal in *AGL/MacGen* stood by the view it had expressed in *Qantas*.¹¹ Until ruled on by a court the ACCC may be unlikely to accept this reasoning, which is fundamental to the purpose and effect of competition laws.
10. It is said that Australian judicial reasoning with regard to dominant firm conduct ‘mask[s] undisclosed policy decisions’,¹² and consequently there is a need for a ‘deeper theoretical understanding’ of the role of economic theory, legal precedent and public policy in the regulation of economic activity.¹³ It has been suggested that Australian judges have tended to rely on ‘commercial intuition’ and that there is a need for legal and economic reasoning that provides certainty and predictability for business.¹⁴ It is submitted that the Review’s proposed composite effects test fails to provide clarification of the underlying policy issues and is equally open to these criticisms.

⁴ Australian Competition Tribunal, *Qantas Airways Ltd* [2004] ACompT 9, paragraph 170.

⁵ David Gerber, *Global Competition: Law, Markets, and Globalisation* (Oxford University Press, 2010), 144.

⁶ Ibid.

⁷ *Qantas Airways*, above n 4, paragraph 185.

⁸ Ibid, paragraph 170: M S Gal, *Competition Policy for Small Market Economies* (Harvard University Press, 2003) 203-205.

⁹ Ibid, paragraph 169.

¹⁰ ACCC’s Report filed in the Australian Competition Tribunal in the *AGL/Macgen* case, p. 18.

¹¹ *AGL Energy Ltd* [2014] ACompT 1, Reasons for Decision, pp. 60-1.

¹² Kathryn McMahon, ‘Competition Law, Adjudication and the High Court’ (2006) 30 *Melbourne University Law Review* 782, 784.

¹³ Ibid, 836.

¹⁴ Michael O’Byrne, ‘Section 46: Law or Economics? (1993) 1 *Competition & Consumer Law Journal* 64, 78; see also Michael O’Byrne, ‘Section 46: Legal and economic principles and reasoning in *Melway and Boral*’ (2001) 8 *Competition & Consumer Law Journal* 1.

11. Even in the US context where there is a more significant body of legislative and judicial experience in the field, 'surprisingly few scholars have attempted to provide either a positive or normative theory of monopolisation law',¹⁵ and consequently 'lack of clarity has been a long running problem'.¹⁶ It has been suggested that these problems have led the US courts to be sceptical of intervening to apply s 2 of the Sherman Act.¹⁷
12. The Review's terms of reference include considering whether Australia's competition law is 'responsive, effective and certain in its support of its economic policy objectives'.¹⁸ *However, the policy objectives are not stated in the terms of reference.* The lack of clarity about policy objectives is evident in the Review's Issues Paper, which seems to endorse the objective of total welfare, i.e. maximising productive efficiency of Australia's resources.¹⁹ However, the Issues Paper characterises competition as rivalry between *businesses* which seek to maximise profit by providing what consumers want.²⁰ This is only one side of the market mechanism: when supply exceeds demand, businesses compete; when demand exceed supply, consumers compete.
13. To summarise the argument made in my article cited above, the conventional conception of "market power" as the ability to reduce output and raise price fails to explain the nexus between that "power" and "exclusionary conduct" and fails to explain conduct which appears to rely on ability to increase output and reduce price. It appears that despite the attention given to 'law and economics' in the US and elsewhere since the 1970s key questions about 'market power' remain unsettled. Australian thinking about market power appears largely untouched by these developments. For example, in their expert's report in the recent merger authorisation case *AGL/MacGen*, Frontier Economics refer to US thinking about 'market power' from 1955, adopted by the Tribunal in 1976, which remains unquestioned in Australia.²¹ Frontier Economics also note that the economic models that inform our concepts of 'market power' are extremes not encountered in the real world,²² but the implications of this for our conception of 'market power' are not commonly explored. It is submitted that we should regard "market power" as a two-way rather than one-way phenomenon which has something in common with

¹⁵ Keith Hylton, 'The Law and Economics of Monopolization Standards' in Keith Hylton (ed) *Antitrust Law and Economics* (Edward Elgar Publishing, 2010), 82, 88.

¹⁶ Ibid, 107; see also Jonathan Baker 'Exclusion as a Core Competition Concern' (2013) *Antitrust Law Journal* 527; Herbert Hovenkamp, *Antitrust Enterprise: Principle and Execution* (Harvard University Press, 2005), 95.

¹⁷ William Kovacic, 'The Intellectual DNA of Modern U.S. Competition Law for Dominant Firm Conduct: The Chicago/Harvard Double Helix' (2007) *Columbia Business Law Review* 1, 71-3.

¹⁸ Competition Policy Review, Australia, *Terms of Reference*, 27 March 2014, paragraph 3.1.

¹⁹ Competition Policy Review, *Issues Paper*, paragraph 1.2.

²⁰ Ibid, paragraph 1.3.

²¹ Frontier Economics, 'Competition Issues' 26 March 2014, Expert's Report prepared for AGL, filed in the Australian Competition Tribunal, paragraph 6.

²² Ibid, paragraph 7.

“corners” and “squeezes” in the literature on market manipulation.²³ Fundamentally, it should be recognised that “market power” is a function of elasticity of demand,²⁴ i.e. cannot be possessed by a dominant firm but can be manipulated.

14. It is suggested that it is for the above reasons that the Issues Paper rightly notes a disturbing lack of clarity, and consequential controversy, in Australia and around the world about misuse of market power. The Draft Report’s discussion of the international regulation of dominant firm conduct, however, suggests a harmony on the subject around the world that is simply not present.²⁵ This submission highlights some issues that should not be overlooked.
15. The ACCC puts the case for an “effects” test on several bases. First, the ACCC says it has long argued that the failure to have an “effects” test is a gap in the law.²⁶ As the Review notes, there has been a long history of reviews which have recommended *against* an “effects” test, so the long standing nature of the debate is not productive to elucidate reasons which can be critically assessed in the current context. The American Bar Association rightly submits that one should critically review ACCC contentions that its litigation defeats justify reform of the law since it is inherently more likely to reflect on the ACCC’s selection of cases than to suggest that the courts have failed to uphold the legislative intention.²⁷
16. Second, the ACCC says it has experience of serious complaints where anti-competitive effects have been alleged by market participants but the ACCC considered that there was not a prohibited purpose.²⁸ *No evidence is provided to support this suggestion of mischief occurring beyond the reach of the current law.* Proponents of the “effects” test believe it is obvious that big business is exploiting its market power to the detriment of consumers, and argue that it is necessary to introduce an “effects” test to make it easier for the ACCC to successfully prosecute dominant firms.²⁹ To develop “evidence-based” policy requires some validation of the “mischief” beyond a conscientious belief held by advocates.

²³ See e.g. Craig Pirrong, ‘Commodity Market Manipulation Law: A (Very) Critical Analysis and a Proposed Alternative’ (1994) 51 *Washington & Lee Law Review* 945

²⁴ See William Landes and Richard Posner, ‘Market Power in Antitrust Cases’ (1981) 94 *Harvard Law Review* 937; Roger Blair and Celeste Carruthers, ‘The Economics of Monopoly Power in Antitrust’ in Keith Hylton (ed), *Antitrust Law and Economics* (Edward Elgar Publishing, 2010) 64.

²⁵ Draft Report pp. 205-6; compare e.g. Brian Facey and Dany Assaf, ‘Monopolization and Abuse of Dominance in Canada, the United States, and the European Union: A Survey’ (2002-03) 70 *Antitrust Law Journal* 513; Paul Crampton, ‘“Abuse” of “Dominance” in Canada: Building on the International Experience’ (2005-06) 73 *Antitrust Law Journal* 803; Hedvig Schmidt, ‘Market power – the root of all evil? A comparative analysis of the concepts of market power, dominance and monopolisation’ in Ariel Ezrachi (ed) *Research Handbook on International Competition Law* (Edward Elgar, 2012).

²⁶ ACCC Submission dated 25 June 2014, p. 77.

²⁷ ABA submission p. 8.

²⁸ ACCC submission p. 77.

²⁹ Allan Fels ‘The Past and Future of Competition Law’ (2004) 23 *Economic Papers* 3, 8-9.

17. Third, the ACCC state that the omission of an “effects” test is inconsistent with international trends, citing an apparently unpublished working draft paper by Professor Andrew Gavil concerning New Zealand’s competition law.³⁰ Again, there is no acknowledgement of the international controversy and divergence in laws and decisions of courts and tribunals around the world. For example, reference could be made to the US Antitrust Modernisation Commission report of 2007, or the European Commission guidance on single firm conduct of 2008, or the US Department of Justice report on single firm conduct of 2009 (subsequently withdrawn), to indicate that this is not a harmonious area of competition law or policy. This submission will examine EU and US laws regarding dominant firm conduct to show that there is no international standard “effects test” to assess dominant firm unilateral conduct.
18. Fourth, the ACCC considers that the problem with the current law is the drafting which has lent itself to unduly narrow interpretation by the courts.³¹ The reality of our legal system is that the legislature enacts laws the meaning of which is determined by the courts (based on the presumed intent of the legislature). It seems to be a common complaint of the executive branch of government that laws and decisions of courts fail to live up to their expectations. It is fundamentally a good thing that those who enforce the law are accountable *not to themselves* but to the public and other institutions of government. The ACCC considers that such problems of interpretation will not occur if the law is changed, because the legislation is an “economic statute”, and this will guide the court’s interpretation.³² This is ironic, a triumph of hope over past experience, and overlooks the often stated view of the courts and judges that they are *applying the law* to determine the rights and liabilities of parties – they are not applying economic theory or, much less, the opinions of economists (which typically differ).³³ The US Antitrust Modernisation Commission recently took a similar view that the opinions of economists are not sufficiently certain and predictable to form a basis for legal regulation.³⁴
19. Fifth, both the ACCC and the Review are critical that s 46 refers to the purpose of harming competitors or deterring competitive conduct by competitors. Courts have observed that the purpose of the legislation is to protect competition rather than individual competitors. However, as competition is intangible and forensically difficult to observe, if not unobservable, the words used in s 46 seem to be a reasonable drafting technique to identify a proxy for “competition” that is forensically determinable. In proposing to change the subject matter from harm to competitors to harm to competition, the Review raises a significant point: it is anomalous that the

³⁰ ACCC Submission p. 77.

³¹ ACCC submission p. 76.

³² ACCC submission pp. 80-1.

³³ Majority in the High Court, *Melway Publishing v Robert Hicks* (2001) 178 ALR 253, 266. See also Sir Anthony Mason ‘Law and Economics’ (1991) 17 *Monash University Law Review* 167, 173; Michael Trebilcock, ‘The Value and Limits of Law and Economics’ in Megan Richardson and Gillian Hadfield (eds), *The Second Wave of Law and Economics* (Federation Press, 1999) 12.

³⁴ *Report and Recommendations* (2007), 82.

legislation gives competitors a civil action. *If harm to competitors is a proxy for harm to the public, then it appears to be economically distorting for competitors to appropriate compensation to themselves.* Many cases under s 46 concern competitors using the provision not for altruistic purposes but for strategic competitive or commercial advantage. Litigation of this kind bears a significant responsibility for the tortured interpretation of the law by the courts.

20. Finally, the ACCC cites recent court decisions in which it says there was a clear anti-competitive purpose and significant anti-competitive effect but, under current law, the s 46 case failed because it could not be demonstrated that anti-competitive harm was the result of the dominant firm exercising its market power.³⁵ It is submitted that this over-states the outcome of recent cases, particularly *Cement Australia*, which is discussed below

“Purpose” and “effect” in Australian competition law

21. It is trite law that a person is taken to intend the “natural and probable consequences” of their actions.³⁶ Thus, “purpose” and “effect” can be analysed as follows:
- 21.1 “Purpose” in ordinary concept is fundamentally objective as it will be difficult to convince a court that the “natural and probable consequence” was not the purpose of the act. However, the position appears to be not so simple in the interpretation the courts have given to the “purpose” test in the CCA *outside* s 46, discussed below.
- 21.2 “Purpose” is bedevilled by the metaphysical problem of “dual purposes”.³⁷ That is, in a zero sum world whatever I do to make myself better off makes someone else worse off. In the context of s 46 it is impossible to distinguish a purpose to advance oneself from a purpose to harm others. According to William Reid, there is support in Australian court decisions to have regard to “rational business judgment” as a way to solve the problem of dual purposes.³⁸ However, s 46 of the CCA provides that one substantial purpose among many is sufficient to satisfy the “purpose” test. Section 46 does not expressly indicate what kind of conduct may be outside the scope of the prohibition, i.e. lawful, though some suggest that conduct which promotes efficiency could be justified on that ground.³⁹ Hovenkamp proposes another solution to the problem of dual purposes, i.e. to be condemned it should be shown that the conduct produces harm ‘seriously disproportionate to the resulting benefits’.⁴⁰

³⁵ ACCC submission p. 79.

³⁶ See e.g. per Kiefel, J in *Aid/Watch Inc v Commissioner of Taxation* [2010] HCA 42, p. 436.

³⁷ Heerey, J (dissenting) in *Melway Publishing v Robert Hicks* (1999) 169 ALR 554, 562; His Honour’s judgment preferred by the High Court of Australia on appeal, (2001) 178 ALR 253, 268.

³⁸ William Reid, ‘*Aspen Skiing* in a Sunburnt Country’ (2005-06) 73 *Antitrust Law Journal* 209, 227-232.

³⁹ O’Byrne, ‘Law or Economics,’ above n 14, 64.

⁴⁰ Hovenkamp, above n 16, 152.

- 21.3 A “purpose” without an “effect” would ordinarily be considered an ancillary offence, i.e. an attempt, rather than principal offending conduct in its own right.
- 21.4 An unintended “effect”, i.e. achieved without purposive conduct, is not something that the law generally condemns except in rare cases of strict liability regimes, e.g. involving personal injury of workers or safety of consumers. It is generally not just to condemn a person for the consequences of conduct which cannot be foreseen or cannot be impugned on the grounds of, e.g. carelessness or recklessness.
- 21.5 An apprehended future effect or possibility of an effect, without purposive conduct, is likewise not something that the law generally condemns. However, that appears to be the interpretation the courts have given to the “effects” test in the CCA *outside* s 46, discussed below.
22. The current Australian “purpose” test is a blunt instrument which does not assist us distinguish self-interested conduct, which should be allowed as a normal incident of competition, from conduct which can be clearly defined to be harmful to the common good. The problem is particularly acute when “harm” is defined not by reference to actual competitors but by reference to the *process* of competition or, even more remotely, by reference to the *welfare effects* presumed to result from competition.
23. According to the ABA submission, “purpose” under US monopolisation law is objective and may be inferred from observed effects.⁴¹ The position in Australia is clouded because the courts have construed “purpose” and “effect” in the context of the “Substantial Lessening of Competition” test as *relational* concepts, i.e. in the context of bilateral conduct it is clearly not necessary in order to condemn conduct that the party’s purpose be shared mutually or in common with the other party.⁴² Hence the discussion in the Australian cases of “subjective purpose” should not be seen as a departure from the usual legal tests that intention, e.g. in contract and trust law, is objective.⁴³
24. In the most recent case mentioned in the ACCC’s submission, *Cement Australia*, the ACCC successfully proved its case that the corporation entered into and gave effect to an agreement having an anti-competitive purpose in contravention of s 45. It is noteworthy that s 45 has an “effects” test, but the court considered that any anti-competitive effect of the exclusive supply contract was *dissipated* by market factors.⁴⁴ The ACCC acknowledges this, but not the implications of it. The concept of effects becoming “dissipated” appears to draw on legal concepts of *causation*, i.e. there was a sufficient break (more an attenuation) in the chain of causation between the anti-

⁴¹ ABA submission p. 7.

⁴² See discussion in *ACCC v Cement Australia Pty Ltd* [2013] FCA 909, pp. 826-831; see also *Universal Music* (2003) 201 ALR 636, pp. 691-693.

⁴³ See e.g. Heydon and Crennan, JJ in *Byrnes v Kendle* [2011] 279 ALR 212, pp. 236-242

⁴⁴ *Cement Australia*, pp. 916-919.

competitive agreement and any anti-competitive effect. Unlike many areas of law where “causation” is a well-established requirement, the “effects” test that appears in s 45 refers to “effects or likely effects”. It has been held that a “likely effect” is one which has “real chance or possibility” of occurring.⁴⁵ That is, it is not necessary that any actual effect occur, or that it need be probable that an effect will be caused by the anti-competitive conduct. It may well be doubted that s 46 should be changed to endorse a policy that legal liability attach to a dominant firm without the need to demonstrate that anti-competitive harm is caused by the exercise of market power.

25. It is clear from *Cement Australia* that “effects” in the context of the SLC test raise issues of causation and analysis of market factors that are forensically more difficult to determine than “purpose”. Further, an “effects” test exposes a dominant firm to potential liability for unintended consequences of its actions and for actions that may have no consequence at all. It is submitted that introducing an effects test into s 46 would raise more problems than it would solve.

Disharmony around the world regarding an “effects” test

26. As noted in paragraph 17 above, the ACCC submission suggests that adoption of an “effects” test would be consistent with international trends, however, the cited source for this proposition is not publicly available. It is submitted that even a cursory examination of the position in the EU and US indicates that there is no international consistency.
27. As is well-known, s 2 of the Sherman Act is a very simple provision, with no express “effects” test but over 120 years of judicial interpretation. The submission of the US Federal Trade Commission notes a judicial shift in the US over a century from “intent” to “effects”.⁴⁶ The FTC summarises the US judge-made law as requiring:
 - 27.1 actual or threatened harm to the competitive process (not merely harm to competitors) and thereby consumers (e.g. restricted market output, higher price levels or reduced innovation);
 - 27.2 which cannot be justified as “competition on the merits” (a concept that involves, e.g. greater efficiency or enhanced consumer appeal).
28. According to the FTC, the plaintiff bears the burden of proving the first element, which can be inferred from available evidence (often circumstantial) and if the defendant proffers evidence of justification, the plaintiff must rebut it to succeed.⁴⁷
29. The Antitrust Modernisation Commission reviewed s 2 of the Sherman Act in 2007 and found the provision not without its problems (e.g. unclear what types

⁴⁵ See discussion in *ACCC v Cement Australia Pty Ltd* [2013] FCA 909, pp. 826-831.

⁴⁶ Federal Trade Commission submission, 22 July 2014, pp 1-2.

⁴⁷ Ibid.

of conduct amount to “competition on the merits”) but recommended that further development should be left to the courts.⁴⁸ Of particular note is that the Commission expressed the hope that the then current enquiry by the FTC and DOJ into dominant firm conduct would provide useful clarification. These hopes were not realised, as the eventual report was released and later withdrawn because the DOJ disagreed with it.⁴⁹

30. The ABA submission notes that there is no US standard for determining “effects” and recommends that if such a test is adopted in Australia, this be left to the courts.⁵⁰ Thus the attraction of the US “effects” test for dominant firm conduct should not be over-stated. Nor is it obvious that Australia will benefit from legislating its own differently worded test, with the detailed application to be developed by the courts over time. It is submitted that this would be a recipe for repeating the past.
31. The EU provision, Article 102 TFEU, is likewise a very simple provision, with no express “effects” test and a considerably smaller body of judicial interpretation. Its purpose is to enhance the operation of the “internal market”. The implied “effects” test arises from the Commission’s 2009 Guidance on enforcement priorities which focuses attention on practices that harm the process of competition and thus adversely affect consumer welfare, e.g. in the form of higher prices, limiting quality or reducing consumer choice.⁵¹ The guidance refers also to conduct of dominant firms that excludes competitors by means other than “competition on the merits”.⁵² The guidance indicates that the focus of enforcement should be on cases where exclusionary conduct adversely affects equally efficient competitors.⁵³
32. The Commission’s Guidance has had an equivocal reception by commentators and the courts.⁵⁴ Liza Gormsen points out inconsistencies in the Guidance, in that it appears to adopt consumer welfare over total welfare as the objective and measure of harm, but the underlying methodology involves an inference of harmful effects rather than requiring evidence of actual effects on consumers.⁵⁵
33. It is submitted that the EU Guidance does not provide a compelling precedent for Australia to follow should it wish to adopt an “effects” test. It is submitted that, if anything, the EU experience indicates *against* an attempt to legislate such a test.

⁴⁸ Report, above n 34, 91.

⁴⁹ Department of Justice (US), ‘Justice Department Withdraws Report on Antitrust Monopoly Law, Press Release 11 May 2009.’

⁵⁰ ABA submission, p. 10.

⁵¹ Commission Guidance 2009/C 45/02, paragraph 19.

⁵² Ibid, paragraph 6.

⁵³ Ibid, paragraph 23.

⁵⁴ See e.g. Caroline Heide-Jorgensen, Christian Bergqvist, Ulla Neergaard and Sune Troels (eds) *Aims and Values of Competition Law* (DJOF Publishing, 2013).

⁵⁵ Ibid, p. 197-8. See also Gormsen, ‘Are Anti-competitive Effects necessary for an Analysis under Article 102 TFEU?’ (2013) 36 *World Competition* 223.

Critical analysis of the Review's composite "effects" test

34. Philip Williams observes that the statute law regarding dominant firm conduct in the EU and US is very vague, but its meaning has been developed by the court's over many years, and doubts that greater clarity in the law in Australia can be achieved by adopting a new provision.⁵⁶
35. The Review has essentially adopted the ACCC submission that the law should be changed to prohibit a corporation having a substantial degree of power from engaging in conduct that has the purpose, effect or likely effect of substantially lessening competition. Williams is equivocal whether the SLC test has sufficient merit to justify change.⁵⁷ It is submitted that a change in the law raises a number of uncertainties that will take years to resolve by litigation:
 - 35.1 The SLC test applies generally to bilateral conduct – it is unclear how this will be interpreted in the context of unilateral conduct, which focuses on the exclusion of competitors. As noted above, the current test focuses on exclusionary conduct – while not essentially designed to protect competitors, the current wording more closely captures exclusionary conduct.
 - 35.2 The phrase "purpose, effect or likely effect" has likewise been interpreted relationally in the context of bilateral conduct – it is unclear how this will be interpreted in the context of unilateral conduct.
 - 35.3 The extension of the prohibition to "effects and likely effects" will capture unintended effects and possible future effects which may not eventuate – this is an undesirable ambit that exposes corporations to liability for consequences that cannot be foreseen.
36. The Review's proposal provides that an accused corporation would have a defence if it proves that the conduct in question would be rational for a corporation that did not have substantial market power and the conduct would be likely to have the effect of advancing the long-term interests of consumers. It is submitted that such a change in the law raises a number of uncertainties that will take years to resolve by litigation:
 - 36.1 The "rational decision" defence does not compensate for the lack of clear causal nexus between the anti-competitive harm and the exercise of market power. Further, it re-opens the question of the hypothetical standard by which conduct is assessed under the current "taking advantage" requirement, i.e. is the conduct possible in a hypothetical competitive market in which market power is absent?

⁵⁶ Frontier Economics, 'Notes on the proposed new s 46', October 2014.

⁵⁷ Ibid, paragraph 13.

- 36.2 Williams is confident that the reference to “the long-term interests of consumers” is a reference to economic efficiency (i.e. total welfare).⁵⁸ As lawyers would say, if that was intended it would have been stated expressly. Having regard to the lack of clarity in Australia and overseas regarding the policy goals, there has to be considerable doubt that “total welfare” rather than “consumer welfare” is intended. More significantly, as Williams points out, this limb of the defence (whatever it means) is forensically unprovable and ought to be deleted.⁵⁹
- 36.3 The compound defence is significantly narrower than the US “competition on the merits” defence (whatever that means). For the reasons set out above in paragraph 21.2, some form of defence is required to the present “purpose” test to overcome the dual purposes problem – it would be simpler to rule out the application of s 4F to s 46 so that conduct is not drawn into s 46 only to be tested under the defence.
- 36.4 The reverse onus of proof is abhorrent given that the matters which must be proved are virtually incapable of proof, presumably intentionally so. As noted above, the US scheme does not reverse the onus of proof, as the plaintiff must ultimately rebut the defence raised by the defendant.

37. In summary, it is submitted that there is no demonstrated need for change and that the Review’s proposed changes would have an undesirable unsettling effect on s 46 jurisprudence. There remains a long-term need to clarify and harmonise laws in Australia and overseas regarding dominant firm conduct. Given the nature of the Review’s brief and timeframe to carry it out, it is submitted that the Review is unlikely to be able to contribute to that project.

“Road testing” the Review’s proposal on leading s 46 cases

38. *Queensland Wire, Melway* – it clearly may be rational not to supply a competitor if the corporation can make more money through its own distribution channel. Williams argues that “rational business decision” alone should be a good defence, in which case the defendant in both these cases could have successfully defended either under the “purpose” or the “effects” test.⁶⁰ The Review’s composite defence and reverse onus would make it virtually impossible to defend.
39. *Boral* – it clearly may be rational to meet competition, and in any event “market power” may evaporate when supply exceeds demand and the incumbent is under attack. Williams argues that “rational business decision” alone should be a good defence either under the “purpose” or the “effects”

⁵⁸ Ibid, paragraph 18.

⁵⁹ Ibid, paragraphs 21 and 27.

⁶⁰ Ibid, paragraph 21.

test, but that the Review's composite defence and reverse onus would make it virtually impossible to defend.⁶¹

40. *Cement Australia* – as I read this case, the court held that any SLC was dissipated by market factors, so an “effects” test under s 46 would not have altered this outcome; however, “rational business decision” alone should be a good defence to the “purpose” test. The Review's composite defence and reverse onus would make it virtually impossible to defend due to the undecidable impact on the “long-term interests of consumers”.
41. In summary it is submitted that there is a need for a defence (and/or the exclusion of s 4F) under the existing “purpose” test. This should not be subject to reverse onus as proposed by the Review, but similar to the US process, the defendant should raise a defence which the plaintiff would then have to rebut in order to succeed.

Implications for the Review's proposed merger clearance process

42. The concept of market power is relevant to another area of competition law – the prohibition of anti-competitive *mergers*. While the specific legal test is whether the merger would be likely to substantially lessen competition, the underlying enquiry is often expressed to be whether the merger is likely to create or enhance market power.⁶² The two concepts are not the same, and should not be equated. Again, the analysis of competition effects has tended to be crude.⁶³ Refinement of our understanding of market power will affect our thinking about mergers. Further, differences of opinion between the ACCC and the Tribunal as to the competing goals of “total welfare” and “consumer welfare”, discussed above at paragraphs 7 to 9, indicate that the process changes proposed by the Review would have a substantive effect on merger clearances.
43. The majority of merger cases are considered under the informal clearance process promulgated by the ACCC. These are, in the first instance, confidential and relatively speedy. Should the ACCC not be convinced by a confidential merger proposal it may conduct a public inquiry before deciding to oppose or not oppose. Under current law an intending acquirer then may choose to apply formally to the ACCC for a determination that the merger would not be likely to substantially lessen competition. Due to the inherent improbability of the ACCC changing its mind, this process has not to date been used. The intending acquirer may alternatively elect either to apply to the court for a declaration that the merger is not anti-competitive or to appeal

⁶¹ Ibid, paragraph 24.

⁶² Herbert Hovenkamp, above n 16, 210.

⁶³ See, e.g. Hovenkamp, *ibid*; Gregory Sidak and David Teece, ‘Dynamic Competition in Antitrust Law’ (2009) *Journal of Competition Law and Economics* available at <<http://ssrn.com/abstract=1479874>> advocate reform of the US merger guidelines, subsequently addressed to some extent in the 2010 guidelines; Richard Feinstein, ‘2010 Revisions to the US Horizontal Merger Guidelines’ (2011) 7 *Competition Law International* 6; US Department of Justice and Federal Trade Commission ‘Horizontal Merger Guidelines’ 19 August 2010; cf Australian Competition and Consumer Commission ‘Merger Guidelines’ November 2008.

to the Tribunal for a merits review. However, under current law neither the ACCC or the court has power to undertake a policy consideration whether on balance there are net benefits to the public of the merger proceeding. Only the Tribunal can do that.

44. Two recent Tribunal decisions reveal a fundamental difference of opinion between the ACCC and the Tribunal as to the principles to be applied in determining public benefits and weighing up any net benefit that may justify the merger. The ACCC is not bound by the Tribunal's approach (unless endorsed by a court as a matter of law) and remains opposed to it. This suggests the likely outcome will differ if the legal process is changed, as recommended by the Review, to require that only the ACCC may make the first instance decision (and that it be permitted to weigh up public benefits). The Review's draft proposal imposes relatively short timeframes on the formal authorisation process, however, as the ACCC would be unlikely to change its mind following any informal review, the process in reality is always headed for appeal to the Tribunal for an independent determination. While there is the prospect of the Tribunal overturning the ACCC on appeal, due to time factors in the context of contested takeovers, it is likely that the first instance decision will finally dispose of the matter. In fact, contested acquisitions are time-sensitive and an announcement of opposition by the ACCC following informal review is often enough to dispose of the matter. It seems inappropriate for the ACCC to be both advocate and decision-maker under a formal process since, on general principles, any person or body having both roles lacks the independence of mind necessary to critically question its own views.
45. AGL is the second intending acquirer in recent years to be attracted by the possibility of obtaining authorisation from the Tribunal. The Tribunal's power to authorise an acquisition is stated in the negative, i.e. it must not authorise the acquisition unless it is satisfied that the acquisition would be likely to result in such a benefit to the public that it should be allowed. It is implicit, however, in the 'public benefit' test that the acquisition would fail the 'competition test' and so the Tribunal weighs up anti-competitive detriment against public benefits. AGL argued that the acquisition would not have the likely result of substantially lessening competition. In theory this could have been validated by declaration of the court, however, the Tribunal has the advantage of weighing up public benefits and detriments rather than simply considering the narrow legal question.
46. The difference of opinion between the ACCC and the Tribunal concerns the weight to be given to merger efficiencies to neutralise perceived anti-competitive detriment. The ACCC Merger Guidelines acknowledge that efficiencies may be 'taken into account', but the ACCC in the *MacGen* case argued that benefits would not be passed on to consumers but would be 'private benefits' enjoyed by AGL in the form of, e.g. lower costs and higher profits. It is unclear whether an Australian court would take these effects into account when determining whether a merger would contravene the competition test, i.e. would be likely to substantially lessen competition in a

relevant market. The Tribunal on the other hand has power to take such considerations into account.

47. The ACCC's public statements shortly before the Tribunal delivered its decision in the *MacGen* case, and the ACCC's recommendation to the Competition Policy Review that the Tribunal's role in merger authorisations be limited, suggests that the ACCC's position is unchanged. It seems reasonable to predict, therefore, that the change in *process* recommended by the Review is likely to change the *outcome* of merger applications.
48. The Review notes that the CCA, and in particular the merger clearance process, is focussed on protecting Australian consumers.⁶⁴ The impact of this focus, in the context of the policy objectives discussed above, on the "national champions" debate⁶⁵ requires further consideration.
49. It is said by business groups that competition law is too focussed on competition in the domestic market and does not pay sufficient attention to the benefits of mergers between Australian companies that operate in the global traded goods sector. The Review notes several responses to this criticism. First, many mergers in Australia which generate scale efficiencies may not adversely affect competition because the markets in Australia are subject to import competition.⁶⁶ However, this focus on markets and competition in Australia again does not address the desirability of Australian business being able to compete in global markets to produce income for Australia.
50. Second, the Review quotes Michael Porter's 1990 classic, *Competitive Advantage of Nations*, to the effect that the best preparation for overseas competition is exposure to intense domestic competition.⁶⁷ This would be valid if the domestic market is large enough to sustain viable businesses. Clearly there is no question of this for the US economy (although, according to Gerber, the same criticisms of US anti-trust law arose during the 1970s when US businesses felt they were hampered by anti-trust laws in their response to international competitors entering the US market).⁶⁸ However, the Australian economy is about half the size of the State of California. Whatever might have been the position in the US up to 1990, it is unlikely to assist the Australian policy debate in 2014.
51. Experience of that last 25 years in fact indicates that Australian start-up businesses in innovative technologies will not justify the required return on capital by carrying on business in the Australian market alone, i.e. in order to raise the necessary capital they must focus on global markets to be viable and to generate the return required to raise capital. Increasingly, in addition, these Australian businesses have recognised that: Australian capital markets (including venture capital markets) do not have the depth required to raise

⁶⁴ Draft Report p. 47.

⁶⁵ Ibid, p. 195.

⁶⁶ Ibid, p. 47.

⁶⁷ Ibid, p. 195.

⁶⁸ Gerber, above n 5, p. 140

necessary capital; to develop a successful business often requires locating where the customers are, typically in European, US or Asian markets; and further, to raise capital often requires locating in the markets where investors carry on business, i.e. Europe, US or Asia. Increasing globalisation and increasing focus on high technology products changes the focus away from traditional manufactured and traded goods, which may be developed in the domestic market, and from that base may launch into overseas markets, where scale economies are critical.

52. The traditional traded goods sector is the focus of the Review's analysis of the subject of "national champions" (arising largely from a recent case in point concerning the acquisition of an Australian dairy company by an overseas acquirer after the ACCC opposed a takeover by an Australian would-be acquirer). However, this analysis is not quite so relevant in the "new" global economy of high technology products, where success requires not an understanding of Australian consumers but of overseas consumers and their needs informed by their particular cultural and market issues.
53. Third, the Review notes that the legislation is concerned with the "economic welfare of Australians, not with citizens of other countries".⁶⁹ This statement skates over the central paradox of competition laws: there is a trade-off between the interests of Australians *as producers*, who must respond to the needs of consumers in their global marketplace to succeed and generate income; and the interests of Australians *as consumers*, whose needs are satisfied by both Australian and overseas produced goods and services. The Review quotes the Productivity Commission to suggest that "there is no *a priori* reason why growth in exports or the substitution of domestic production for imported products or services increases (or decreases) public welfare", and that to encourage same may in fact lead to a misallocation of Australia's resources and "ultimately reduce community incomes".⁷⁰ This reasoning may well miss the point that in an increasingly global economy the nexus between the welfare of Australian consumers and the allocation of Australia's productive resources becomes more and more tenuous. While the Review's discussion of the "national champions" issue *seems* to dispose of the concerns of industry, it is submitted that without taking account of the experience of Australia's innovative technology start-up sector the discussion lacks the depth necessary to adequately address the issue.
54. One consequence of the continued focus on "markets in Australia" appears to be an odd tilting of the playing field that *disadvantages* Australian companies in merger cases compared to their global competitors. Taking the recent dairy industry experience, for example, an Australian would-be acquirer having a substantial competitive overlap with the takeover target in Australia may be precluded by our merger law from the acquisition, whereas its overseas competitors in global markets may not be so precluded. The Review states that "allowing mergers to create a national champion may benefit the shareholders of the merged businesses but could diminish the welfare of

⁶⁹ Draft Report p. 193.

⁷⁰ Ibid, p. 197.

Australian consumers”.⁷¹ This statement seems to reflect the rather narrow views of the ACCC regarding “public benefits” (which as noted in this submission have been rejected by the Tribunal). As the Tribunal pointed out in the *Qantas* case,⁷² increased profits of the merged entity contribute to GDP, and so serve the interests of Australian consumers, i.e. the paramount interest of Australian consumers is to have an income with which to consume.

55. Accordingly, it is submitted that the current merger review processes ought not be changed. Further, it is submitted that the Review ought to definitively endorse “total welfare” as the over-riding policy objective informing the competition law regulation of dominant firm conduct and mergers.

⁷¹ Ibid, p. 195.

⁷² *Qantas Airways*, above n 4, paragraph 185.