Business Council of Australia

submission

Submission to the Competition Policy Review

JUNE 2014

Working to achieve economic, social and environmental goals that will benefit Australians now and into the future

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Submission to the Competition Policy Review: Summary Report

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Contents

The Business Council of Australia (BCA) is a forum for the chief executives of Australia's largest companies to promote economic and social progress in the national interest.

This is the BCA Submission to the Competition Policy Review. It comprises a Summary Report and a Main Report, and includes a detailed set of recommendations for consideration by the Competition Policy Review panel.

Key points

▶ Robust competition grows the economy

- Vigorous and robust competition within well-considered policy and regulatory frameworks is essential for a resilient and growing Australian economy in the 21st century.
- Nationally the benefits of market competition and a competitive business environment include better use of our limited physical, human and capital resources, the creation of high-value jobs and a growing national income.
- Competition provides a strong incentive for businesses to improve quality, reduce costs and innovate to meet the needs of consumers. Competition therefore should lift business competitiveness, driven by both the formal devices of competition policy and competition law and the informal device of business reputation.
- Competition is an inherent feature of a healthy society because competitive, profitable businesses create jobs and generate community wealth over the long term. This provides a sound revenue base, which enables government to play its role in meeting the needs of all Australians where government services are essential, including addressing disadvantage.
- This review should both extend the coverage of Australia's competition policy frameworks into new areas of the economy and test whether the current rules for competition remain suitable for the global competitive landscape in which businesses and consumers will function in the years ahead.

▶ Global markets have changed our competitive environment

- The BCA believes it is time for Australia's policy settings to adopt a global mindset. This mindset is one which recognises that virtually all goods and services are tradeable, and that the empowered, informed and technologically equipped consumer is redefining the competitive landscape.
- Markets are becoming more dynamic and globally integrated. Australian businesses are increasingly able to export into a broader range of markets and become part of global supply chains. Australian consumers can more readily purchase from international outlets. Australian consumers can access markets both globally and domestically; Australian businesses have to be globally competitive to access global markets and to succeed in domestic markets.

- Declining transaction costs and technology change are breaking up value chains and driving disintermediation, with profound implications for business models. Conversely, because Australian consumers have more choices, Australian businesses are subject to increasing trade exposure in areas where they were not previously subjected.
- Pervasive technology change is redefining consumer access and scale. Business needs to be able to react and respond quickly with new products or business models if they are to retain or grow customers.
- Australia's competition policy frameworks must be designed to reflect this new competitive landscape and to encourage productivity and innovation. Getting competition policies right and administering them well are critical to high-performing Australian businesses and a high-performing Australian economy.
- In these changing global markets, competition in a market is less about the number of local participants or the market share of the key players, and more about the conduct of participants within a market and the points of access for consumers.

▶ **Poor application of regulation has a serious impact**

- Regulation has an important role to play in upholding critical rights and providing legitimate safeguards, but to be effective regulation must be properly thought-through and applied sensibly.
- Efforts by business to comply with unnecessary or poorly designed and administered regulation simply displace productive wealth-generating activities like innovation and investment in new technology.
- Poor regulation also frustrates attempts by companies to lower costs and reorganise their operations in response to competitive pressures and structural transition that is occurring through the economy.
- There will be significant costs to consumers and to living standards if we do not adopt the global mindset and if competition policy, and regulatory policy and design, do not keep pace with the changing competitive landscape.
- Regulatory failure has negative impacts on business competitiveness, investment and jobs, which ultimately leads to worse outcomes for consumers and the community overall.
- The quality of decision making, timeliness and transparency on the part of regulators must keep up with the complexity and speed of commercial activity in the modern economy. Poor application of competition law prevents businesses from being productive and innovating and imposes substantial opportunity costs on the economy.

▶ **Competition law must adapt to a changed economic environment**

- It is timely that the government is conducting this broad review into competition policy in Australia. Australians continue to benefit today from the positive economic outcomes that resulted from the Hilmer review and the National Competition Policy reforms that resulted.

- This review can continue in that tradition by further extending competition and growing Australia's international competitiveness, having regard to the changing nature of global markets and the rise of technology.
- Against the backdrop of stagnating multifactor productivity, a declining terms of trade, and high cost structures, Australia needs to embark on another round of structural reform. There is an opportunity for well-designed competition policy to play a lead role in reforms that will drive the next phase of Australia's economic growth.
- This will require extending competition into more areas of the Australian economy, and removing excessive regulation that is impeding competition in the new global and technological context in which Australia operates.

▶ Review recommendations should boost competition across the economy

- The review panel should make recommendations to governments that set Australia up to be more competitive by reinvigorating efforts to unleash the market economy with more purposeful market design. This will require:
  - A competition policy framework that reflects a global mindset, recognises the new competitive landscape in which Australian businesses are operating, and amends the Competition and Consumer Act accordingly.
  - Broader pro-competitive reforms that make regulatory design and approvals processes more efficient, extend competition into public sector markets and improve government service provision.
  - Improving the efficiency and effectiveness of competition law in some areas, including the formal merger process, provisions covering predatory pricing, price signalling and some per se prohibitions, and making the national access regime more efficient.
  - Improving the focus and scope of Australia's regulatory institutions by considering a separate national pricing and access regulator and introducing clearer accountabilities for regulators.
  - Establishing new institutions to drive the reduction of regulatory barriers to competition across the federation.

▶ Competition policy review is one part of a strategic reform agenda

- There are many other ways that regulation can impact on competition, and therefore competitiveness. In this submission, we have generally not commented on areas of regulation that are subject to other upcoming reviews. This includes:
  - the effect of workplace laws on competition and competitiveness, to be reviewed by the Productivity Commission
  - proposals to extend unfair contract terms to business, currently under review by the Commonwealth Treasury
  - the impact of the tax system on competition, which will be addressed in the Commonwealth white paper on taxation reform.

- The review of competition policy should complement other government initiatives underway to open the Australian economy to competition and lift competitiveness, including the government's Red Tape Reduction program, the negotiation of free trade agreements, and bilateral agreements for approvals under the Environment Protection and Biodiversity Conservation Act.

1. The new competitive landscape

Issues

The review comes at an important time for the Australian economy. Australia's economy is expected to grow slightly below trend for the next 12 months, while the transition from record levels of resources investment to broader industry growth is expected to see business investment decline in coming years.

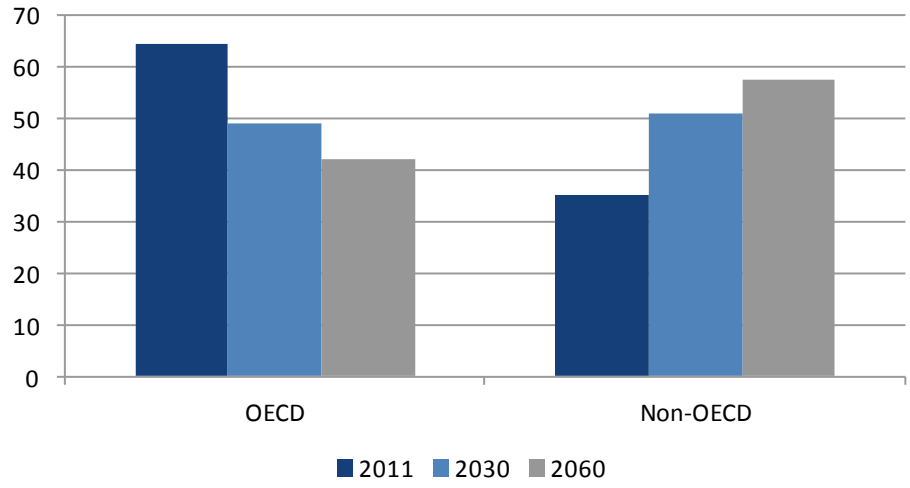
Australia will also confront long-term economic challenges, with an ageing population placing ongoing pressure on economic growth.

At the same time, there are both considerable opportunities and threats brought about by globalisation and the rise of technology. This provides a profoundly different backdrop to the work of the competition policy review than that confronting the Hilmer review in 1992.

Emerging markets are now increasingly important drivers of global economic growth and will account for a greater share of the global economy, as illustrated in Figure 1. To date, Australia has been successful at capturing growth opportunities from China, which now represents almost a third of Australian exports, up from just 2 per cent in 1990–91.

Figure 1: Growth in emerging markets

Per cent of global GDP



Source: OECD, 2012a. Note: Measured in 2005 purchasing power parity.

The opportunity for this review is to undertake the unfinished business of removing barriers to competition with the objective of improving our national competitiveness. Breaking down barriers to competitiveness is a key to unlocking innovation and lifting our national productivity.

As a medium-sized open economy, our long-term success and ability to take advantage of new market opportunities will be very much tied to our

competitiveness. At present, Australia's competitiveness is lagging behind other countries.

The competitive pressures from a relatively high Australian dollar are only exacerbated by an increasingly uncompetitive business environment.
The World Economic Forum places Australia 21st out of 148 countries on its Global Competitiveness Index, down from 15th place a few years ago.

The review must develop its framework for competition policy with the new competitive global and technological landscape in mind.

Forces like digitisation and globalisation are changing the demands on competition law and other regulation. Barriers to competition are being lowered, consumers are becoming more empowered and traditional barriers to entry are being broken down. This demands a changed mindset from governments and regulators when drafting and administering regulation, recognising that goods and services are increasingly tradeable, consumers are digitally empowered and markets are changing even more rapidly than in the past.

Regulation that reflects this new competitive landscape will deliver the full benefit of these developments to Australian consumers and promote our national competitive position.

Against the backdrop of stagnating multifactor productivity, a declining terms of trade, and high cost structures, Australia needs to embark on another round of structural reform. There is an opportunity for competition policy to play a lead role in reforms that will drive the next phase of Australia's economic growth.

This will require extending competition into more areas of the Australian economy and removing excessive regulation that is impeding competition. Australia's economic opportunities will not be realised by making regulation more intrusive or giving more powers to competition regulators.

- ***Goods and services are increasingly tradeable***

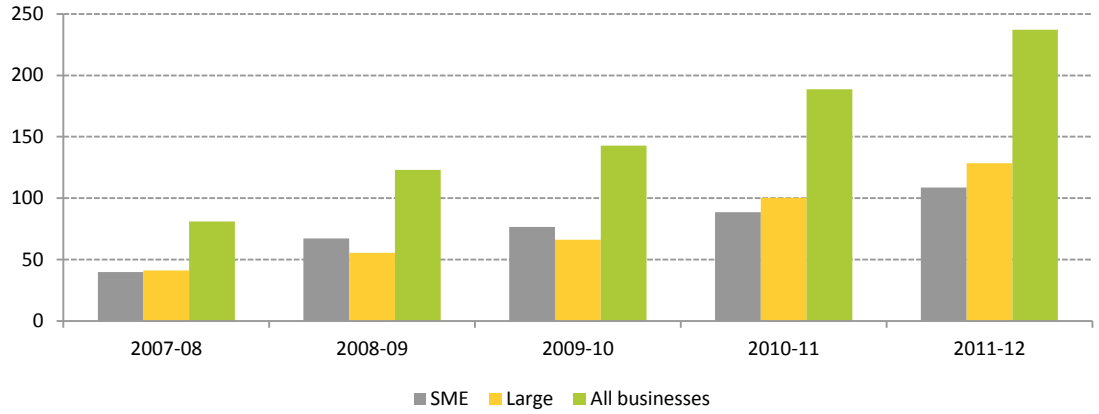
Digitisation and globalisation have reduced the costs and increased the consumer convenience of buying and selling goods and services across borders.

For example, books, music, financial, legal and secretarial services are easily accessible from many markets across the internet. All of this means that Australian companies have considerable global opportunities, but they also face considerable global competition in domestic markets.

The Boston Consulting Group estimated that by 2016 the internet economy will comprise at least $4.2 trillion in G20 economies. Australian companies' experience is consistent with this trend, with substantial increases in internet income.

Figure 2: Internet income for Australian businesses

$ billion



Source: ABS, *Selected Characteristics of Australian Business*, cat. no. 8167.0. Note: Internet income is defined as income resulting from goods and services ordered over the internet, where the commitment to purchase is via the internet.

▶ *Consumers are digitally empowered*

Through consumer websites and forums as well as social media, real-time feedback and data capture, consumers are increasingly shaping the goods and services that companies provide. Last year, 78 per cent of consumers researched a product or service on their smartphone (IPSOS, 2013). In the last 12 months, online retail sales have increased by 6.4 per cent and now represent around 6.6 per cent of traditional retail sales (NAB, 2014).

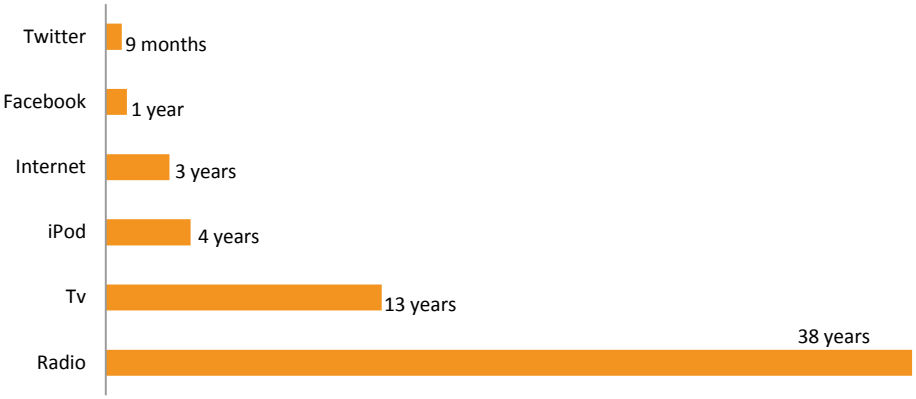
▶ *Markets are rapidly changing*

Markets have always been dynamic, but global and digital forces are speeding up the timeframes in which products and services, and the companies providing them, undergo major transformations.

Australian-based businesses – large and small – are increasingly able to export into a broader range of markets. In the same way, Australian consumers can more readily purchase from international outlets. Declining transaction costs are breaking up value chains and driving disintermediation.

As illustrated in Figure 3, digital platforms, consumer demand and developing markets are driving exponentially faster take-up of new technologies.

Figure 3: Social technologies: Time to reach 50 million users



Source: McKinsey Global Institute, 2012

Implications

As the Australian market becomes more integrated with international markets, the impact of unique Australian regulations or other costs on business will become more visible as barriers to competition. This changing competitive landscape has a number of important implications for regulators and policymakers, including:

- ***Competition remains paramount to economic progress***: Competition and open markets are the best way to drive productivity, but we need to adjust the boundaries in which we think about markets to reflect the new competitive landscape. This means taking into account the increasing points of access for consumers and the changing structures of global supply chains and supplier participation in supply chains. A fundamental objective should remain to protect the competitive process, rather than individual competitors.
- ***Long-term interest of consumers remains a sound objective***: Despite these rapidly evolving trends, the starting principle of putting the long-term interest of consumers at the centre of competition policy remains sound. By 'long-term interest' we mean that consumers are best served by a competition policy framework that recognises that investment, innovation and productivity are important for providing consumers with greater choice and quality at competitive prices over time. Over the long term, we do not believe that consumer interests are always served by the simplistic measures of the lowest prices to consumers of today or the number of players in any given market.
- ***Government must look at markets through a global lens***: Domestic markets that appear less competitive or concentrated at first glance are likely to be much more competitive when considered, where appropriate, through a global lens. Even if a global competitor has not entered the Australian market, lower barriers to entry and the mere threat of entry provide strong incentives for vigorous competition from incumbents. In some instances, technology will facilitate a rapid build-up of scale, but in other areas globalisation will mean that Australian firms are competing with specialised global firms.

- ***Time is everything***: With markets changing more rapidly, businesses need to allocate capital and make decisions even more quickly to take advantage of new markets. The timeliness and consistency of regulatory decisions and approvals in this business environment is paramount. Australian companies will need to be more agile to respond to the pressure of a highly competitive landscape.
- ***Regulation may not keep pace***: The timeframes for designing, drafting and implementing regulation mean it is inevitable that in many cases, prescriptive regulation will not keep pace with these trends. This places greater pressure on governments and regulators to develop sensible non-regulatory, administrative and outcomes-based solutions in consultation with business.

Recommendations

1. The panel should design a competition policy framework that reflects a global mindset by promoting flexibility, innovation and productivity in the national interest of enhancing Australia's competitiveness.
2. The Competition and Consumer Act (CCA) should be amended to clarify that in any competition assessment, the global dimension of markets must be taken into account, and dynamic competitive effects in markets are to be preferred over static measures such as historical concentration.

2. The opportunity for broader pro-competitive reforms

The Hilmer review led to a comprehensive competition policy reform agenda in Australia under National Competition Policy. Despite the successes of those reforms, there remains in place today a wide set of policy settings across Commonwealth, state and local governments that, intended or otherwise, continue to create barriers to competition and, in turn, our competitiveness. Many of the pro-competitive reforms that could be made are referred to as the 'unfinished business' of competition policy reform in Australia.

Removing regulatory barriers to competition

The BCA has identified a range of regulations and instruments that can have the effect of impeding competitive markets. It is not feasible to draw an arbitrary line between those regulations that should be in scope for this review, and those that should not. What the review must do is develop priorities based on an assessment of materiality both now and in the future. Key groupings of regulatory barriers to competitiveness that the BCA has identified include:

- ***Permits, licences, approvals and other regulations that restrict business growth:*** for example, overly onerous professional licensing requirements.
- ***Regulations that limit the ability to compete:*** for example, restrictions on retail trading hours.
- ***Regulation that restricts ease of movement of resources across state markets:*** such as trade licensing arrangements.

- ***Regulation and policies that restrict the ease and speed of meeting growing export markets:*** for example, anti-competitive coastal shipping regulation and slower product approvals in areas like medical devices than international peers.
- ***Delays to regulatory approvals:*** for example, delays from planning and zoning which limit the ability of businesses to enter new markets, or expand operations in a timely way.

These barriers do not just emerge from existing regulation. A lack of disciplined application of regulatory impact processes has also seen new anti-competitive restrictions introduced. Similarly, the conduct of regulators themselves in terms of timeliness and transparency of processes can limit the speed with which Australian companies can adjust and compete.

These sorts of barriers come at a considerable cost to the economy and Australia's competitiveness. For example:

- A recent study found that in Queensland alone, removing restrictive retail trading regulations would provide an annual boost to the economy of $200 million.
- Cabotage restrictions under the Coastal Trading Act 2012 are causing Australian firms to pay shipping rates that can be up to double the rates offered by foreign ships, adding tens of millions of dollars to their cost base, and making their operations less viable as a result.
- It recently took Cochlear, an Australian-based exporter of medical devices 14 months longer to gain product approval in Australia than in Europe. (A number of countries require a device to be approved in its country of origin before it can be approved for use in the export destination country. Therefore after obtaining regulatory approval in Europe, it took an additional 14 months before Cochlear could even start to apply for product registrations in other key markets such as India.)
- In an illustration of the potential gains in reducing approval times, the Productivity Commission has found that expediting the average approval process for oil and gas projects would increase the value of projects by 10 to 20 per cent with billions of dollars of income gains for Australians.

There are numerous examples of these sorts of regulatory barriers, that if removed or streamlined would, on a cumulative basis, significantly boost the competitiveness of our economy and its productive potential.

In an increasingly dynamic global competitive landscape, it follows that business needs to be increasingly agile to compete. Regulation that impedes the ease and timeliness with which businesses can restructure or innovate to more effectively compete simply detracts from Australia's potential growth.

Recommendations

3. Within three years, states and territories should implement mutual recognition for occupational licences that would enable people with valid licences in one state to work in another state, based on the 'drivers licence' model.

4. Remove the legislated cabotage restrictions in the Coastal Trading Act 2012 to move to an open, globally competitive coastal trading sector, with foreign and Australian vessels continuing to be subjected to all other Australian laws.
5. Repeal the Australian Jobs Act, which mandates government-approved Australian Industry Participation Plans for private investment projects over $500 million.
6. Australian governments should adopt as a principle that where a regulated good or service is tradeable, and subject to a regulatory approval by a European Union, a United States, or Canadian national regulator, then there should be a strong presumption in favour of automatic recognition of those countries' approval. This is a process that individual Australian jurisdictions should be prepared to adopt unilaterally.
7. Australian governments should implement measures to deliver more timely and predictable decision making regarding planning, zoning and other land development, underpinned by a suite of reforms that involves all states and territories:
   - conducting improved strategic planning that provides land-use permissibility for economic development, including infrastructure, major energy, industrial and resource projects, in the same way as is done for future housing settlements
   - committing to introduce progressive targets to shift 80 per cent of the share of development (residential and commercial) towards streamlined processes – that includes code-assessable development
   - adopting a single major project approval process for major energy, resource, infrastructure and industrial projects based on a dedicated assessment track that includes one statutory timeframe from Environmental Impact Statement exhibition through to a project decision, and all secondary approvals.
8. Australia's governments must immediately set a timetable and process for aligning state-based retail trading hours, and coordinate a state-based reform agenda for removing the most restrictive and inconsistent regulatory restrictions affecting the retail sector.
9. Reviews of anti-competitive legislation or other policy settings should continue to apply the National Competition Policy principles.
10. All governments should have robust, legislated, two-stage Regulatory Impact Statement processes in place that explicitly test all new regulatory proposals against the competition principles, and this process should be overseen in each jurisdiction by an independent agency.
11. Any exemption from the Regulatory Impact Statement process should be approved by the leader of a jurisdiction, with the reasons published and a post-implementation review undertaken.

Extending competition into public sector markets

There remain considerable opportunities to expose government activities and organisations to greater competition so as to generate better outcomes for consumers, users of subsidised services, and for taxpayers.

Opening these activities to competition will help Australia move towards:

- world-best provision of education, health care and other government services for the benefit of the broader community
- more competitive supply of critical inputs to businesses, for example in rail, port, and energy services, that are needed by those businesses to succeed in global markets.

More than 20 years after the Hilmer report, it remains the case that a great deal of economic and potentially competitive activity remains beyond the reach of competition law in the hands of local, state and territory, and Commonwealth governments. Extending the competition law to these areas could be partly achieved by expanding the definition of 'carrying on a business', but would also require positive reform of legislation and regulations by the various levels of government.

Many free or subsidised services delivered by government represent a large part of the economy that has historically been much less exposed to competition than other services. In aggregate, this is a large proportion of the nation's total output. Traditional public sectors, including health care and social assistance, public administration and safety, and education and training, accounted for 17 per cent of Australia's industry gross value added in 2012–13. Achieving greater efficiency in this area therefore has significant potential economic gains, while lifting service quality.

The long-term interests of the community should be prioritised over the short-term budget goals of governments. Governments that sell assets should ensure that pro-competitive regulatory frameworks are in place to promote ongoing efficient investment and to safeguard consumers, even if the sale price is lower. This includes the application of the Council of Australian Governments (COAG) Competition Principles Agreement when reforming public monopolies.

But imposing greater market discipline is critical in meeting the increasing demands on the services delivered by government. For example:

- The share of government expenditure on health and ageing is expected to increase substantially from around a quarter to a half over the next 40 years.
- Total real spending on infrastructure over the next 10 years will be around $760 billion, including over $300 billion coming from governments and public corporations (Deloitte Access Economics, 2013).

Delivering high-quality goods, services and infrastructure in the most effective and efficient manner possible will require the consideration of:

- regulatory regimes that promote infrastructure investment
- continued privatisation of government enterprises

- outsourcing of some government service provision
- rigorous application of competitive neutrality principles and requirements where government businesses continue to provide goods and services.

It is widely recognised that private ownership of infrastructure brings better capital discipline, greater efficiency and, in many cases, improved service. Many government businesses have been privatised in the last three decades, but as Infrastructure Australia notified its 2013 report to COAG, there remain up to $60 billion of water assets and up to $60 billion in electricity network and generation assets that could be transferred to the private sector, enabling efficiencies in operation and the release of funds for new infrastructure investment.

Recommendations

12. Government service delivery should, as far as possible, follow market principles and be fully contestable to drive innovation and better service delivery, with priority given to health, education, and transport and infrastructure services.
13. Australia's governments should recommit to the competitive neutrality policy and implement nationally agreed procedures for its application that set out:
    - how each government will implement competitive neutrality policy as they move to promote competition in government service delivery
    - a clear process for responding to any recommendations arising from an investigation by the independent competitive neutrality complaints regulator
    - transparent and accessible reporting on the government's response to findings by the independent competitive neutrality regulator, including remedial actions taken
    - principles for identifying and specifying non-commercial objectives of government businesses and how those activities should be transparently funded
    - guidance on how competitive neutrality should be applied to new, start-up government businesses, for example, on the matter of the length of time over which a commercial rate of return should be achieved.
14. Australia's governments should pursue a renewed agenda for upgrading infrastructure regulation to enhance competition and meet the future needs of the Australian economy. A new agreement should include reforms that will promote new and efficient investment in infrastructure, including commitments towards:
    - enhanced consistency, capability and performance of Australia's economic regulators
    - a new timetable for privatising infrastructure businesses to capture efficiencies from private ownership and unlock public funds (including via the Recycling Assets Fund)
    - reforms to pricing infrastructure that move towards full recovery of the efficient costs of public infrastructure provision, including an adequate risk-adjusted return on investment.

15. Prior to the sale of any Commonwealth, state, territory or local government businesses with natural monopoly characteristics, a review consistent with the 1995 National Competition Principles Agreement should be undertaken to promote pro-competitive outcomes where possible. This should include putting in place appropriate access arrangements, even where this has the effect of reducing the sale price of the asset.
16. Governments should promote efficient investment and use of road transport infrastructure through adoption of broad-based user charging, as part of comprehensive tax reform and reform of Commonwealth and state funding arrangements.
17. The Commonwealth Government's review of the federation should assess how to strengthen incentives for states and territories to more actively search out more competitive forms of service delivery, such as the current Grants Commission arrangements.
18. The Productivity Commission should be given inquiries that separately look at each of the main areas of state and territory service delivery (education and early childhood; health and human services; justice and transport) to examine the potential to increase competitive provision, drawing on the lessons from Australian and international jurisdictions that have already implemented such models.

3. Competition law

Sound principles

Australia has a strong competition law framework. However, there are areas in which the law and its administration could be improved to promote efficiencies and reduce costs. At present, aspects of the competition framework impose unnecessary costs and delays by requiring compliance with overly prescriptive regulations, discouraging vigorous competition due to uncertainties in the law, and potentially hindering the efficient use of capital by adopting an overly narrow approach to mergers.

Australia's competition law should be aligned as closely as is possible with these international best-practice principles:

(I) long-term consumer welfare should be the overriding goal

(II) aim to protect the competitive process, rather than individual competitors

(III) be consistent with best practice competition law

(IV) minimise use of 'per se' prohibitions

(V) focus law economy wide, not sector specific

(VI) aim for simplicity to reduce compliance costs

(VII) don't unduly impede legitimate business interactions.

Priorities for competition law reform

As a result of iterative changes to the legislation over a number of years responding to in many cases “issues of the day”, the Competition and Consumer Act contains areas that are inconsistent, impractical, excessive and in some instances not reflecting the new competitive landscape. Many of these iterative changes which have occurred are inconsistent with sound principles of competition law, and should be reconsidered.

Prime examples for reform are listed below.

- ***Market definition and competitive effects analysis***
  - The administrative approach to market definition can be at times unduly narrow and overly focused on market concentration rather than the dynamics of competition. In these cases, some competitive constraints, including global sources of competition, where relevant, are not taken into account when defining the relevant market.
  - An overreliance on market concentration and the structure-conduct-performance paradigm in merger assessment is unhelpful and can fail to take into account the impact of new and innovative small entrants or technology that has lowered barriers to entry. This is particularly acute in merger assessments.
- ***Formal merger process***
  - The availability of this alternative to the informal process, particularly in potentially contentious cases, is desirable and should be retained. However, the formal merger clearance process has not been used because it is unduly complicated by strict technical formal requirements for a compliant application, including for example, the detailed and prescriptive standard form application (Form O, Reg 73), which is onerous and inflexible.
  - This procedure is not attractive to merger proponents, evident in the fact that the formal clearance process has not been used in almost 10 years.
- ***Predatory pricing***
  - Recent amendments to section 46 have moved Australia away from global practice and have the potential to work against aggressive pricing that is legitimate competitive behaviour in the best interests of consumers.
  - Uncertainty over the underpinning concepts of the Birdsville amendment will only act to further discourage vigorous price competition and increase prices to consumers.
- ***Price signalling***
  - Advertising prices to consumers is absolutely fundamental to effective competition and public signals about prices also keep consumers informed.
  - Current prohibitions relating to price signalling in the CCA are long, complex and inconsistent with international best practice.
  - The real risk of benign or pro-competitive commercial communications being caught by the prohibitions has led to a complex set of exceptions.

- This reflects the fact that it is practically impossible to separate desirable public price competition from detrimental 'price signalling'. If legislators get this wrong, then it is to the detriment of consumers.
- The difficulty with current provisions applied to one sector of the economy also demonstrates that applying these prohibitions more broadly would be unworkable.
- The extent of any gap in the Australian law has not been established; but given that the law already prohibits any attempt to enter into or induce a collusive arrangement, and allows an understanding to be inferred from the circumstances, any gap is likely to be narrow. The current price signalling provisions are greatly disproportionate to any problem and should be repealed.

▶ ***'Per se' prohibitions***

- The CCA contains strict and absolute prohibitions in relation to resale price maintenance and third-line forcing.
- These prohibitions do not meet the best practice threshold for such a strict prohibition. The threshold requires that the conduct be inherently anti-competitive with no redeeming public benefit in the overwhelming majority of cases. In contrast, many or most instances of third line forcing and resale price maintenance will not be anticompetitive, will offer substantial public benefits, or both.

▶ ***National Access Regime in Part 3A***

- The regime's function is broadly to promote efficiency, but it should be used sparingly and not negatively impact on incentives to invest. Today the regime largely serves as a backstop for cases not covered by industry-specific regimes, but the experience to date shows that it can create significant regulatory risk for greenfields investment. It does this by exposing investors to the possibility of a lengthy and costly declaration process and the risk of access arrangements that materially impact on return on investment.
- The panel should find ways to reduce regulatory costs and risks on investment and give careful consideration to whether the regime remains the optimum way to regulate private investment given Australia's considerable future infrastructure needs.
- At the very least, we believe the review panel should investigate options to improve the operation of the National Access Regime to give clearer guidelines to potential investors and streamline the costly declaration process.

No 'effects' test

In addition to these issues in the current CCA, the BCA continues to reject the proposal put by some that the CCA should include an effects test in section 46. We do not believe that the benefits of this proposal would outweigh the costs and agree with the Dawson review's finding that such a test would inappropriately extend the application of section 46 of the CCA to legitimate business conduct and

discourage competition. That is, the effect of such a test would be to substantially lessen competition.

We have formed this view based on the following factors:

- Prohibiting unilateral behaviour based on its effect on competitors would lead to a very different competitive landscape to the current landscape, in which unilateral behaviour is judged according to its purpose. Any such change might protect individual competitors, but it would lessen competition.
- The role of purpose in distinguishing between vigorous competition and anti-competitive behaviour has been recognised by the High Court since the Queensland Wire case and by every review of the trade practices legislation.
- Discerning a corporation's purpose may not always be straightforward, but the courts now have four decades of experience in doing so, and have developed increasingly sophisticated tools and principles to assist them. Courts have found a proscribed purpose in many high-profile cases, and have awarded more than $34 million in penalties in section 46 cases since the Dawson review.
- A careful analysis of international jurisprudence reveals that purpose is widely used as a tool to distinguish between beneficial vigorous competition and detrimental anti-competitive conduct.
- An effects test would be inconsistent with the principles that competition law should not unduly impede legitimate business interactions; should be simple to understand and implement; and should have long-term consumer welfare as its overriding goal.

Recommendations

19. As a guiding principle, Australia's competition law must be consistent with international best practice. Consequently, it should:
    - have as a clear objective the promotion of long-term consumer welfare by protecting the competitive process rather than individual competitors
    - be aligned with the best elements of US and EU anti-trust laws, noting that Australian businesses operate in increasingly globalised markets
    - this will enhance Australia's competitiveness.

Enhancing the effectiveness of the general competition law

20. The Treasury, in consultation with business, competition law practitioners and the ACCC, should review the formal clearance mechanism, including the regulations, to remove unnecessary restrictions and requirements which have acted as a deterrent to its use.
21. The 'per se' prohibition against cartels and exclusionary provisions should be clarified to ensure that they apply only to horizontal arrangements between competitors, and the joint venture exemption should be extended to apply both to non-contractual arrangements and to joint ventures other than for the supply of goods or services.
22. The conduct prohibitions should be streamlined, and a public benefit defence adopted in the CCA, to reduce the reliance on costly and time-consuming

administrative notifications and authorisations processes so as to improve the overall operation of the law.

National Access Regime under Part 3A

23. Improve the application of access regulation to greenfield infrastructure projects, for instance, through improved use of the ineligibility provisions or by agreeing any access arrangements upfront, before investments are made.

24. The panel should give consideration to whether the existing National Access Regime remains the optimum way to regulate private investment that will be required to fund Australia's considerable infrastructure needs into the future.
    - At the very least, the panel should investigate options to improve the operation of the National Access Regime to give clearer guidelines to potential investors and streamline the costly declaration process.

Removing parts of the law that do not contribute to stronger competition

25. The following sections of the CCA should be repealed:
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    - the price signalling provisions
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Avoiding changes that have not been proven to enhance competition

26. Some proposed changes risk harming vigorous competition and it has not been demonstrated that there is a clear net public benefit in:
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    - providing structural remedies (i.e. divestiture powers) beyond the context of a breach of the merger provisions
    - providing a 'cease and desist' power for the ACCC
    - increasing maximum penalties
    - changing the private profitability test for declaration under Part IIIA of the CCA.

4. Regulatory institutions

Roles and responsibilities

Any assessment of whether regulatory institutions are meeting the needs of the modern economy must ask whether the structure of Australia's core competition-related regulators is best placed to deliver the required outcomes.

The ACCC combines these functions:

- Competition, including mergers, cartels and other activities that can affect competition.
- Consumer protection and product safety.
- Pricing and access regulation of monopoly infrastructure (which includes the ACCC's own pricing and access roles in telecommunications, water and prices oversight of airports, as well as the Australian Energy Regulator, which is housed within the ACCC).

Many international jurisdictions combine competition and consumer regulatory functions in one organisation. Australia and New Zealand are unusual in having all three core competition regulatory functions combined in the one body.

The review panel should consider the merits of creating a separate national pricing and access regulatory body in Australia. This could be a centre of excellence and capability around access and pricing, and enhance the consistency and application of these principles nationally.

This new body would combine the pricing and access regulation responsibilities currently held by the ACCC, the AER and state and territory regulators. This would leave the ACCC to focus on its competition, consumer protection and product safety functions.

The BCA acknowledges there may be economies of scale and scope that support the retention of the ACCC's existing model, but it also has its drawbacks. These are:

- The regulation of businesses with substantial market power under the third function is by its nature an intrusive role and one where the regulator is involved in effectively shaping a market. When mixed with the first two functions, this could have the potential to skew decision making on important competition and consumer matters.
- When the National Competition Council, Australian Energy Market Commission (AEMC) and state pricing and access regulators are added in, Australia has eleven separate pricing and access regulation agencies for a country of 23 million people. This can lead to:
  - The risk of inconsistent approaches to similar issues across jurisdictions and sectors, adding to compliance costs and uncertainty for businesses operating in multiple jurisdictions.
  - Fragmentation of capacity, knowledge and expertise of specific issues and industries across different jurisdictions.

- Difficulties managing the peaks and troughs of their workload. With longer regulatory cycles it can be difficult to retain capacity and expertise, or skill-up quickly when a new issue emerges, such as an access dispute.

A new national pricing and access regulatory body could overcome these drawbacks and lead to improved regulatory performance. We recognise there might be substantial transitional costs of changing the model, and these costs would need to be rigorously assessed against the benefits of reform.

Regulator performance

Good regulation that is well administered can be pro-competitive. But regulation that is administered in a way that is uncertain, slow, or unnecessarily complex and expensive, can dull competition in markets and negatively impact on economic growth. The review panel can address business concerns by improving regulator performance in these areas:

- expectations and oversight
- clarifying policy roles
- timeliness
- the use of compulsory investigatory notices
- transparency
- use of the media.

Expectations and oversight

For regulators that impact on competition, including the ACCC, there is room for improvement in terms of:

- Stronger independent oversight of performance.
- Clarity of timeframes, publication of performance and explanations for failing to meet timeframes.
- Clarity and transparency of purpose, including through public statements of expectation and adherence with clearly documented risk-based approaches to compliance and enforcement.
- Better incentives for timely regulatory decisions and for undertaking reforms to streamline processes.

The Australian Government has committed to each minister issuing charter letters to the chairs and chief executives of Commonwealth regulatory agencies outlining the minister's broad policy intent and expectations with respect to their policy and administrative powers.

The BCA endorses this approach and recommends that the letters be made public. Regulators should operate within governance frameworks that provide them with incentives to balance rigorous enforcement with efficiency and facilitating economic progress, while continually improving their processes.

A critical aspect of enhancing accountability is improving the performance oversight framework. Independent regulators are accountable to parliament via the minister responsible for their legislation. This accountability must ensure that their overall efficiency and effectiveness is subject to appropriate scrutiny, without undermining the independence of their decision making on specific matters. External oversight should considered.

Clarifying policy roles

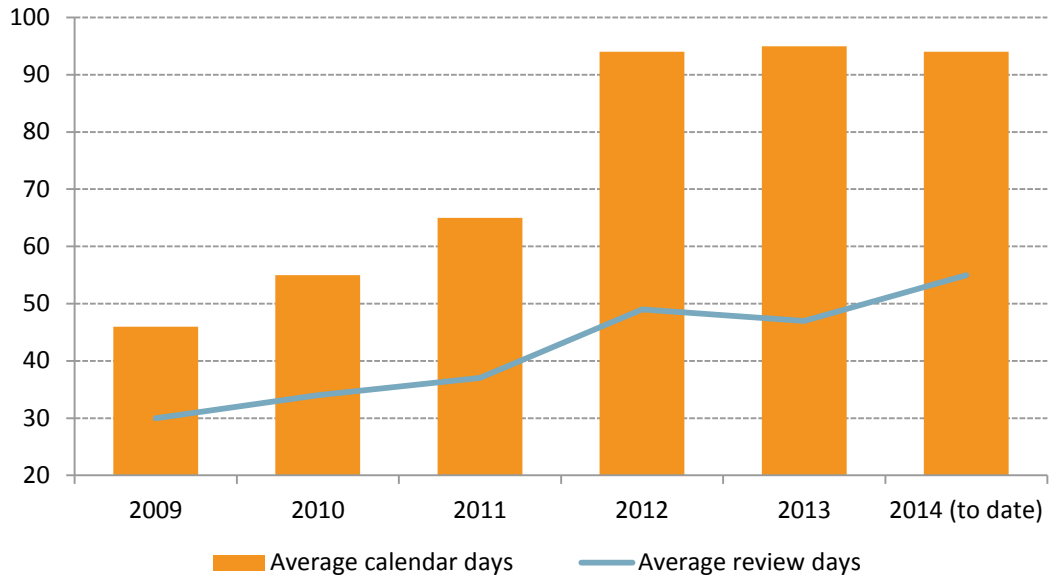
As a general rule, it is not appropriate for regulators to make policy. The Commonwealth and state and territory governments should continue to address sector-specific concerns through judicious use of targeted market studies that focus on the public interest, rather than the interests of specific competitors.

However, it is not appropriate for a regulator to have the general power to initiate its own formal market studies. Detailed market studies or reviews should only be initiated by the government where there is clear evidence of systemic problems or significant public concerns that need to be addressed. Providing a regulator with such a power would risk undue interference in competitive markets in the absence of any clear problems, would impose unjustified costs, and would encourage 'fishing expeditions' to circumvent appropriate limits on the regulator's investigative powers.

Timeliness

Time taken on merger review processes has increased substantially in recent years, with average review days increasing from 30 in 2009 to 55 in 2014.

Figure 4: Time taken for ACCC to review mergers over time, 2009–2014



Source: ACCC Merger Register. Note: 'review days' exclude days on which the ACCC has suspended the review to await information from merger parties or coordinate with overseas agencies.

In general, it is acknowledged that the ACCC is responsive over time to concerns in relation to its administrative clearance process. For instance, following feedback since the Dawson review, the ACCC adapted its process to publish detailed explanations of issues in complex merger matters.

Nonetheless, best practice regulation would involve a form of annual process performance review whereby transparent data on the ACCC clearance review time periods could be examined and opportunities to improve the process would be identified. This process would best be conducted by an independent peer review.

Compulsory investigatory notices

The use of compulsory investigatory notices (section 155 notices) has increased significantly over the past financial year, rising to 358 notices from 175 in 2011–12. BCA member experience suggests that these notices are being framed more broadly than in previous years, and becoming more time consuming and costly to comply with. BCA members are increasingly concerned about the broad scope of 155 notices, and believe there should be more clarity as to their purpose and intent. In the case of mergers this can involve searching millions of documents, reviewing tens of thousands of documents and producing thousands of confidential documents in full, even where only a small portion of the document contains the relevant material.

Given the costs imposed by these processes, there would be benefit in requiring an annual benchmark review of the ACCC's use of s155 notices, including a review of the costs of production and the utility of the information provided.

Transparency

There is an issue in relation to the transparency for merger parties of the information and analysis upon which the ACCC makes decisions. There is a real risk that information and analysis that is not tested may be unreliable or information and data provided by merger parties is obscured. Various improvements by the ACCC over the years have not addressed the fundamental problem that merger parties do not have access to, and an opportunity to respond to, the record before the ACCC Commissioners make their decision.

As Christine Varney, former Assistant Attorney-General of the United States Department of Justice's Antitrust Division has identified, transparency is vital to fair process:

> Regardless of the substantive outcome of a government investigation, it is important that parties involved know that the process used to reach that outcome was fair. The two concerns – substance and process – go hand in hand. Complaints about process lead to concern that substantive results are flawed, whereas a fair, predictable, and transparent process bolsters the legitimacy of the substantive outcome. Both are important. (2009)

Use of the media

The issue of regulator conduct in the media is relevant to the ACCC, particularly where there is public discussion of matters which are subject to private investigation on foot, or matters before the courts.

The Dawson review recognised that it was valuable and appropriate for the ACCC to use the media in many circumstances, particularly in educating and informing businesses and consumers about their rights and obligations under the legislation. However, in the case of ongoing investigations or legal proceedings, the review was concerned that the ACCC should ensure that its use of the media did not interfere with due process.

The review accordingly recommended that a media code of conduct should be developed, in consultation with interested parties. The BCA notes that this recommendation has not been implemented and business remains concerned about the potential of investigations being prejudiced by the media conduct of interested parties, including the ACCC.

Implications

Poor or inefficient administration of competition policy by regulators can impose significant economic costs from:

- ***Unnecessary delays*** to approvals, decisions and other regulatory processes thereby deterring investment and economic growth, with significant costs for the community and government.
- ***Uncertainty*** over timeframes for decisions, or the approach that a regulator will take in a particular matter, which creates investment risk.
- ***Excessive compliance costs*** where the regulator takes an overly burdensome approach to enforcement, compliance and its information-gathering powers.
- ***Regulatory spread*** as regulators make a concerted effort to expand their powers to fulfil what they consider to be their rightful objectives.

The posture of regulators has a significant influence on the agility of firms and their propensity for taking risk. If Australia's business environment is to encourage innovation and global competitiveness, regulators need to strike the right balance – efficiently enforcing the law and encouraging economic progress that is in the national interest.

Recommendations

Roles and responsibilities

27. The Competition Policy Review should assess whether there is merit in some consolidation of pricing and access regulators, including related functions from the ACCC, Australian Energy Regulator and state and territory regulators.

Clearer accountabilities

28. All governments should implement a new performance and accountability code for all regulators in omnibus legislation. Such legislation should include provision for:
    - A statutory objective applying to all non-economic regulators to promote economic progress in the discharge of their various functions.
    - A balanced performance reporting framework around regulator performance that would assess not only the enforcement and compliance activities of

regulators but the extent to which these are undertaken efficiently, with a particular focus on whether their practices unnecessarily hinder competition.

- Regulators to prepare annual public 'Statements of Intent' that outline the basis for measuring the success of the regulator, in agreement with the portfolio.
- Regulators to establish public targets on streamlining their processes to reduce regulatory burden and reduce barriers to competition (including through measurable reductions in delays) each year.
- Regulators to document, regularly update and adhere to a risk-based approach to compliance and enforcement activities.
- Charter letters from ministers to the chairs and chief executives of regulatory agencies should be made public.
- Regulators should publish standard timeframes for decision making and explain where performance not been met.

Improving performance

29. The ACCC's informal merger clearance processes should be improved, with an examination of the merits of:
    - Implementing an annual independent benchmark review of ACCC merger clearance processes. By focusing on process improvements, it would seek to identify opportunities to enhance timeliness and develop ways to better target the use of investigatory notices, but would not revisit the merits of the substantive decisions made by the independent regulator.
    - Revising the merger process guidelines to adopt a practice of transparent disclosure to the merger parties of the record on which the ACCC makes its informal clearance decisions, subject to appropriate confidentiality arrangements.
    - Implementing a form of internal merits review of ACCC informal clearance decisions by a panel of Associate Commissioners not involved in the day-to-day operations of the ACCC. This review would be 'on the papers', with oral submissions from the parties.
30. Regulators' public communications, particularly during the course of investigations and court proceedings, should be consistent with a code that protects due process and the reputations of those who have not had a court finding against them. Such a code would be applicable to all regulators.
31. Regulators should not have the general power to initiate their own formal market studies.

5. Institutions to drive ongoing reform

Issues

Establishing and successfully implementing a wide-ranging program of reform to break down regulatory barriers to competition will require a coordinated effort across all levels of government.

State governments require incentives to initiate and undertake difficult microeconomic reforms that have a national benefit. This is because proportionately fewer of the fiscal benefits of productivity-enhancing reforms accrue to state governments. This is due to national taxation arrangements which see less than 50 per cent of state government revenue collected through state government taxes; the remaining revenue is comprised of Commonwealth grants, the GST and charges.

The recent approach to incentivising states to undertake microeconomic reforms that have a national benefit has been through National Partnership Agreements. This approach has not delivered the desired results. For example, the Seamless National Economy Reforms have not delivered all the productivity-enhancing outcomes that were intended.

A new approach is needed for two reasons. Firstly, the approach taken under the Seamless National Economy, which was characterised by close Commonwealth oversight of milestones that were often not related to reform outcomes, is ill suited to incentivising state government reform.

The Commonwealth adopted a ‘micromanagement’ approach to incentivising states to deliver reforms. This approach focused on administrative outcomes – such as producing reports or Regulation Impact Statements – rather than reform outcomes. Consequently, states were able to achieve most milestones without necessarily delivering reform benefits on the ground. There were also national partnerships to deliver Commonwealth-own initiatives, which did not necessarily have the buy-in of state governments.

Secondly, many of the big gains from microeconomic reform do need national coordination but they do not need a national approach. National partnerships are inherently a joint reform agreement between the Commonwealth and states, and this form is ill suited to incentivising state-only reform.

The need for a major focus of the review to be on establishing an effective institutional framework to implement reform is underlined by the lack of progress on many of the regulatory barriers outlined – planning and zoning regulation, trade licensing and retail trade restrictions. This is despite being on the national reform agenda and subject to Productivity Commission reviews.

Implications

If competition policy reform is seen as a Commonwealth-only responsibility focused on the CCA without an effective institutional framework to drive all governments to be accountable for reform, then Australia will not realise the benefits of major microeconomic reform.

Barriers to competition permeating state and local regulation will largely remain in place continuing to detract from productivity growth and Australia's competitiveness will lag further behind. Business costs will be higher than they otherwise would be and consumers will have less choice and pay more for goods than they otherwise would.

The Commonwealth Government will forego the fiscal dividend of productivity improvements achieved through reforms. Even a long-run GDP increase of one per cent would deliver over $5 billion to the Commonwealth budget annually within 10 years.

Australia must find a better way of getting microeconomic reform implemented, rather than repeatedly analysing and making recommendations about the same regulatory barriers. Modelling a framework on the past success of National Competition Policy is a sensible place to start.

Recommendations

32. Commonwealth, state and territory leaders should commit to implementing a comprehensive package of reforms to remove barriers to competition that embody a new global mindset. This pro-competitive package should include agreement to implement:
    - a renewed program to engage all governments in reviewing and reforming anti-competitive legislation
    - robust processes to prevent new anti-competitive provisions in regulation
    - amendments to align Australia's competition law framework with international best practice principles
    - measures that ensure all the nation's regulators contribute to removing unnecessary barriers to competition and thereby foster national prosperity
    - reforms to drive competitive neutrality in government service provision through proper adherence to competitive neutrality principles, outsourcing and privatisation.
33. The Commonwealth should agree to share increased tax revenue resulting from the implementation of reforms, by providing an ongoing funding stream of substantial and untied productivity payments to the states and territories. This funding stream should not have a specified end-date, and should be indexed by inflation and population growth.
34. The funding should be 'money at risk', with any jurisdiction not fully meeting its commitments having funds withheld. The Productivity Commission should annually and publicly assess the progress of each jurisdiction in achieving the objectives of the intergovernmental agreement. This assessment should include public recommendations to the Commonwealth Treasurer regarding the withholding of any productivity payments.
35. Extend the Productivity Commission's ongoing annual benchmarking program by establishing rolling audits of the cumulative regulatory burden in each industry sector at least every five years, with recommendations for streamlining regulation.

Recommendations

1. The panel should design a competition policy framework that reflects a global mindset by promoting flexibility, innovation and productivity in the national interest of enhancing Australia's competitiveness.
2. The Competition and Consumer Act (CCA) should be amended to clarify that in any competition assessment, the global dimension of markets must be taken into account, and dynamic competitive effects in markets are to be preferred over static measures such as historical concentration.
3. Within three years, states and territories should implement mutual recognition for occupational licences that would enable people with valid licences in one state to work in another state, based on the 'drivers licence' model.
4. Remove the legislated cabotage restrictions in the Coastal Trading Act 2012 to move to an open, globally competitive coastal trading sector, with foreign and Australian vessels continuing to be subjected to all other Australian laws.
5. Repeal the Australian Jobs Act, which mandates government-approved Australian Industry Participation Plans for private investment projects over $500 million.
6. Australian governments should adopt as a principle that where a regulated good or service is tradeable, and subject to a regulatory approval by a European Union, a United States, or Canadian national regulator, then there should be a strong presumption in favour of automatic recognition of those countries' approval. This is a process that individual Australian jurisdictions should be prepared to adopt unilaterally.
7. Australian governments should implement measures to deliver more timely and predictable decision making regarding planning, zoning and other land development, underpinned by a suite of reforms that involves all states and territories:
   - conducting improved strategic planning that provides land-use permissibility for economic development, including infrastructure, major energy, industrial and resource projects, in the same way as is done for future housing settlements
   - committing to introduce progressive targets to shift 80 per cent of the share of development (residential and commercial) towards streamlined processes – that includes code-assessable development
   - adopting a single major project approval process for major energy, resource, infrastructure and industrial projects based on a dedicated assessment track that includes one statutory timeframe from Environmental Impact Statement exhibition through to a project decision, and all secondary approvals.
8. Australia's governments must immediately set a timetable and process for aligning state-based retail trading hours, and coordinate a state-based reform agenda for removing the most restrictive and inconsistent regulatory restrictions affecting the retail sector.

9. Reviews of anti-competitive legislation or other policy settings should continue to apply the National Competition Policy principles.
10. All governments should have robust, legislated, two-stage Regulatory Impact Statement processes in place that explicitly test all new regulatory proposals against the competition principles, and this process should be overseen in each jurisdiction by an independent agency.
11. Any exemption from the Regulatory Impact Statement process should be approved by the leader of a jurisdiction, with the reasons published and a post-implementation review undertaken.
12. Government service delivery should, as far as possible, follow market principles and be fully contestable to drive innovation and better service delivery, with priority given to health, education, and transport and infrastructure services.
13. Australia's governments should recommit to the competitive neutrality policy and implement nationally agreed procedures for its application that set out:
    - how each government will implement competitive neutrality policy as they move to promote competition in government service delivery
    - a clear process for responding to any recommendations arising from an investigation by the independent competitive neutrality complaints regulator
    - transparent and accessible reporting on the government's response to findings by the independent competitive neutrality regulator, including remedial actions taken
    - principles for identifying and specifying non-commercial objectives of government businesses and how those activities should be transparently funded
    - guidance on how competitive neutrality should be applied to new, start-up government businesses, for example, on the matter of the length of time over which a commercial rate of return should be achieved.
14. Australia's governments should pursue a renewed agenda for upgrading infrastructure regulation to enhance competition and meet the future needs of the Australian economy. A new agreement should include reforms that will promote new and efficient investment in infrastructure, including commitments towards:
    - enhanced consistency, capability and performance of Australia's economic regulators
    - a new timetable for privatising infrastructure businesses to capture efficiencies from private ownership and unlock public funds (including via the Recycling Assets Fund)
    - reforms to pricing infrastructure that move towards full recovery of the efficient costs of public infrastructure provision, including an adequate risk-adjusted return on investment.

15. Prior to the sale of any Commonwealth, state, territory or local government businesses with natural monopoly characteristics, a review consistent with the 1995 National Competition Principles Agreement should be undertaken to promote pro-competitive outcomes where possible. This should include putting in place appropriate access arrangements, even where this has the effect of reducing the sale price of the asset.
16. Governments should promote efficient investment and use of road transport infrastructure through adoption of broad-based user charging, as part of comprehensive tax reform and reform of Commonwealth and state funding arrangements.
17. The Commonwealth Government's review of the federation should assess how to strengthen incentives for states and territories to more actively search out more competitive forms of service delivery, such as the current Grants Commission arrangements.
18. The Productivity Commission should be given inquiries that separately look at each of the main areas of state and territory service delivery (education and early childhood; health and human services; justice and transport) to examine the potential to increase competitive provision, drawing on the lessons from Australian and international jurisdictions that have already implemented such models.
19. As a guiding principle, Australia's competition law must be consistent with international best practice. Consequently, it should:
    - have as a clear objective the promotion of long-term consumer welfare by protecting the competitive process rather than individual competitors
    - be aligned with the best elements of US and EU anti-trust laws, noting that Australian businesses operate in increasingly globalised markets
    - this will enhance Australia's competitiveness.

Enhancing the effectiveness of the general competition law

20. The Treasury, in consultation with business, competition law practitioners and the ACCC, should review the formal clearance mechanism, including the regulations, to remove unnecessary restrictions and requirements which have acted as a deterrent to its use.
21. The 'per se' prohibition against cartels and exclusionary provisions should be clarified to ensure that they apply only to horizontal arrangements between competitors, and the joint venture exemption should be extended to apply both to non-contractual arrangements and to joint ventures other than for the supply of goods or services.
22. The conduct prohibitions should be streamlined, and a public benefit defence adopted in the CCA, to reduce the reliance on costly and time-consuming administrative notifications and authorisations processes so as to improve the overall operation of the law.

National Access Regime under Part 3A

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Business Council of Australia

Submission to the Competition Policy Review: Main Report

JUNE 2014

Business Council of Australia ABN 75 483 216

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Contents

1. THE NEW COMPETITIVE LANDSCAPE

This is the main report of the BCA submission to the competition policy review. It contains background information and a more detailed explanation of changes required to the competition law.

This report starts by considering the new competitive landscape within which Australian businesses operate. On many levels the Australian economy and the global economy have changed markedly since the Hilmer review in 1993.

Our submission also recognises that the review of competition policy is being undertaken at a challenging time for Australia's economy. It will be vitally important to improve competition in order to:

1. *Lift productivity* to support higher economic growth, which will be under pressure from an ageing population.
2. *Strengthen the flexibility and resilience of the economy*, by supporting investment that will grow jobs that draw on a mobile and highly capable workforce at all levels of qualification.
3. *Boost Australia's ability to seamlessly integrate into developing economies* so as to respond to increasing international competition as a result of the profound and rapid changes in technology and globalisation.
4. *Unleash the power of markets* to generate benefits for the community, evident in the National Competition Policy (NCP) experience.

The review provides the opportunity to set out a blueprint for governments that will strengthen how and where competition extends across the Australian economy. This will contribute to our businesses being more competitive in global markets.

1.1 Productivity and innovation are critical for economic growth

The last 50 years of average annual economic growth of 3½ per cent has transformed the life of Australians. Education levels have increased, with large increases in the numbers of students staying at school till Year 12 and going on to further education. Housing has improved, as have transport links. Life expectancy is high. In increasingly competitive capital markets, Australia has attracted foreign investment, which has supported employment and increased choices offered to consumers across a wide range of products and services.

But, over the next 40 years, to maintain such a high standard of living, Australians will need to overcome a number of challenges and exploit a number of opportunities for growth, including the increasing economic relationship with the rapidly growing countries of our region.

So the country faces two choices. It could adopt the path of:

- less reform, where growth slows to 2.7 per cent on average (as the working-age population declines, as outlined in the latest Intergenerational Report). Under this scenario, by 2053 Australia will be a $4 trillion economy supporting an ageing population, having never sought to actively lift economic competitiveness or offset looming demographic disadvantages

- more reform, as it did in the 1980s, 1990s and early 2000s, and seek to restore growth rates to levels more like the average 3.5 per cent that has been achieved in the past. By 2053, Australia would be a $6 trillion economy, having taken international competitiveness seriously and made active decisions to offset the emerging demographic challenges.[1]

The BCA advocates the latter path, which is one where all Australians can enjoy the benefits of higher incomes, more and better jobs and greater wealth across all generations.

In many respects, the restructuring of many government-dominated markets that occurred two decades ago are government reforms that will assist Australia adapt to these new challenges. Businesses and markets are, by their nature, much more nimble and responsive to changing conditions. It seems widely recognised that government can best contribute to strong banking and insurance markets through robust regulation – not through ownership. Freight rail operations are mostly the province of the private sector, and the privatisation of electricity generation, and electricity and gas networks, has largely been successful. Farmers are free to grow what they want and sell to whom they wish, rather than being subject to the decisions of statutory monopolies.

1.2 A more flexible and resilient economy

More vigorous competition across the economy has created incentives for individuals and businesses to innovate – to produce products more cheaply, or to develop products that better meet the needs of their customers – which in turn has made businesses more globally competitive.

Both Professor Hilmer and former Productivity Commission Chairman Gary Banks have highlighted the importance of enhanced competition to innovation and competitiveness, in particular through its positive impact on strengthening the flexibility and resilience of the economy.

As Professor Hilmer recently noted:

> Competition is a very powerful force. It's one of the forces that's shaped not just an economy but a society. There are others: there's patriotism, there's relationships with families and other people, but competition is a powerful force. People like winning, people like competing, and if you unleash competition you generally get tremendous results. (2014, p. 4)

Competition gives consumers power, as businesses either meet their client's needs or are ultimately forced from the market. Hilmer also described the other complementary incentive policies such as taxation and corporate governance arrangements and capital markets, which encourage boards to focus on performance (rather than conformance), as well as flexible labour markets.

These incentive policies are distinguished from enablers (Hilmer) or capability policies (Banks). These include policies to improve infrastructure, education and skills, general public services, or the innovation system. Effective policies in these

1. Economy calculations are based on 2011-12 dollars

areas allow, but don't on their own encourage, performance improvements by businesses, and thus productivity growth.

The OECD's 2013 review of the literature has highlighted that businesses facing more competition experience faster productivity growth. This comes from a combination of individual firms improving in the face of the competition from more productive firms, and from more efficient rivals taking market share. The OECD also highlighted a growing literature that more vigorous product market competition improves management quality, by driving out the very poorly managed firms.

A range of policies can encourage more robust competition:

- Reductions in trade barriers, including tariff and other requirements, can expose domestic producers to greater competition from international suppliers, and allow Australian business to compete more effectively in international markets.
- Liberal foreign direct investment rules can facilitate new entry into domestic production, bringing new technology, products and management approaches.
- Structural reform of statutory monopolies can introduce competition into sectors where it previously was not permitted.
- Effective competition law enforcement can reduce the prevalence of cartel behaviour, mergers that lessen competition, or misleading behaviour by businesses that harms competition.
- A reform of legislation that limits or restricts competition and other arrangements can enable businesses to compete more vigorously in existing markets.

Policies that facilitate new firms entering markets and allow existing firms to change rapidly can also allow the economy to respond flexibly to economic shocks and structural change. At the moment, as mining investment slows, resources will need to move to other areas of the economy. However, if there are long delays associated with growing a new or existing business, then it becomes more difficult for people and business inputs to be redeployed in the face of changing demands.

1.2.1 Defining competitive markets?

Changes to competition policy should acknowledge that more vigorous competition which delivers broad benefits does not necessarily require more competitors in a market.

A simplistic view of the world would equate how competitive a market is with the number of participants or the market share of the key players in that market. However, this approach has been proven to give too much emphasis to the structure of the market, at the expense of a focus on the conduct within a market.

As the literature on competition has developed, a consensus has emerged that it is the degree of *contestability* – that is, the threat of entry or loss of market share – rather than current levels of market concentration, that drives the intensity of competition.

A market can be concentrated but still highly competitive, if it is open and contestable and the switching costs are low for consumers (Exhibit 1). Australia's

low trade barriers, and open approach to inbound investment, along with a generally sound business environment, make entry by new participants a real threat in most Australian industries. Digitisation and increasing globalisation have only reinforced this external competitive pressure.

Australia has many examples of concentrated industries with vigorous competition. The two main newspaper groups accounted for a combined market share of 86 per cent in 2011, but competed vigorously both for readers and advertisers (ABC, 2013). The two main brewing groups have 83 per cent of the beer market but competition from other drink makers, imports and craft brewers provides a strong competitive discipline (IBISWorld, 2014a). The two main soft drink manufacturers have 86 per cent of the market, but compete with each other and other small players (IBIS World, 2014b). JB Hi-Fi was reported to have 52 per cent of recorded music sales in 2012, but this is a product line that has faced vigorous competition from digital downloading sites and (more recently) streaming services (Deloitte, 2012).

Some very fragmented markets may not generate the benefits of competitive rivalry that more oligopolistic markets do in terms of innovation in products and services. For example, the supply of various building trades is made up of many small firms, often a self-employed plumber, electrician or carpenter, as well as some larger firms. While the prices that tradespeople may be able to charge builders will vary with the building cycle, the innovation in these areas does not come from small start-ups but tends to come from suppliers, or from the practices of larger firms. For example, the large number of individual taxi operators has not seen them compete effectively on quality or price, although this is changing with the advent of new technology in this sector.

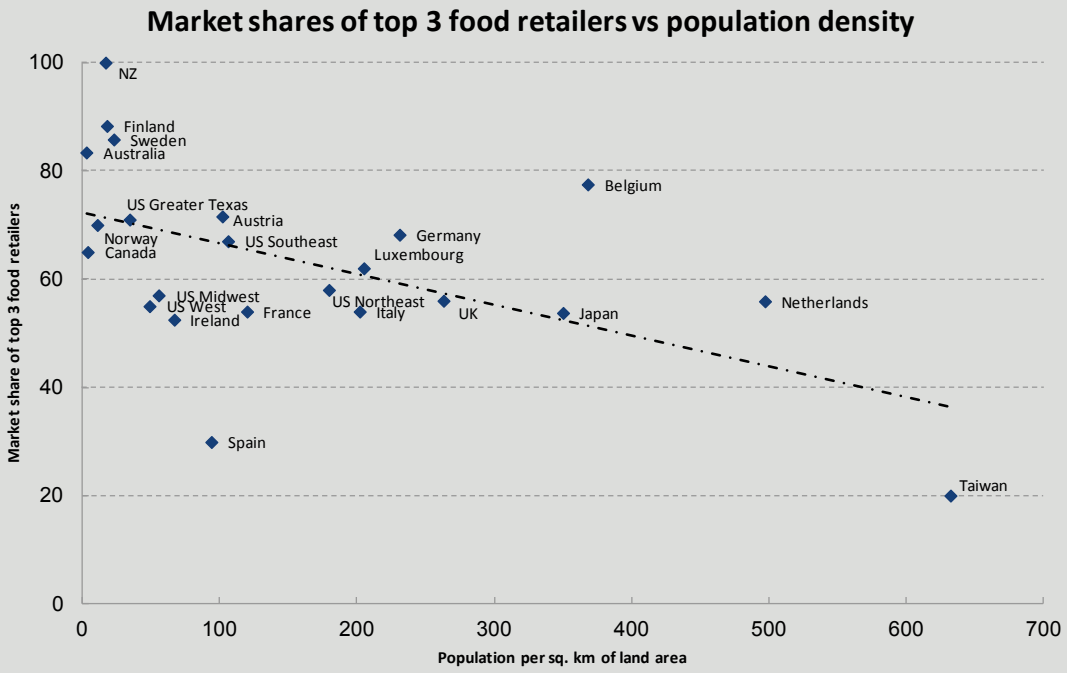
Exhibit 1: Concentrated markets: How do Australian supermarkets compare?

Much of the public comment about the effectiveness of competition policy in Australia has focused on the market share of Australia's two largest supermarket chains. Some commentators cite data that shows the combined market share of Australia's largest supermarket chains is greater than that of the United States, and the United Kingdom. But these are markets of 300 million and 60 million consumers respectively, and any comparison can be misleading and requires more thorough analysis and explanation.

When the Australian market of 23 million consumers is compared to smaller markets a different picture emerges. The publicly available data of the shares of the three largest food retailers indicates that the Australian food retailing market is less concentrated than that of Sweden, Finland, and New Zealand. The level of market concentration is somewhat higher than that of Austria, Belgium, and the larger German market.

Comparing market share by population density reveals that markets with lower population densities tend to have higher market concentrations. This is as a result of the greater need for economies of scale, scope and density for distribution, store oversight and marketing across a more geographically dispersed network. In contrast, markets with relatively higher population densities tend to support low market concentration, suggesting the benefits of consolidation in those markets are relatively smaller.

Market shares of top three food retailers versus population density



Source: BCA estimates based on data from various sources, including IBIS World, USDA, Euromonitor, World Bank, IMF and US Census Bureau.

1.2.2 Dynamic nature of markets

Even where high market share has provided the potential for some firms to exploit a degree of market power, such high market share can be transitory in increasingly dynamic markets. For example, Nokia had 41 per cent of the world mobile phone market at its peak, but that has reportedly dropped to 11.5 per cent in the first quarter of 2014, down 5 per cent in the last 12 months (Whitney, 2014).

Creating a business environment where growing businesses can thrive and challenge incumbents is critical. The OECD's *Science, Technology and Industry Scoreboard 2013* reported that while young firms (five years old or less) accounted for only about 20 per cent of non-financial business sector employment over the past decade, they generated nearly half of all new jobs (OECD, 2013b). Other recent analysis in the United States has highlighted that it is young businesses, rather than merely small businesses, that generate the most jobs (Hilmer, 2014; Haltiwanger, et al., 2010).

These growing businesses, often with innovative products and/or business models, face greater challenges than established businesses (large or small) in dealing with regulatory approvals and putting in place processes to meet regulatory standards. Growing businesses can be a new and small start-up, or new businesses supported by a larger parent, such as Bunnings Hardware, but with a different business model.

The higher impact of regulation on growing businesses was borne out by a 2013 survey in New Zealand, where 40 per cent of businesses considering expansion found regulation a barrier to that growth, compared to 34 per cent of all business (Colmar Brunton, 2013). This is despite New Zealand having a substantially more streamlined regulatory environment than Australia according to international comparisons.

1.3 Becoming more globally competitive

The next two decades will require Australia to improve its ability to seamlessly integrate into the economies of our neighbours. The profound and rapid changes to technology and increasing globalisation have increased the extent to which all our businesses are exposed to international competition.

However, the last decade has seen Australia's international economic competitiveness decline across a range of measures (Exhibit 2). The Productivity Commission reported that Australia's productivity growth between 2007 and 2010 was lower than eight peers – France, Germany, Sweden, Ireland, the United Kingdom, the United States of America, Singapore and South Korea (PC, 2014a). Alongside this low rate of productivity growth, the high Australian dollar has put further pressure on trade-exposed sectors.

Exhibit 2: Australia's international competitiveness

During the last decade Australia's productivity growth has languished and international competitiveness across a range of measures has declined:

- The World Economic Forum placed Australia 21st out of 148 countries on its Global Competitiveness Index, down from 15th place a few years ago.
- The World Economic Forum identified labour regulation, government bureaucracy and tax rates as the most problematic factors for doing business in Australia.
- The World Economic Forum placed Australia 23rd out of 138 countries on its Enabling Trade Index 2014, down from 15th place in 2010.
- A study of manufacturing cost competitiveness across 25 countries by the Boston Consulting Group (BCG) found Australia had the highest absolute costs and the largest decline in competitiveness (equal to Brazil) over the last decade.
- Australia's retail and wholesale sectors are 20 per cent less productive than the average productivity of their global competitors, according to a study by Deloitte.

Sources: WEF, 2013 & 2014; BCG, 2014; Deloitte 2013.

Countries compete for investment and skilled labour by creating the best opportunities for business to thrive. Several other small and sophisticated open economies have positioned themselves to grasp the opportunities ahead in part by creating world-class regulatory systems, while retaining essential regulatory protections. For example, highly ranked smaller economies according to the 'Doing Business' project were Singapore (ranked no. 1), New Zealand (no. 3), Denmark (no. 5) and Norway (no. 9). Australia was ranked no. 11 (World Bank, 2013).

Regulation that reflects this new competitive landscape will deliver the full benefit of these developments to Australian consumers and promote our national competitive position.

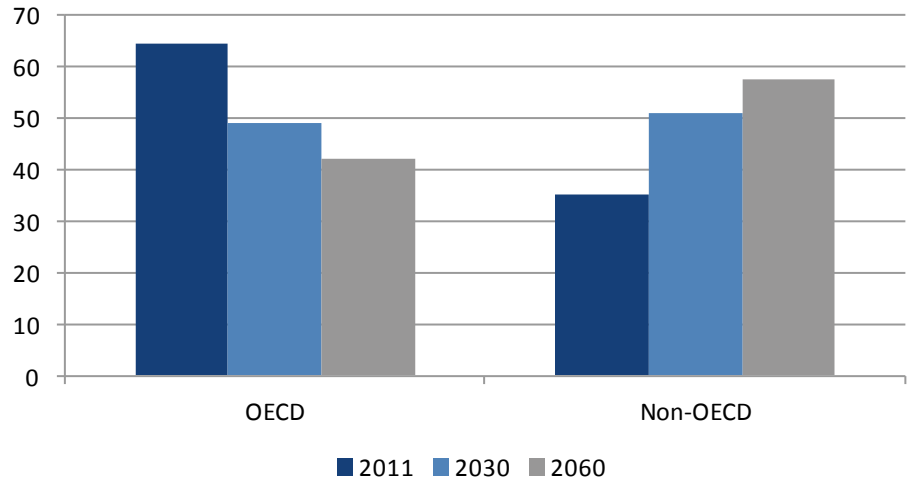
1.3.1 Adapting to changing technology and globalisation

The challenge facing this review is to set out a program that will help transform the economy for the next 20 years, as the program coming out of the 1993 National Competition Policy Review (the Hilmer review) helped prepare Australia for the last 20 years. A wide range of markets are being transformed by technology and other forces (Exhibit 3).

The external environment facing the small and large Australian businesses that generate wealth has changed dramatically. At the same time, this presents considerable opportunities for growth, particularly from emerging markets in Asia. Emerging markets are now increasingly important drivers of global economic growth and will account for an increasing share of the global economy, as illustrated in Figure 1. To date, Australia has been successful at capturing growth opportunities from China, which now represents almost a third of Australian exports, up from just 2 per cent in 1990–91.

Figure 1: Growth in emerging markets

Per cent of global GDP



Source: OECD, 2012a. Note: measured in 2005 purchasing power parity.

As a result, Australian companies are facing a different set of suppliers, customers and competitors than was the case 20 years ago. Trade barriers and transport costs have fallen, and many countries in our region developed to the point where they can produce goods that previously would have been only manufactured in more advanced countries. Cars come from Thailand, Korea and China in increasing numbers. Our clothing comes from Vietnam and China. And in return, Australia has met the demand from these rapidly developing countries for minerals, high-quality food, tertiary education and, increasingly, tourism.

Australia must become an integral part of Asia's growth story, and our policy settings should make it easier for Australian firms to establish a presence in the region. Our firms should be able to strengthen our linkages by bringing in the best

and brightest talent from the region and help their Australian staff gain experience working in Asian markets.

Exhibit 3: Examples of rapidly changing markets

Technology can transform established markets in a very short time, confronting some incumbent businesses with losses in market share and falling prices, and others with exciting market opportunities, while challenging existing regulatory and tax settings.

Taxis: Australian-based businesses – large and small – are increasingly able to export into a broader range of markets. In the same way, Australian consumers can more readily purchase from international outlets. However, as the Australian market becomes more integrated with international markets, the impact of unique Australian regulation or costs of business will become more visible as barriers to competition.

Medicines: Controls on prescription medicines could be challenged by the growth in internet sales in some markets. While this is permitted under the government's Personal Importation Scheme, the growing familiarity of online purchasing and increasing cost of Australian prescriptions and doctor visits may see this source of medicines grow. Under the scheme, individuals may import a three-month supply (at the maximum dose recommended by the manufacturer) of unapproved therapeutic goods into Australia without any approval required by the TGA provided a range of conditions are met including that the goods are for that person's own treatment or the treatment of their immediate family, and that they do not supply (sell or give) the medicine to any other person.

Web browsers: The rapid pace of technological change can, in some cases, make potentially costly regulatory intervention unnecessary. For example, competition regulators in the late 1990s became concerned that Microsoft's Internet Explorer had become the dominant web browser through its bundling with the Windows operating system. Both the United States Government and European Union initiated costly and time-consuming legal action. However, technology evolved and Internet Explorer's share dropped from 67 per cent in 2008 to 16 per cent in 2014, half that of Google Chrome's 38 per cent share, and only slightly more than the 14 per cent share of Firefox, a browser produced by a not-for-profit foundation.

Sources: StatCounter, undated; TGA, 2013.

The historical distinction between 'tradeable' and 'non-tradeable' sectors has been broken down.

More markets are becoming part of the tradeable sector. Digitisation and globalisation have reduced the costs and increased the consumer convenience of buying and selling goods and services across borders. For example, books, music, financial, legal and secretarial services are easily accessible from many markets across the internet. All of this means that Australian companies have considerable

global opportunities, but they also face considerable global competition in domestic markets.

The Boston Consulting Group (2012) estimated that by 2016 the internet economy will comprise at least $4.2 trillion in G20 economies. Australian companies' experience is consistent with this trend, with substantial increases in internet income, as illustrated in Figure 2.

Figure 2: Internet income for Australian businesses

$ billion

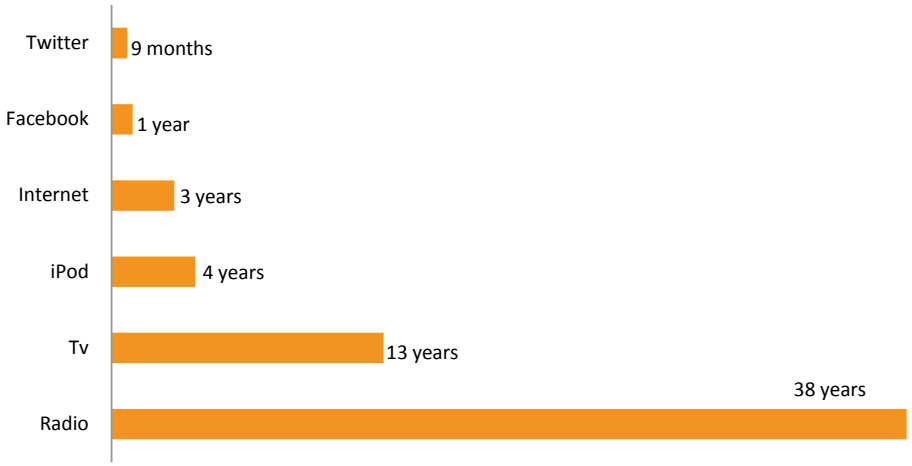
Source: ABS, Selected Characteristics of Australian Business, cat. no. 8167.0. Note: Internet income is defined as income resulting from goods and services ordered over the internet, where the commitment to purchase is via the internet.

Australian-based businesses – large and small – are increasingly able to export into a broader range of markets. In the same way, Australian consumers can more readily purchase from international outlets. However, as the Australian market becomes more integrated with international markets, the impact of unique Australian regulation or costs of business will become more visible as barriers to competition.

Declining transaction costs are breaking up value chains and driving disintermediation. Some assets (such as data captured on shoppers' transactions) are being repurposed to aid entry into previously unrelated businesses. For example, Australian airlines are offering dynamic currency conversion, and retailers are entering financial services.

Technology is also affecting competitive consumer dynamics in many sectors (Exhibit 3). Price comparison and customer review websites and social media are lowering consumers' search costs, allowing them to find and compare more detailed information about products. Distribution of goods is being transformed by online platforms, while businesses producing digital products, such as applications, books and music for mobile phones and tablets are using iTunes, Google Play and Amazon, among others, as distribution platforms. The pace of technological change and its adoption by consumers is accelerating (Figure 3).

Figure 3: Social technologies: Time to reach 50 million users



Source: McKinsey Global Institute, 2012

In many areas – although it is hard to predict where – the regulatory and policy environment will have to adapt to future realities in a timely way. For example, the idea that the best way to protect consumers purchasing travel services was through a costly state-based licensing regime imposed on Australia's travel agents may have been true 20 years ago. But in the 21st century when internet-based booking services were a growing competitive threat, regulation needed to be reformed. In late 2012, Consumer Affairs Ministers began the two and a half-year transition to abolishing this regulatory scheme (Ministerial Council on Consumer Affairs, 2012).

1.4 Unleashing the power and benefits of markets

Australia has been a world leader in pro-competitive reforms in the past. The 1980s, 1990s and 2000s were decades of broad-based pro-competitive regulation across all levels of Australian government.

In April 1995 COAG agreed to the National Competition Policy reforms, which had six key components:

- Extending the application of the competition law's conduct provisions to government enterprises and unincorporated entities such as the professions.
- A regulation review process that reformed legislation to remove unnecessary restrictions on competition.
- Restructuring principles that reformed government monopolies in infrastructure to introduce competition.
- Competitive neutrality arrangements that applied to government businesses competing with private sector firms.

- Access regimes that applied to natural monopoly infrastructure and introduced competition in upstream and downstream markets.[2]
- Price surveillance of businesses with very high levels of market power.

These reforms generated benefits across the economy (Exhibit 4).

In addition, there were important pro-competitive trade, financial market, aviation, shipping, telecommunications, corporatisation, tax, and labour market reforms that both preceded and continued during the implementation of National Competition Policy.

In reflecting on Australia's experience, Professor Hilmer noted: "Australia's GDP growth – after years of sluggish performance – became one of the strongest in the OECD between 1993 and 2005. There was also a substantial increase in productivity since the [National Competition Policy] reforms were implemented." (2013, p. 2)

The OECD noted:

> The National Competition Policy (NCP) legislative review programme stands out as one of the most important regulatory reform initiatives in Australia's history. The programme delivered important economic benefits to Australia and it has been promoted by the OECD to its members as a model approach. (2010, p. 99)

The World Bank has also gone on to suggest that the Australian experience of driving broad-based pro-competitive reform has offered important lessons for other federal nations (Alba, 2010).

[2] While access regimes have arguably worked at a sectoral level, such as electricity transmission lines and gas pipelines, the results of the Part IIIA Declaration regime are more ambiguous.

Exhibit 4: Benefits of previous competition reforms

The Productivity Commission estimated the economy-wide benefits of the National Competition Policy reforms on three occasions:

- In 1995, prior to the implementation of the reforms, it estimated that, at the 'outer envelope', Australia's level of real gross domestic product (GDP) would be 5.5 per cent higher once the productivity gains, price rebalancing and other changes associated with the reforms had fully worked their way through the economy. One of the simplifying assumptions of this modelling was that the level of employment would remain unchanged.
- In 1999, the commission undertook a similar 'outer envelope' exercise for a smaller subset of NCP reform – largely reforms of major infrastructure and statutory marketing arrangements for agricultural products – that it considered were of particular relevance to rural and regional Australia and projected a boost to GDP in the longer term of 2.5 per cent. The modelling assumed that all labour market gains are taken in the form of real wage increases, rather than higher employment. The modelling did not seek to estimate the impact of other reforms, such as competitive neutrality, which affected the subsequent competitive tendering and contracting that some states required by local governments.
- In 2005, the commission estimated the gains from productivity improvements and price changes observed over the 1990s in selected infrastructure services had led to a boost of 2.5 per cent in GDP. This exercise covered NCP and related pro-competitive reforms in the electricity, gas, urban water, telecommunications, urban transport, ports and rail freight sectors. This modelling did not seek to estimate gains in the 2000s, nor make allowance for longer-term dynamic benefits of more competitive markets, arising from stronger incentives on providers to improve productivity and innovate.

While each of the modelling exercises identified substantial economic impacts of the reforms that were included, the commission was not able to estimate the direct impact of all the reforms and thus incorporate them in the estimates. And while employment grew strongly over the period these reforms were implemented (and unemployment fell), the modelling was all based on conservative assumptions regarding the impact of increased competition on employment.

In addition to the economy-wide benefits, there were direct benefits for customers of greater competition over the last 20 years, including:

- increased convenience from longer shop opening hours
- relaxation of liquor regulations applying to restaurants and bars

Exhibit 4 continued

- reduced rail freight rates in the second half of the 1990s, ranging from 8 per cent for wheat to up to 42 per cent for some coal freight
- greater choice and lower prices of telecommunications services
- lower fares from increased domestic airline competition
- reduced impact of the drought on the farm sector arising from a water trading regime that separated water property rights from land title and allowed trading
- lower prices for conveyancing after the removal of the legal profession's monopoly.

Sources: BITRE, undated; Sims, 2013; PC, 1999 & 2005

1.4.1 Getting competition policy right

Enhancing competition can yield substantial benefits, but how markets evolve is always hard to predict, so it is critical to carefully design changes to increase the benefits and mitigate the risks.

The regulation of costly infrastructure, such as rail lines associated with mining projects and other similar assets, has proved challenging. While access regimes can enhance competition in upstream and downstream markets, there is also the risk that both uncertainty and access conditions will discourage infrastructure owners from making additional capital investments, or compromise the efficient operation of the infrastructure.

Designing interventions to increase the transparency of markets and thus empower consumers can be difficult and can have unintended impacts (Exhibit 5). The requirements of greater disclosure for financial services has led to voluminous product disclosure statements but limited evidence of benefits to most consumers.

However, a wide range of regulation intended to meet sound policy objectives can have anti-competitive impacts. Planning regulation can slow the entry of new retailers, while approval processes can delay the introduction of new medical devices. Regulation of the taxi sector has hindered the growth of competitive web-based firms, while overseas regulation of short-term house rentals has affected some new business models, such as those of Airbnb. Coastal shipping controls have restricted competition from international vessels and put Australian businesses that rely on moving their output by ship at a disadvantage to imported products.

Exhibit 5: Competition law gone wrong: The 'Loi Galland' and French prices

Regulation designed to protect businesses rather than the competitive process can have the unintended consequence of increasing consumer prices.

The Galland Act (Loi Galland) forbids French retailers from selling products below their 'actual invoiced prices'. That is, it forbids passing on individually negotiated rebates granted by producers (for example, in exchange for aisle-end display of their products) to consumers in the form of lower prices. In France, as elsewhere, large retailers' supply contracts contain a multitude of clauses that make it hard to estimate the retailer's actual purchase price. For example, a retailer may negotiate a discount or rebate for increasing annual sales of a product, or specific display placement.

The Act led to higher industry-wide floor prices for each brand's products, reducing intra-brand competition between retailers. Boutin and Guerrro of the French statistical agency noted that: "This increased profits for producers and retailers at consumers' expense." They estimated that the Act raised prices by as much as 1 per cent.

Source: Boutin & Guerrero, 2008

1.5 Implications for the review

The changing nature of the competitive landscape, and the economic challenges faced by Australia to lift productivity and workforce participation, provide the key context for the review which has a number of important implications for regulators and policymakers. These are:

- ***Competition remains paramount to economic progress***: Competition and open markets are the best way to drive productivity, but we need to adjust the boundaries in which we think about markets to reflect the new competitive landscape. This means taking into account the increasing points of access for consumers and the changing structures of global supply chains and supplier participation in supply chains. A fundamental objective should remain to protect the competitive process, rather than individual competitors.
- ***Long-term interest of consumers remains a sound objective***: Despite these rapidly evolving trends, the starting principle of putting the long-term interest of consumers as the centre of competition policy remains sound. By 'long term interest' we mean that consumers are best served by a competition policy framework that supports innovation and productivity that leads to consumers realising greater choice and quality at competitive prices. A short term focus emphasise immediate benefits at the expense of business investment in valuable new products and services that will deliver benefits to consumers over time. These points were noted by ACCC Chair Rod Sims:

  > For me, it follows ... that the ACCC's core role is protecting and enhancing the long-term interests of consumers. It is worth focusing on the importance of this "long-term" element when discussing the interests of consumers. Some could argue that price controls and inadequate regulated rates of return would, by delivering lower prices, be in the best interests of consumers. I believe, however, that such mechanisms are not in the long-term interests of consumers. While consumers may benefit from lower prices in the short term, supply side incentives will be damaged and the level of economic activity and innovation will be reduced over the longer term, to the detriment of consumers. (Sims, 2011)

- ***Government must look at markets through a global lens***: Domestic markets that appear less competitive or concentrated at first glance are likely to be much more competitive when considered, where appropriate, through a global lens. Even if a global competitor has not entered the Australian market, lower barriers to entry and the mere threat of entry provide strong incentives for vigorous competition from incumbents. In some instances, technology will facilitate a rapid build up of scale but in other areas globalisation will mean that Australian firms are competing with specialised global firms.
- ***Time is everything***: With markets changing more rapidly, businesses need to allocate capital and make decisions even more quickly to take advantage of new markets. The timeliness and consistency of regulatory decisions and approvals in this business environment is paramount. Australian companies will need to be more agile to respond to the pressure of a highly competitive landscape.
- ***Regulation may not keep pace***: The timeframes for designing, drafting and implementing regulation means it is inevitable that in many cases, prescriptive

regulation will not keep pace with these trends. This places greater pressure on governments and regulators to develop sensible non-regulatory, administrative and outcomes-based solutions in consultation with business.

At its core, the issues the panel must examine these key questions:

1. What are the unfinished competition policy reforms that we should adopt to remove regulatory barriers to competition and to enable the community to benefit from exposing government services to more competition?
2. Does our competition law serve us well?
3. Are our regulatory institutions helping or hindering?
4. Do we have the right institutions to drive reform?

Finally, implementation will be critical. The BCA notes that many of the recommendations from public inquiries, such as those of the Productivity Commission, even when they are supported are not implemented in a timely manner. Identifying potential reforms does not seem to be as much of a challenge as getting them implemented on the ground. Addressing these issues would be the basis of achieving real change for the benefit of all Australians.

Recommendations

1. The panel should design a competition policy framework that reflects a global mindset by promoting flexibility, innovation and productivity in the national interest of enhancing Australia's competitiveness.
2. The Competition and Consumer Act should be amended to clarify that in any competition assessment, the global dimension of markets must be taken into account, and dynamic competitive effects in markets are to be preferred over static measures such as historical concentration.

2. THE OPPORTUNITY FOR BROADER PRO-COMPETITIVE REFORMS

This review appropriately asks how Australia's broader competitive framework can have a positive impact on Australia's economy in the years ahead.

We see this as an opportunity to highlight problems and make recommendations in two key areas:

- removing regulatory barriers to competition.
- Extending competition into public sector markets.

There is a plethora of regulatory and other barriers that constrain the ability of businesses to compete by introducing new products and services, entering new markets, and growing in existing markets.

Good regulation manages risk, such as a health, safety or financial risk to the community. Regulation should manage risks efficiently to provide significant benefits, without imposing costs that substantially offset these benefits, such as reduced competition or more costly and poorer quality goods and services.

Poor regulation can have a direct and large impact on competition or can collectively create disincentives to compete. Consequently, it is not feasible to draw an arbitrary line between those regulations that should be in scope for this review, and those that are unimportant.

2.1 Removing regulatory barriers to competition

2.1.1 Pro-competitive regulation and growth

As noted in Chapter 1, the changing global business environment will rapidly affect Australian businesses of all sizes. This requires governments to adopt a global and pro-competitive mindset in how they regulate.

Australia has a sophisticated but complex regulatory environment. Businesses seeking to open a new facility, introduce a new product or service, or change their business model often have to navigate a complex set of approvals and compliance requirements.

This can absorb a lot of the time of a business's senior leadership. For example, an Australian Institute of Company Directors survey indicated that board members spend on average about one-quarter of their time on 'red-tape' compliance (AICD, 2014, p. 63). As Professor Fred Hilmer recently observed:

> ... governance does affect the performance of firms in terms of their ability to take risks and innovate. The governance focus in the 1990s was about performance. I was on a number of boards and the mantra was: "What can you do to encourage shareholder wealth creation". That's not the case right now. Right now it's "Will we get the remuneration report through, how can we keep the auditors happy?" It's all about conformance, and it permeates the boardroom and the management so you get far too much time and attention shifting from performance, because the time has to come from somewhere. (2014, p. 10)

While good regulation can be a driver of innovation, when regulation is overly complex, prescriptive, slow or uncertain, it can be a barrier, and make all firms less competitive than they otherwise would be.

Regulation that creates undue barriers to entry and limitations on the ability of firms to compete is found in Commonwealth, state and territory, and local government laws, particularly through requirements to obtain licences, permits and approvals. Other policy arrangements, such as purchasing rules or discretionary grants, can affect competitive markets by favouring some providers over others (Exhibit 6).

Exhibit 6: Examples of regulation that can restrict competition

Some restrictions on competition were not removed following the Legislative Review Program, either because they were assessed at the time to be in the public interest, or because governments were not willing to make the required changes.

Other restrictions on competition have been introduced through subsequent legislation, often with no or limited evidence that the competition impacts have been robustly assessed. Examples of the breadth of remaining regulation that restricts competition and warrant review in any future Legislative Review Program include:

- Regulation requiring imported cars to be modified to meet Australian-specific car design standards, as these differ from those of the United States and the European Union, restricting the scope for parallel imports and importation of second hand cars.
- Restrictions on the parallel importation of commercial quantities of books by booksellers.
- Concessional excise treatment of domestically produced ethanol while imported ethanol pays full excise.
- The displaying of discounted fuel prices on fuel retailers' price boards is specifically regulated in New South Wales and South Australia.
- A restricted number of taxi licences are issued in all state and territories, and competition from hire cars mostly restricted.
- Packaged liquor can be sold by hotels in regional Western Australia on Sunday, but not by specialist packaged liquor stores.
- Retail pharmacies can only be owned by pharmacists (whereas no such restrictions exist on medical practices in Australia, nor on pharmacies in the United Kingdom, the Netherlands, Norway, Canada and the United States).
- Restrictions on pharmacists administering vaccinations and reissuing prescriptions for long-term conditions.
- Genetically modified crops cannot be grown in South Australia and Tasmania (but can be grown in all the other mainland states).
- The sale of fresh potatoes is restricted in Western Australia (but nowhere else in Australia).
- Owner driver and independent contractor regulation are subject to industry-specific regulation in Western Australia, Victoria and New South Wales (but not other states).
- Compulsory workers' compensation insurance and third party personal injury transport insurance is only available from government monopoly providers in some states.

Sources: BCA, 2013a; Bignell, 2013; Duckett et. al., 2013; Mossialos & Mrazek, 2003; Woolworths, 2013. Note: Parallel importing is when a product made legally (i.e. not pirated) abroad is imported without the permission of the intellectual property right-holder (e.g. the trademark or patent owner). (WTO, undated).

2.1.2 Regulation that impedes competition

Regulation can affect competition in a number of ways. The OECD notes that competition can be adversely affected by:

- **Undue barriers to entry:** including limits on the number of firms permitted; the granting of exclusive rights to specific suppliers; the establishment of a lengthy and costly process to obtain licences, permits or authorisations required for operation or other start-up procedures; limits on the ability of some types of firms to provide a good or service; and start-up procedures beyond obtaining the permit.
- **Limitations on the ability of firms to compete within a market:** such as by regulating the ability to set prices, limiting the freedom to advertise, and treating incumbents and new entrants differently. Providing subsidies can also distort competition within markets and reduce incentives to innovate.
- **Reducing the incentives of suppliers to compete:** through self-regulatory or co-regulatory regimes that encourage publication of information on competing firms' outputs, sales, costs, or prices;[3] or exempting the activity of a particular industry or group of suppliers from the operation of the general competition law. (OECD, 2014a, p. 2)

The BCA notes that there are many other ways that regulation can impact on competition, and therefore competitiveness, but we have generally not commented on areas of regulation that are subject to other upcoming reviews. This includes the effect of workplace laws on competition and competitiveness (to be reviewed by the Productivity Commission), proposals to extend unfair contract terms to business (currently under review by the Commonwealth Treasury), and the impact of the tax system on competitiveness (addressed in the Commonwealth White Paper on taxation reform).

Some forms of regulation also have the potential to have a positive effect on competition by reducing search or switching costs faced by customers. It can also contribute to building customer trust, for example, through the regulation of trade measurement, the protection of the integrity of financial markets, ensuring consumer guarantees meet minimum standards and are honoured, or ensuring food standards.

Undue barriers to entry

Permits, licenses, approvals and similar processes

At the time of the Hilmer review there were numerous barriers to entry to be addressed. For example, monopoly statutory marketing of agricultural products that prevented farmers from selling their products through alternative channels, and regulation that prevented non-lawyers from offering conveyancing. Government monopolies also existed in energy retailing and rail freight.

[3] Publication of an individual business's prices that reduces search cost for consumers will generally be pro-competitive, but self-regulatory agreements that actively encourage members to adopt 'recommended prices' or require participants to only present prices in a specific form have the potential to be anti-competitive.

Now there are fewer absolute restrictions on entry, with the taxi and pharmacy sectors being the most notable exceptions. Instead there are a large number of activities that are subject to requirements for permits, licences, approvals, registration or some similar process.

While there is no comprehensive national data, of Victoria's 59 regulatory units, 54 (or 90 per cent) administer regulatory regimes that involve permits, licences, approvals, registration or some similar process. The associated burdens that hinder entry include:

- delay costs
- compliance costs (the time and resource costs of ensuring and demonstrating compliance with regulation)
- financial costs (the fees and charges levied by regulators).

These regulators issue 390 different types of requirements and 2.1 million were issued or renewed in 2012–13 (VCEC, 2013, p. 14). No other jurisdiction reports this level of information.[4]

Overly onerous requirements can discourage new entrants joining an industry, growing their business, or for those towards the end of their career, retaining their registration. The NSW Small Business Commissioner noted:

> Since being appointed as the NSW Small Business Commissioner I have conducted two Listening Tours around the State to hear directly from businesses about the impediments they face which negatively impact on their business growth. Some of the most common complaints I hear are regarding the delays and administrative burden caused by licence applications and procedures. The current licensing system has a tendency to impose rules to hinder growth rather than provide solutions to encourage new jobs, promote sustainable development and create thriving business environments. (2012, p. 1)

These approvals also come with conditions that raise costs. Mandatory continuing professional development (CPD), while potentially important for some occupations and for some industry participants, can impose substantial costs, while solid evidence of benefits is difficult to find. The building sector is one area where some states impose mandatory CPD, while others do not. The VCEC noted that the Allen Consulting Group had estimated the annual cost would have been $5.2 to $5.9 million in 2004. Smaller builders noted that the cost would fall disproportionately on those participants, and thus it could discourage entry. The evidence it would lead to better outcomes was less certain, and the VCEC recommended against proceeding until a rigorous cost–benefit analysis had been completed (VCEC, 2005).

Where the same requirements are imposed on those working full-time as those in part-time work, CPD imposes a higher cost on those re-entering an occupation part-time and on those seeking to transition to part-time work at the end of their

[4] In 2012, the NSW Government commissioned IPART to examine licensing and it reported that NSW has about 776 different types of licences, most of which are issued by departments and agencies, and about 50 by local governments (IPART, 2013).

career. This is particularly important when, as noted earlier, Australia is facing a looming demographic challenge, and governments are seeking to increase workforce participation, particularly of key groups such as mothers and mature-aged workers. However, some regulations permit part-timers to undertake the same work, but with less CPD time, casting doubt on whether the mandated training is truly essential to ensure that an identified regulatory problem is addressed.

Restrictions on new business models

In many cases regulation that imposes restrictions on competition is adopted where either less anti-competitive restrictions could be used or the regulation is unnecessary. An example of unnecessary and anti-competitive legislation is the Queensland Government response to greater competition facing taxis from regulated hire cars using new smartphone apps. Rather than welcoming this increase in competition facilitated by technology, it passed an amendment to the transport legislation that:

> The operator of a public passenger service must not require or allow the driver of a vehicle being used to provide the service, other than a taxi, to use a taximeter or a similar instrument to calculate, during or after a journey, the amount of the fare for hiring the vehicle for the journey. (Queensland Government, 2012)

The problem being addressed was not one of public safety, or consumer protection (the usual argument for regulating taxi services) but that hire cars could now easily calculate fares based on the actual trip, rather than only provide a quote in advance. The Second Reading Speech and accompanying explanatory notes made no mention of the adverse impact on competition, nor any public benefits from this anti-competitive regulatory change.

Regulatory approval processes are a critical tool for ensuring that only safe products are available for sale; that the impacts of one business's activities on the amenity of its neighbours are managed, and that the environmental values are protected. And approvals inevitably take time. However, they can also have a substantial impact on competition (Exhibit 7).

Delays and uncertainty in regulatory approvals of all types can impose large costs, and be a significant barrier to entry and the development of new products and services. Some of the delays are caused by unnecessarily complicated approval processes, including referrals to other agencies within a jurisdiction, while in other cases the delays are caused by the practices of the regulator.

In an illustration of the potential gains in reducing approval times, the Productivity Commission (2009) has found that expediting the average approval process for oil and gas projects would increase the value of projects by 10 to 20 per cent with billions of dollars of income gains for Australians.

The issue of improving regulator performance is discussed in Chapter 4 of this submission.

Exhibit 7: Examples of where regulatory delays have affected the introduction of new entrants, new products, or the growth of more competitive suppliers

Retail sector: Woolworths has highlighted how regulatory approval timelines for liquor licensing can vary across Australia. Approvals of new packaged liquor outlets take on average four times as long to be approved in Western Australia compared to New South Wales and Victoria, and involve legal fees nine and 49 times higher respectively. Woolworths noted that the delays can mean that prospective landlords are reluctant to be involved in a process so uncertain and fraught with regulatory risk, with applicants forced to pay holding rent for lengthy periods with no guarantee of a favourable outcome. The costs and uncertainty of the approval process can discourage competitive entry into this market.

Medical devices: Cochlear is an Australian-based exporter of medical devices. A key regulatory issue it faces is that a number of countries require a device to be approved in its country of origin before it can be approved for use in the export destination country. In one recent case, approval for an important product innovation took 14 months longer in Australia than in Europe. That is, after obtaining regulatory approval in Europe, it took an additional 14 months before Cochlear could even start to apply for product registrations in other key markets such as India. As a result, Cochlear was several years behind its European competitor in getting its product into a number of key markets.

Source: Woolworths, 2013; Roberts, 2012

Planning and zoning delays

Uncertainty, costs and delays caused by inefficient planning and zoning decisions significantly impact on competition by limiting the ability of business to enter new markets or to expand their operations in a cost-effective and timely way.

The issues and solutions proposed above are not new; they have been raised in a series of Productivity Commission reports (2009, 2011, 2013a & 2014c) and in COAG reforms (2008 and 2009). However, it is clear that state and territory governments have not sustained coordinated reform, and current major project assessment processes remain unproductive and uncompetitive.

The extent to which planning decisions affect competition depends on the characteristics of the industry. The ACCC's 2008 inquiry into the grocery sector identified access to suitable sites as a barrier to entry that was affected by regulation. A number of submissions to that inquiry argued that local planners should be more attuned to competition issues, and the ACCC noted that planning processes should have regard to competition issues, particularly in the supermarket sector.

In addition to ensuring the criteria for zoning decisions have regard to the competition impacts, there is also a need to carefully design processes to

minimise unnecessary delays. Encouraging states and territories to implement more timely and certain approval processes, while retaining appropriate local inputs and controls, will have pro-competitive impacts. It is clearly an area where there is scope for substantial improvement. The Productivity Commission found that:

> The regulations and agencies involved in planning, zoning and development assessments constitute one of the most complex regulatory regimes operating in Australia. This regulatory system is not like most other regimes which have a clearer delineation between policymaking, regulation writing and administration. (2011a, p. xxvi)

Major projects also have important competition impacts. Better transport links (whether road, rail, ports or airports) allow goods and people from one location to more effectively compete with suppliers in another location. Interconnections between the previously largely separate state gas and electricity networks have led to a competitive national market, and timely approval of future augmentation will be important to strengthening these markets.

The BCA has focused much of its recent work on planning and approval processes on those processes applying to major projects. It has developed a single major project approval model for state significant resources, industrial and infrastructure projects. It builds on the recommendations of the Productivity Commission and Australian and international elements of best practice.

The single major project approval incorporates all secondary approvals. This new single approval would be facilitated by a lead agency framework that provides a gateway to business investment facilitated by a single point of contact to manage major project assessment and approval. It is a separate assessment track that includes one umbrella statutory timeframe from Environmental Impact Statement (EIS) exhibition through to a project decision.

The total assessment timeframe from pre-application consultation to a decision could be 9 to 12 months – a reduction of some 2 to 3 years based on current experience, all without lowering the standards of final outcomes. If these sorts of results can be achieved consistently, it would facilitate competition in upstream and downstream markets.

Limits on ability to compete

Trading hours regulation on retailing

An example of a sector subject to substantial regulation of its operations is retail, which is one of Australia's most important sectors, employing more than 1.2 million people in 2013.

This sector is facing a new competitive threat. The advent of online retailing has changed the competitive landscape for Australia's retailers. Online retailing did not exist 20 years ago at the time of the Hilmer review, but today it is a fast-growing feature of competition, currently for selected goods and many products that can be delivered digitally, but increasingly for a wider range of products.

The retail sector is open to new domestic and foreign ‘bricks and mortar’ entrants, but is subject to regulatory controls, such as restrictions on trading hours, and sometimes slow and uncertain planning and zoning processes. The result is that across the economy Australia’s retailers are, on average, 20 per cent less productive than our global competitors, according to Deloitte estimates (2013). And the very size of the retail industry means anything that lifts its economic performance is important to the national economy. One key aspect that affects the flexibility of the sector, and the use of its capital, is the range of restrictions on shop trading hours (Exhibit 8).

Exhibit 8: Controls on retail trading hours

The National Competition Policy reform process contributed to deregulation of shop trading hours, with few restrictions remaining in the Australian Capital Territory, Northern Territory, Tasmania and Victoria. The Productivity Commission, in its 2011 report *The Economic Structure and Performance of the Australian Retail Industry*, looked at the remaining restrictions and recommended completely deregulating trading hours across Australia, but little has changed.

In Western Australia, hardware stores cannot open before 11am on Sundays if they stock both light bulbs and light fittings. This is because the *Retail Trading Hours Regulation 1988* prohibits the sale of light fittings before then. Light bulbs, yes, light fittings, no. A petrol station can sell pantyhose after 9.00pm on Thursdays – but it is illegal to sell underpants. A petrol station can sell film and flash bulbs on Sundays before 11.00am – but not a digital camera's memory card.

In New South Wales, the *Retail Trading Act 2008* makes Boxing Day shopping legal in 40 local government areas, but illegal in another 112. This gives rise to all sorts of inconsistencies and inconvenience. Boxing Day shopping is legal in Dungog, Cowra and Narrandera but illegal in Parramatta, Newcastle and Wollongong. The fact that the law picks winners and advantages some while disadvantaging others is not lost on David Borger, the Director of the Western Sydney Business Chamber, who has called for the law to be reformed: "Political leaders talk about creating more jobs and business opportunities in Western Sydney – here is the opportunity to do it with a stroke of the pen. It is time to bring retail trading on Boxing Day into the 21st century."

In South Australia, the *Shop Trading Hours Act 1977* prevents shops in Adelaide from opening before 11am on a Sunday. But an exemption is available that allows shops to open early if they sell "asbestos cement sheet and articles". In Adelaide, on a Sunday, it is illegal to sell a boat.

In Queensland, the *Trading (Allowable Hours) Act 1990* outlines a complex and confusing set of restrictions on trading hours. For example, on Saturdays, shops in South East Queensland must close by 5pm, but in inner-city Brisbane by 5.30pm, in the "City Heart" of inner-city Brisbane by 7pm, in New Farm by 9pm and on the Gold Coast by 10pm. The trading hours of 'Exempt shops' are unrestricted, but the list of such shops includes soap shops, temperance beverages shops and video cassette shops, but not hardware stores. The Queensland Competition Authority recommended deregulating trading hours and reported that such a reform would benefit Queensland by $200 million a year. This Act has yet to be reformed.

Meanwhile, online retailing is growing, with Australia Post responding to competition from other parcel delivery firms by opening its branches for parcel pickup and dispatch on Saturdays. There are no state government regulations on the operating hours of websites.

Source: BCA, 2013b; Deloitte, 2014; PC, 2011b; QCA, 2013; Woolworths, 2013

Restrictions on advertising

Regulation in New South Wales and South Australia specifically prohibits fuel retailers from advertising the discounted prices they offer for fuel. For several years, ministers responsible for consumer affairs around Australia have been considering whether to impose a national standard on fuel price boards, which would only allow retailers to advertise the discounted offer, but not the resulting discounted price. From a competition policy perspective, making any terms and conditions of special offers clear is a common requirement, and prohibiting the advertisement of discounted prices seems an unusual intervention.

Reducing flexibility

Sometimes regulation can restrict the ability of a business to redeploy its resources, either to respond to changing demand or operational issues (Exhibit 9). Examples include restrictions on the ability to re-deploy staff, for example, where they are subject to occupational licences in one state which doesn't permit them to practise that occupation in another. Zoning and planning can delay growing businesses from moving to larger premises, or opening new outlets.

Exhibit 9: Unnecessary complexity hindering competition: Virgin Australia

Australia has one of the world's most open aviation markets outside the European Union, and allows majority foreign ownership of domestic airlines, and limited foreign investment in Australia's international airlines.

To comply with the international regulatory framework, Virgin Australia is required to hold two Air Operator's Certificates (AOCs) – domestic and international – from the Commonwealth Government's Civil Aviation Safety Authority (CASA). The requirements in each certificate are intended to achieve safety objectives consistent with CASA's mission, which is to: "enhance and promote aviation safety through effective regulation and by encouraging the wider aviation community to embrace and deliver higher standards of safety" (CASA, 2013, p. 6).

The way CASA's regulations operate means they unnecessarily hinder flexibility by allowing each of Virgin Australia's pilots and aircraft to be attached to only one of these AOCs. An aircraft or pilot on the international certificate cannot fly a domestic route for the other airline or vice versa, despite many of Virgin Australia's aircraft and pilots having the identical capability and training so that they can safely operate on both domestic and short-haul international routes. If the aircraft and pilots could be simply listed on both certificates, Virgin Australia would be able to more efficiently redeploy capacity as demand changes and provide more flexibility in scheduling. This would enable Virgin Australia to compete more effectively with other airlines in the region and to better meet the needs of the nation should aircraft need to be deployed in times of crisis. The current CASA legislation does not provide for multiple AOCs to be managed within one group by the same management system despite the obvious benefits, from both a safety and economic basis, that could be achieved.

Virgin Australia also operates to several Pacific Islands using aircraft registered and flown from both New Zealand and Australia. Even though these are identical aircraft, they are subject to different maintenance support arrangements due to variations between the Australian and New Zealand safety regulations, again adding to costs and reducing flexibility to compete with regional carriers. By way of example, Air New Zealand is able to accept local national qualifications of maintenance staff (for example in Fiji) for the servicing and dispatch of their aircraft into Nadi. For a Virgin Australia aircraft registered in Australia, CASA regulation will require the establishment of a complete Part 145 Maintenance Organisation to enable the same simple maintenance activity.

Source: CASA, 2013; Virgin Australia, personal communication, 3 March 2014

Some regulation is set at a reasonable level, either at a state or Commonwealth level, but differs from that of other jurisdictions without any evidence of a material benefit from those differences. As a result, a product or service might need to be

changed, or separately tested or assessed prior to sale in a new market. This can lead to higher costs to compete in, or enter the Australian market, and/or impose delays on the introduction of new products or business models.

Occupational licensing

In July 2008 COAG agreed to develop a national occupational licensing scheme that would cover occupations relating to: air conditioning and refrigeration; building; electrical work; land transport; maritime operations; plumbing; and property agents. In December 2013, after five years of investment and consultation, the scheme was abandoned with no reasons provided. During this period the states and territories had received payments under the National Partnership Agreement to Deliver a Seamless National Economy.

After abandoning the COAG process, states agreed to work together via the Council for the Australian Federation (CAF) to develop alternative options for minimising licensing impediments to improving labour mobility. However, to date there are no proposed timelines for advancing this approach.

CAF is considering reforms based on the 'drivers licence' model, which could be implemented on a unilateral, bilateral, multilateral or national basis. Queensland has already implemented some reforms along these lines for employed electricians. State and territory governments have decided that the decision on whether to implement occupational licensing reforms will rest with individual governments and they will each have the flexibility to opt-in to reforms over time. This is consistent with a competitive federalism approach that reduces the risk of increasing regulatory burdens through harmonisation, but does not create strong incentives for governments to reform quickly in the national interest.

Different state-based occupational licensing requirements reduce the ability of people to relocate to a new job when this involves additional training and licence fees and delays in obtaining formal recognition. Licences that are valid only in one state also make it more difficult for small and large firms to service national markets and respond to changing demands. Businesses that bring together skilled trades from around Australia can minimise the time a plant is offline during annual shutdown, or move quickly to address an unexpected breakdown. Currently, businesses must ensure that all workers hold appropriate state-mandated qualifications and licences applicable to any regulated activity.

The issue is not insignificant. About 1.7 per cent of the Australian workforce changes states each year (PC, 2014b); 2.1 per cent of the work force (or more than 200,000 workers) were involved in long-distance commuting in 2011, up 37 per cent over the previous five years.

It is essential that states and territories develop a reform plan that provides the community with confidence that the regulatory objectives will be achieved in a timely manner. The issues relating to strengthening incentives to deliver timely reform are addressed in Chapter 5.

Access to global skills

Barriers to growing exports

A key constraint on the ability of our service industries to compete effectively are immigration arrangements. People are becoming more globally mobile, and Australia competes with other countries in attracting overseas students and tourists. Australia needs to ensure that our migration laws manage security and quality-of-life risks, for example, while making fair and timely decisions. Unduly complex administrative processes and delays in obtaining student and tourist visas make Australian qualifications and holidays less appealing compared with those in other countries, and the impact on competition in key markets should be one of the considerations in decision making in this area.

Another example of a regulation that impacts on competition in the export of services relates to Tuition Protection Service levies, which are imposed on providers who offer education and training to international students. The scheme that is funded by these levies is designed to protect the considerable investment international students make in an Australian education and to protect and enhance Australia's reputation as a destination of choice for international students. However, after introducing the levy scheme, the then minister subsequently made a determination in 2012 which exempted all government schools and government-owned Technical and Further Education (TAFE) institutions as they were assessed to offer 'negligible risk', but did not exempt any private providers (Evans, 2012). No Regulatory Impact Statement accompanied this instrument, nor was there any mention of competitive impacts in the explanatory memorandum. This regulatory decision gives rise to issues of competitive neutrality, which is discussed in Chapter 5.

The 457 visa scheme is a very important part of Australia's economic policy settings. Businesses overwhelmingly prefer to hire Australians first. Australian workers typically have a deep understanding of the local markets in which they operate. It is also cheaper and faster to fill skills requirements from the local workforce where there is a suitable local candidate. But the 457 visa scheme is very important for promptly filling roles with temporary skilled migrants where there are genuine skills shortages. Temporary skilled migration enables firms to enter new markets and compete with incumbent firms knowing that their immediate skills shortages can be overcome with temporary skilled migrants.

The BCA submission to the 457 visa review (BCA, 2014) outlined in more detail a range of measures that can streamline this program to make it more pro-competitive, while retaining important integrity measures to ensure that domestic workers are not disadvantaged, nor temporary workers exploited.

The new model for growth of the Australian economy will make it vital that businesses establish stronger presences in Asia. This makes it even more crucial that locally employed staff in the region can readily gain experience at the Australian operations, while Australian staff equally are able to gain experience working in Asia.

One area of regulation that affects the trade competitiveness of Australian businesses is Australia's coastal shipping regulation. The regulations provide contestability rights to Australian general licensed vessels over foreign vessels using temporary licences, which causes higher shipping rates as well as administrative and other costs. This can have a particularly large impact on some industries and in some parts of Australia. The higher transport costs make it cheaper in some cases for businesses and consumers to buy imports than Australian goods, many of which are produced in regional areas. The regulations have the effect of preventing regional areas from expanding their economies and integrating with the growing economies of the Asian region.

Since the introduction of the Coastal Trading (Revitalising Australian Shipping) Act 2012, for example, it has become cheaper to import some final product directly rather than manufacture locally, risking Australian jobs and investment. Impacts include:

- Cabotage restrictions under the Coastal Trading Act 2012 are causing Australian firms to pay shipping rates that can be up to double the rates offered by foreign ships, adding tens of millions of dollars to their cost base, and making their operations less viable as a result.
- One company saw freight charges increase since 2012 by over $3,000 a day up and down the east coast of Australia.
- Another company estimates that 1,000 hours a year is required to comply with the current regulatory arrangements (BCA, 2013e).

The Panel can recommend, alongside the concurrent government review of coastal shipping, that Australia should move to an 'open coast' in regulating the coastal trading sector by removing cabotage restrictions from the Coastal Trading Act. The Commonwealth should implement this reform to provide a much-needed boost to competitiveness across the economy.

Recognising international approvals

As noted earlier, future growth will involve being more seamlessly integrated into the markets of developing countries. In many cases they will be most familiar with, and accepting of, the regulatory standards of the European Union or the United States.

Australian consumers and businesses can increasingly purchase goods from overseas suppliers quickly and cheaply. They can be offered a wide range of choices by overseas suppliers. Very often the same or very similar product may be sold on the Australian market after it has been granted approval, or slightly modified for sale in Australia.

Businesses are also increasingly part of global supply chains and to be competitive must have access to the broadest range of specialist inputs. Where they are local operations of international businesses, the formulations of the products they produce may be based on the inputs available in the larger overseas markets. As the various plants of multinationals compete to be the regional or global production base, they need to be sure that all the necessary inputs are readily available in the Australian market.

The lack of recognition of international regulatory approvals can consequently hinder entry into new markets, as well as increase the costs and reduce the choices offered to consumers.

Many products that are sold in the Australian market must be subject to a separate regulatory approval process, even though they have been approved in other advanced country markets. For example, Accord noted that the Therapeutic Goods Administration had previously accepted that secondary sunscreen products that met the United States Food and Drug Administration standards, or those of their counterpart in the European Union, would not require additional SPF testing to the Australian Standard. Reforms intended to reduce the regulatory burden by involving NICNAS (National Industrial Chemicals Notification and Assessment Scheme) in oversight of this sector led to an increase in the burden. They report that the Director of NICNAS decided, without any impact assessment or justification, that separate testing was required.

This lack of recognition of international approvals imposes additional costs and delays on importers, and can increase the prices paid by Australian customers of those products, and in some cases limit choice of products available from Australian suppliers.

While each of these additional regulatory approvals may seem small on their own, they can have a substantial impact on the pace of innovation by individual businesses, and the cumulative impact can have a detrimental effect on competition. Australian businesses who think only locally and gain the necessary approvals can serve a market of 23 million people. In contrast, a product that has been approved for sale in one European country is automatically approved for sale across 28 countries (with a total population of 500 million), while an approval for sale in the United States provides access to at least 316 million consumers. Increasingly, Australian producers who have niche products have no choice but to think globally from the start. Australian producers require timely approvals to be competitive.

Reducing the incentives to compete

The third category of regulatory barriers to competition identified by the OECD was those provisions that reduce the incentives of suppliers to compete. The changes to the general competition law following the Hilmer review largely addressed any arrangements that permitted self-regulatory or co-regulatory regimes that encouraged publication of information on competitor's outputs, sales, costs, or prices. Statutory marketing schemes were reformed and professional association mandatory price lists were no longer legal. In addition, arrangements that exempted the activity of a particular industry or group of suppliers (such as unincorporated entities and sole practitioners) from the operation of the general competition law were reformed. The statutory exemptions in this area are now limited to examples such as the exemption of aspects of liner shipping arrangements under the Competition and Consumer Act (see Chapter 3).

2.1.3 Better regulatory processes

Australian governments' Regulatory Impact Statement processes have largely failed to deliver. Governmental organisations such as the OECD, and the Productivity Commission, and business organisations such as the BCA have long advocated the implementation of robust Regulatory Impact Statement (RIS) processes. To date, it is fair to say that the formal processes have seldom incorporated all the aspects of best practice, and implementation has been patchy. While there are good examples of where adherence to the RIS process has led to better outcomes, there are also many examples where important regulatory proposals have been allowed to bypass this process for political reasons, or where the process has been undertaken as a mere compliance process and not contributed to better decision making.

Of critical importance to this review will be ensuring governments commit to implement best-practice RIS processes, with a particular focus on enhancing competition assessments within those processes.

The BCA has been a strong supporter of a two-part RIS process, where the evidence is collected on the nature and extent of the policy problem, and thus the potential need for government to intervene is rigorously tested at the earliest stage, and well before the government has committed to act. Too often, governments have announced that they are planning to regulate, or commenced consultation on options, before establishing exactly what problem they are seeking to solve, and having collected evidence on the extent to which it is having a real impact on welfare or the environment.

In 2012, the BCA outlined its Standards for Rule Making, which provided best practice principles and standards against which government processes could be assessed.

When the Regulatory Impact Statement process moves to examining options, it would seem that more recently there is much less of a focus on identifying barriers to competition than when National Competition Policy compliance was more vigorously.

Professor Fred Hilmer has been critical of the RIS process for seeking to combine 'red-tape' reviews with competition reviews. He argues that different skill sets are required, with a competition review focusing on the impact of regulation on markets, and requiring a sound understanding of how businesses operate and compete, micro-economic literacy, and legal training (2013, p. 15). He notes that assessing regulatory effectiveness requires a background in policy analysis, while dealing with 'red tape' requires a different set of skills, typically in process mapping and workflow analysis.

However, if the RIS is prepared by the relevant policy department (which has the skills in policy analysis for this subject area), which actively consults with businesses to understand how they operate and are likely to react to any regulatory options, and is rigorously overseen by an appropriately skilled gatekeeper institution (which should apply a competition policy lens, and have the micro-economic literacy skills, and the ability to understand legal instruments), then it may be feasible to address Professor Hilmer's concerns.

Reducing red tape can be achieved through redesigning or eliminating regulation and this requires similar skills to those used to prepare a new regulatory proposal, and a RIS. However, if regulatory burdens are being reduced through administrative streamlining this is, indeed, a very different task, and as he notes, needs to be supported by different people than those assessing new regulatory proposals.

RIS exemptions

Some of the most egregious examples of the regulatory impact process failing has been where it has been bypassed completely. Currently, there are few consequences for governments failing to comply with their own processes, in the absence of a legislated process and robust independent oversight of the analysis by an expert body, and oversight of the process by the parliament.

Incorporating a commitment to implement the RIS processes well, and ensuring there are fiscal consequences for not doing so, will be important to drive better regulatory design in any new regulation. During the period when National Competition Policy was being implemented, there was substantial scrutiny on any new regulation that might impose a restriction on competition. This was undertaken by each jurisdiction, and overseen by the National Competition Council in its annual payment assessment role. However, since the payments lapsed, the attention to competition impacts in government processes appears to have waned.

Effective implementation

The lesson from the National Competition Policy reform era was that undertaking a broad-ranging and robust process of reviewing anti-competitive arrangements was a challenging task.

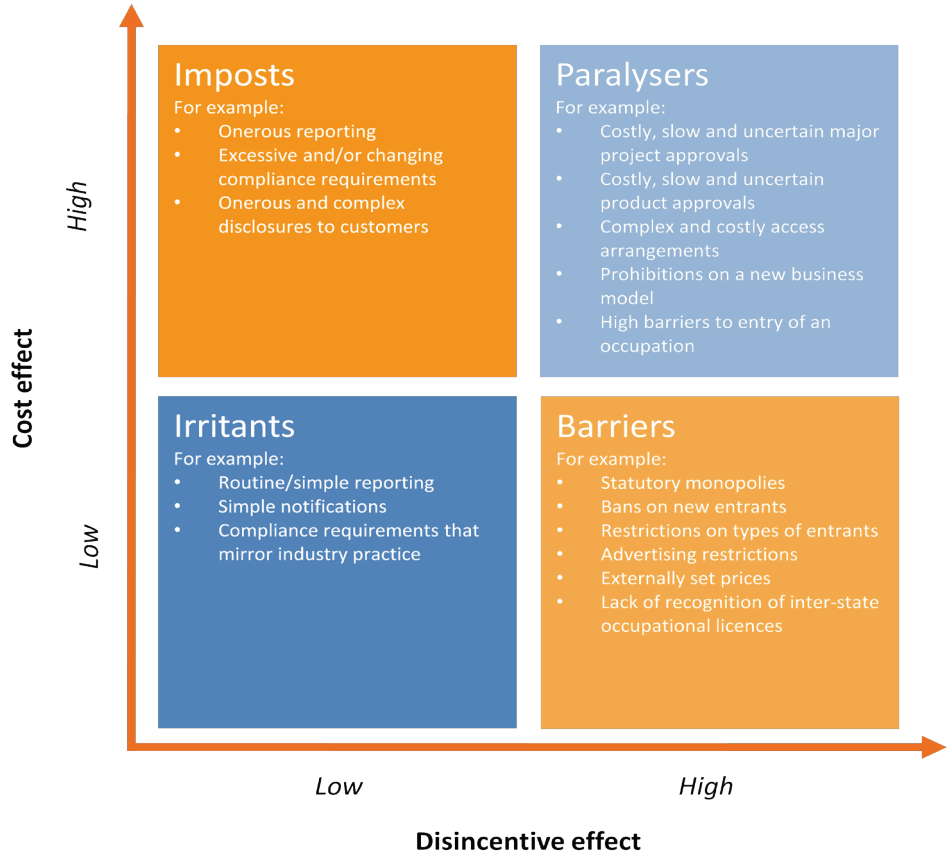
Strong institutional arrangements are critical to ensuring the implementation of such a reform program, and this is discussed in greater detail in Chapter 7.

In addition to these arrangements, effective implementation will require a clear framework for prioritising reforms, robust principles and clear implementation plans.

Prioritising reforms

In prioritising regulation reform, Professor Hilmer has highlighted the importance of distinguishing between regulation that imposes costs, from that which restricts competition (Figure 4). Some regulation imposes limited administrative or compliance costs – for example, a ban on new entrants – but has a serious impact on competition, and thus broader economic costs. An example of this is limits on the number of taxi licences issued in most Australian cities. Other regulation imposes both high direct costs, and is a substantial constraint on new entrants. Costly, slow and uncertain approval processes are an example of regulation that imposes both high compliance costs and can be a substantial constraint on competition.

Figure 4: Categories of red tape



Source: Hilmer, 2014; BCA analysis

Other regulation may impose substantial compliance costs, but if these costs are borne pretty much equally by existing businesses and new entrants, and don't constrain competitive behaviour, then these costs may have limited impacts on competition. While removing this sort of regulation will boost the economy, it may have a smaller long-term impact.

In recommending how governments prioritise the reform of anti-competitive regulation, there may be value in the panel tackling this in three tranches:

- **First** would be to commence immediately a concerted and timely attack on the areas of reforms from the Seamless National Economy agenda that have an impact on competition, and have not fully met expectations as to outcomes. High priorities include reforms to: occupational licensing; land use planning and zoning, chemicals and plastics; access arrangements, particularly for greenfield investments; road reform; and energy, particularly retail price deregulation, demand-side participation, and harmonisation of legislation.
- **Second** would be to implement the outstanding pro-competitive regulatory reform recommendations over the last decade of the Productivity Commission, and other independent public reviews, including those undertaken by state and

territory bodies.[5] After identifying all those recommendations which have not been implemented to date, there should be a careful re-examination of all those where recommendations were not accepted at the time, or accepted in principle, to ensure that the case to not proceed stands up to scrutiny.

- **Third** would be to develop an action plan to address other anti-competitive legislation at all levels of government. This may involve reviewing individual Acts (as was done during the Legislative Review Program under the National Competition Policy Agreements) or taking a sectoral approach that more effectively examines the cumulative burden, with rolling audits every five years (that is, reviewing all building sector regulation, or all mining regulation) (BCA, 2013c). Sectors where anti-competitive regulation was identified during the National Competition Policy review process as high priority, but was not subsequently reformed, such as that applying to the taxi sector, could prioritised.

Development of an action plan to address the other anti-competitive legislation will require careful consideration of which regulation is best reviewed and reformed by individual states (allowing different approaches consistent with competitive federalism), and those regulations where a national approach is required because the market being regulated is national or international, and the costs of disparate approaches will be higher.

Robust principles and clear implementation plans

Key to the success of National Competition Policy was the application of robust principles across a large number of reviews. These principles placed the onus of proof on those who sought to retain a restriction on competition, to demonstrate that this was in the community's interest.

The independence, level of consultation and rigour of the analysis of these reviews did not always reflect the impact on the community of the legislation being assessed. In 1999, the National Competition Council released guidelines for the undertaking of these reviews, and these guidelines could serve as the basis of determining how a new phase of more targeted reviews might be undertaken (CIE, 1999).

It will also be important that reviews set out clear and realistic, but ambitious, draft implementation plans. After these plans have been considered by governments, alongside the recommendations of each review, these plans will form the basis of monitoring of progress at achieving real change.

Recommendations

3. Within three years, states and territories should implement mutual recognition for occupational licences that would enable people with valid licences in one state to work in another state, based on the 'drivers licence' model.

[5] This would go further than the BCA's proposal that the Commonwealth Government undertake a stocktake of – and implement, as appropriate – all of the 155 recommendations from the Productivity Commission's annual reviews of regulatory burden that were undertaken from 2007 to 2011 (2013, p. 4).

4. Remove the legislated cabotage restrictions in the Coastal Trading Act 2012 to move to an open, globally competitive coastal trading sector, with foreign and Australian vessels continuing to be subjected to all other Australian laws.
5. Repeal the Australian Jobs Act, which mandates government-approved Australian Industry Participation Plans for private investment projects over $500 million.
6. Australian governments should adopt as a principle that where a regulated good or service is tradeable, and subject to a regulatory approval by a European Union, a United States, or Canadian national regulator, then there should be a strong presumption in favour of automatic recognition of those countries' approval. This is a process that individual Australian jurisdictions should be prepared to adopt unilaterally.
7. Australian governments should implement measures to deliver more timely and predictable decision making regarding planning, zoning and other land development, underpinned by a suite of reforms that involves all states and territories:
   - conducting improved strategic planning that provides land-use permissibility for economic development, including infrastructure, major energy, industrial and resource projects, in the same way as is done for future housing settlements
   - committing to introduce progressive targets to shift 80 per cent of the share of development (residential and commercial) towards streamlined processes – that includes code-assessable development
   - adopting a single major project approval process for major energy, resource, infrastructure and industrial projects based on a dedicated assessment track that includes one statutory timeframe from Environmental Impact Statement exhibition through to a project decision, and all secondary approvals.
8. Australia's governments must immediately set a timetable and process for aligning state-based retail trading hours, and coordinate a state-based reform agenda for removing the most restrictive and inconsistent regulatory restrictions affecting the retail sector.
9. Reviews of anti-competitive legislation or other policy settings should continue to apply the National Competition Policy principles.
10. All governments should have robust, legislated, two-stage Regulatory Impact Statement processes in place that explicitly test all new regulatory proposals against the competition principles, and this process should be overseen in each jurisdiction by an independent agency.
11. Any exemption from the Regulatory Impact Statement process should be approved by the leader of a jurisdiction, with the reasons published and a post-implementation review undertaken.

2.2 Extending competition into public sector markets

The focus of this chapter is on driving more competition in government service provision through proper adherence to competitive neutrality principles, outsourcing and privatisation.

Following the recommendations of the Hilmer Review, section 2A and 2B now provide that the Crown is bound by the entirety of the CCA in right of the Commonwealth, by Parts IV and XIB and related provisions in right of each state and territory, and by Part IV in relation to a local government body, so far as they *carry on a business* either directly or by an authority or controlled company.

'Carrying on a business' does not require that the business is carried on for profit, though it generally involves 'activities undertaken as a commercial enterprise in the nature of a going concern' or 'activities engaged in for the purpose of a profit on a continuous and repetitive basis'.[6] Section 2C provides that certain activities do *not* amount to carrying on a business, including imposing or collecting taxes, levies or fees for licences; granting, refusing, revoking, suspending or varying licences; or the acquisition of primary products by a government body.

Further, section 51(1) provides that anything specifically authorised by legislation or regulations must be disregarded in deciding whether a contravention of Part IV of the CCA. The ACCC lists around 80 pieces of Commonwealth, state and territory legislation that specifically exclude Part IV, including legislation in one or more jurisdictions relating to health services, water and sewerage, liquor, racing and gambling.

As a result, more than 20 years after the Hilmer Report it remains the case that a great deal of economic and potentially competitive activity remains beyond the reach of the competition law in the hands of local, state and territory, and Commonwealth governments. Extending the competition law to these areas could be partly achieved by expanding the definition of 'carrying on a business' but would also require positive reform of legislation and regulations by the various levels of government.

There are real opportunities to expose government activities to greater market disciplines so as to generate better outcomes for consumers, users of subsidised services, and for taxpayers. Reform can benefit businesses that rely on the competitive supply of inputs, such as rail, port, and energy services to be able to succeed in global markets, and the broader community, which expects worlds-best education, health care and other government services.

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6 Fasold v Roberts (1997) 145 ALR 548 per Sackville J. It has been held that the Australian Postal Commission, the then Australian Telecommunications Commission, the Australian Government Publishing Service and the Queensland Department of Natural Resources and Mines (in its licensing of bulk real estate data) were carrying on a business. It has also been held that many government services are not carrying on a business, including the NSW Department of Agriculture, the Commonwealth Department of Immigration and Multicultural Affairs (in providing and tendering for immigration detention guarding and escort services), the Commonwealth in providing health benefits and medical and dental services, and the Trade Practices Commission (and presumably the ACCC).

The free or subsidised services delivered by government represent a large part of the economy that has historically been much less exposed to competition than other services. In aggregate this is a large proportion of the nation's output; 17 per cent of Australia's industry gross value added in 2012–13 is what the ABS describes as the 'non-market' sector – that is, health care and social assistance, public administration and safety, and education and training where government dominates (PC, 2014a). Many of the people who deliver these 'non-market' services are employed by governments, which accounted for 16.2 per cent of total employment in June 2013 (ABS, 2013a & 2013b).

Many government businesses have been privatised in the last three decades, but as Infrastructure Australia notified its 2013 report to COAG, there remain up to $60 billion of water assets and up to $60 billion in electricity network and generation assets that could be transferred to the private sector, enabling efficiencies in operation and the release of funds for new infrastructure investment.

The National Commission of Audit identified 10 Commonwealth Government businesses that operated in contestable markets and thus it considered could be privatised, noting that in some cases there would need to be revised regulatory arrangements and the introduction of access regimes (NCOA, 2014).

Ensuring the adequacy of regulatory frameworks is a precondition for both Commonwealth and state government sales generating the most community benefits. The regulatory frameworks – the rules, and the institutions that will administer them – must provide sufficient certainty to attract investors prepared to pay the full value of the assets, while encouraging competition and innovation in upstream and downstream industries.

2.2.1 Competitive neutrality

The National Competition Agreements required every jurisdiction for the first time to apply a consistent high-level framework for competitive neutrality. However, each jurisdiction was free to implement competitive neutrality as it saw fit, and (it would seem) with differing levels of rigour.

Some jurisdictions gave responsibility for oversight of competitive neutrality to independent agencies or regulators (the Australian Government's Competitive Neutrality Complaints Office sits with the Productivity Commission, in Victoria it is within the VCEC), while others had this responsibility within a department.

Achieving a competitively neutral business environment involves both actions by the government agency that is engaging in business activities (whether it is Australia Post, a public hospital competing against private providers, TAFE institute or university) and those setting the policy arrangements relating to the market in which the business is engaged.

The government agency engaged in business must ensure it prices appropriately, but also crucially does not gain any unfair advantage by virtue of its relationship with government that is not available to its private competitors, such as through access to information (including impending regulatory or policy changes). Addressing these sorts of issues can involve careful management of any consultation with government policymakers.

Those responsible for regulatory and other policy arrangements that could impact on both public and private competitors also need to be very mindful of the impact on different business. For example, as outlined in Chapter 2, a decision to exempt government providers of international education from a levy designed to protect tuition fees does not seem to have explicitly considered the impact on competitive neutrality and how those impacts might be avoided. It is critical that competitive neutrality policy, and the complaints process, actively addresses these sorts of issues, as well as those related to the behaviour of government businesses.

2.2.2 Incentives for private investment in infrastructure

As noted in Chapter 3, at the time of the Hilmer reforms many infrastructure services were provided by inefficient public monopolies. The high cost and poor quality of infrastructure inputs were holding back the competitiveness of businesses right across the economy and Australia's productivity rates were well behind international averages. The key challenge identified by the review was to create incentives to better manage and use existing infrastructure through reform of infrastructure governance and regulation.

There has also been a shift to contestability by tendering out public infrastructure provision and tapping into private sector efficiencies, capabilities and ideas. For major new greenfield infrastructure, Australia has been a leading user and innovator in the application of the public–private partnership model, leading to improvements in project outcomes.

Today, the challenges for infrastructure provision are to:

- Complete market-based infrastructure reforms in sectors and jurisdictions that have lagged behind and create the opportunities for extending private ownership and management.
- For privately held infrastructure, ensure competitive market conditions are working to encourage new investment that will expand capacity to meet the needs of a growing economy and population.

It is widely recognised that private ownership of infrastructure brings better capital discipline and greater efficiency. The Productivity Commission recently said that:

> ... there has been an increasing trend of private sector involvement in the delivery of public infrastructure in much of the world. This reflects a growing recognition of the potential efficiency benefits of private sector involvement compared with the alternative of public sector delivery, including stronger incentives for the private sector to more efficiently build and operate some infrastructure and to better manage the associated risks. (2014c, p. 90)

A key development since the Hilmer review is the rise in the number of investors wanting a stake in private infrastructure. Superannuation and pension funds are now major investors in infrastructure and looking to acquire more of these assets, due to the close alignment of returns from infrastructure and their financial objectives.

The potential pool of funds is large and growing. Australia's superannuation system is set to rise from $1.6 trillion in funds under management today, to around

$6 trillion by 2037. Globally, the OECD estimates just one per cent of US $20 trillion in global pension fund assets is invested in infrastructure (2013b, p. 15). The demand for sound, stable investments from these private sources is expected to increase substantially.

Private investment not only brings private disciplines to asset management, it also allows governments to recycle the proceeds from asset sales into new greenfields projects (e.g. via the Asset Recycling Fund). This overcomes the current fiscal constraints to paying for new infrastructure provision and means the community benefits by getting access to new infrastructure much faster.

The main opportunities for private investment are in the areas where governments continue to operate businesses such as water supply, electricity networks, rail freight networks, road networks, ports, airports (outside the capital cities), postal services, and telecommunications (through the National Broadband Network). The BCA has considers a principles-based approach is important when assessing whether physical infrastructure should be publicly or privately owned and/or operated (Exhibit 10).

Exhibit 10: BCA principles on infrastructure ownership, regulation and pricing

The following criteria should determine whether an asset is owned privately or by governments, and how that asset should be operated:

- Governments should sell infrastructure assets where the private sector already owns other like-assets and provides other like-services (this effectively demonstrates adequate policies are already in place to protect consumers).
- Private ownership should be preferred where appropriate arrangements can be established for the infrastructure service in any of these three ways:
  - There is a market price set by an effective and contestable market for the infrastructure service.
  - There is a regulated price that allows an adequate return on an efficient investment while also protecting the interests of consumers.
  - There is an implicit contract price that a government agrees with the owner of the infrastructure on behalf of public users (includes community service obligations).
- Government ownership should only be preferred where it can be demonstrated that it is necessary for achieving the community's objectives with respect to infrastructure provision, for example, demand risk on some new greenfield projects.
  - These businesses should be sold once the project has matured.
  - Government-owned infrastructure should outsource delivery and operations based on competitive long-term contracts.

Source: BCA 2013d

Pro-competitive outcomes

Some government businesses that have been identified for sale will have monopoly power, or perform regulatory functions that create an actual or perceive conflict. It is important that prior to the sale of any such business that the structural issues are addressed, and measures put in place to enhance competition where appropriate (Exhibit 11). This enables potential buyers to have a clear understanding of what they are buying, and should allow customers to raise any issues or concerns they may have. This minimises the risk of pressure for post-sale regulation in subsequent years that can undermine the confidence of investors and their willingness to invest in growing these businesses. As discussed in Chapter 3, any third party access regulation must strike the right balance between allowing an adequate return on a private investment and ensuring competitive market outcomes, for example, through access determinations and price-setting.

The high potential for regulatory failure in this space, coupled with the risks for future investment where investors consider regulatory risks are too high, means that regulatory interventions should mostly occur where there is a clear, rather than marginal, net economic benefit.

With Australia's economy and population set to grow strongly in the years ahead, we should guard against policies that might cause investors to be excessively cautious in undertaking major private investments in long-term risky infrastructure capital assets.

Exhibit 11: Competition Principles Agreement 1995 and privatisation

Section 4 of COAG's Competition Principles Agreement (1995) addressed structural reform of public monopolies, including the need to review the scope for pro-competitive reforms prior to the sale of public monopolies. The agreement did not require that these reviews were public, and so it is not clear whether and how such analysis has been undertaken prior to recent sales/long-term lease of assets such as the NSW and Queensland ports.

4. Structural Reform of Public Monopolies

- (1) Each Party is free to determine its own agenda for the reform of public monopolies.
- (2) Before a Party introduces competition to a sector traditionally supplied by a public monopoly, it will remove from the public monopoly any responsibilities for industry regulation. The Party will relocate industry regulation functions so as to prevent the former monopolist enjoying a regulatory advantage over its (existing and potential) rivals.
- (3) Before a Party introduces competition to a market traditionally supplied by a public monopoly, and before a Party privatises a public monopoly, it will undertake a review into:
  - the appropriate commercial objectives for the public monopoly
  - the merits of separating any natural monopoly elements from potentially competitive elements of the public monopoly
  - the merits of separating potentially competitive elements of the public monopoly
  - the most effective means of separating regulatory functions from commercial functions of the public monopoly
  - the most effective means of implementing the competitive neutrality principles set out in this Agreement
  - the merits of any community service obligations undertaken by the public monopoly and the best means of funding and delivering any mandated community service obligations
  - the price and service regulations to be applied to the industry
  - the appropriate financial relationships between the owner of the public monopoly and the public monopoly, including the rate of return targets, dividends and capital structure.

Source: COAG, 2007 (the 1995 agreement was amended in 2007)

Greater competition between road and rail freight

One of the most important areas where there is scope to improve competition is between transport modes for freight. Earlier in the submission, we recommended measures that would free up restrictions on competition in coastal shipping. However, the pricing of access to roads for freight remains an area where it is

critical that there is further implementation of reforms that have already been subject to rigorous cost–benefit analysis.

The better use of cost-reflective user charging to fund increased transport infrastructure, and promote better use of existing infrastructure, particularly for freight traffic, will be crucial to manage growing demand over the next two decades. To the extent that this improves transport flows, this would serve to improve competition by facilitating businesses competing in national rather than more local markets.

Such reforms will have an added bonus of creating a better market environment for the privatisation of the Australian Rail Track Corporation Ltd (ARTC), which was recommended by the National Commission of Audit. This recommendation recognised the need to examine an appropriate access regime, implications for ARTC's leases, and wider considerations stemming from the intergovernmental agreement that established the ARTC.

2.2.3 Subjecting government services to competition

Australian governments have introduced competitive delivery of key government services to the community in many areas. However, there are many other government-funded services across Australia that could potentially be delivered in this way.

Competitive tendering of inputs is used by the private as well as public sectors. Spotless Group Holdings Limited, which operates facility, laundry and linen services for both public and private organisations in Australia and New Zealand, estimates that 47 per cent of the market it competes in is currently outsourced. While this proportion continues to grow, a greater proportion of these markets in Japan (66 per cent) and New Zealand (58 per cent) are outsourced (Spotless Prospectus, 2014).

Increased use of competitive tendering/contestability to deliver government services has been a theme in the recent NSW (2012), Queensland (2013) and Commonwealth (2014) Commissions of Audit.[7] The South Australian Sustainable Budget Commission (2010) also called for increased contestability in selected services. Each of these reports has noted that greater use of competitive arrangements to deliver government services will help governments to manage budgetary pressures, and deliver services that better meet, and are more responsive to, changing community needs and expectations.

The main opportunities to increasing contestability for governments services that have been identified in these government audits include:

- health, including public hospital and medical transport services
- vocational education and training services
- correctional services

[7] The issues surrounding contestability were also extensively examined in the Industry Commission (a predecessor to the Productivity Commission) report *Competitive Tendering and Contracting by Public Sector Agencies (1996).*

- road maintenance
- passenger rail services and infrastructure
- water operations and maintenance
- port operations
- individual supports to people with disabilities
- certain visa processing tasks
- departmental corporate and IT services.

The main barriers to increasing contestability in the provision of public services appear to be:

- poor incentives to increase the contestability of government services, including lack of profit motive in the public sector and risk aversion arising from the adversarial nature of politics
- insufficient contract management and market design skills in the public sector
- limited ex-poste evaluation of the impacts of contestability, and 'what works'.

Governments should only deliver services where they are best placed to deliver them efficiently and effectively. Where services delivered by government are also provided by private and community organisations, such as health and education services, non-government organisations should have the opportunity to deliver these services on behalf of government (BCA, 2013d).

Where possible, the design of competitive arrangements should provide recipients with some degree of choice of provider, noting that this may require careful design of new market arrangements.

Moreover, even where governments retain the responsibility for actual service delivery (e.g. defence and the police), they should actively competitively tender the provision of inputs to those services (such as information technology services, payroll, call centres, maintenance, and catering) wherever this is economic.

Even where a government is currently best placed to deliver a particular service, the cost, quality and effectiveness should be periodically benchmarked against other jurisdictions and the non-government and private sectors to ensure that this remains the case. In addition to providing 'competition by comparison', such benchmarking can support reassessments of the potential for service contestability, which should provide incentives for increased efficiency.

- The conditions and incentives that have previously led to governments (local, state and national) adopting more competitive models of service delivery include the implementation of particular rewards and sanctions that encourage all government agencies to rigorously test competitive options for service delivery.
- The current level of allocation of Commonwealth funding to the states, with high vertical fiscal imbalance and the Commonwealth Grants Commission frameworks, dulls the rewards to an individual state from undertaking a reform that is politically unpopular but lowers its cost of service delivery. Funding

arrangements need to reward reformers, particularly those which reform early and thus may have to manage more challenging implementation issues.

- The review's national (rather than jurisdiction-based) focus should assist it to focus on developing ways of using intergovernmental arrangements, including funding arrangements, to strengthen incentives as a way to promote more widespread adoption of pro-competitive reforms.

Incentives for states and territories to reform service delivery

Moving from traditional delivery models to more competitive arrangements involves challenging market design issues, including how to equip consumers to effectively take advantage of increased choice. The design of the National Disability Insurance Scheme (NDIS) appears to be considering these issues. While the NDIS design will build on earlier Western Australian and Victorian reforms of disability services (Exhibit 12), it will also need to recognise the importance of creating sufficient scale of contracts and long-term certainty about the policy settings to encourage substantial private sector investment and new innovative services that better meet the needs of people with disability.

The Commonwealth Government announced in the 2014–15 Budget that it will develop and implement a Contestability Framework. The Commonwealth Department of Finance is to establish a three-year program of work to review government functions against the Contestability Framework, in consultation with relevant agencies. These reviews offer opportunities for more government functions to be delivered through alternative and contestable approaches (Commonwealth Government, 2014, p. 116).

There have been examinations of the potential for greater use of competition and outsourcing in the whole-of-government reviews undertaken by recent incoming federal government, but each of these has only focused on one jurisdiction. The last national examination of these issues was undertaken by the Industry Commission (a predecessor of the Productivity Commission), which reported in 1996. Commissioning a series of independent and public inquiries examining the potential for greater use of competition in the delivery of key areas of government services would enhance government and community understanding of what works currently, where the largest gains have been found to be, and practical lessons on how to implement such changes.

Exhibit 12: Improving government services through the use of entitlements

In Victoria, extensive use is made of individual support packages (ISP) which allow people with disability to purchase a range of services from private providers within a set budget. These can range from low-cost, low-support to high-cost, high-support packages. Lower-cost packages build on family and community supports, and higher-cost support may include 24-hour support accommodation services.

Victoria has a well-developed system for self-directed supports. Essentially, people with disability are supported to develop a plan and if in receipt of an ISP, can choose the supports provided within the available resources.

Evidence from the Victorian experience indicates that where individuals and their families are given the choice, they tend to select different services from those they would otherwise have received. In some cases, individuals and their families need assistance to develop their places and choose their services, and a variety of support and funding mechanisms are available to help people select services.

A significant portion of Victoria's disability services budget is provided directly to service providers who support people with disability. Around 300 agencies are registered to deliver disability services. A growing share of the disability budget is allocated through ISPs.

Source: Victorian Government, 2011

Recommendations

12. Government service delivery should, as far as possible, follow market principles and be fully contestable to drive innovation and better service delivery, with priority given to health, education, and transport and infrastructure services.
13. Australia's governments should recommit to the competitive neutrality policy and implement nationally agreed procedures for its application that set out:
    - how each government will implement competitive neutrality policy as they move to promote competition in government service delivery
    - a clear process for responding to any recommendations arising from an investigation by the independent competitive neutrality complaints regulator
    - transparent and accessible reporting on the government's response to findings by the independent competitive neutrality regulator, including remedial actions taken
    - principles for identifying and specifying non-commercial objectives of government businesses and how those activities should be transparently funded
    - guidance on how competitive neutrality should be applied to new, start-up government businesses, for example, on the matter of the length of time over which a commercial rate of return should be achieved.
14. Australia's governments should pursue a renewed agenda for upgrading infrastructure regulation to enhance competition and meet the future needs of the Australian economy. A new agreement should include reforms that will promote new and efficient investment in infrastructure, including commitments towards:
    - enhanced consistency, capability and performance of Australia's economic regulators
    - a new timetable for privatising infrastructure businesses to capture efficiencies from private ownership and unlock public funds (including via the Recycling Assets Fund)
    - reforms to pricing infrastructure that move towards full recovery of the efficient costs of public infrastructure provision, including an adequate risk-adjusted return on investment.
15. Prior to the sale of any Commonwealth, state, territory or local government businesses with natural monopoly characteristics, a review consistent with the 1995 National Competition Principles Agreement should be undertaken to promote pro-competitive outcomes where possible. This should include putting in place appropriate access arrangements, even where this has the effect of reducing the sale price of the asset.
16. Governments should promote efficient investment and use of road transport infrastructure through adoption of broad-based user charging, as part of comprehensive tax reform and reform of Commonwealth and state funding arrangements.

17. The Commonwealth Government's review of the federation should assess how to strengthen incentives for states and territories to more actively search out more competitive forms of service delivery, such as the current Grants Commission arrangements.
18. The Productivity Commission should be given inquiries that separately look at each of the main areas of state and territory service delivery (education and early childhood; health and human services; justice and transport) to examine the potential to increase competitive provision, drawing on the lessons from Australian and international jurisdictions that have already implemented such models.

3. COMPETITION LAW

The question of whether the current competition laws are working effectively to promote competitive markets, given increasing globalisation, changing market and social structures and technological change, is a vital one in the broader context of this review.

The elements of microeconomic reform at stake in this review all have at their heart the promotion of competition, rather than regulation, as the primary mechanism for providing goods and services as efficiently as possible to the public. However, these reforms will fail to deliver their potential public benefits if there are inefficiencies in the competition law itself.

A world-class, balanced and responsive competition law framework will deliver the full benefits of competition in an increasingly global economy in which new technologies are frequently disrupting and transforming markets. Conversely, defects in the competition law framework will be magnified as new markets are contested and anti-competitive regulations are eased.

3.1 Sound principles

Australia has a strong competition law framework. However, there are areas in which the law and its administration could be improved to promote efficiencies and reduce costs. At present, aspects of the competition framework impose unnecessary costs and delays in requiring compliance with overly prescriptive regulations, risk discouraging vigorous competition due to uncertainties in the law, and may hinder the efficient use of capital by adopting an overly narrow approach to mergers.

In addition to much-needed microeconomic reform, this review provides a crucial opportunity to ensure that the economy-wide competition law appropriately supports that reform.

The object of the CCA is “to enhance the welfare of Australians through the promotion of competition and fair trading and provision of consumer protection”.[8]

The promotion of public welfare has been recognised as the chief objective of competition law and policy by an increasing body of economic analysis and jurisprudence internationally. An emerging set of principles underpinning this objective can also be discerned from economics and law worldwide.

Australia’s competition law should be aligned as closely as is possible with these international best-practice principles of competition law.

(I) Long-term consumer welfare should be the overriding goal

Competition delivers benefits to consumers through lower prices, improved choices and superior services, which is irrespective of the size or number of competitors in a given market. There are also broader community benefits of vigorous competition which helps businesses to innovate, grow, and create jobs.

[8] Section 2, *Competition and Consumer Act 2010.*

The Review of Competition Provisions of the Trade Practices Act (the Dawson review) noted the importance of competitive markets to consumer welfare:

> Competitive markets make an important contribution to increasing efficiency and productivity in the economy, thereby improving the welfare of Australians... (p. 5)
>
> In economic terms, welfare will be enhanced by rising living standards in the form of higher incomes in real terms and an increase in consumer choice, by sustainable high economic growth, and by a lower unemployment rate. These benefits flow when human and other resources are used more efficiently to increase productivity and to maximise returns on investment. Competitive markets are the key to economic efficiency. (Dawson et al., 2003, p. 29)

The World Trade Organization found that this is a widespread objective of competition policy worldwide:

> A goal that is widely viewed as a central purpose of competition policy and is used as the leading overall guidepost for the application of competition law in a number of major jurisdictions is that of consumer welfare. Under this approach, a fundamental criterion for the application of such policy to particular business arrangements is whether the arrangements in question have a detrimental impact on the prices charged to and/or the array of choices available to consumers. Even in jurisdictions where competition policy is also intended to serve other economic and social goals, the promotion of consumer welfare is generally acknowledged to be an important or even a central goal of such policy. (1999, p. 6)

The US Antitrust Modernization Committee further noted an increased focus on consumers and away from particular competitors and market structures:

> During the 1960s and early 1970s antitrust decisions from the Supreme Court sometimes seemed more directed to protecting small businesses than to protecting competition that would benefit consumers through lower prices, improved quality, or innovation...
>
> Economic research found pro-competitive reasons to explain highly concentrated markets – that is, that the most efficient firms were winning the competitive struggle and thereby achieving high market shares. Some economists and lawyers further contended that effective competition did not require dozens of little firms, but instead could occur with relatively few firms in a market...
>
> For the last few decades courts, agencies, and antitrust practitioners have recognized consumer welfare as the unifying goal of antitrust law. ‘Few people dispute that antitrust’s core mission is protecting consumers’ right to the low prices, innovation, and diverse production that competition promises. (Garza et al., 2007, pp. 34–35)

(II) Aim to protect the competitive process, rather than individual competitors

Modern competition policy is directed at maximising consumer welfare – through the promotion of competition – rather than protecting individual competitors, classes of competitor or particular market structures.

The principle that competition law is designed to promote and protect competition for the benefit of consumers and even at the expense of competitors has

consistently been recognised by the High Court in cases from *Queensland Wire*[9] to *Melway*[10] and *Boral*.[11] It has been affirmed in the *Blunt Report into Small Business and the Trade Practices Act*, the Hilmer review, the Dawson review and the Senate Inquiry into the effectiveness of the *Trade Practices Act 1974* in protecting small business. Internationally, it has been reiterated by the US Supreme Court,[12] the European Court of Justice[13] and the World Trade Organization.

The Antitrust Modernization Committee noted the central role of consumer choice in shaping market outcomes and market structures:

> Consumers choose the winners and losers in the competitive process, however, through their purchasing decisions. If consumers desire diversity, for example, then they will be willing to pay for it... Firms that best meet consumers' desires in the most cost-effective way will succeed, while those that do not may fail. The competitive process can often be seen as unfair to those who lose. Nonetheless, it is competition itself – not the presence of a particular competitor – that best serves consumer welfare. (Garza et. al., 2007, p. 325)

(III) Be consistent with best practice competition law

By applying sound antitrust principles informed by an examination of international experience, reflecting that Australia has a medium-sized, open economy rapidly becoming more tightly linked to increasingly globalised markets.

Convergence with international best-practice competition law is itself emerging as an important principle of competition policy worldwide, not only to promote the ideal operation of domestic markets but to allow firms to compete more effectively across markets.

Increased convergence on international best-practice competition law will benefit Australian companies seeking to move into other markets, and Australian consumers who will benefit from increased competition from international firms.

The Commonwealth minister responsible for competition policy, the Hon. Bruce Billson MP, highlighted the importance of international convergence:

> We have taken on board some wise counsel from the Prime Minister's Business Advisory Council to recognise that we are now part of a global economy and we need to make sure that our laws are world's best practice.
>
> We need to ensure where other jurisdictions have seen and acquired insights that perhaps aren't embraced in our own policy approach, that we at least make sure we are world's best practice (2014).

This approach echoes the findings of the Antitrust Modernization Commission:

> Notwithstanding the large number of antitrust regimes worldwide, multinational antitrust enforcement generally has not generated significant inconsistencies or

[9] (1989) ATPR, para 40-925.
[10] (2001) ATPR, para 41-805.
[11] (2003) ATPR para 41-915.
[12] *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc*., 429 U.S. 477, 488 (1977).
[13] *Oscar Bronner v Mediaprint* [1998] ECR I-7791, opinion of AG Jacobs at 58.

> conflict among nations. Indeed, significant convergence based on sound principles of competition law has occurred and is continuing to occur on both procedures relating to multinational enforcement and the core substance (if not the details) of antitrust and competition law...
>
> Divergence can create problems of at least three types. First, companies may be subject to conflicting and inconsistent laws, creating uncertainty as to the legal standards applicable to their business arrangements. Second, companies must comply with the procedural requirements of multiple jurisdictions, potentially increasing their costs significantly, particularly with respect to notification requirements for mergers. Third, different countries may ultimately impose different, and inconsistent, remedies with respect to the same conduct or transaction. (Garza et. al., 2007, p. 213)

(IV) Minimise use of 'per se' prohibitions

Competition law should only prohibit specific conduct per se where that conduct would in the overwhelming majority of cases result in a substantial lessening of competition and clear public detriment, and cases for exemptions that do have a public benefit are only rarely established.

The Hilmer review recognised the limited conditions in which *per se* prohibitions would be appropriate**:**

> The anti-competitive impact of some kinds of conduct may be so unambiguous that they should be prohibited outright without having to demonstrate their impact in each particular case. Where this conduct can be defined with sufficient certainty, prohibition of it *per se* will often be warranted...
>
> *Per se* prohibitions are appropriate where conduct has such strongly anti-competitive effects that it is almost always likely to lessen competition (pp. 28 & 54).

Similarly, the Antitrust Modernization Committee noted the danger of overreliance on *per se* prohibitions as working against consumer interests:

> [T]he courts, scholars, and antitrust practitioners have reached consensus that – although appropriate in particular limited circumstances – *per se* rules can all too often condemn business conduct that actually benefits, not harms, consumers …
>
> Increased flexibility and improved economic understanding can be seen in the evaluation of both joint and unilateral conduct under the Sherman Act, where courts have largely turned away from the application of *per se* rules of automatic illegality and moved toward rule of reason analysis (Garza et. al., 2007, pp. 3, 29 & 38).

(V) Focus law economy wide, not sector specific

Competition law should be applicable to all forms of business enterprise across the economy and not be narrowly targeted at sector specific issues.

The Hilmer review rejected a sectoral approach to competition law**:**

> The Committee does not believe that it is the role of the competitive conduct rules to protect any particular sector of society, and does not believe that the competition rules should be used to achieve objectives contrary to economic efficiency (p. 74).

The Dawson review affirmed the principle of general application:

> The competition provisions should apply generally and consistently to business conduct without regard to the nature of the industry in which the conduct occurs. Efficiency, and consequently welfare, may suffer if the regulation of competition is not uniform. Differing regulatory treatment of different sectors of the economy will provide differing incentives for investment and effort by discouraging participation in particular sectors and will detract from the ability of markets to allocate resources in an efficient manner. Productivity, growth and welfare may then all suffer...
>
> The Committee does not favour the introduction of competition measures specifically directed to particular industries to respond to perceived shortcomings in the relevant markets. Often the complaint when analysed is not about reduced competition but about the structure of the market which competition has produced. Concentrated markets can be highly competitive. It may be possible to object to the structure of such markets for reasons of policy (the disappearance of the corner store, for example), but not on the grounds of lack of competitiveness. (p. 36)

(VI) Aim for simplicity to reduce compliance costs

Competition laws should be simple and clear enough to be understood by all business people and communicated throughout an organisation, including through internal compliance programs. There should be reasonable clarity or certainty to business people as to when certain conduct may be prohibited and when it is permitted.

The role of certainty in supporting business compliance and implementation of competition law was recognised by Sir Garfield Barwick in proposing the Trade Practices Act 1965**:**[14]

> [T]here must be certainty for businessmen as to what they may or may not do. This, to my mind, is important in relation to any economy, but it is imperative in our case. We are in a stage of development which calls for courage and initiative on the part of our businessmen. Our growth and the prosperity of all of us can only suffer, and suffer grievously, from uncertainty and resultant timidity on their part...

It is also important that the legal prohibitions are meaningful to the conduct engaged in by business. For example, while an overriding goal of promoting competitive markets can support effects-based standards, competition laws that prohibit conduct by reference to the purpose of the conduct can be more meaningful to business people and provide clearer guidance as to appropriate conduct, while at the same time supporting the overriding goal of prohibiting conduct that is likely to be anti-competitive in effect.

Further, certainty is not simply promoted by additional prescription in contrast to broadly framed, appropriately targeted prohibitions. In fact, excessive prescription (and the inherent complexity that comes with it) may make the law less easy to comprehend, as recognised by the framers of the 1974 *Trade Practices Act*:

> It is of course desirable that uncertainty be kept to the minimum in this as in any other law. But it is questionable whether detailed drafting leads to more certainty.

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[14] *Australian Proposals for Legislation for the Control of Restrictive Practices and Monopolies*, 6 December 1962.

> Often it does no more than obscure the broad purpose of a provision. (Enderby, 1974)

(VII) Don't unduly impede legitimate business interactions

Competition law should not unduly impede legitimate business interactions, recognising the commercial dynamics and constraints at work in markets.

It is critical that the competition law protects vigorous and legitimate competition at the same time as preventing anticompetitive behaviour. As the High Court noted in Queensland Wire**:**[15]

> Competition by its very nature is deliberate and ruthless. Competitors jockey for sales, the more effective competitors injuring the less effective by taking sales away. Competitors almost always try to 'injure' each other in this way.

The Hilmer review elaborated on this principle:

> As the High Court has observed, the very essence of the competitive process is conduct which is aimed at injuring competitors. A firm that succeeds in aggressive competitive conduct may drive other firms from the market and achieve a position of pre-eminence for an extended period. It does not necessarily follow, however, that the competitive process will be damaged by the conduct or that the potential for competition will be diminished, even if the immediate manifestations of the successful competitive conduct may suggest it. Firms should be encouraged to compete aggressively by taking advantage of new and superior products, greater efficiency and innovation. There is a serious risk of deterring such conduct by too broad a prohibition of unilateral conduct. (p. 70)

A law that regulates commercial conduct, as competition laws do, will necessarily stifle business activities, involve costs of compliance and delay, and remove commercial flexibility. There is a risk that competition laws, by imposing costs and reducing commercial flexibility, work against the interests of consumers. Even relatively straightforward prohibitions for which there may be administrative exemption mechanisms will impose such costs. It is for this reason that the laws should be well framed to address clear cases of anti-competitive conduct, without recourse to administrative exemption mechanisms to address a poorly specified law.

The remainder of this section will highlight each of the key areas of CCA that should be revised to promote competitive markets (given increasing globalisation, changing market and social structures and technological change). The BCA's views on each of the relevant provisions in the Competition Law are set out in further detail in the rest of this chapter.

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[15] *Queensland Wire Industries vs The Broken Hill Proprietary Company* (1989) 167 CLR 177 per Mason CJ & Wilson J at 191.

3.2 Priorities for competition law reform

3.2.1 Defining markets and analysing competition effects

The issues paper notes that 'markets' are the central concept in the CCA by which competition is assessed, and that increasing globalisation, changing market and social structures, and technological change are all impacting on the competitiveness of markets. The issues paper asks whether, given structural changes in the economy over time, the definitions of "market" in the CCA operate effectively and work to further the objectives of the CCA.

This is an important question, as an unduly narrow or static approach to market definition and competitive effects analysis is likely to exclude a consideration of important competitive elements and lead to the over-application of the CCA. Any over-application of the CCA will impede the ability of business to dynamically respond to changing market conditions and efficiently deliver products and services that consumers value. Conversely, an unduly broad market definition may permit conduct that is detrimental to consumers. However, recent experience suggests that the more significant risk is that approaches to these issues have become unduly narrow, static and out of step with contemporary jurisprudence and economics, and that the CCA has been over-applied.

These risks may be reduced by changes to the regulator's processes, most critically in relation to merger reviews, and may also be mitigated by amendments to the CCA itself.

As noted in Chapter 1, it is critical that the approach to defining and analysing competition in markets does not unduly restrict the analysis of the dynamic factors at play in many industries. For example, traditional "bricks and mortar" businesses are increasingly facing competitive pressure from global entities that are internet-based. Further, technological change and innovation are driving down entry costs in many markets and creating conditions for disruptive competition as new products and new modes of delivery are offered to consumers.

Importantly, the jurisprudence on market definition and competitive effects assessment emphasises that while the identification of the relevant market is a purposive exercise[16] focused on the area or areas of close competition, the delineation of the market should comprehend the maximum range of business activities and the widest geographic area within which, if given a sufficient economic incentive, buyers can switch to a substantial (that is, material) extent from one source of supply to another, and sellers can switch from one production plan to another.[17] The jurisprudence makes clear that this broadest field of material substitution possibilities is also to be assessed against *long-run*

[16] Mason CJ and Wilson J *Queensland Wire Industries Pty Ltd v The Broken Hill Pty Co Ltd* (1988-89) 167 CLR 177 at 187; French J in *Singapore Airlines Ltd v Taprobane Tours WA Pty Ltd* (1992) ATPR ¶41-159; Burchett J in *News Ltd v Australian Rugby Football League Ltd* (1996) ATPR ¶41-466

[17] *Queensland Co-operative Milling Association Ltd and Defiance Holdings Ltd* (1976) ATPR ¶40-012; Re Tooth Co Ltd and Tooheys Ltd (1979) ATPR ¶40–113

substitution possibilities rather than *short-run* and *transitory* situations.[18] A long-run focus allows the market to be defined to capture the field of actual or potential rivalry between firms.[19]

The approach of the courts has also been to emphasize an approach to market definition and competitive effects that is commercially realistic.[20] The operation of the purposive approach to market definition and the flexibility it entails reflect the fact that markets and market definitions can change over time as competition in those markets changes.

Notwithstanding this jurisprudence and the ACCC Merger Guidelines (2008b), there is a risk that in practice the administrative approach to market definition can become unduly narrow, static and short-sighted.[21] Further, there is a risk that the approach to competitive effects analysis can become formulistic and overly reliant on market concentration rules of thumb, which overemphasizes the number of competitors rather than the dynamic competitive process.[22] This risk is exacerbated if concentration measures are based on narrow market definitions reflecting current patterns of supply rather than likely or potential competitive constraints over time.[23] There is also a very real risk that the adoption of hypothetical competitive counterfactuals becomes the critical issue in competition assessments.[24] In particular, there is a very real risk that theoretical counterfactual

[18] Queensland Co-operative Milling Association Limited (1976) 25 FLR 169 at 190; Tooth & Co Limited and Tooheys Limited (1979) 39 FLR 1 at 38; Australian Gas Light v Australian Competition and Consumer Commission (No 3) (2003) ATPR ¶41-966

[19] Queensland Wire Industries Pty Ltd v The Broken Hill Pty Co Ltd (1988-89) 167 CLR 177 per Deane J and Dawson J, NT Power Generation Pty Ltd v Power and Water Authority (2004) ATPR ¶42-021

[20] *Australian Competition and Consumer Commission v Metcash Trading Limited* (2011) 198 FCR 297; *Australian Gas Light Company v Australian Competition & Consumer Commission (No. 3)* [2003] FCA 1525.

[21] Recent examples of the ACCC adopting narrow or static market definitions in its assessment of mergers include its review of Carsales' proposed acquisition of Trading Post, in which it adopted markets for the supply of online automotive classified advertising to dealer (commercial) advertisers and to private advertisers (ACCC, 2013c), and its review of NAB's proposed acquisition of AXA, in which it adopted a market for the supply of retail investment platforms for investors with complex needs. In the Carsales matter, the ACCC disregarded the high degree of supply- and demand-side substitutability and the role of new online business models through Google and eBay/Gumtree (ACCC 2013d). In the NAB matter, the competitive constraints provided by viable substitutes, including new products, were not taken into account in this matter(ACCC 2010).

[22] For instance, the ACCC recently has applied a rule of thumb that a merger between two of the three key players is likely to substantially lessen competition unless it can be shown that other constraints will apply or that the target is failing, such as likely growth from the competitive fringe or further market entry. See, for example, the ACCC's review of Pact Group's proposed acquisition of Viscount, where the ACCC accepted that barriers to entry were low and the competitive fringe could grow. Also see the ACCC's review of Virgin Australia's proposed joint venture to operate Tiger Airways, and Pact Group's proposed acquisition of Drum Reconditioners NSW where the ACCC accepted that the targets were 'failing firms'.

[23] That is, market shares are based on 'stock' measures which show the total number of customers supplied by each firm. A more dynamic way to examine market shares is to examine the 'flow' measures which show the number of customers that were won over a recent period. In a situation where barriers to entry and expansion are not insurmountable, the 'flow' measures better reflect the current competitive dynamic as they are forward looking.

[24] For a discussion of the ACCC adopting rival bidder counterfactuals which were critical to the assessment of the competition issues in merger reviews, such as the counterfactuals adopted in

scenarios can skew assessments and result in some acquirers being preferred over others.[25] These risks are such that markets can be defined, and competitive effects analysed, in ways that are independent of market conditions and conditions for entry and expansion or otherwise ignore commercial realities.

The risks of a narrow approach to market definition and competitive effects are real. The fact that these risks can in theory be mitigated through recourse to the courts is not an answer to the dangers they pose in terms of delay, cost and efficiency-enhancing transactions that are abandoned without judicial challenge.

The CCA provides little practical guidance to the assessment and definition of markets and the approach to competitive effects analysis.[26] It is not explicit that the geographic dimension of a market can extend beyond Australia, or that many of the section 50(3) factors identified in merger assessment should be considered in any competitive analysis. While a considerable body of jurisprudence has evolved around the approach to market definition and competitive effects assessment,[27] without further legislative guidance on these concepts, particularly the need to examine competitive dynamic effects, there is a real risk that a narrow or static approach to markets and competitive effects will be adopted in practice. The area in which this is most acute is in the administration of section 50 of the CCA (discussed separately in Chapter 4), but the issue is a more general one.

The risks arising from a narrow approach to market definition and competitive effects could be reduced by strengthening the formal and informal merger processes to make them more responsive, transparent and accountable, as discussed below and in Chapter 4.

To further mitigate these risks, the CCA's guidance on these issues could be strengthened by specifying in section 4E that the geographic dimension of market may include those listed in section 50(6) and may extend beyond Australia; and expanding section 4E and/or 4G to include reference to some of the dynamic factors currently listed in s 50(3) of the CCA. For example:

- the actual and potential level of import competition in the market
- the height of barriers to entry to the market
- the extent to which substitutes are available in the market or are likely to be available in the market

its assessment of Metcash's proposed acquisition of Franklins, NAB's proposed acquisition of AXA, Caltex's proposed acquisition of Mobil's retail assets and Woolworths' proposed acquisition of Karabar supermarket, see, Morelle Bull and Danielle Wood, The fairest of them all? Rival bidder counterfactuals in Australian merger clearance, (2012) 19(3) Competition and Consumer Law Journal 231, 239.

[25] See ACCC v Metcash Trading Limited [2011] FCA 967

[26] Markets are technically defined in section 4E as being markets in Australia and to include goods and services which are substitutable or otherwise competitive with each other. A specific definition of geographic market scope is included in section 50 (6) for the purpose of merger assessments, making clear that the market may be national, state-wide, regional or local; and similarly section 50 (3) provides a list of factors that the Court must take into account in its competitive effects analysis in respect of mergers.

[27] *Re Queensland Co-operative Milling Association Ltd and Defiance Holdings Ltd* (1976) ATPR ¶40-012; *Re Tooth Co Ltd and Tooheys Ltd* (1979) ATPR ¶40–113.

- the dynamic characteristics of the market, including growth, innovation and product differentiation.

3.2.2 The mergers context

The ACCC's approach to the assessment of the competitive effects of mergers is set out in its Merger Guidelines (2008b). These Guidelines are a valuable guide to the assessment of competitive effects of mergers.

However, as noted above, there is a risk, reflected in concerns arising out of some cases,[28] that the approach adopted by the ACCC to merger reviews can be unduly narrow or static and consequently some of the relevant competitive constraints on the merged entity are not considered. As the ACCC's informal clearance process is not currently open to any form of transparent internal review process, this risk can be significant (see Chapter 4).[29]

In the late 1990s and early 2000s the ACCC explicitly examined mergers according to a strict structure–conduct–performance (SCP) paradigm[30] to draw conclusions as to competitive effects.

However, the SCP paradigm has largely been overtaken in more recent economic theory, which recognises that it is conduct, such as the strategic behaviour of firms, that determines the structure of the market and the performance of other firms.[31] Although the ACCC's 2008 Merger Guidelines set out a more dynamic approach to assessing competitive effects, it appears that the ACCC continues to place a high degree of reliance on market concentration and the SCP paradigm, particularly in cases that involve a merger between two of the three key players (a "3 to 2" or a "2 to 1").[32]

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[28] See ACCC v Metcash Trading Limited [2011] FCA 967; also Stephen Bartholomeusz, "Murray Goulburn didn't get a chance to compete fairly against Saputo", Business Spectator 21 January 2014: "With the Australian Competition and Consumer Commission defining markets quite narrowly and looking at the impact of mergers on domestic competition and consumers, obtaining approval can be a protracted and difficult process."

[29] While challenge to the ACCC's decision is available in the Federal Court, this route is rarely practical for businesses given it is costly and time consuming.

[30] According to the SCP paradigm, a market's performance depends on the conduct (behaviour) of its firms, which in turn, depends on the structure (factors that determine the competitiveness of the market). The SCP paradigm was developed at Harvard by Edward S. Mason and Joe Bain (1959).

[31] See Philip Williams and Graeme Woodbridge, "The Relation of Efficiencies to the Substantial Lessening of Competition Test for Mergers: Substitutes or Complements?" Australian Business Law Review, December 2002 at p. 435; Robertson, D., "The Regulatory Assessment of Mergers (and Things like Mergers)" (2000) 7 CCLJ 201; Smith, R. & Round, D., "A Strategic Behaviour Approach to Evaluating Competitive Conduct" (1998) 5(1) Agenda 25; Round, D., & Smith, R., "The Strategic Approach to Merger Enforcement by the ACCC: A Comment" (1998) 26 ABLR 227; Smith, R. & Round D., "Competition Assessment and Strategic Behaviour" (1998) 19 European Competition Law Review 225 at 232–233; Round, D. & Smith, R., "Strategic Behaviour and Taking Advantage of Market Power: How to Decide if the Competitive Process is Really Damaged?" (2001) 19(4) New Zealand Universities Law Review 427; Caron Beaton-Wells and Brent Fisse, Australian Cartel Regulation, Melbourne: Cambridge University Press, 2011 at p. 129.

[32] The matters include Virgin Australia's proposed joint venture to operate Tiger Airways, Woolworths' proposed acquisition of a site in Glenmore Ridge, Heinz's proposed acquisition of

While the existing state of the world can be informative when considering the future state of the world, it is important that all section 50(3) factors are integrated into the analysis as relevant to a consideration of whether a merger substantially lessens competition. The level of concentration in a market is one factor among nine and it should not be elevated above other factors.

It is important to ensure that market definitions in merger matters are defined in a way that places sufficient weight on the dynamic changes in markets, including in the way goods are supplied and consumed. The impact of globalisation and the rise of online media and sales, as well as challenges posed by new entrants, are all relevant factors that should be fully considered in defining markets and considering competitive effects. Placing insufficient weight on the impact of new and innovative but currently small entrants, or to underestimating the constraint offered by new product and distribution alternatives, has the potential to result in backwards-looking decisions which unnecessarily penalise incumbents and have the potential to stifle innovation, efficiency and, ultimately, competition.

It is also important that market definitions are not applied in a 'bright line' or 'hard and fast' way. Even after markets are defined in merger matters, out-of-market constraints should also be considered. This is a particularly important issue when local market mergers are being assessed and the local market is framed around the target business by a certain kilometre radius or driving distance. To ignore, out-of-market constraints, such as those currently constraining the acquirer in the local market, is to analyse the competitive dynamic in a way that is divorced from commercial reality.

In its recent decision to authorise AGL's acquisition of Macquarie Generation,[33] the Tribunal strongly disagreed with the ACCC's reliance on market structure and concentration to predict harm:

> There is nothing inherently wrong with a market in which three large firms compete vigorously for market share where there are incentives to steal customers away from rivals. It is behaviour that matters, not structure per se. It appears to the Tribunal that it has been invited to assume that the "Big 3" will not constitute a competitive market principally on the basis of their combined market share immediately post-acquisition on an assumption that competition between them would become muted over time. In the opinion of the Tribunal, oligopolies should not be thus prejudged…
>
> The competitive environment that is likely to exist in that situation may be hostile for small, non-integrated retailers or it may present niche opportunities. However, the Tribunal cannot conclude that a more atomistic market structure that favours a particular class of competitors is intrinsically better for consumers in the long run. It is the competitive mindset that matters, not market structure.

The merger factor relating to the level of concentration in the market (s 50(3)(c)) may be one reason that too much weight may be placed on static and historic measures of concentration at the expense of the other factors, many of which will

Rafferty's Garden, Nestle's proposed acquisition of Pfizer's infant formula business, and Sonic Healthcare's proposed acquisition of Healthscope's pathology businesses, among others.

[33] Re Application for Authorisation of Acquisition of Macquarie Generation by AGL Energy Limited [2014] ACompT 1

be more important in an assessment of modern markets. At the very least, section 50(3)(c) should be amended to read:

> the current and likely level of concentration in the market in the long term;

Consideration should be given to removing merger factor (c) altogether and leaving concentration to be taken into account in merger factor (f), that is:

> the likelihood that the acquisition would result in the acquirer being able to significantly and sustainably increase prices or profit margins;

Since this factor is really the ultimate test of market power, it does not seem appropriate that measures such as concentration, which are at best proxies or indicators of that test, should be elevated to the same level in competition assessment.

Improving merger processes

Improvements to both the formal and informal merger processes would support the principles that competition law should not unduly impede legitimate business interactions; should reflect international best practice; and should have long-term consumer welfare as its overriding goal.

The BCA considers that while the current merger processes are working adequately, there is the potential to significantly improve them by incorporating a flexible review mechanism into the ACCC's informal clearance process. This is discussed in Chapter 4 where the focus is on enhancing regulator performance. The suggestions to improve the formal merger clearance process are set out below.

The formal merger clearance processes

The Dawson review recommended the adoption of a formal clearance mechanism. Such a process was intended to work as an important alternative to the informal clearance process, by which a merger party could gain a formal exemption from section 50 where it could establish, to the satisfaction of the ACCC (or, on appeal, the Tribunal) that its acquisition would not substantially lessen competition.

The availability of this alternative to the informal process, particularly in potentially contentious cases, is desirable and should be retained. However, the formal merger clearance process has not been used, in part because it is unduly complicated by strict technical formal requirements for a compliant application, including for example, the detailed and prescriptive standard form application (Form O, Reg 73), which is onerous and inflexible.[34]

The fact that the Australian formal clearance process has not been used in almost 10 years is evidence that the procedure is not attractive to merger proponents. The BCA does not consider that the formal clearance mechanism should be complicated by strict technical formal requirements when it is the merger

[34] CCA section 95AE. Form O requires a great deal of information, much of which may be irrelevant to the circumstances of the merger in question. See http://accc.gov.au/system/files/Form%20O%20-%20Application%20for%20s50%20merger%20clearance.pdf

proponent that bears the onus of establishing to the ACCC's satisfaction that the acquisition does not substantially lessen competition. If the ACCC is not satisfied, it can refuse clearance.

Retaining authorisation of mergers

Merger parties also have the option of approaching the Tribunal for merger authorisation, on the grounds that public benefits associated with the merger outweigh any anti-competitive detriments. This process has only been used in two matters,[35] with one withdrawn and one current.

There is an important role for merger authorisation on public benefit grounds and this process should be retained. In particular, the ability to seek authorisation directly from the Australian Competition Tribunal provides an important alternative to the ACCC's formal and informal clearance processes.

The body of precedent built up and applied by the Tribunal gives an important degree of certainty to matters brought before it, and there is no justification for requiring a refusal by the ACCC before approaching the Tribunal. It is also to be hoped that the potential for direct application to the Tribunal may have some influence on the speed, transparency and accountability of the clearance processes – a measure of competition within the competition framework itself.

3.2.3 Reforming Section 46

No 'effects' test

The role of purpose in section 46 has been the subject of debate since its inception. Several approaches to an effects test for section 46 have been proposed, from simply adding "effect or likely effect" to the existing section (Evans et al., 1984) to a new section prohibiting a corporation with substantial market power from engaging in any conduct or behaviour that has the purpose, effect or likely effect of substantially lessening competition (TPC, 1989; Fels, 2014). Effects tests have been considered by every major review of the legislation, and have been rejected without equivocation on every occasion (as outlined in the appendix of this submission at exhibits A. 2, A.3 and A.4).

The function of the purpose test is to distinguish behaviour that manifests vigorous and effective competition from behaviour that prevents or deters competition. The immediate effects of both kinds of behaviour may be identical: both may damage or even eliminate competitors. But prohibiting unilateral behaviour based on its effect on competitors would lead to a very different competitive landscape to the current landscape, in which unilateral behaviour is judged according to its purpose. Any such change might protect individual competitors, but it would lessen competition.

That is, the current section 46 test examines purpose to achieve the pro-competitive effect of encouraging vigorous competition for the benefit of

[35] Murray Goulburn Co-Operative Co Limited has withdrawn its application for authorisation of a proposed acquisition of Warrnambool Cheese & Butter, while AGL Energy Limited's proposed acquisition of Macquarie Generation assets is still before the Tribunal.

consumers while preventing misuse of market power directed at excluding competitors.

Market participants should be encouraged to focus on increasing their efficiency, reducing their prices and improving their services in order to win customers. That is the essence of competition and the best guarantee of public benefit. They should not also be forced to consider the possible impact of their actions on their competitors, in effect to protect their competitors from competition: that would be the antithesis of the competitive process and would deprive the public of its benefits. Examples of conduct that might be caught by an effects test are listed in Exhibit A.3 in the appendix.

The role of purpose in distinguishing between vigorously competition and anti-competitive behaviour has been recognised by the High Court since the Queensland Wire case[36] and by every review of the trade practices legislation, as set out in Exhibit A.5 in the appendix. Most recently, the Dawson review examined all previous suggestions of an effects test and considered that:

> Not only would the introduction of an effects test alter the character of section 46, but it would also render purpose ineffective as a means of distinguishing between legitimate (pro-competitive) and illegitimate (anti-competitive) behaviour… The introduction of an effects test would be likely to extend the application of section 46 to legitimate business conduct and discourage competition. (p. 80)

Discerning a corporation's purpose may not always be straightforward, but the courts now have four decades of experience in doing so, and have developed increasingly sophisticated tools and principles to assist them. Courts have found a proscribed purpose in many high-profile cases, and have awarded more than $34 million in penalties for section 46 cases since the Dawson review, as set out in Exhibit A.5 in the appendix. The ACCC continues to take on new section 46 cases, including recent actions against Visa and Pfizer, under the "purpose" test.

The ACCC has asserted that, although it has never lost a section 46 case on the basis of purpose, it has on occasion chosen not to commence proceedings following complaints from market participants because it has not found sufficient evidence of a proscribed purpose. The ACCC does not assert that it *believed* that there was an anti-competitive purpose that it was unable to prove, only that it believed there had been an anti-competitive effect. This suggests that the law is operating exactly as it was intended in focusing on a company's competitive purpose, rather than on unintended consequences, in order to promote competition overall.

The ACCC continues to take on new section 46 cases, including recent actions against Visa and Pfizer, under the "purpose" test.

Finally, a careful analysis of international jurisprudence reveals that purpose is widely used as a tool to distinguish between beneficial vigorous competition and detrimental anti-competitive conduct, as set out in Exhibit A.6 in the appendix.

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[36] *Queensland Wire Industries v Broken Hill Proprietary Company* (1989) 167 CLR 177 at 191.

An effects test would be inconsistent with the principles that competition law should not unduly impede legitimate business interactions; should be simple to understand and implement; and should have long-term consumer welfare as its overriding goal.

Combining an effects test with an relaxing or even elimination of the requirement that a company must *take advantage* of its market power for conduct to be prohibited, as has been suggested to the Review, would compound these problems, move the provision even further away from a principled approach to competition law, and further damage competition for the possible benefit of some competitors but the ultimate detriment of consumers.

Predatory pricing and the Birdsville amendment

Predatory pricing is perhaps the area in which vigorous, beneficial competition and anti-competitive conduct become most difficult to distinguish. Aggressive pricing is generally of great benefit to consumers and is in many ways the purest and most effective form of competition. It may only harm consumers in the long term if it drives out competitors such that the price predator no longer feels constrained by actual or potential competition and can raise prices above competitive levels.

The difficulties of predatory pricing have been recognised by courts and regulators, as set out in the appendix. As noted by the US Supreme Court in Brooke Group:[37]

> [P]redatory pricing schemes are rarely tried, and even more rarely successful, '… and the costs of an erroneous finding of liability are high. [T]he mechanism by which a firm engages in predatory pricing – lowering prices – is the same mechanism by which a firm stimulates competition; because "cutting prices in order to increase business often is the very essence of competition... mistaken inferences... are especially costly, because they chill the very conduct the antitrust laws are designed to protect."'… It would be ironic indeed if the standards for predatory pricing liability were so low that antitrust suits themselves became a tool for keeping prices high.

Recent amendments to section 46 have attempted to codify a particular interpretation of predatory pricing after the High Court's decision in *ACCC v Boral*. Instead, they have significantly obscured the issue. Subsections 4A and 1AA (the "Birdsville" amendment) both rely on the untested concepts of "sustained period" and "relevant cost", and subsection 1AA adds the further concept of a "substantial share". These ideas may in future be elucidated by the courts, at considerable cost and with no indication that they offer any advantage over the much better-defined concepts that they are designed to clarify or replace. In the meantime, uncertainty over the meaning of these terms and the effect of these provisions will discourage vigorous price competition and increase prices to consumers.

Further, in providing that predatory pricing may be shown even without likely recoupment, subsection 1AAA risks undermining the rationale for regulating predatory pricing, which is to prevent consumer harm in the long term. The courts have found that the likelihood of recoupment is not legally essential to a finding of

[37] *Brooke Group v Brown & Williamson* 509 U.S. 209 (1993).

predatory pricing, but it is internationally recognised as an important tool in determining the intention of a corporation and the consumer harm or benefit that may result from its pricing decisions. It has evolved with economic consideration of predatory pricing: for example, recognising that potential recoupment from other markets should be taken into account. Subsection 1AAA risks downplaying a vital tool that goes to the heart of the predatory pricing prohibition.

The Australian courts have evaluated claims of predatory pricing under the general principles of section 46 by reference to the established and current international economic and jurisprudential analysis and continue to refine and implement key concepts and tests. As markets grow more dynamic and more exposed to overseas competition it is even more dangerous to assume that aggressive pricing is anti-competitive in the absence of clear consumer detriment.

Recent amendments to section 46 unnecessarily complicate the legal framework, decreasing rather than enhancing certainty for businesses of all sizes, and threatening vigorous price competition that benefits rather than harming consumers. They are inconsistent with the principles that competition law should not unduly impede legitimate business interactions; should be simple to understand and implement; should reflect international best practice; and should have long-term consumer welfare as its overriding goal.

3.2.4 Agreements between competing firms

Cartel provisions

The most serious forms of agreements between competitors that constitute exclusionary provisions, as defined in section 4D, are separately addressed by the cartel provisions: that is, price-fixing, capacity-fixing, market-sharing, and bid-rigging. Other examples of agreements between competitors should be judged under the general section 45 prohibition against agreements that substantially lessen competition. Streamlining these sections would promote the principles that the competition law should be as simple as possible to understand, and that the use of *per se* prohibitions should be minimised.

The Federal Court has recently handed down two conflicting decisions raising uncertainty over the scope of the *per se* prohibitions in relation to competitor agreements (s 45, s 4D and Part IV Division 1). *ACCC v ANZ*[38] and *ACCC v Flight Centre*[39] both involved suppliers who sold goods or services through dual-distribution models: that is, both through an intermediary agent or broker, and direct to the end customer through an internal distribution channel or online. In both cases the ACCC alleged that, despite the seemingly vertical nature of their relationships, the parties were nonetheless competitors for the purposes of the cartel provisions under the CCA.

In *ACCC v ANZ*, Dowsett J held that no contravention was established because ANZ and the brokers who distributed ANZ mortgages as agents were not found to

[38] *ACCC v Australian and New Zealand Banking Group Limited* [2013] FCA 1206.
[39] *ACCC v Flight Centre Limited (No 2) [2013] FCA 1313.*

have been competitors capable of engaging in price fixing. In contrast, Logan J in *ACCC v Flight Centre* held that Flight Centre and certain airlines, whose airfares Flight Centre distributed as agent, were competitors and that Flight Centre's conduct did constitute an illegal attempt to engage in price fixing.[40]

The Flight Centre case raises serious implications for the assessment of vertical supply arrangements under the CCA. These uncertainties will not only impede business through the increased compliance burden of monitoring existing vertical arrangements, but will have a chilling effect on entry into traditional markets by new service offerings, such as online brokers and referral and comparison providers. Precisely in those markets where increased flexibility and growth opportunities should be fostered, the uncertainties of the Flight Centre case will have the opposite effect.

The potential for anti-competitive harm as a result of vertical supply arrangements is appropriately addressed by a substantial lessening of competition test under either section 47 or section 45. The uncertainty created by *ACCC v Flight Centre* may persist for some time, as the case may be appealed all the way to the High Court, and even then may be decided on another point of law. Certainty would be best provided by amending the legislation to ensure that the *per se* prohibitions are only intended to apply in respect of horizontal arrangements between competitors.

This amendment would be consistent with the principles that competition law should minimise the use of *per se* prohibitions; should not unduly impede legitimate business interactions; should be simple to understand and implement; should reflect international best practice; and should have long-term consumer welfare as its overriding goal.

The joint venture exception

Joint ventures are exempted from the cartel provisions, subject to certain conditions that considerably reduce the practical and commercial application of the exception, and consequently the economic benefits and efficiencies to be gained from genuine joint venture arrangements.[41]

First, the exception applies only in respect of contracts, or arrangements and understandings which were intended to be or were reasonably believed to be contracts.[42] This limitation fails to take into consideration the rapidly changing and increasingly competitive global markets in which modern joint ventures are being developed and implemented, and in which many arrangements are made quickly and informally. A more flexible approach to this aspect of the exception is

[40] Flight Centre has appealed to the Full Federal Court, while the ACCC has cross-appealed for higher penalties.

[41] Acknowledged in *Supplementary Explanatory Memorandum and Correction to the Explanatory Memorandum, Trade Practices Amendment (Cartel Conduct and Other Measures) Bill 2008 (Cth)*: "Joint ventures have an important role to play in Australia's economy, and can be pro-competitive, particularly when they are employed as a means of developing new products or services or producing existing products or services more efficiently."

[42] Section 44ZZRO of the CCA.

necessary to enable businesses to take full advantage of the benefits derived from pro-competitive strategic alliances.

Second, the exception only applies in respect of joint ventures which relate to the production of goods and services and does not extend to joint ventures which relate to the acquisition of goods or services, the marketing of goods or services, or research and development. This distinction is arbitrary and excludes many forms of pro-competitive collaboration.

These two limitations prevent businesses from relying on the joint venture exception in respect of what could otherwise be genuine and pro-competitive alliances. Further, the complexities in applying the limitations in day-to-day business interactions results in an unnecessary regulatory burden being placed on businesses to satisfy themselves (and where necessary the regulator and/or the courts) that a genuine joint venture initiative adheres to the various statutory requirements. The resulting uncertainty and delay ultimately leads to legitimate joint ventures being abandoned and growth opportunities being lost.

The joint venture exception is subject to other limitations that effectively safeguard against potential abuses: for example, it only applies where a cartel provision is for the purposes of the joint venture. The two limitations discussed are unnecessarily restrictive and should be removed from the joint venture exception requirements. This removal would be consistent with the principles that competition policy should not unduly impede legitimate business interactions; should apply consistently across the economy; should be simple to understand and implement; and should have long-term consumer welfare as its overriding goal. It would also bring the CCA closer to international best practice, in this case represented by the amendments introduced by the New Zealand *Commerce (Cartels and Other Matters) Amendment Bill*, which created an exemption for cartel provisions that are reasonably necessary for any collaborative activity that does not have the purpose of substantially lessening competition.

Price signalling

The current prohibitions relating to price signalling in the CCA are long, complex, and inconsistent with international best practice; they apply on a narrow sectoral basis and are not suitable for general application. Public statements by industry participants in a range of sectors have occasionally been cited as actions that should be captured by broadening of the price signalling provision of the CCA. These statements have often been contained in routine share market disclosures or in interviews with the financial press and are not appropriate for regulation under the CCA. Equally, there has been no suggestion of any private statements of concern in these sectors, and to regulate them would seriously interfere with efficient business operations. Overall, the evidence suggests that sectors such as banking, fuels, airlines and telecommunications, which are all areas where some have raised concerns, are all highly price competitive, and there has been no evidence of consumer detriment that would support extending (or even retaining) this regulation of public and private information disclosure.

Moreover, if there ever were any evidence of any anticompetitive price-signalling, the CCA already gives broad powers to prosecute this conduct – an attempt to

arrive at an anticompetitive understanding is unlawful under Australian law – unlike many other jurisdictions. Prosecuting unilateral conduct that falls short of an attempted anticompetitive understanding would risk chilling legitimate and pro-competitive statements with no evident harm to competition.

The price signalling provisions apply to unilateral conduct of a firm. In this form they are inconsistent with economic theory and general competition law provisions. The only circumstances in which competition laws prohibit unilateral conduct is in respect of firms with substantial market power that abuse that market power position. The only economic theory that would support a prohibition directed to information exchanges and price signalling is one which was grounded in concerns as to collusion or facilitating collusion between market participants.

In contrast to the price signalling provisions, EU and US antitrust laws require an element of concerted conduct, reciprocity, coordination or mutuality between competitors in order for the disclosing conduct to be prohibited. In fact, no developed foreign competition law regime has adopted prohibitions on the type of unilateral information disclosures proscribed in the current CCA.

It is clear that the current price signalling provisions are not well directed. In an attempt to contain the significant possibility of unintended consequences arising from prohibiting unilateral disclosures of information, the current provisions introduce an extensive range of arbitrary legislative stop-gaps – including limiting application of the price signalling laws to prescribed goods and services (presently limited to the banking sector) and through the codified exceptions that attempt to carve out the many pro-competitive or benign forms of disclosure that remain legitimate business conduct. This reflects a recognition of the difficulties in separating legitimate public price information from damaging price signalling, which are set out more fully in Exhibit A.8 in the appendix.

These complex exceptions in the price signally provisions of the CCA reflect an implicit acknowledgment that there is a real risk of benign, if not pro-competitive, commercial communications being caught by the prohibitions. The exceptions are vague, complex and remarkable in their nature and scope compared to any other provisions of the CCA. Moreover, they were specifically introduced in the context of concerns raised in relation to the financial services sector, so are ill-adapted to any economy-wide application of the law. Were the laws to be applied more broadly, it would be necessary to consider, sector by sector, what carve outs might be required to prevent unintended consequences in each case.

Arrangements amongst competitors to share information which are anti-competitive in purpose or effect should properly be the subject of the CCA. However, there is no substantive evidence that there is any gap in the Australian law. The CCA does extend to such conduct, and the provisions are unnecessary given the capacity of the general prohibitions of the CCA to address anticompetitive information exchanges and price signalling conduct. Specifically, although evidence of ‘commitment’ and ‘meeting of minds’ remain necessary in establishing an ‘understanding’, it is possible to infer these elements having regard

to the circumstances of the conduct, including any disclosures, communications, and exchanges in question.[43]

Further, the CCA already prohibits any attempt to enter into or induce a collusive arrangement or understanding, and therefore sufficiently covers the conduct targeted by the price signalling laws. For example, the ACCC has successfully prosecuted unilateral attempts in circumstances where there was no concluded agreement but one competitor simply sent a written memorandum to another,[44] made two telephone calls to competitors,[45] submitted a quote to a competitor[46] or engaged in a series of conversations with a competitor.[47]

The US and EU prohibitions discussed above address the fact that their laws do not prohibit attempts to enter into a collusive arrangement or understanding, and so do not provide a relevant comparison for Australian law.

3.2.5 Agreements between firms in a supply chain

Vertical arrangements should not be 'per se' illegal

The best practice principles of competition law provide that conduct should only be prohibited *per se* where in the overwhelming majority of cases it will be anti-competitive with no redeeming public benefit. Neither resale price maintenance nor third line forcing satisfy this requirement.

Third line forcing delivers substantial consumer benefits in many cases, particularly where it is cheaper to sell two or more products in combination due to efficiencies in production or distribution. These benefits outweigh any detriments to the public in the overwhelming majority of cases, as demonstrated by the very small proportion of third line forcing notifications that are overturned by the ACCC. As set out in Table 1, in the five years from 2009 to 2013 a total of 1845 exclusive dealing notifications (almost all for third line forcing) were allowed to stand and only two were revoked.

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[43] *ACCC v TF Woollam & Son Pty Ltd* [2011] FCA 973; *Norcast S.AR.L v Bradken L*td (No 2) (2013) 302 ALR 48.

[44] *Trade Practices Commission v Tubemakers of Australia Ltd* (1983) 47 ALR 719.

[45] *Australian Competition and Consumer Commission v George Weston Foods Ltd* [2000] FCA 690.

[46] *Australian Competition and Consumer Commission v J McPhee & Son (Aust) Pty Ltd (No. 3)* (1998) ATPR (Digest) ¶46-183, 50,321; BC9800654; *J McPhee & Son (Aust) Pty Ltd v Australian Competition and Consumer Commission* [2000] FCA 365; (2000) 172 ALR 532.

[47] *Trade Practices Commission v Parkfield Operations Pty Ltd and Another* (1985) 62 ALR 267.

Table 1: Third line forcing notifications on the ACCC register

Year	Allowed to stand	Revoked	Withdrawn
2009	320	2	3
2010	285	0	7
2011	339	0	0
2012	433	0	7
2013	468	0	1

Source: ACCC notification register. Note: in addition, 18 notifications were withdrawn, sometimes following objections raised in the ACCC's market enquiries, but often because promotional arrangements had ceased.

Notification of third line forcing may only require nominal lodgement fee, but the legal fees (whether in-house or external) and the cost of management time involved in preparing notifications and responses to information requests and market inquiries add up to a significant impost on businesses engaging in conduct that is pro-competitive in 99 per cent of cases but is prohibited *per se* for purely historical reasons.

It is also well recognised that resale price maintenance can provide substantial efficiencies, particularly in the wide range of circumstances in which inter-brand competition is more important than intra-brand competition. As noted by the US Supreme Court in removing the US's long-standing (and less restrictive) *per se* prohibition against resale price maintenance in 2007:[48]

> [E]conomics literature is replete with pro-competitive justifications for a manufacturer's use of resale price maintenance… A single manufacturer's use of vertical price restraints tends to eliminate intra-brand price competition; this in turn encourages retailers to invest in tangible or intangible services or promotional efforts that aid the manufacturer's position as against rival manufacturers. Resale price maintenance also has the potential to give consumers more options so that they can choose among low-price, low-service brands; high-price, high-service brands; and brands that fall in between… Resale price maintenance, in addition, can increase interbrand competition by facilitating market entry for new firms and brands.

Manufacturers are increasingly selling directly to the public either online or through vertically integrated retail outlets. Resale price maintenance is a legitimate business strategy to align the interests of the non-vertically integrated manufacturers with their distributors and retailers, enabling them to implement a competitive distribution channel in competition with vertically integrated brands. Further, the *per se* prohibition on resale price maintenance can force businesses into distribution models that they would not otherwise efficiently engage in, such as agency distribution models. The fact that the prohibition can be avoided, through a change in distribution model from one based on sale to a distributor and resale to one based on supply to an agent for sale on behalf of the supplier, points to the

[48] *Leegin Creative Leather Products, Inc. v. PSKS, Inc.* 551 U.S. 877 (2007) at 886.

absence of a strong rationale for the prohibition and the unnecessary costs that it can impose on business.

The current treatment of resale price maintenance and third line forcing is inconsistent with the principles that competition law should minimise *per se* prohibitions; should apply equally across the economy; should impose the lowest possible compliance costs; and should have long-term consumer welfare as its overriding goal.

All vertical arrangements could effectively be dealt with under the general prohibition against contracts, arrangements or understandings that substantially lessen competition under section 45. However, if sections 47 is to be retained, then the prohibition on third line forcing in section 47 (6) and (7) should be subjected to the same competition test. Resale price maintenance conduct would also fall for consideration under section 47. If section 48 is retained, it should be subject to the same competition test.

Maintaining the related party exception to third line forcing

Conditional supply or acquisition by related bodies corporate has not been considered third line forcing since the 2006 amendments following the Dawson review. The absence of this exception was long seen as an anomaly that arbitrarily discriminated against particular corporate structures.

The exception has recently been called into question in relation to the conditional supply of petrol and groceries by related suppliers.[49] However, the ACCC's power to regulate these arrangements does not appear to be diminished by the related party exception and the general competition law should not be changed in response to a perceived sectoral issue. As recognised by the Dawson review, in the absence of the related party exception, corporations could avoid the third line forcing prohibition by restructuring their operations, involving considerable expense for no end benefit.

The related party exception is consistent with the principles that competition law should apply equally to all forms of business enterprise; should not unduly impede legitimate business interactions; should minimise the use of *per se* prohibitions; and should have long-term consumer welfare as its overriding goal. It should be retained.

3.2.6 No case has been made for expanding section 50

Consistent with the principles set out in section 3.1 and the BCA's longstanding position on these issues, there is no case for expanding section 50 beyond its existing application, for example to further address creeping acquisitions or impose market caps (BCA, 2008 & 2009). Such changes would not be targeted at a clearly identifiable, economy-wide problem, and instead would be targeting a perceived sectoral issue and would have the effect of protecting individual competitors. These changes would be detrimental to the competitive process and,

[49] See for example interview between Alan Jones and Minister Billson on 2GB, 20 February 2014, viewed 6 June 2014, at <http://bfb.ministers.treasury.gov.au/transcript/005-2014/>.

therefore, to the overall business and investment environment and would affect ordinary and legitimate business behaviour (BCA, 2008 & 2009).

3.2.7 Exemptions and defences

The operation of the CCA would be enhanced by a simplified and more principled approach to the design of exemptions and defences. A more principled approach would reduce the need for complex individual exemptions or for business to rely on time consuming and costly administrative processes to authorise otherwise efficient or pro-competitive conduct.

Collaborative arrangements, joint ventures and conditional supply arrangements are a common part of everyday commercial activities – and are generally efficient and pro-competitive. While there are benefits of the use of both legislated exemptions and defences, the CCA would benefit from a holistic review to test whether there is scope for reframing a number of the existing defences in a simplified and more principled manner.

Examples of the kind of uncertainty and ambiguity created for business by highly detailed, overlapping or inconsistent drafting of the current exemptions includes:

- There is uncertainty about the operation of the partnership exemption in s 51(2) and whether it extends to protect participants in relation to conduct for the purpose of establishing the partnership (but before it commences).
- The related corporations exemptions under s 44ZZRN and s 45(8) do not apply unless all parties to the contract, agreement or understanding are related corporations. There is no economic justification for excluding guarantors or other third parties that are a party to the contract, agreement or understanding from the scope of the exemption.
- The joint venture exemptions under the cartel provisions (ss44ZZRO and 44ZZRP) are complex and subject to narrow limitations that lack economic justification and are unique to Australia. The approach to joint ventures under the cartel provisions is also different to the joint venture defence in s 76C for conduct that would otherwise contravene the prohibitions on anti-competitive conduct and collective boycotts (in s 45(2)).
- The ‘anti-overlap’ exemptions in ss 44ZZRS and 45(6) and the definition of a ‘competition condition’ under s 44ZZRD(4) do not exclude liability in many cases where one competitor enters into a supply agreement with another where the supply deal is pro-competitive or efficiency-enhancing.
- It is not clear that there remains any economic justification for legislated industry specific exemptions, such as employment conditions and international liner shipping. The latter exemption is not consistent with the principle that the CCA itself should not be targeted at sector-specific issues. Sector specific issues are best addressed through authorisation, which would be a transparent process of testing the claimed public benefits of such arrangements.

There is a strong case for these and other exemptions and defences to be holistically reviewed, with a focus on reducing the current reliance on prescriptive

and narrowly drafted exemptions, in favour of economically principled ones. This would promote the principles that competition law should apply equally across the economy; and should be as simple as possible to understand and impose the lowest possible compliance costs.

3.2.8 Notifications and authorisations

The ability to gain an exemption through authorisation or notification of conduct that may otherwise potentially contravene the CCA, on the basis of an offsetting public benefit, is a valuable feature of the current law. This feature of Australian law provides certainty, which has been important to underpin significant commercial transactions and investments and to facilitate otherwise beneficial cooperative conduct. These processes have also been well administered by the ACCC. However, as noted in the earlier discussion of notifications for third line forcing, the use of *per se* prohibitions married with a reliance on notifications and authorisation, can impose substantial compliance costs on business (and the ACCC which has to administer the system) without a clear public benefit.

Regardless of how well the authorisation or notification processes are administered, they are a 'second best' response to allowing otherwise efficient or pro-competitive conduct and there remain costs and inefficiencies, including that:

- parties are required to prepare and lodge formal applications with the ACCC, and pay lodgement fees (this often also involves retaining legal counsel)
- the timeframe for authorisation is typically up to 6 months for most conduct and, while interim authorisation is available, it is only granted in clear cases and often does not permit full or irreversible implementation during this period
- the ACCC is required to undertake a public consultation process (including engaging with other stakeholders, some of which may be competitors) about the proposed conduct and publishes information about the conduct on its public registers
- the ACCC is required to commit resources to dealing with applications, even in cases where the benefits are clear-cut.

These costs could be avoided through the better design of the primary conduct provisions, and in particular through the adoption of a public benefit defence. The concept of public benefit is well defined in Australian jurisprudence through the Australian Competition Tribunal. It aligns well with 'rule of reason' and efficiency defences in place in the US and other competition law jurisdictions.

The "rule of reason" test was expressed by the US Supreme Court in the following terms:[50]

> The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition.

[50] *Chicago Board of Trade v. United States*, 246 U.S. 231

Canada has a statutory defence in merger cases before the Competition Tribunal, which applies where there are "gains in efficiency that will be greater than, and will offset, the effects of any prevention or lessening of competition" resulting from the merger.[51]

European courts and regulators have also recognised an efficiency defence to Article 102 dominance cases. The European Court of Justice has found that exclusionary effect s "may be counterbalanced, or outweighed, by advantages in efficiency which also benefit the consumer"[52] Similarly, the European Commission has considered that "a dominant undertaking may also justify conduct leading to foreclosure of competitors on the ground of efficiencies that are sufficient to guarantee that no net harm to consumers is likely to arise."[53]

More broadly, in South Africa the *Competition Act 1998* provides a defence to most of its conduct provisions where a party can show "technological, efficiency or other pro-competitive, gains" which outweigh the anti-competitive effect of an act or agreement.[54]

A simple defence could be provided for in relation to a contravention of the competition law provisions of the CCA, particularly where authorisation would otherwise be available, where the respondent party can establish that the conduct resulted in an overall public benefit. Parties seeking certainty would continue to apply for authorisation, but where public benefits would manifestly exceed any lessening of competition they could assume the risk of having to prove the defence at a later date.

3.2.9 Remedies, powers and pecuniary penalties

Additional remedies and penalties have recently been suggested, including in response to perceived sectoral issues. No case has been made for any change to the current range of remedies, penalties and regulator powers. Moreover, as noted elsewhere in this submission, modifying the general law to address perceived competition issues in one sector is not consistent with a principled approach to competition law to. This is particularly the case where all other options to remove barriers to effective competition in a sector have not been exhausted.

Divestiture powers

A private members Bill which would allow the Courts to direct a corporation reduce its market share or market power within two years has been introduced by Senator Xenophon. The explanatory memorandum notes that the provisions are a response to the high concentration of many Australian retail markets, including grocery, fuel, liquor and hardware.

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51 §96, Canadian *Competition Act*.

52 Case C-95/04 P, *British Airways plc v. Commission* [2007], ECR I-2331.

53 Paragraph 30, *Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings*, OJ C 045 , 24/02/2009

54 At sections 4(1), 5(1), 8(c) and (d) and the upcoming section 10A(1).

The BCA addressed divestiture in detail in its submission to the Dawson review, noting that proposals seemed focused on market share measures rather than conduct, and that difficulties could arise if a suitable purchaser was not available for divested assets, leading to loss of services for rural and regional communities (2002a, p. 112). More recently, analysis by prepared for Coles Supermarkets by Dr Alistair Davey (2012) has highlighted the international experience with this power, and the practical challenges this has presented.

The Griffiths and Cooney Reports previously recommended against divestiture due to its unpredictable results, including that the target could be left less productive, efficient, profitable or even viable – and so reducing rather than enhancing consumer welfare.

The Hilmer review and Dawson review noted that divestiture was only appropriate in the case of a merger or acquisition that resulted in a substantial lessening of competition (the existing power), and not in the case of a misuse of market power. The Hilmer review considered that a general divestiture remedy would be arbitrary, would be likely to remove efficiencies, could disrupt entire industries, and would often be ineffective since those industries could change substantially while divestiture was being completed. The Dawson review explained*:*

> ... divestiture is inappropriate in this context because there is no clear nexus between the assets to be divested and the contravening conduct. For example, identifying the specific assets to be divested to preclude a corporation from taking advantage of its market power for a proscribed purpose would be difficult at best and arbitrary at worst. (p. 162)

The BCA suggests, as argued elsewhere in this submission, that if there are concerns in particular sectors, then a more productive approach is for the government to refer sector-specific market studies to the appropriate body that address all the factors that might affect competitive conduct.

'Cease and desist' powers

The first question here is whether there is a problem with the current arrangements, whereby the ACCC can seek injunctions from the Federal Court if it seeks a business to cease and desist a specific action.

The second question is whether the option of providing administrative powers to issues 'cease and desist' orders has benefits that exceed the costs of less transparency and a lower standard of proof than court proceedings, and thus a lower level of accountability. It is not clear what would be the benefits of such a power as there is no evidence of consumer detriment from the current expedient processes of seeking a court-ordered interim/interlocutory injunctions.

Penalties

Penalties under the CCA capture up to three times the calculated benefit of the contravention or 10 per cent of annual turnover (which may easily be 100 per cent of annual profits). These maximum penalties are higher than any other penalties in Australia (for example under the Corporations Act).

Although some of the inputs into maximum penalty calculations are lower than in other jurisdictions (the US has a headline maximum of $100 million), others are higher or in line (the US only goes up to twice the accrued benefit, and in the EU fines have an overall cap of 10 per cent of annual turnover).

3.2.10 The national access regime

The national access regime (NAR) in Part IIIA was introduced following the Hilmer review. At the time much of Australia's infrastructure was publicly owned or recently privatised. There was considerable scope for making more efficient use of the infrastructure by facilitating access by third parties, thereby growing effective competition in related upstream and downstream infrastructure markets.

Today the environment is considerably different. Industry-specific infrastructure access regimes, many certified under the NAR, are now widespread, meaning the role of the national access regime to decide access determinations is mainly as a backstop for cases not covered elsewhere.

Furthermore, Australia faces a challenge to create incentives for private investment in infrastructure that can expand the productive capacity of the economy and grow national income. Yet the experience to date has revealed costs and risks associated with the NAR that can create a disincentive for long-term private investment. There is considerable regulatory risk for greenfields investment due to the possibility of a lengthy and costly declaration process under the NAR and to the imposition of access arrangements that can materially impact on return on investment.

The changing context within which the NAR should be evaluated was recognised by the then Productivity Commission Chair, Gary Banks, who said in 2012:

> The economic landscape within which these … regulatory arrangements now operate is very different from what it was when the NCP was conceived. As well as the implications of a marked shift from public to private provision of infrastructure services, the policy priority has tilted from the need to achieve efficient use of existing assets to the need for efficient investments in new infrastructure to accommodate burgeoning demand. (p. 1)

The Productivity Commission reviewed the national access regime in 2013. The report found that "it has not been possible to quantify the economic impacts of the regime or its effect on economic growth and productivity".[55] We agree with many of the commission's recommendations to improve the regime, for example that criterion (f) should be changed to positively require that declaration be in the public interest, and not simply that it is not contrary to the public interest.

However, the difficulties confronted by the commission in assessing the costs and benefits of the NAR and the considerable costs experienced by businesses with recent experience of the NAR, among other reasons, lead us to not support these recommendations in the report:

55.PC, *National Access Regime Inquiry Report*, 2014, p. 244.

- The ‘natural monopoly’ test should not replace the ‘private profitability test’ for deciding whether it is ‘uneconomical to duplicate another facility’ under criterion b
- The recommendation that the Act make clear ACCC powers to direct expansions should not lead to any enhanced powers to direct businesses to extend or expand a facility. The circumstances where a regulator should be able to force a business to alter its property should be absolutely exceptional.

The BCA also considers that there is substantial merit in the panel considering how best to promote the resolution of access issues before large and irreversible investment decisions are made, instead of imposing obligations post-investment. This is in keeping the Hilmer review, which said:

> ... [W]herever possible the likely obligations to provide access should be made clear before an investment is made, whether that be through licensing requirements of a new or the acquisition of an asset formerly owned by government. (p. 251)

The existing mechanisms to obtain regulatory certainty prior to developing a greenfields project (e.g. the ineligibility provisions) contain a number of drawbacks and are very rarely used. A number of BCA members are making more detailed submission on this issue.

More fundamentally, the BCA considers that there is an opportunity for the panel to give greater consideration to whether the existing NAR remains the optimum way to regulate private investment that will be required to fund Australia’s considerable infrastructure needs into the future. As others have noted Australia is the only country with a National Access Regime.

At the very least, we believe the review panel should investigate options to improve the operation of the National Access Regime to give clearer guidelines to potential investors and streamline the costly declaration process.

3.2.11 Sector-specific regulation and market studies

Given the broad-ranging scope of the current review, it is not appropriate to seek to replicate the sort of detailed sectoral review that has been undertaken to examine the particular issues for specific sectors.

However, the Commonwealth and state and territory governments should continue to address sector-specific concerns through judicious use of targeted market studies that focus on the public interest, rather than the interests of specific competitors.

Activity in key markets should continue to be monitored carefully under existing government and regulatory functions and powers, given the importance of these markets to Australian consumers and the broader economy. However, detailed market studies or reviews should only be initiated by the government where there is clear evidence of systemic problems or significant public concerns that need to be addressed; it is not appropriate for a regulator to have the general power to initiate its own market studies.

Such a power would risk undue interference in competitive markets in the absence of any clear problems, would impose unjustified costs and would encourage

'fishing expeditions' to circumvent appropriate limits on the regulator's investigative powers. In these circumstances the regulator should be required to make a case to the government that a review is necessary, and the government should decide on the most appropriate body to conduct any investigation or study. In this context it should be noted that the ACCC's role is to address anticompetitive conduct rather than to engage in market design or engineer pro-competitive outcomes: these are broader questions of micro-economic reform and are more appropriately undertaken by the government on advice from the Productivity Commission.

Where market studies are undertaken, it is important that they do not impose a disproportionate cost burden on industry participants in the absence of any clear issue or wrongdoing. Preference should be given to voluntary participation in market studies and industry participants should be able to determine the breadth and depth of information they provide. Further, to ensure procedural fairness these market studies should continue to deliver recommendations to the government that may be addressed by industry participants, rather than resulting in binding outcomes of any kind. There is currently nothing to stop the ACCC from undertaking its own market assessments on publicly available or voluntarily provided information; but providing it with even the potentially very costly and disruptive powers to issue mandatory investigative notices and compel testimony is not justified in the absence of a clear problem.

This is particularly the case in an economy like Australia's, which has had the benefit of many decades of microeconomic reform and effective competition law enforcement, and in which the effect of burdensome regulation and government intervention is emerging as a more pressing issue than entrenched market dysfunction. Market power studies granted to regulators in other jurisdictions should be considered in the light of the history and structure of industries and competition frameworks in those jurisdictions and are not necessarily relevant to Australia.

It is notable that when independent and rigorous reviews of key markets have been undertaken they have concluded that pro-competitive policy reforms are better targeted by dealing with any regulatory or other government imposed barriers to entry or reducing consumer switching costs specific to that sector. They have not identified competition concerns that are best addressed by changes to the general competition law.

In general, market studies such as those referred to the Productivity Commission in a wide range of sectors, to major standalone reviews such as the current Financial Sector Inquiry, and to the ACCC in the petrol and supermarket sectors, have rightly been focused on the public interest rather than any sectoral perspective, and have undertaken rigorous studies and adopted public processes.

To the extent that there is concern about competition in a particular key national market, and such a study is likely to lead to recommendations for policy reform, then market studies referred to the Productivity Commission will generally be the appropriate option. When key markets have been carefully scrutinised those markets have generally been found to be workably competitive. In particular:

- **2008 Grocery Inquiry:** The ACCC conducted a review into the competitiveness of the grocery industry and concluded that 'public debate overstates the structural problems within grocery retailing' and that "retail competition is workably competitive" (p. 67). Further, the ACCC concluded that "the positions of Coles and Woolworths [do] not represent a level which, of itself, requires market reform" (p. 49).
- **2007 Petrol Price Inquiry:** At the time, ACCC considered that competition had increased with the entry of the supermarket chains. More recently, in 2011, the ACCC reported that "there is evidence indicating competitive tension including the greater availability of Australian standard fuel in the Asia Pacific region; growth of independent importers; …and growth of independent retail chains." (p. xxi, 39).
- **Energy:** The AER in its annual *State of the Energy Market* report analyses the state of competition at the various functional levels in electricity and gas. Comparing the report released at the end of 2013 with the inaugural 2007 report shows that competition in gas and electricity retail and electricity generation/gas production has been increasing over time (AER, 2013).

Indeed, since the fuel and grocery inquiries were conducted in the mid 2000s, competition in these markets has increased, not decreased:

- **Groceries:** In the Metcash case, the Federal Court found that the level and intensity of retail competition in the grocery sector is 'extreme and is increasing'.[56] Further, the Productivity Commission in 2011 noted that 'barriers to entry for retail are not substantial" and that "the grocery sector is facing significant competition from new entrants with different business models, primarily ALDI and most recently Costco" (2011b). In this regard, the BCA notes that ALDI's growth rate is higher than either of the major supermarket chains. Since opening its first store in 2001, ALDI now has 340 stores on Australia's east coast and is now embarking on plans to open up to 110 stores in South Australia and Western Australia in the coming years (ALDI undated). Roy Morgan (2014) also reported that, as of December 2013, ALDI's customer base has quadrupled from eight years ago, and that it now accounts for 10.3 per cent of the grocery dollars spent.
- **Fuel**: Costco recently announced it is entering the Australian fuel retail market with Costco-branded service stations. It is reported that Costco's Brisbane service station officially opened operations mid-May 2014 at a price 15c a litre cheaper than nearby service stations (Gough & Snowden, 2014). Such pricing is likely to increase competition in the industry to the benefits of the consumer. Moreover, the role of independent imports has continued to grow, up more than fivefold accounting for about 26 per cent of total imports in 2012−13, compared with 5 per cent in 2007–08 (ACCC, 2013b).

Any concerns about sector-specific competition despite the above evidence should not be addressed through sector-specific changes to the general competition law,

[56] *Australian Competition and Consumer Commission v Metcash Trading Limited* [2011] FCA 967, [260].

but through broader sectoral reviews of all the accumulation of regulation that affects competition (see Chapter 2). That approach would be consistent with the principles that competition law should apply equally across the economy; should protect competition and not individual competitors; and should have long-term consumer welfare as its overriding goal.

3.2.12 Other matters raised in the issues paper

The issues paper examined a number of other areas that the BCA recognises may be important for some stakeholders, but which we have not provided detailed analysis.

Unfair and unconscionable conduct

The BCA considers that the unconscionable conduct provisions of the CCA work effectively in their current form.

However, the Commonwealth Government committed during the last election campaign to extending unfair contract terms to business to business transactions. The BCA has previously argued that the benefits of this additional regulation of business transactions has not been shown to outweigh the costs.

The Commonwealth Treasury is currently undertaking a consultation process on behalf of Consumer Affairs Australia and New Zealand, and this is the appropriate avenue for examining this issue in further detail.

Secondary boycotts

The secondary boycott provisions address an important objective but there are legitimate concerns that they may in some cases be overly difficult to prove, particularly cases associated with industrial action. The BCA supports any changes to law or procedure that are appropriate to ensure that the objectives of the provisions are met.

Codes of conduct

The code framework as currently provided in the CCA is adequate and does not need amendment. In establishing the content of industry codes, given that the code framework was intended to enable industry groups and affected groups to codify their practices in a transparent and accountable fashion, the views of those industry groups and affected groups ought to be given primacy, particularly in relation to the level of commercial flexibility to be retained between parties.

Recommendations

19. As a guiding principle, Australia's competition law must be consistent with international best practice. Consequently, it should:
    - have as a clear objective the promotion of long-term consumer welfare by protecting the competitive process rather than individual competitors
    - be aligned with the best elements of US and EU anti-trust laws, noting that Australian businesses operate in increasingly globalised markets
    - this will enhance Australia's competitiveness.

Enhancing the effectiveness of the general competition law

20. The Treasury, in consultation with business, competition law practitioners and the ACCC, should review the formal clearance mechanism, including the regulations, to remove unnecessary restrictions and requirements which have acted as a deterrent to its use.
21. The 'per se' prohibition against cartels and exclusionary provisions should be clarified to ensure that they apply only to horizontal arrangements between competitors, and the joint venture exemption should be extended to apply both to non-contractual arrangements and to joint ventures other than for the supply of goods or services.
22. The conduct prohibitions should be streamlined, and a public benefit defence adopted in the CCA, to reduce the reliance on costly and time-consuming administrative notifications and authorisations processes so as to improve the overall operation of the law.

National Access Regime under Part 3A

23. Improve the application of access regulation to greenfield infrastructure projects, for instance, through improved use of the ineligibility provisions or by agreeing any access arrangements upfront, before investments are made.
24. The panel should give consideration to whether the existing National Access Regime remains the optimum way to regulate private investment that will be required to fund Australia's considerable infrastructure needs into the future.
    - At the very least, the panel should investigate options to improve the operation of the National Access Regime to give clearer guidelines to potential investors and streamline the costly declaration process.

Removing parts of the law that do not contribute to stronger competition

25. The following sections of the CCA should be repealed:
    - the 2007–08 amendments to section 46, including the 'Birdsville' amendment
    - the price signalling provisions
    - the per se prohibitions on resale price maintenance and third line forcing
    - the prohibition in section 45 against exclusionary provisions defined in section 4D.

Avoiding changes that have not been proven to enhance competition

26. Some proposed changes risk harming vigorous competition and it has not been demonstrated that there is a clear net public benefit in:
    - introducing an 'effects' test into section 46 and removing the 'take advantage' principle
    - removing the related bodies corporate exemption from third line forcing
    - extending section 50 to further address creeping acquisitions or to impose market caps

- providing structural remedies (i.e. divestiture powers) beyond the context of a breach of the merger provisions
- providing a ‘cease and desist’ power for the ACCC
- increasing maximum penalties
- changing the private profitability test for declaration under Part IIIA of the CCA.

4. REGULATORY INSTITUTIONS

Good regulation that is well administered can be pro-competitive. But regulation that is administered in a way that is uncertain, slow, or unnecessarily complex and expensive, can dull competition in markets. While all of Australia's regulators can have an impact on competition, the focus of this chapter is largely on those which can have the greatest impact across the economy.

While the BCA does agree that in many cases Australia's regulators perform well by international standards, there are opportunities for improvement, particularly in terms of lifting governance and accountability to improve incentives for regulatory efficiency. Recent work undertaken by the BCA found that while the powers and scope of regulators have grown in recent years, there are weaknesses in the current performance and accountability framework for regulators (BCA, 2013c).

4.1 Roles and responsibilities

Any assessment of whether regulatory institutions are meeting the needs of the modern economy must first ask whether the structure of Australia's core competition-related regulators is best placed to deliver the required outcomes with markets which are changing in response to global forces.

Australia has 11 core competition-related regulators, including the ACCC, the AER, the National Competition Council (NCC), the Australian Competition Tribunal, and the eight state and territory economic regulators.

The OECD has noted that the ACCC is generally regarded as an efficient and effective regulator by stakeholders and internationally (2010, p. 29). The BCA is not aware of any specific assessment of the performance of Australia's pricing and access regulatory functions.

Several jurisdictions combine the competition and consumer protection regulatory functions in one body (Exhibit 13), Australia and New Zealand are unusual in having all three core competition regulatory functions across almost all industries (except those regulated by state counterparts) in one body, in Australia's case the ACCC:

- competition – mergers, cartels and other activities that can affect competition
- consumer protection and product safety
- pricing and access regulation of monopoly infrastructure – in the ACCC and the AER.

There are benefits and costs of this structure, and potential transitional issues if any changes were made.

There will inevitably be tensions between some businesses and the regulatory agencies charged with regulating competition and/or prices and access. In Australia, the concerns expressed by BCA members in relation to the ACCC tend to be focused on:

- The potential for the combination of what can be adversarial pricing and access interactions to skew decision making on important competition and consumer protection matters.
- Concerns that mergers and investigations are not sufficiently timely.
- Insufficient recognition of the high costs on business (and thus ultimately their customers) of many requests for the provision of detailed information for mergers and investigations, and a focus on targeting those requests to minimise those costs on the parties and other affected businesses.
- Some compliance priorities that do not seem to be risk-based, in that they are not explicitly linked to evidence of real harm to long-term consumer welfare.
- Concerns that the media is being actively used to criticise firms before the outcome of a prosecution is known.[57]

Some of these concerns also arise in discussions about other regulators across the economy.

With respect to access and pricing regulators, there are structural solutions, such as separating out the various pricing and access responsibilities that the ACCC currently supports, including those of the AER, which are discussed below.

[57] The Dawson review recommended the ACCC adopt a media code of conduct which included as one of its principles that 'with the object of preserving procedural fairness, commentary on the commencement of court proceedings by the ACCC should only be by way of a formal media release confined to stating the facts (2003, p. 190)'.

Exhibit 13: Competition regulation enforcement internationally

USA

- Competition – both the Federal Trade Commission and Antitrust Division of the Department of Justice
- Consumer protection – both national and state level
- Product safety – United States Consumer Product Safety Commission
- Pricing and access regulation – industry-specific regulators at both the national and state levels

UK

- Competition and consumer protection – Markets and Monopoly Commission and local governments
- Pricing and access regulation – industry-specific regulators at the national level

Ireland

- Competition and consumer functions are planned to be merged
- Pricing and access regulation – industry-specific regulators at the national level

Canada

- Competition – Competition Bureau
- Consumer protection – both the national and provincial levels
- Product safety – national level by Health Canada
- Pricing and access regulation – industry specific regulators at the national and provincial levels

New Zealand

- Competition, consumer and pricing and access – all within the Commerce Commission.

Source: BCA analysis

The establishment of independent regulators, and the provision of access, was a significant improvement on what had gone before, but nearly 20 years later Australia now has experience with operating eight separate independent state and territory regulators of prices and access,[58] in addition to the AER (which covers electricity and gas networks), and the ACCC's regulation of telecommunications, water and pricing oversight of airports. Separately, the National Competition

[58] State and territory regulators cover sectors where infrastructure operators have market power such as ports, rail, and water, and other areas still subject to price regulation, including taxis fares and tow truck charges, and including government charges such as public transport fares and local government rates.

Council makes access declarations and certifies state and territory access regimes.[59]

Having 11 separate agencies administering regulation for a country of 23 million people has the potential to lead to a number of problems:

- The risk of inconsistent approaches to similar issues across jurisdictions and sectors, which adds to the compliance costs for businesses operating in multiple jurisdictions, and for all affected businesses creates greater uncertainty as to how particular issues might be addressed.
- Limited capacity, knowledge and expertise in any one jurisdiction of specific issues and industries. While the regulators can buy in expertise from independent consultants, their small size means they have less in-house expertise to be smart buyers of this advice.
- Difficulties managing the peaks and troughs of their workload. With regulatory cycles that can and should be longer term (typically five years or more) in any one jurisdiction, it can be difficult to retain current capacity and expertise, or skill up quickly when a new issue emerges, such as an access dispute.

On the other hand, it could be argued that the current model provides scope for competitive federalism, with some regulators adopting different approaches to how they administer regulation. However, under the current arrangements it is hard to see how this is driving better administration of the regulation of physical infrastructure.

The current model of the ACCC (and support for the AER and NCC) also combines the regulation of businesses with substantial market power, such as energy and water networks, rail networks, and ports, and fixed line telecommunications (which by its nature tends to be an adversarial role and one where the regulator is involved in designing a market) with the competition and consumer regulator. The BCA believes this leads to the potential for the latter functions to be overly influenced by the perspectives and day-to-day challenges of the former role.

In addition, while the energy markets have highlighted the benefits of the separation of the rule maker (the Australian Energy Markets Commission) from the administration and enforcement function (the Australian Energy Regulator), this model has not been able to be applied more broadly.

While the functions of consumer protection and enforcing the general competition provisions of the CCA are broadly complementary, as reflected in the number of regulators worldwide whose responsibilities address both of these functions, the addition of responsibility for access and pricing regulation in the ACCC has the potential for actual or perceived conflicts between the ACCC's rule-making and enforcement roles.

One advantage of the breadth of the ACCC's functions may be that its important rule-making and market-structuring roles are less susceptible to regulatory capture

[59] In addition, the AEMC makes the energy rules and provides advice to ministers on market development.

by the industries it works with most intensively. However, this risk would be mitigated by a separate pricing and access regulator that operated across a range of industries under a range of state and territory regimes.

A national (rather than Commonwealth) regulator could bring together responsibilities for:

- pricing and access regulation, and administration and enforcement of market rules for electricity, gas, telecommunications, ports, water and rail, currently undertaken by the ACCC, AER and state and territory regulators. It would also be responsible for any price monitoring roles of the ACCC, including major airports. Ideally the regulations it would oversee would be nationally consistent, but administered having regard to the different circumstances in each state and territory. However, where there were benefits of competitive federalism through the willingness of different states to try alternative, and potentially more competitive approaches, it would be feasible for the regulator to administer regulation that varied across jurisdictions.
- other pricing functions currently undertaken by state regulators on reference from a state minister, such as taxis, tow trucks, and public transport fares.

This could be a centre of excellence and capability around access and pricing, and enhance the consistency and application of these principles nationally.

A national rule making body could:

- Be the rule maker for Australian electricity and gas markets, and other markets where governments have agreed to uniform rules, such as water.
- Provide market development advice to governments, including working with states and territories to develop nationally consistent access regimes where state regimes are currently in place.

The benefits and costs of such a restructuring are worthy of examination, and could build on the lessons of the energy sector, which has a structure that separates the market rules and policy advice function from the function of administering and enforcing the rules. In addition, the new national regulator would be able to more effectively benchmark the performance of all the participants in each sector, rather than the subset which each state and territory regulator currently oversees. However, there would be substantial transitional costs of such a model, and the benefits would need to be rigorously assessed.

4.2 Regulator performance

The performance and accountability framework for Australia's regulators that affect competition within the economy should be fundamentally strengthened to more closely align with best practice. As the Banks taskforce suggested "... the actions and attitudes of regulators, like those of business, are shaped by the incentives they face as well as by the requirements placed on them" (Banks, 2009, p. 159).

Business concerns are borne out by surveys of experience dealing with regulators. The March 2014 *ACCI National Red Tape Survey* found that 71 per cent of respondents considered regulation was poorly explained by regulators and 60 per

cent thought it was inconsistently enforced. When asked about different ways of finding out useful information, 30 per cent of respondents disagreed that making face-to-face inquiries provided useful information, while 37 per cent had the same view about telephoning the department or agency. The same survey found dealing with local government 'very' or 'extremely' complicated.

In 2012, the BCA set out standards that highlighted the importance of regulation being administered by regulators in the most efficient manner possible to facilitate economic progress (Exhibit 14). The BCA's follow-up report outlined the benefits of establishing a new performance and accountability code, backed by legislation (BCA, 2013c). This is consistent with the UK Government's approach of implementing a regulator's code that includes a statutory requirement that all regulators, "should carry out their activities in a way that supports those they regulate to comply and grow. (BRDO, 2014, p. 3)

System-wide improvements in regulation-making processes can lead to improved regulator performance. The Commonwealth, state and territory governments have implemented Regulatory Impact Statement processes, and announced regulation reduction strategies, with the aim of reducing the amount of regulation and improving the quality of what remains. When done well, these measures can make an important contribution to a more efficient regulatory framework (see Chapter 2), but they only address half the challenge and must be accompanied by improvements in the way in which regulation is administered and enforced.

Throughout section 4.2 below the ACCC's informal merger clearance process is used a case study for illustrating some of the broader concerns raised by business about regulator performance. This process was chosen because performance data is more readily available compared to other regulatory processes overseen by regulators in Australia.

4.2.1 Expectations and oversight

The best way to drive greater accountability for each regulators' contribution to prosperity is to have them operating within a new legislative framework that provides incentives to balance rigorous enforcement with efficiency and facilitating economic progress while continually improving their processes.

Clear Statements of Expectations from ministers supplement the higher-level guidance provided by each regulator's legislative framework and promote transparency through their publication and annual reporting.

The Australian Government has committed to each minister issuing charter letters to the chairs and chief executives of Commonwealth regulatory agencies outlining the minister's broad policy intent and expectations with respect to their policy and administrative powers (Coalition, 2013). The BCA endorses this approach. These appear to be similar to the Statements of Expectations that were issued by Howard Government ministers, and it will be important that these statements or charter letters are made public to improve transparency and accountability.

The Victorian Government has implemented a similar approach in issuing five of its largest regulators with 'Reducing Red Tape Statements of Expectations' to clarify their responsibilities to reduce regulatory burden. In 2014, the Victorian

Government started a process to put broader statements of expectations covering all aspects of performance and accountability in place for all 50 Victorian regulators of business, with reporting of progress in their annual reports (Victorian Government, 2013 & 2014).

Exhibit 14: BCA standards for regulator performance

In 2012, the BCA set out standards that sought to highlight the importance of regulation being administered by regulators in the most efficient manner possible to facilitate economic progress. The standards were:

- The government's expectations of a regulator are transparent, and are clearly within the scope of the regulator's powers.
- There is a clear separation of roles between policymakers and regulators.
- Regulators follow a risk-based approach to enforcement and compliance activities.
- Regulatory decisions are timely.
- Regulators are continuously streamlining their processes.
- Regulators adopt a client-focused approach to regulated parties.
- Regulatory decisions are fair and contestable.
- Regulators are subject to regular and meaningful performance assessment and reporting.

Source: BCA, 2012; BCA, 2013b

A critical aspect of enhancing accountability is improving the performance oversight framework. Independent regulators are accountable to parliament via the minister responsible for their legislation. This accountability must ensure that their overall efficiency and effectiveness is subject to appropriate scrutiny, without undermining the independence of their decision making on specific matters.

For example, governments around the world are encouraging their regulators to be more risk-based in their administration and enforcement of regulation. Done well, this minimises the cost imposed on compliant businesses and others being regulated, while directing resources to those who impose the highest costs on society. Requiring regulators to publicly demonstrate that they are adopting this approach does not involve second-guessing their choices, only that the general approach is subject to scrutiny.

The BCA examined the public information about the compliance and enforcement priorities of several of Australia's largest regulators in 2013. It found that the Australian Taxation Office (ATO) and the Australian Prudential Regulation Authority (APRA) had well-defined risk-based approaches (although in the latter case, some argue it may be overly risk-averse). In contrast, it is difficult to confirm how ACCC and the Australian Securities and Investments Commission (ASIC) applied a risk-based approach to compliance and enforcement (BCA, 2013c). More transparent reporting that outlines how enforcement priorities are linked to

evidence of real consumer detriment would seem critical for regulators with such high public profiles.

The Commonwealth Government is currently developing a whole-of-government regulator performance framework drawing on advice it has sought from the Productivity Commission (2014d). The intention is that this framework should allow for a comprehensive assessment of regulator interaction with business and the broader community, and be applicable to all Commonwealth regulators.

4.2.2 Timeliness

Delays in regulatory approvals can have substantial competitive effects by delaying and/or raising the costs of entry and of launching new products or business models, as outlined in Chapter 2. These delays will often be a function of both the design of the regulation and of how the regulator administers the regulation.

Delays in finalising investigations can also have impacts on competition if, during the course of the investigation, it remains unclear whether particular conduct is legally permitted or not.

BCA members have highlighted issues their businesses have faced in working with a wide range of Commonwealth, state and local government regulators. They have noted that the time to get approvals, whether it is for a major new plant, or an innovative product, can be a major barrier to new investments or innovation. Members have also commented that the uncertainty about when and whether approval will be granted can be a substantial disincentive, with businesses sometimes making decisions not to proceed with an investment or transaction because of the uncertainty and risks. Business leaders have also noted that the complexity of compliance can also have impacts on whether a business enters a new market and competes.

Currently there is not a process to promote continuous streamlining of regulators' processes. While this is a general challenge for all regulators that issue approvals, it is most acute in relation to the ACCC's informal merger review process.

Case study in timeliness: improving the ACCC's informal merger review process

The administration of section 50 of the CCA, which prohibits anti-competitive acquisitions (including mergers), is one of the most active areas of ACCC activity and one of the most important for the competitive performance of the Australian economy. In general, mergers and acquisitions provide strong benefits to consumers as a critical element in the efficient functioning of the economy. In particular, mergers perform the important functions of:

- enabling firms to achieve efficiencies, such as economies of scale or scope, and diversify risk across a range of activities
- allowing productive capital to move between businesses

- enabling existing firms to reposition their businesses in response to dynamic market changes, including business innovation through the application of expertise and core assets to new markets, or restructuring through acquisition
- providing a mechanism for owners to exit the business, which can include: entrepreneurial start-up investors where the ability to sell a successful start-up business to an existing firm is often the key incentive for the start-up in the first place; governments through privatisation to exit from a competitive or potentially competitive market; or private businesses in changing markets in which existing businesses can no longer provide a sustainable return on capital
- providing a mechanism to replace the managers of underperforming firms.

In the overwhelming majority of mergers, sufficient competitive tension remains after the merger to ensure that consumers and suppliers are at least no worse off. Mergers are also a critical aspect of competitive capital markets. The market for corporate control puts pressure on managers to continually improve their businesses lest they be taken over by another firm. Mergers and acquisitions also create opportunities for entrepreneurs to sell their businesses to others that are better placed to grow it to the next stage.

It is therefore essential that the merger clearance processes:

- are prudent and expeditious
- are highly conscious of – and do not impose – unnecessary costs and delay on merger parties
- give full weight to the dynamic and competitive nature of markets over time
- are not based on presumptive positions that may impede the efficient transformation of incumbent businesses in dynamic and globally competitive markets.

There is a very real risk to growth and productivity if merger review processes impede desirable mergers due to the cost, delay or unduly conservative competition assessments. Equally, an overly permissive merger process could harm competition, so it is recognised that careful judgement is required, and thus it is essential that there an embedded process of continuous improvement of this activity.

There are currently three approval mechanisms for mergers under section 50: the longstanding informal clearance process, and two other mechanisms introduced following the Dawson review, namely the formal clearance process (not used to date) and direct application to the Tribunal for authorisation (one application withdrawn and one current). The discussion in this chapter focuses on the informal process, which accounts for the vast majority of merger activity.

The BCA member experience with the ACCC informal clearance process suggests there are four areas where there are opportunities for improvement: more timely decisions; reduced investigatory burden; greater transparency of material relied on by the ACCC; and strengthening the approach to competition assessments and market definition. The particular areas for improvement are discussed below, with specific recommendations. Moreover, these issues are highly relevant to any

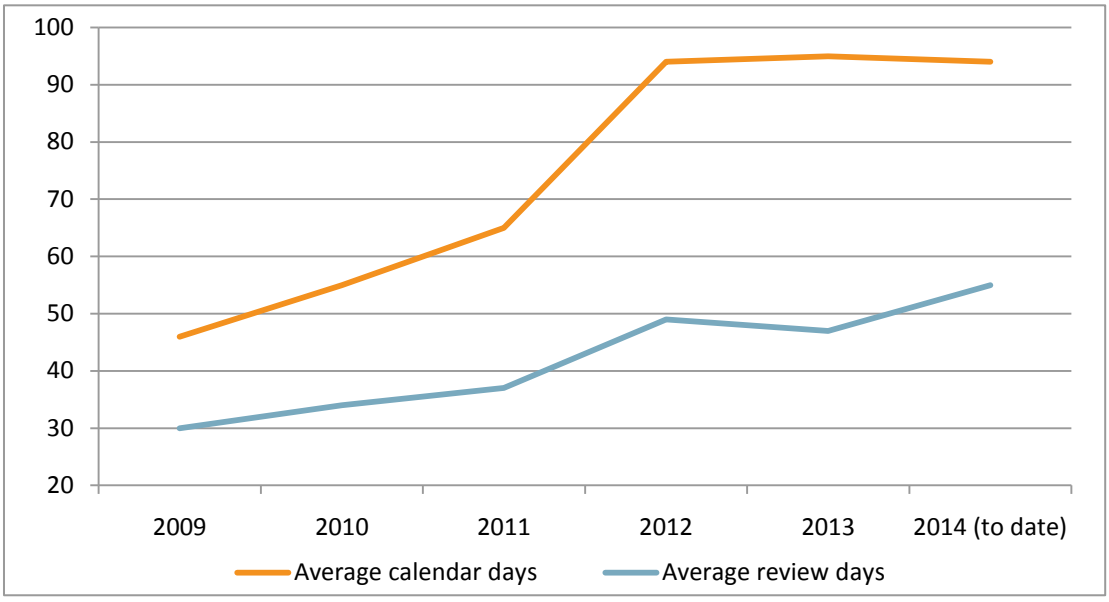
regulatory process within the competition policy framework, and the lessons and recommendations derived from the following analysis could usefully be generalised and applied to a wide range of processes.

The informal merger review process, in the main, allows for mergers, particularly those which are unlikely to raise competition issues, to be dealt with quickly. However, recent experience (as reflected in merger clearance statistics) suggests that the process is taking significantly longer, delaying decisions and imposing significant commercial costs.

Based on a review of the transactions on the public register from 2009 to 2014, the ACCC's average review days (as per the ACCC's public timeline on the mergers register, which does not include the days when the ACCC has suspended the timeline) have increased from 30 in 2009 to 55 in 2014. This increase is reflected in the differences between the current and previous editions of the ACCC's Process Guidelines. In the 2006 Merger Review Process Guidelines, the ACCC indicated that the assessment period for mergers was 2 to 8 weeks (up until the decision or the release of the Statement of Issues which would take the review to the second stage), while in the current Process Guidelines (ACCC, 2013a), the assessment period for the first stage is now 8 to 12 weeks (including 2 weeks of pre-assessment).

In terms of the average elapsed calendar days between the start and the end of the ACCC's review (which is a more relevant metric from a commercial transaction perspective), the percentage increase over the past five years is even greater, with the average number of calendar days having more than doubled since 2009, from 46 to 94 days (or 7 to 13.5 weeks) (Figure 5).

Figure 5: Time taken for ACCC to review mergers over time, 2009–2014 (YTD)



Source: ACCC Merger register. Note: 'Review days' exclude days on which the ACCC has suspended the review to await information from merger parties or coordinate with overseas agencies.

The drivers behind this time increase may be varied. One reason advanced by the ACCC is that it is required to adopt a more rigorous assessment process following the *Metcash* decision. However, it is unclear why the outcome in that case should warrant a wide ranging change in the clearance process resulting in such a marked increase in average review periods.

Another possible reason is the general drop in merger and acquisition activity over the past few years, which may be encouraging the ACCC to review each transaction in more detail, resulting in an increase in the average time per review.

The ACCC has introduced a pre-assessment phase to fast-track the review process for more straightforward matters. The pre-assessment stage has the potential to be of benefit in some cases. However, while this process is in its early stages, it appears it has not led to a reduction in review periods. Further, it may reduce the review period for some straightforward matters (which may have had a shortened review under the previous arrangements in any event), but appears to be lengthening the review period for other matters. In particular, once the pre-assessment stage is completed, the public review stage is undertaken by a new investigations team which must re-review the same information before proceeding, resulting in an unnecessary additional step. Further, it appears that the experience with the pre-assessment process is that it often takes longer than the two weeks estimated in the Process Guidelines (ACCC, 2013a), as shown in Table 2.

Table 2: Time taken in merger review, average calendar days

Matter type	Pre assessed days	Review days	Total days
Pre-assessment only	18	N/A	18
Pre-assessment and then public review	54	105	159

Source: ACCC Merger register; confidential data from BCA members. Note: for 'pre-assessment only', the data were calculated for six matters that were only considered in the pre-assessment stage. For 'pre-assessment and then public review', the data were calculated for two matters that were not able to be pre-assessed and were then publicly reviewed.

In general, it is acknowledged that the ACCC is responsive over time to concerns in relation to its administrative clearance process and will adapt it following feedback.

Nonetheless, best practice regulation would involve a form of annual process performance review under which where transparent data as to the ACCC clearance review time periods could be examined and opportunities to improve the process could be identified. This process would best be conducted by an independent peer review.

The ACCC could also consider whether it is appropriate to have an automatic pre-assessment stage for all matters, and to consider the benefits of that process as

against the former process of a very quick preliminary ACCC review "on the papers" within the overall informal merger review timeline. Alternatively, the ACCC could allow parties to request the pre-assessment stage be bypassed, and the merger proceed straight to the public review stage, in the interests of time. Where parties considered that there was a reasonable chance of gaining approval at the pre-assessment stage, then this option would still be available.

4.2.3 Use of compulsory investigatory notices

The ACCC has the power to require the production of information and documents under section 155 of the CCA. It uses this power to investigate a range of conduct, including in informal merger reviews. The use of this power has increased significantly over the past financial year, rising to 358 notices from 175 in 2011–12 (ACCC & AER, 2012 & 2013).

Case study in use of CINs: improving the ACCC's informal merger review process

There is no separate data as to the use of notices for merger reviews. However, BCA member experience suggests that it is becoming more common practice for the ACCC to issue compulsory notices to each of the merger parties and also third party competitors and even key customers in merger reviews. BCA member experience suggests that these notices are being framed more broadly than in previous years, and becoming more time-consuming and costly.

The volume of material required to be produced and the cost of complying with these notices is substantial. Table 3 below summarises the time taken to respond to section 155(1)(b) Notices (compulsory document requests), the average volumes of documents that are being searched across, reviewed and ultimately produced and the average legal costs for merger parties as distinct from third parties in recent years. This data has been provided by BCA members and is aggregated and made anonymous.

Table 3: Time and cost of responding to compulsory investigatory notices requesting documents (2012–13)

s155(1)(b) Notice addressee	Average time given to respond to Notice	Average no. of docs searched	Average no. of docs reviewed	Average no. of docs produced	Average legal cost associated with response
Merger party	30 days	2 million	39,000	2100	$200,000
Third party (competitor or customer)	21 days	1.3 million	12,000	1250	$70,000

Source: confidential data from sample of BCA members. Note: The data for merger parties were calculated for 13 matters in which merger parties received a s155(1)(b) Notice. The data for third parties were calculated for four matters in which third parties received a s155(1)(b) Notice.

The current arrangements do not provide any oversight of the use of the power to require the production of documents and information. Oversight is needed to ensure the use of the power has regard for the cost of that production and the delay of production and review, as against the benefits in terms of relevance and utility of the material obtained. It is unclear whether the ACCC has taken any steps to inform itself of the costs of the production of such material. There is currently no disclosure of any internal process of reviewing the use of such notices and their overall utility.

Moreover, the ACCC currently has a practice of insisting on full production of a document notwithstanding that only a small portion of a document may contain relevant material. For example, the ACCC may request the production of management reports which may cover the entire scope of a company's operations, whereas its inquiry may relate to only one aspect of that business, and routine business reporting on matters such as human resources may have no relevance to the ACCC inquiry.

Insisting on formal compliance through full production of non-relevant parts of documents imposes a number of costs, including the cost of reviewing non-relevant parts of documents for privilege and other issues, and the simple costs of management and review of voluminous non-relevant material. A general principle that businesses should be able to keep confidential and not be required to produce non-relevant parts of documents is appropriate. This is routinely accepted in voluntary production to the ACCC and in court discovery and subpoena processes.

While it is recognised that such powers are an important part of the ACCC's investigatory tool set for merger reviews, the powers to demand information should be used judiciously. Given the costs imposed by these processes, there would be benefit in requiring that an annual benchmark review of ACCC clearance processes include review of its use of s155 notices, including a review of the costs and utility of production. Such a review could aim to develop protocols that ensure in the future that the disclosure of non-relevant confidential business records is not be required as part of the ACCC investigatory process. Ultimately, this should lead to the tightening up of the ACCC's internal processes of preparing s155 notices, and discussions with recipients.

Independent annual reviews of the actual processes of a sample of mergers could consider the drivers underlying the increase in time taken for the ACCC to assess mergers, as well as the increased use of compulsory information powers, both of which impose significant time and cost burdens on parties.

4.2.4 Transparency

Australia's complex and fragmented regulatory system can make it difficult for businesses – large and small – to understand what they must do to comply. As the Productivity Commission's report on *Regulator Engagement with Small Business* noted*:*

> Effective communication by regulators is essential for achieving good regulatory outcomes. Put simply, it is no good having well-designed regulatory regimes if the

> businesses that are affected are either unaware of regulatory requirements or face substantial barriers in accessing or understanding information about them. (2013c, p. 142)

Improving the clarity of regulatory requirements, particularly when these requirements are expressed in terms of the outcomes that must be achieved for compliance, would allow firms to develop innovative competitive solutions to meet their customer's needs.

Clearer communication on websites, and through publications and other means, can also reduce the costs of entry and ongoing compliance costs.

As Christine Varney, former Assistant Attorney-General of the United States Department of Justice's Antitrust Division has identified, transparency is vital to fair process:

> Regardless of the substantive outcome of a government investigation, it is important that parties involved know that the process used to reach that outcome was fair. The two concerns – substance and process – go hand in hand. Complaints about process lead to concern that substantive results are flawed, whereas a fair, predictable, and transparent process bolsters the legitimacy of the substantive outcome. Both are important. (2009)

Case study in transparency: improving the ACCC's informal merger review process

Transparency presents a particular issue in the informal merger review process in terms of access to the merger parties of the information and analysis on which the ACCC makes potentially contentious decisions which are not supported by either the merger parties or potentially by a third party. In such contentious cases, there are two issues.

First, because staff papers that inform the decision-making process are not disclosed to the parties in advance of contentious decisions, there is currently a very real risk that information and analysis from third parties may be unreliable or that information and data provided by merger parties is obscured. When ACCC Commissioners make such decisions on this untested material, there is necessarily an inherent risk that the decision itself will be unreliable.

Second, the lack of information about how the ACCC makes these informal decisions does not build understanding and confidence in the practical application by the ACCC of its published guidelines and processes. Allowing the merger parties to access the record on which the ACCC decision is based would be consistent with best practice, for example, by the European Commission and the United Kingdom's Competition Commission (Williams, 2014).

The ACCC has recognised the later consideration in the past and has developed some informal practices, for example through the use of transparency letters and the Statement of Issues. However, these procedures do not address the fundamental problem that merger parties do not have access to, and an opportunity to respond to, the record before the ACCC Commissioners when they make contentious decisions that can have major commercial impacts.

Where there are issues of confidentiality, it should be possible for the ACCC to disclose only some information on an external counsel and experts-only basis.

Any disclosure regime, particularly prior to a decision, needs to be mindful of the potential for such a process to create further delays. Consequently, any disclosure pre-decision should be limited to those cases where the recommended approach is likely to be contentious, either with the merger parties or an affected third party.

A decision made under the informal processes not to approve a merger or acquisition can have substantial commercial consequence, and yet given the dynamic nature of markets and the costs of litigation, it may not be viable to contest such a decision. For this reason, there seems to be a strong case to examine the potential for the ACCC to establish an internal review process relating to these decisions. The aim of this process would be to strengthen the existing processes, while avoiding any risk of compromising the ACCC's independence in these matters.

One option would be to allow merger parties to seek an internal review of the ACCC's decision by a panel of Associate Commissioners with expertise in competition law and economics (but who are not otherwise involved in ACCC business). The merger parties could make oral submissions to the panel based 'on the papers'; that is, on the material that had been submitted by them and by third parties in the ACCC review process. The Associate Commissioners could be asked to either: endorse the original decision; recommend that the original decision makers review their decision based on a statement of reasons from the review panel, or on additional information that the panel may recommend be sought. Alternatively, the ACCC could allow this panel of Associate Commissioners to overturn the original decision, and make a new decision, on delegation from the ACCC.

While we consider that such a review panel process should be actively considered, further work would be required to establish its parameters and processes, to enable its costs and benefits to be more fully assessed.

4.2.5 Use of the media

Engaging with the media is one way in which regulators promote understanding of what is acceptable conduct, thus encouraging compliance. It can also prompt complainants to come forward with evidence of non-compliance. Many regulators issue media releases at the conclusion of court proceedings, and engage in proactive media strategies to inform the community.

The Dawson review recognised that in the case of general competition regulation it was valuable and appropriate for the ACCC to use the media in many circumstances, particularly in educating and informing businesses and consumers about their rights and obligations under the legislation. However, in the case of ongoing investigations or legal proceedings, the review was concerned that the ACCC should ensure that its use of the media did not interfere with due process:

> It is the responsibility of the ACCC to ensure that its provision of information to the media is consistent with due process and that there is confidence in the way in

> which it conducts itself. This extends beyond information supplied through formal printed media releases and includes informal commentary. (p. 183)

The risks involved in regulators' use of the media have been outlined by courts and tribunals in Australia, notably by the Trade Practices Tribunal in *Eva v Southern Motors Box Hill*:[60]

> [A]dverse publicity initiated by the prosecuting authority itself requires special consideration. If the matter is publicised ahead of the trial and widely and in terms likely to induce public censure of the parties concerned and those parties are in day to day business relationships with the public, then there is obvious danger of injury to the lawful business of the parties which from a practical point of view may have the effect of effectuating a cumulative punishment.

It is widely recognised that prosecutors are held to a particular standard in ensuring due process and procedural fairness, and are charged with serving justice rather than securing a conviction.[61] Even where a regulator pursues a civil penalty against a corporation, there is a real risk of reputational and financial harm from adverse publicity that interferes with due process.[62]

The review accordingly recommended that a media code of conduct should be developed, in consultation with interested parties, based on the following principles:

- The public interest is served by the ACCC disseminating information about the aims of the Act and the ACCC's activities in encouraging and enforcing compliance with it. This extends to information about proceedings instituted by it, but an objective and balanced approach is necessary to ensure fairness to individual parties.
- The code should cover all formal and informal comment by ACCC representatives.
- While it may be necessary for the ACCC to confirm or deny the existence of an investigation in exceptional circumstances, the ACCC should decline to comment on investigations.
- With the object of preserving procedural fairness, commentary on the commencement of court proceedings by the ACCC should only be by way of a formal media release confined to stating the facts.
- Reporting the outcome of court proceedings should be accurate, balanced and consistent with the sole objective of ensuring public understanding of the court's decision.

The review noted that these principles could be considered for inclusion in the Legal Services Directions issued by the Attorney-General relating to

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60 (1977) 15 ALR 428 at 437. See also *Cassidy vs Medical Benefits Fund of Australia* (No. 2) [2002] FCA 1097 at 94; *Electricity Supply Association of Australia Ltd v ACCC* [2001] 189 ALR 109 at 143.

61 *Berger v US* (1935) 295 US 78 at 88.

62 See K. Yeung, 'Is the Use of Informal Adverse Publicity a Legitimate Regulatory Compliance Technique?' Paper presented to the Australian Institute of Criminology Conference, Current Issues in Regulation: Enforcement and Compliance, Melbourne, 3 September 2002.

Commonwealth Legal Services, which include the Model Litigant obligations. To date, these principles have not been developed into any public code or guidance.

Codifying these principles for all regulators would make clear that the position of a regulator in an investigation or enforcement action is similar to that of the Crown in a prosecution case, and carries similar obligations to due process and procedural fairness. This standard is already applied under the Australian Government Investigation Standards (HOCOLEA, 2011)[63] but more guidance could be given as to its application. For example, the NSW Barristers' Rules adopted by the Office of the Director of Public Prosecutions provide that unsolicited media questions may be answered where:[64]

(i) the answers are limited to information as to the identity of the parties or of any witness already called, the nature of the issues in the case, the nature of the orders made or judgment given including any reasons given by the court;

(ii) the answers are accurate and uncoloured by comment or unnecessary description; and

(iii) the answers do not appear to express the barrister's own opinions on any matters relevant to the case.

Similar principles are enshrined in the local rules of US District Courts, which prohibit disclosure to the media of any information that has a substantial likelihood of interfering with a fair trial or otherwise prejudicing the due administration of justice, and in particular:

> ... with respect to an investigation, the government's disclosure of information is limited to confirming its existence and general scope, gaining the public's assistance in catching a suspect, or warning the public of any dangers. In a prosecution, the government may only disclose information that confirms the particulars surrounding the suspect's arrest, the identity of the investigative agency, the length of the investigation, the nature of any items seized, the nature of the charges, and the scheduling of the case in court. (Vinegrad, 1999, p. 237)

US Department of Justice policy also provides that any press release "announcing the arrest or indictment of any defendant contain the express caution that the charges are merely accusations and that the defendant is presumed innocent unless and until proven guilty."(Vinegrad, 1999, p. 237)

The BCA considers that the principles identified by the Dawson review are relevant and appropriate to any regulator's use of the media, and should be generalised and developed into a code that applies to all regulators of business. The contents of this code should also be incorporated in the Model Litigant Obligations of the Legal Services Directions 2005 (OPC, 2012) and the Australian Government Investigation Standards (HOCOLEA, 2011), and any state and territory equivalent guidance.

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63 Section 1.10 provides that "information released to the media should not prejudice a person's right to a fair hearing or the legal process".

64 Bar Rule 59 of the NSW Barristers' Rules, adopted by Guideline 32 of the NSW Office of the Director of Public Prosecutions, Prosecution Guidelines (2007).

4.2.6 Clarifying policy roles

As discussed in Chapter 3, the Commonwealth and state and territory governments should continue to address sector-specific concerns through judicious use of targeted market studies that focus on the public interest, rather than the interests of specific competitors.

However, it is not appropriate for a regulator to have the general power to initiate its own market studies. Such a power would risk undue interference in competitive markets in the absence of any clear problems, would impose unjustified costs and would encourage 'fishing expeditions' to circumvent appropriate limits on the regulator's investigative powers. In these circumstances the regulator should be required to make a case to the government that a review is necessary, and the government should decide on the most appropriate body to conduct any investigation or study.

Recommendations

Roles and responsibilities

27. The Competition Policy Review should assess whether there is merit in some consolidation of pricing and access regulators, including related functions from the ACCC, Australian Energy Regulator and state and territory regulators.

Clearer accountabilities

28. All governments should implement a new performance and accountability code for all regulators in omnibus legislation. Such legislation should include provision for:
    - A statutory objective applying to all non-economic regulators to promote economic progress in the discharge of their various functions.
    - A balanced performance reporting framework around regulator performance that would assess not only the enforcement and compliance activities of regulators but the extent to which these are undertaken efficiently, with a particular focus on whether their practices unnecessarily hinder competition.
    - Regulators to prepare annual public 'Statements of Intent' that outline the basis for measuring the success of the regulator, in agreement with the portfolio.
    - Regulators to establish public targets on streamlining their processes to reduce regulatory burden and reduce barriers to competition (including through measurable reductions in delays) each year.
    - Regulators to document, regularly update and adhere to a risk-based approach to compliance and enforcement activities.
    - Charter letters from ministers to the chairs and chief executives of regulatory agencies should be made public.
    - Regulators should publish standard timeframes for decision making and explain where performance not been met.

Improving performance

29. The ACCC's informal merger clearance processes should be improved, with an examination of the merits of:
    - Implementing an annual independent benchmark review of ACCC merger clearance processes. By focusing on process improvements, it would seek to identify opportunities to enhance timeliness and develop ways to better target the use of investigatory notices, but would not revisit the merits of the substantive decisions made by the independent regulator.
    - Revising the merger process guidelines to adopt a practice of transparent disclosure to the merger parties of the record on which the ACCC makes its informal clearance decisions, subject to appropriate confidentiality arrangements.
    - Implementing a form of internal merits review of ACCC informal clearance decisions by a panel of Associate Commissioners not involved in the day-to-day operations of the ACCC. This review would be 'on the papers', with oral submissions from the parties.
30. Regulators' public communications, particularly during the course of investigations and court proceedings, should be consistent with a code that protects due process and the reputations of those who have not had a court finding against them. Such a code would be applicable to all regulators.
31. Regulators should not have the general power to initiate their own formal market studies.

5. INSTITUTIONS TO DRIVE ONGOING REFORM

The majority of the opportunities to implement reforms that promote greater competition identified in this submission would generate the greatest benefits by being implemented across all levels of government. Here the Competition Policy Review Panel can make its greatest contribution. It has the opportunity to recommend a new governance model to drive competition nationally and across all sectors. Unlike many of the more narrowly based reviews, it is not limited to examining how to strengthen incentives to grasp competition opportunities in service delivery in only one jurisdiction (like the Commissions of Audit), or issues of reforming regulation relating to one sphere or sector (like many of the Productivity Commission inquiries).

This is possibly the most difficult, but important, task facing the panel. To make substantial and lasting progress on removing these impediments, experience has shown that effective intergovernmental arrangements need to be put in place (Exhibit 13). The right institutional structures have the potential to build commitment that delivers over the long term, rather than being at the mercy of the passions of individuals or the vagaries of political cycles.

Additionally, the dynamic nature of markets and of government regulation and service delivery means that competition policy reform will be a continuing task for all governments – implying that whatever intergovernmental arrangements are put in place, they need to be enduring in nature.

The model outlined in this submission builds on the National Productivity Payments model that the BCA proposed in its *Action Plan for Enduring Prosperity* (BCA, 2013e).

Exhibit 13: Lessons from the Seamless National Economy and the National Competition Policy institutional processes

The lessons from National Competition Policy, and to a lesser extent, the more recent Seamless National Economy reforms, have been widely discussed. Common themes include:

- Necessity of preparing the ground well before proceeding with reform.
- Bring high level political drive and constant attention.
- A broad-based and integrated reform program spreads the cost and benefits of adjustment.
- Agreements need to combine agreed principles with some jurisdictional latitude and flexibility in their application.
- Reform commitments need to be clear and carefully prioritised.
- An effective public interest test is fundamental, with the onus of proof on those seeking to retain anti-competitive regulation or other arrangements, to establish the benefits for the broader community.
- Good processes are needed to secure good outcomes – independent, public and transparent review processes for important reviews, with careful consideration to sequencing, priority of effort, and which issues should be addressed nationally, and which are best dealt with separately by each jurisdiction.
- Privatise for efficiency and competition, not to maximise sale proceeds.
- Sharing the benefits of reform through payments is critical.
- Payments need to be sufficient amounts to incentivise implementation of difficult reforms.
- Important to reward action that leads to outcomes (National Competition Policy), not just process steps (Seamless National Economy).
- An independent national (not Commonwealth Government) oversight institution will be needed, with a transparent assessment process, annual reporting against outcomes, and a critical analysis of each jurisdiction's progress.
- The independent body – not Commonwealth ministers – should assess the extent of any withholding of payments
- There must be fiscal incentives for Commonwealth to reform, not just states and territories.
- Must have long-term process – minimum 10 years – then ongoing oversight and rewards.
- National reforms, particularly in contentious policy areas, have proved harder to implement than state-specific changes. Trade measurement and business names reforms were easier than OH&S and occupational licensing.

Sources: BCA analysis; PC, 2005; Sims, 2013; Hilmer, 2014

5.1 Renewed commitment to national reform

The BCA has outlined its initial thinking on governance arrangements to drive reform, but this is the area where detailed discussions with governments, with oppositions, and through active communication with broader community stakeholder groups will be key. This will contribute to building a broad level of support for a reform agenda that all governments can endorse, and which has more chance of being implemented over the next decade.

The intergovernmental agreement, like the successful 1995 *Competition Principles Agreement* (COAG, 1995), should contain the high-level outcomes and associated funding arrangements, with the detailed implementation plan following shortly afterwards. It will be critical that all jurisdictions commit to delivering practical outcomes – that is, on-the-ground changes, such as removal of restrictive legislation, sale of suitable government businesses – not just undertaking processes (such as undertaking a review) or producing outputs (such as establishing a new entity).

5.2 A new incentive model: productivity payments

Higher growth means higher tax revenues for the Commonwealth and state and territory governments. However, given the level of vertical fiscal imbalance in Australia[65] and the difference in tax bases, the Commonwealth gains a higher share of any growth dividend.

A proposed new incentive model is for a new intergovernmental agreement to be structured essentially as a joint venture where all jurisdictions contribute to the cost of reforms but all share more evenly in the fiscal benefits through productivity payments.

The magnitude of these payments would need to both be sufficient to create strong incentives for all governments to implement reforms but be proportionate to the fiscal dividend. The annual National Competition Policy payments grew from $396 million in 1997–98 ($605 million in 2014 dollars), to $834 million in 2005–06 ($1.011 billion in 2014 dollars).

Indicative estimates suggest that if the package of states and territories reforms generated an increase in the rate of GDP growth by 0.1 per cent per annum, then the Commonwealth could make annual payments to the states of more than $300 million per year in 2016–17, growing to $5.0 billion by 2025–26, without having an adverse effect on the Commonwealth Budget. Of course, when a detailed package has been formulated it may be considered that it will have a smaller impact on growth. Any incremental funding would make an important contribution to the ability of states and territories to deliver better services. This calculation makes no allowance for the impact of pro-competitive reforms on employment and thus any resulting saving in Commonwealth expenditures on benefit payments (see Appendix B).

[65] The Commonwealth raises more than it spends, and transfers funds to the states that are able to raise less revenue than they spend.

The payments would be triggered by the delivery of tangible reforms that generate higher growth, in contrast with the Seamless National Economy packages, which in many cases rewarded milestone activities (such as undertaking a review or setting up a national regulator) rather than outcomes (such as legislating the review recommendations, or the commencement of national regulation). The start of the payments would be lagged to allow time for the delivery of reforms (and thus higher growth and tax revenues), and would grow over time if, and only if, more reforms are delivered allowing the economy to respond to the opportunities created by the reforms.

The payments would stop growing after 10 years, when all of the reforms would be expected to have been bedded down and not contributing to further growth. However, subject to the Commonwealth and all states and territories meeting their ongoing commitments (particularly regarding gate-keeping institutions to prevent back-sliding, and implementation of competitive neutrality measures) the payments would continue at the same per capita level in real terms, which would reflect the ongoing contribution of those reforms to higher output levels.

Under this model, states and territories would only share the fiscal benefits arising from those aspects of the agreement that generate greater growth and thus Commonwealth tax revenues. Those reforms that generate only budget savings or permit more and better services to be delivered by a state or territory government, would not be subject to the arrangements for sharing the fiscal dividend unless they could be shown to contribute to higher Commonwealth revenues. Consequently, the incentive for states and territories to undertake pro-competitive reforms to government service delivery would come through greater transparency of each jurisdiction's approach and outcomes, rather than financial incentives.

It would also not be necessary to provide funds to support privatisation, as that was addressed through the April 2014 COAG Agreement and the establishment of the Asset Recycling Fund announced in the 2014–15 Commonwealth Budget.

The competition payments from 1996–97 to 2005–06 made under the National Competition Policy agreements shared some of the Commonwealth's fiscal dividends from reform, and were generally considered crucial in both gaining national agreement to proceed with reform and keeping the momentum during the implementation phase (Productivity Commission, 2005; Hilmer, 2104; Sims, 2013).

It would be important for local governments to be involved, as they were with the National Competition Policy reforms. State governments can either mandate that all councils must comply (and ideally include this obligation in their local government Acts as was done with some jurisdictions under National Competition Policy) or make compliance voluntary. A model where state governments share some of the fiscal dividend with their local governments – as was done by Queensland, Victoria and Western Australia with the National Competition Agreements payments – would allow each local government to decide whether to participate, or whether to forego these funds.

5.3 Independent oversight of implementation

The key challenges in setting up enduring intergovernmental institutions is to identify appropriate governance arrangements that:

- ensure the most important reforms are identified and prioritised for action
- all jurisdictions are appropriately incentivised to follow through on their commitments
- any funding is secure from short-term budgetary pressures and political exigencies.
- Where payments are made, they are done so on the basis of outcomes rather than administrative milestones.

The experience of the National Partnership to Deliver a Seamless National Economy demonstrates that commitment to delivering agreed reforms can wane following a change of government. Good institutional arrangements will not only drive high-quality reforms but also engender trust between the states and the Commonwealth that reform and funding commitments will be honoured.

The Productivity Commission could be assigned the role of assessing whether each jurisdiction, including the Commonwealth, is delivering its agreed outcomes, and making recommendations on whether each jurisdiction warrants receiving the specified 'Productivity payments', or whether some amount should be withheld. It will be important to assign this role to an independent organisation such as the Productivity Commission given the COAG Council Reform Council is being disbanded.

5.4 An outcomes-based payments process

There are two key issues relating to assessments of any amounts of the productivity payments that might be withheld, due to non-compliance with the intergovernmental agreement:

- *What criteria should determine the amount withheld*? After 2000, COAG advised the National Competition Council when assessing the quantum of any withholding of funding to take into account the relevant state or territory's overall commitment to implementation, the effect of that state or territory's reform efforts on other jurisdictions, and the impact of the failure to undertake a particular reform. Applying any such criteria is likely to be a matter of judgement, but clear principles and a requirement to provide reasons for any adverse decision will be critical to maintaining support for what would be a long-term reform effort.
- *Who should assess performance and apply the criteria*? Under the Competition Principles Agreement process (COAG, 1995), the NCC both assessed performance and made recommendations of any amounts that should be withheld from jurisdictions that it considered were non-compliant. This was a successful model, although its recommendations were a highly contested judgement by those affected. In contrast, under the Seamless National Economy agreement, the COAG Reform Council was tasked with making assessments as to whether specified milestones had been met, but it was the Prime Minister who

assessed if any funds should be withheld. Ultimately, even though many milestones were missed, and some states withdrew their agreement to key deliverables, no jurisdiction had any payments withheld by the then Prime Minister.

Based on this experience, and consistent with the Competition Principles Agreement approach, the assessment body should make recommendations to the Commonwealth Treasurer about any withholding of payments, and unless he/she made an alternative assessment within a specified time, payments should be made based on this advice, which would then be made public. This is largely consistent with the model applying to the Commonwealth Grants Commission advice, and treats the assessments of eligibility for payment (and any advice on withholding payments) as a technical compliance, rather than political, process.

5.5 Improving the performance of the Commonwealth government

The Competition Principles Agreement process was very successful at driving many reforms. However, the Commonwealth Government, which was not subject to any withholding of payments, had a relatively poor performance in terms of meeting its obligations (NCC, 2004). By 2004, by which time all the 'priority' legislation should have been reviewed and been made compliant, the Commonwealth had completed only 60 per cent, along with South Australia. The only jurisdiction which had done less by 2004 was Western Australia (46 per cent). In contrast, New South Wales, Victoria, Queensland, Tasmania and the Australian Capital Territory had dealt with many challenging areas of reform and had at least 80 per cent of priority legislation compliant, while the Northern Territory had 79 per cent (PC, 2005, p. 19).

The design of the new institutional arrangements will need to carefully consider how best to create incentives for all jurisdictions to meet their reform commitments.

Recommendations

32. Commonwealth, state and territory leaders should commit to implementing a comprehensive package of reforms to remove barriers to competition that embody a new global mindset. This pro-competitive package should include agreement to implement:
    - a renewed program to engage all governments in reviewing and reforming anti-competitive legislation
    - robust processes to prevent new anti-competitive provisions in regulation
    - amendments to align Australia's competition law framework with international best practice principles
    - measures that ensure all the nation's regulators contribute to removing unnecessary barriers to competition and thereby foster national prosperity
    - reforms to drive competitive neutrality in government service provision through proper adherence to competitive neutrality principles, outsourcing and privatisation.
33. The Commonwealth should agree to share increased tax revenue resulting from the implementation of reforms, by providing an ongoing funding stream of substantial and untied productivity payments to the states and territories. This funding stream should not have a specified end-date, and should be indexed by inflation and population growth.
34. The funding should be 'money at risk', with any jurisdiction not fully meeting its commitments having funds withheld. The Productivity Commission should annually and publicly assess the progress of each jurisdiction in achieving the objectives of the intergovernmental agreement. This assessment should include public recommendations to the Commonwealth Treasurer regarding the withholding of any productivity payments.
35. Extend the Productivity Commission's ongoing annual benchmarking program by establishing rolling audits of the cumulative regulatory burden in each industry sector at least every five years, with recommendations for streamlining regulation.

APPENDIX A: COMPETITION LAWS: ADDITIONAL ANALYSIS

This appendix provides additional information to supplement the arguments set out in Chapter 3 of this submission.

A.1 The 'effects test' proposal

In Section 3.4 of this submission, the BCA's recommendation that an effects test not be introduced in the CCA was outlined. Below is further analysis in support of this position.

Is there robust evidence of a problem?

First, is there solid evidence of a problem that needs to be addressed?. The Dawson committee doubted that proving purpose was difficult, noting that the courts had found a proscribed purpose in cases including Queensland Wire Industries v. BHP, Melway Publishing v. Robert Hicks, ACCC v. Boral, ACCC v. Universal Music Australia, Rural Press v. ACCC and the first instance of ACCC v. Australian Safeway Stores.

Exhibit A.1 illustrates that since the last examination of this issue in 2003, the ACCC has continued to successfully take section 46 cases by establishing an anti-competitive purpose.

Exhibit A.1: Is proving 'purpose' a problem?

Section 46 cases successfully prosecuted using the current legislation, since the last review of this issue in 2003:

- ACCC v Safeway: the Full Federal Court confirmed the proscribed purpose found in two incidents by the primary judge, and also found a proscribed purpose in two additional incidents. Penalties amounted to $8.9 million for these four breaches.
- ACCC v Baxter: Baxter Healthcare was found to have taken advantage of its market power for the purpose of deterring or preventing its potential competitors from competing in the market for peritoneal dialysis (PD) fluids by bundling PD fluids with its sterile fluids, over which it had a monopoly. The Full Federal Court imposed $4.9 million in penalties.
- ACCC v Cabcharge: The Federal Court agreed with the parties that Cabcharge had taken advantage of its market power for the purpose of preventing Travel Tab/Mpos from providing alternative payment processing systems, and had engaged in predatory pricing of its taxi meters for the purpose of preventing the supply of alternative taxi meters. $14 million in penalties were imposed.
- ACCC v Ticketek: The Federal Court agreed with the parties that Ticketek had taken advantage of its market power for the purpose of deterring or preventing Lasttix from engaging in competitive conduct in the market for ticketing-related services. $2.5 million in penalties were imposed.
- ACCC v Eurong Beach Resort: The Federal Court agreed with the parties that Eurong Beach Resort had taken advantage of its market power in the market for barge services to Fraser Island for the purpose of eliminating or substantially damaging a rival barge company by charging below the cost of fuel and wages. $900,000 in penalties were imposed.
- ACCC v Fila: The Federal Court agreed with the parties that Fila had taken advantage of its market power in the wholesale market for AFL-licensed apparel for the purpose of deterring or preventing other wholesalers from competing. $3 million in penalties were imposed.

The benefits versus the costs of regulatory intervention

Second, if a substantial problem is established that might warrant regulatory intervention, what are the costs and benefits of the various options (including doing nothing). The main costs of an 'effects' test are the uncertainty it would create for business when deciding whether to engage in specific competitive conduct, and the consumer detriment arising from muted competition. The introduction of an effects test would have a chilling effect on competitive conduct, particularly as would be very difficult to establish clear rules that could be communicated throughout the organisation about what is and is not permitted. Consequently, such a change would not be consistent with the principle of making

the law as simple as possible, nor the principle of avoiding unduly impeding legitimate business interactions.

The practical consequences of an "effects" test

As the BCA argued in its supplementary submission to the Dawson review, it is straightforward to develop examples of the sorts of decisions that, while having a pro-competitive purpose, may inadvertently have the effect of lessening competition (Exhibits A.2, A.3. and A.4; BCA, 2002b).

Exhibit A.2: Hypothetical application of an effects test: Carbon/Fibre Limited

Over the last 10 years, Carbon/Fibre Limited has grown to become one of the largest manufacturers of wearable technology in Australia. Its success is a combination of strategic management, efficiency and innovation in design. Its wearable technology products are very popular with consumers and retail stores are very keen to stock them.

As a result, Carbon/Fibre enjoys considerable bargaining power when it comes to retailers, and receives significantly better trading terms than most of its smaller rival manufacturers. Many retail stores reserve considerable floor space to be taken up by Carbon/Fibre promotional material, mannequins and display screens, whereas other manufacturers are charged a fee for such an arrangement.

Wearable technology is tailored to the user which makes a retail presence advantageous. This means that many of the smaller manufacturers find it more expensive and more difficult to compete with Carbon/Fibre. They accuse Carbon/Fibre of misusing its market power with the effect of deterring or preventing competitive conduct as they cannot obtain retail exposure.

Under the current purpose test in s 46 of the CCA, it could be argued that Carbon/Fibre's conduct is intended simply to reduce its costs and to increase efficiencies, which is pro-competitive and not intended to prevent competitive conduct.

However, if an "effects" test were added to the proscribed purposes of section 46, this pro-competitive purpose may become irrelevant if it can be shown that Carbon/Fibre's conduct had the effect of preventing entry or preventing or deterring other manufacturers from engaging in competitive conduct.

If a broader prohibition against taking advantage of substantial market power with the effect of substantially lessening competition were added to the CCA, Carbon/Fibre might fall foul of that prohibition depending on its rivals' level of efficiency and innovation – matters beyond its control and often properly beyond its knowledge.

Exhibit A.3: Hypothetical application of an effects test: IoT Limited

Due to network effects, IoT Limited has become the dominant provider of a software platform that connects smart appliances, from home security to intelligent heating and cooling systems; its flagship application enables refrigerators to automatically order groceries when they are empty.

Unfortunately the whitegoods manufacturers have proved incapable of conforming their products to IoT's application programming interface, resulting in a range of newsworthy mistakes that threaten the credibility of the IoT platform itself.

IoT decides to cancel the API credentials of all non-complying refrigerator manufacturers and commence production of its own line of Internet refrigerators. Several of these manufacturers, who have invested heavily in development and production, go out of business.

Under the current s 46 test, IoT's purpose is not a prohibited one – it simply wanted to protect the value of its product and the integrity of its brand. However, an "effects" test could find IoT in breach of section 46, as its conduct damaged and eliminated several competitors and may have substantially lessened competition in the refrigerator market, even though its purpose was commercially legitimate.

Exhibit A.4: Hypothetical application of an effects test: Pharmacorp

Pharmacorp has achieved a substantial degree of market power through its efficient operations, its use of innovative technology and research methods and its commitment to R&D. The market in which Pharmacorp operates is relatively mature and Pharmacorp has enjoyed a relatively high and stable market share for a number of years although there are two smaller rivals operating in the same market, one of which is Medico.

Pharmacorp decides to diversify its operations into a related market in order to achieve satisfactory returns for its shareholders. Accordingly, it commits substantial funds to the research and development of a revolutionary new treatment, Wonderdrug. Pharmacorp supports the launch of Wonderdrug with a vigorous marketing campaign and the new product quickly becomes the leading treatment in its market.

Unbeknown to Pharmacorp, one of its rivals, Medico, had also embarked upon research and development into a similar drug therapy. However, upon learning of Pharmacorp's product and witnessing its success in the market, Medico decides to abandon the development of its own competing product.

Pharmacorp took advantage of its market power, particularly its brand recognition, to achieve a high level of market penetration ahead of its rivals. Pharmacorp developed its product with a view to diversifying its operations and achieving satisfactory returns for its shareholders. No anti-competitive purpose could be inferred and all Pharmacorp's internal documents supported Pharmacorp's legitimate commercial rationale for developing and launching the product.

However, the effect of Pharmacorp's use of its market power has been to prevent a new player from entering the market, even though Pharmacorp launched a new product and thereby increased consumer choice. Under an "effects" test, proceedings could be brought against Pharmacorp for anti-competitive conduct.

Past reviews

Third, it is useful to examine how earlier Australian reviews have assessed the merits of introducing an effects test into Australia's competition law. This issue has been examined in 1979, 1989, 1991,1993 and 2003. As outlined in Exhibit A.5, the proposal has been rejected on each occasion for reasons that remain compelling.

Exhibit A.5: Previous reviews' consideration of an "effects" test

The Blunt report (1979):

> It is only purposive misuse of market power and not inadvertent conduct or efficiency inspired conduct that should be at risk. Accordingly, we recommend that the purpose element should remain because we consider it is fundamental to a provision dealing with misuse of market power (p. 69).

The Griffiths report (1989) :

> [T]he bulk of the evidence suggests that no change to the section is required ... Given that the High Court [in Queensland Wire] has now provided significant clarification of the existing wording of the section, the Committee is of the view that any major changes to the wording would at this time be a retrograde step which could lead to renewed uncertainty if new and untested provisions were substituted. (p. 40)

The Cooney report (1991) :

> [I]n a provision directed explicitly at misuse of market power it is appropriate that a distinction between purpose and consequence be retained ... To prohibit the taking advantage of market power where this has or is likely to have the effect of, for example, preventing a person from engaging in competitive conduct would unduly widen the operation of the prohibition. It would force corporations to evaluate the potential effect of their every action on their competitors and potential competitors.
>
> The Committee accepts that the process of effective competition involves engaging in conduct the potential effect of which is to produce the very ends proscribed in section 46, and considers that prohibiting such conduct by reference to its effect may challenge the competitive process itself (p. 96).

The Hilmer review (1993):

> As the High Court has observed, the very essence of the competitive process is conduct which is aimed at injuring competitors… Firms should be encouraged to compete aggressively by taking advantage of new and superior products, greater efficiency and innovation. There is a serious risk of deterring such conduct by too broad a prohibition of unilateral conduct. The Committee takes the view that an effects test is too broad in this regard..
>
> ... The courts have indicated that they are alert to the distinctions which the legislature has attempted to make. There is a growing body of case law dealing with misuse of market power, and over time the limits of the existing provision will be explored. The current provision has the advantages over an effects test of an appropriate interpretation and a greater level of certainty for businesses ... (p. 70)

The Dawson review (2003)

> Not only would the introduction of an effects test alter the character of section 46, but it would also render purpose ineffective as a means of distinguishing between legitimate (pro-competitive) and illegitimate (anti-competitive) behaviour ... The distinction is sometimes a difficult one, but it is one that section 46 seeks to maintain and in doing so seeks to balance the risk of deterring efficient market conduct against the risk of allowing conduct that would damage competition and reduce efficiency ...
>
> An effects test would apply and capture behaviour with an adverse impact on competitors, but not necessarily on competition. The introduction of an effects test would be likely to extend the application of section 46 to legitimate business conduct and discourage competition (p. 70).

International experience

Finally, as it becomes more important that Australia adopts international best practice in competition law, it is useful to examine the international experience in this area.

The suggestion that Australia is alone in applying a purpose rather than effects test in assessing the misuse of market power, based on analysis of the international jurisprudence, was rejected by the Dawson review (Exhibit A.6). Although the laws of many jurisdictions do not refer to purpose as explicitly as section 46 in examining the unilateral conduct of firms with substantial market power, these jurisdictions frequently rely on purpose in the same way as Australia does.

Exhibit A.6: International experience of purpose in misuse of market power cases

The Dawson review noted:

> It is clear that in the United States an attempt to monopolise under the Sherman Act 1890 requires a specific intent and monopolisation itself requires an element of wilfulness. Section 79(1) of the Canadian Competition Act 1985 adopts an effects-based test for proscribed 'anti-competitive acts', but the Canadian Competition Tribunal has held that purpose is a necessary component of an 'anti-competitive act'. In New Zealand ... the introduction of an effects test to section 36 was rejected because it would unduly expand the scope of the section so as to deter efficient commercial activity and would increase the risk of error in determining whether or not conduct was in breach of the legislation ...
>
> The Committee is of the view that international practice, so far as it is of assistance, does not indicate that the introduction of an effects test to section 46 would be appropriate.(2003, p. 79)

Beyond the jurisdictions identified by the Dawson review, the interpretation of the relevant legislation often relies on purpose. For example, the European courts may look at intention in predatory pricing investigations under article 102 of the Treaty on the Function of the European Union:

> The exclusionary consequences of a price-cutting campaign by a dominant producer might be so self-evident that no evidence of intention to eliminate a competitor is necessary. On the other hand, where the low pricing could be susceptible of several explanations, evidence of an intention to eliminate a competitor or restrict competition might also be required to prove an infringement ... (Azko Chemie vs Commission (1991) C-62/86)

Equally, the European Court of Justice has held that an apparent misuse of a dominant position could be excused by an objective justification (including the protection of a firm's commercial interests) as long as that was the firm's true purpose:

> Although it is true, as the applicant points out, that the fact that an undertaking is in a dominant position cannot disentitle it from protecting its own commercial interests if they are attacked, and that such an undertaking must be conceded the right to take such reasonable steps as it deems appropriate to protect its said interests, such behaviour cannot be countenanced if its actual purpose is to strengthen this dominant position and abuse it.(United Brands vs. Commission (1978) C-27/76).

A.2 Previous consideration of predatory pricing

In section 3.4.2 of this submission, the BCA's recommendation relating to predatory pricing in the CCA was outlined. The issues associated with regulating predatory pricing while protecting legitimate price competition has been recognised by several recent reviews.

US Antitrust Modernization report:

> As the Supreme Court has observed, if a court erroneously concludes that a firm has engaged in illegal predatory pricing, "the costs of [such] an erroneous finding of liability are high" because firms may be reluctant to cut prices aggressively if they fear predatory pricing allegations. Overdeterrence could harm consumers...
>
> The improbability of predatory pricing schemes, combined with the certainty that lower prices benefit consumers, persuaded the Supreme Court to select a test that may fail to capture all instances of predatory pricing, but will not incorrectly condemn price discounting. (Garza et al., 2007, p. 86)

The US Department of Justice, *Competition and Monopoly: Single-firm Conduct under Section 2 of the Sherman Ac* noted:

> Price cutting is a core competitive activity. Consumers prefer lower prices to higher prices, and they benefit when firms aggressively compete to price as low as possible. Price competition enables consumers to secure desired products and services for less. Thus, alongside the broad consensus that predatory pricing can be anticompetitive, there is general recognition that, in the words of one treatise, "[a]ntitrust would be acting foolishly if it forbade price cuts any time a firm knew that its cuts would impose hardship on any competitor or even force its exit from the market." In the absence of clear standards, distinguishing harmful predation from procompetitive discounting is often difficult and runs the risk of erroneous condemnation, which can discourage firms from engaging in beneficial price competition and thus "chill the very conduct the antitrust laws are designed to protect. (2008, p. 49)

The Senate Economics References Committee Inquiry into the Effectiveness of the Trade Practices Act 1974 in Protecting Small Business noted:

> While the Committee agrees that recoupment is not a necessary element of predatory pricing for the purposes of s. 46, evidence of an intention to recoup losses suffered during a period of alleged predatory pricing should be considered by the court. Such evidence may contribute to the court's view that a corporation has engaged in predatory pricing; however, the absence of an intention to recoup should not invalidate an allegation of predatory pricing. (2004, p. 18)

The Senate Economics References Committee Minority Senators' Report noted:

> The issue of recoupment is important, in particular because it often provides the best test of whether price-cutting is a genuine exercise in competition or has a predatory intent. (A firm which is genuinely competing on price does not plan to recoup its foregone revenue from the elimination of its competitor; a firm which is engaged in a predatory pricing strategy almost invariably will.) Rather, Government Senators consider that recoupment should be one of the criteria to which the court may (and ordinarily will) have regard in determining whether price-lowering behaviour is predatory. (2004, p. 87)

A.3 Price signalling: the international experience

In section 3.5 of this submission, the BCA's recommendation that the price signally provisions in the CCA be repealed was outlined. Below is further analysis in support of this position.

One case that illustrates the difficulties of difficulty of separating legitimate public price information from price signalling is the US ethyl case (Exhibit A. 7)

Exhibit A.7: The difficulty of separating legitimate public price information from price signalling

The US's Federal Trade Commission (FTC) brought proceedings against four manufacturers of lead antiknock gasoline additives under section 5 of the Sherman Act which proscribes "unfair methods of competition". However, the Court in this matter found that the specific practices complained of were adopted by the parties for legitimate business reasons.

The practices complained of were not concerted actions but unilateral actions carried out independently. The parties had not entered into any formal or express price-fixing agreements but set their prices on the basis of several specific practices within the framework of a highly oligopolistic market structure. Such practices included:

- advance notice of price changes whereby the four firms gave notice to their customers of price increases at least thirty days in advance of the effective date of the price increase
- press notices issued by the firms concerning price increases
- uniform delivered pricing whereby the firms quoted antiknock prices only on the basis of a delivered price inclusive of transportation and quoted the same delivered price regardless of the customer's location
- "most-favoured-customer" clauses whereby any discounts off the uniform delivered price granted to a single customer were extended to all customers of the seller.

The FTC submitted that, although these practices were of a non-collusive, non-predatory, and independent nature, the manufacturers collectively had the effect of substantially lessening competition by eliminating a number of uncertainties about price determination and facilitating parallel pricing at non-competitive levels higher than might have otherwise existed.

The Court emphasized the need to draw a line between anticompetitive conduct and legitimate conduct that is normal acceptable business behaviour. Applying this distinction, the Court held that the mere existence of an oligopolistic market structure in which a small group of companies engaged in conscious parallel pricing an identical product did not violate antitrust laws. The Court stated that labelling one producer's price change in such a market as a 'signal,' parallel price changes as 'lock-step,' or prices as 'supracompetitive' did not make such pricing an 'unfair' method of competition. Rather, the Court was of the view that to hold as such would be to condemn any such price increase or moves, however independent they may be.

In formulating general principles in respect of the distinction between anticompetitive and legitimate price signalling (the latter being legitimate business practice) the Court held that before business conduct in an oligopolistic industry may be labelled 'unfair' within the meaning of section 5 of the Sherman Act, a minimum standard demands that, absent a tacit agreement, at least some indicia of oppressiveness must exist, such as:

- evidence of anticompetitive intent or purpose on the part of the producer charged; or
- the absence of an independent legitimate business reason for its conduct.

Source: George Hay, 'Facilitating Practices: The Ethyl Case (1984)' in John E. Kwoka, Jr. and Lawrence J. White (eds) 1999, *The Antitrust Revolution – Economics, Competition, and Policy,* Oxford University Press, Oxford

APPENDIX B: FISCAL PAYOFFS FROM REFORM

The likely fiscal dividend of reforms the Competition Policy Review might propose will not be able to be estimated until the final package of reforms are developed. However, it is feasible to develop some indicative estimates of the potential payoffs of various growth scenarios, using the Commonwealth budget papers' sensitivity analysis.

Table 4 provides two potential scenarios of the benefits of state and territory reforms to Commonwealth tax revenues. The benefits would be realised in the form of a 0.1 per cent (or 0.25 per cent) increase in the rate of growth for 10 years and thus a 1.0 per cent (or 2.5 per cent) increase in long-run GDP. The resulting potential fiscal dividends to the Commonwealth could be shared with the states and territories in recognition of their share of the reform effort. The revenue sharing should continue into the future, as long as there is continued compliance with the ongoing aspects of the agreement (such as gate-keeping) in recognition of the permanent increase in output and thus the Commonwealth revenue base.

Table 4: Potential Commonwealth fiscal dividends, indicative scenarios (2014,$ million)

	Long run GDP increases by 1.0 per cent	Long run GDP increases by 2.5 per cent
2016–17	$300	$800
2017–18	$700	$1,700
2018–19	$1,100	$2,700
2019–20	$1,500	$3,700
2020–21	$2,000	$4,900
2021–22	$2,500	$6,200
2022–23	$3,000	$7,600
2023–24	$3,700	$9,100
2024–25	$4,300	$10,800
2025–26	$5,000	$12,600
2025 onwards	$5,000	$12,600

Source: BCA calculations based on sensitivity analysis and forecasts from Commonwealth Treasury Budget Paper 1, 2014. Note: The increased rate of growth is assumed to be consistent over the 10-year reform program.

GLOSSARY

ABS	Australian Bureau of Statistics
ACCC	Australian Competition and Consumer Commission
AEMC	Australian Energy Market Commission
AER	Australian Energy Regulator
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
ATO	Australian Taxation Office
BCA	Business Council of Australia
BCG	Boston Consulting Group
COAG	Council of Australian Governments
CPD	Continuing Professional Development
EIS	Environmental Impact Statement
G20	Group of Twenty
GDP	Gross domestic product
GST	Goods and services tax
IA	Infrastructure Australia
NAB	National Australia Bank
NCC	National Competition Council
NCP	National Competition Policy
OECD	Organisation for Economic Co-operation and Development
RIS	Regulatory Impact Statement
TAFE	Technical and Further Education
WEF	World Economic Forum

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