Agreements and Competition Law in Australia

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Section 1: Introduction

The *Competition and Consumer Act 2010* (Cth) (formerly *Trade Practices Act 1974* (Cth)) (CCA) has definitely been more effective than previous attempts to introduce effective competition into Australian law. That said, the Act is almost forty years old and it may be time to consider a fundamental restructure of the competition provisions. The Government's recently announced 'root and branch'[1] review provides an opportunity for this. The objective of this article is to consider how sections 45, 47 and 48 could be altered to address the competition issues arising in an economy which is radically different from that which existed in 1974. In addition, the CCA is extremely proscriptive and has become increasingly complex. This reduces its efficiency in application and adds both to compliance and litigation costs: There may be value in simplification. Section 2 of the article examines Australia's chequered history when it comes to competition law regulation and explains how the CCA has come to take the form it has taken. Section 3 focusses specifically on the approach to agreements of various sorts that was incorporated into the CCA and identifies key changes made subsequently. It is concluded that there is little substance to the view that horizontal and some vertical agreements should be dealt with in separate prohibitions. Section 4 then considers the consequences of folding s 47 (and s 48) into s 45. The following two sections then identify issues separate to simplifying the treatment of agreements. Section 4 explains the approach of the courts to the evidence required for successful prosecution of contracts, arrangements or understandings, a threshold requirement of s 45. The difficulties experienced in prosecuting such matters are then discussed. The next section of the paper extends the discussion by identifying phenomenon in modern economies that create even greater complexity, making some conduct that is likely to have collusive anti-competitive consequences, tacit collusion, seemingly impossible to prosecute successfully. Finally, some conclusions are drawn and recommendations for change are suggested.

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[1] At the time of writing, only draft terms of reference were available. These are available at: http://www.australiancompetitionlaw.org/reports/2014rootbranch.html.

Section 2:

Australia's first competition law was modelled on the Sherman Antitrust Act and was incorporated into the Australian Industries Preservation Act 1906 (AIPA). This Act was passed shortly after Federation in response to claims from the country's fledgling manufacturing industry that if it were to grow it needed protection from import competition, perhaps an early use of the infant industries argument popularised by Sir John McEwan in the period following the Second World War. The *quid pro quo* for protection was the requirement to pay a living wage, that is, one capable of supporting a married man with two children (this became the basic wage). The AIPA contained four core prohibitions. Sections 4 and 7 prohibited all persons from entering into anti-competitive combinations and conduct amounting to monopolisation (respectively) in relation to trade or commerce between the states or with countries overseas. Sections 5 and 8 prohibited constitutional corporations from entering into anti-competitive combinations and engaging in monopolisation in all circumstances. All four prohibitions included a requirement that the defendant intended to control supply of goods to the detriment of the public.

Even though the AIPA was amended on several occasions to reflect rulings on the breadth of the Federal Government's power to make laws with respect to corporations, and changes in economic thinking,[2] as competition law the Act failed. This can be explained largely by two early High Court cases: *Attorney General v The Adelaide Steamship Co Ltd* (Coal Vend Case)[3] and *Huddart Parker & Co Pty Ltd v Moorehead* (Huddart Parker).[4] The Coal Vend Case involved an agreement between the majority of coal mine owners in a mining district in New South Wales to restrict output and raise prices. They also entered into exclusive agreements with shipping companies to support the output and price restriction agreements. The coal mine owners stated that they entered into the agreements because of increased competition from new mines that produced coal cheaper than that produced in the mines owned by the parties to the agreement. It was argued that this conduct breached the anti-competitive combinations prohibitions. As noted above, these prohibitions were

[2] *Australian Industries Preservation Act 1907* (Cth) (This Act resolved burden of proof issues and enforcement issues related to the Comptroller-General's powers to require persons to answer questions or produce documents); *Australian Industries Preservation Act 1909* (This Act repealed the two prohibitions (sections 5 and 8) that had been ruled unconstitutional in *Huddart Parker & Co Pty Ltd v Moorehead* (1909) 8 CLR 330 and introduced a form of exclusive dealing prohibition (sections 7A and 7B)), *Australian Industries Preservation Act 1910* (Cth) (This Act deleted the words 'to the detriment of the public' from section 4 and replacing them with 'with intent to destroy or injure'. The words were 'with intent to control, to the detriment of the public, the supply or price of any service, merchandise or commodity' were also deleted from section 7 and replaced with 'and was not destructive of or injurious to any Australian industry'. A reasonableness defence was also introduced.); the *Australian Industries Preservation Act 1930* (This Act created an exemption for certain provisions in carriage of goods contracts).

[3] (1913) 18 CLR 30 (an appeal from the High Court decision in *The Adelaide Steamship Co Ltd v Attorney General* (1912) 15 CLR 65).

[4] (1909) 8 CLR 330.

only contravened where combinations were engaged in 'with intent to restrain trade or commerce to the detriment of the public'. This meant that, in the words of the High Court, 'mere intent to restrain trade or commerce without the further intent to cause detriment to the public is not sufficient'.[5] As a result, parties were able to justify anti-competitive conduct on the basis that it brought about some larger benefit to the public. Such an argument was successful in the Coal Vend Case. The High Court took the view that the agreement was 'lawful and even laudable'[6] being 'to the advantage and not the detriment of the public at large',[7] despite acknowledging that the agreement would lead to a rise in the price of coal. This price rise would be more than offset by the benefits the court thought the agreement generated, namely putting the Newcastle coal trade on a satisfactory basis which in turn would enable coal owners to receive adequate remuneration and pay adequate wages.

In reaching its decision, the High Court noted that 'cut-throat [competition] is not now regarded by a large portion of mankind as necessarily beneficial to the public'.[8] This sentiment was also reflected on appeal in Lord Parker of Waddington's judgment when his Lordship observed:

> [T]he prices prevailing when negotiations for this agreement commenced were disastrously low owing to the "cut-throat" competition which had prevailed for some years … It can never be, in their Lordships' opinion, of real benefit to the consumers of coal that colliery proprietors should carry on business at a loss, or that any profit they make should depend on the miners' wages being reduced to a minimum.[9]

Two of the court's findings significantly limited the reach of the anti-competitive combinations prohibitions under consideration. First, the court found that it was necessary to show that the defendant intended to harm the public. Second, it was necessary to prove that the defendant(s) intended to raise prices. These findings also limited the scope of the monopolisation prohibitions as these prohibitions also included a requirement that that defendant intended to control supply of goods to the detriment of the public.

[5] (1912) 15 CLR 65, 73.
[6] (1912) 15 CLR 65, 91.
[7] Ibid
[8] (1912) 15 CLR 65, 73.
[9] (1913) 18 CLR 20, 47-48. The High Court described an unreasonable price as one 'beyond all reason which …shock[s] the ordinary sense of fair play': (1912) 15 CLR 65, 95.

The finding in the second case, Huddart Parker, did not narrow the scope of the prohibitions. However, two of the four prohibitions contained in the AIPA were declared unconstitutional. As noted above, the anti-competitive combinations and the monopolisation prohibitions applied to persons engaged in interstate or overseas trade and to corporations in all circumstances. The prohibitions that applied generally to persons (sections 4 and 7) were pinned to the trade or commerce power.[10] The prohibitions that applied specifically to corporations (sections 5 and 8) were said to be based on the corporations power.[11] The latter provisions were held to be unconstitutional because the High Court found that the corporations power did not give the Commonwealth the power to regulate all trading activities engaged in by trading corporations. Influenced by the now discredited 'reserved power' doctrine, the High Court was keen to ensure that there was no intrusion on the States' rights to regulate intrastate trade. This significantly restricted the scope of the corporations power and 'the power law dormant for nearly 60 years'[12].

The result of the AIPA's failure, as a survey by Karmel and Brunt recorded, was an economy where price fixing and resale price maintenance (RPM) were the norm, as were other anti-competitive agreements.[13] The inevitable consequence of these anti-competitive practices was an inefficient economy which sheltered behind a plethora of measures to protect local businesses from import competition. In recognition of this a new competition law was introduced in 1965, the *Trade Practices Act 1965* (Cth) (TPA65) the purpose of which was 'to preserve Competition in Australian Trade and Commerce to the extent required by the Public Interest.'[14] Unlike the AIPA, this was modelled on British law. Potentially anti-competitive agreements had to be registered and were then assessed by the Trade Practices Commissioner. The TPA65 was also ruled unconstitutional in *Strickland v Rocla Concrete Pipes Ltd*[15] (Strickland). Rocla Concrete was charged with failing to register details of certain agreements with the Commissioner in breach of section 35 of the TPA65. Section 35 was general in nature and purported to apply to persons, corporate or not. The Commonwealth argued that section 7 overcame the fact that such a provision would be beyond the legislative competence of the Federal parliament. Section 7 was a 'reading down' provision that attempted to relate the requirements of the Act to a number of constitutional heads of power (including the corporations power and the trade or commerce power) in a manner similar to that

[10] Section 51(i) of the Constitution gives the Federal Government the right to make laws with respect to 'trade and commerce with other countries'.
[11] Section 51(xx) of the Constitution gives the Federal Government the right to make laws with respect to 'foreign corporations, and trading or financial corporations formed within the limits of the Commonwealth'.
[12] Leslie Zines, 'The High Court and the Constitution' (Federation Press, 2008 5th ed), 107.
[13] Peter H. Karmel and Maureen Brunt, 'Structure of the Australian Economy (F.W. Cheshire,1962), 94-96.
[14] Available at: http://www.comlaw.gov.au/Details/C1965A00111.
[15] (1971) 124 CLR 468.

adopted in section 6 of the CCA today. As the agreements in question did not relate to interstate or overseas trade, Rocla Concrete was said to be caught because it was a constitutional corporation. The High Court held that section 7 was ineffective in its attempts to ensure that the prohibitions contained in the TPA65 were constitutionally valid largely because section 7 attempted to narrow the scope of a broadly expressed prohibitions which, as expressed, were beyond the scope of the Commonwealth's legislative power rather than to extend the scope of a constitutionally valid provision to other circumstances (as the current s 6 of the CCA does). However the decision is more significant because of the court's decision to revisit the Huddart Parker decision. Noting that the 'reserved powers' doctrine, which had been so influential to the reasoning in Huddart Parker, had been 'exploded'[16] in another context in *Amalgamated Society of Engineers v Adelaide Steamship Co Ltd*[17] the High Court overruled the restrictive interpretation given to the corporations power in Huddart Parker and held that at the very least laws regulating the trading activities of trading corporations were laws with respect to corporations.[18]

The decision of the High Court in Strickland dramatically increased the Commonwealth's ability to pass laws regulating the conduct of constitutional corporations. This reinterpretation led to the passage of the *Restrictive Trade Practices Act 1971* (Cth). This Act was largely a re-enactment of the TPA65, correcting the constitutional errors made by the drafters of the TPA65 and highlighted by the High Court in Strickland. The constitutionality of this Act was never ruled upon. However, it was repealed and replaced only three years into its operation by the *Trade Practices Act 1974* (Cth) (TPA) when the decision was made to move to a prohibition-based competition law system (similar to that in the AIPA) rather than one that a notification scheme (such as that set up by the TPA65).[19]

There have been numerous reviews of the TPA, resulting in changes being made to the core prohibitions, but the basic structure of Part IV, which contains the conduct prohibitions, has remained in-tact.[20] In 1977 the prohibition against anti-competitive agreements was recast. The requirement to show a 'restraint of trade' was removed and in its place, the 'substantial lessening of

[16] *Strickland v Rocla Concrete Pipes Limited* (1971) 124 CLR 468, 485 (per Barwick J).
[17] (1920) 28 CLR 129.
[18] (1971) 124 CLR 468, 489.
[19] The TPA was chiefly pinned to corporations power, although it also relies on the trade and commerce, territories. banking, postal and telegraphic services, external affairs and incidental powers (see section 6).
[20] Major reviews include Swanson Committee (1977), Blunt Committee (1979), Griffiths Committee (1989), Cooney Committee (1991), Hilmer Review (1993) and Dawson Review (2003). In addition, there were numerous government inquiries, and several by the Productivity Commission (for details of all reviews undertaken see: http://www.australiancompetitionlaw.org/reports.html.)

competition' test was introduced. Further, price fixing was deemed to be per se illegal.[21] In 1986 further amendments were made. The threshold requirement for the misuse of market power prohibition was lowered and two new merger prohibitions were introduced.[22]

The first significant overhaul of the Act occurred in 1995 in response to recommendations made by the Hilmer Review.[23] This overhaul saw the introduction of the Pt IIIA access regime, the application of the Act to the commercial activities of government, the introduction of truly national competition laws through the passage of the National Competition Code, the establishment of the National Competition Council, as well as the repeal of the price discrimination prohibition.

Significant changes to the regulation of anti-competitive agreements were introduced in 2009[24] in response to recommendations made by the Dawson Committee.[25] Criminal sanctions now apply to some cartel conduct and hard core cartel conduct provisions were transferred from section 45 to a newly created Part IV Division 1.[26] As noted above, the TPA was renamed in 2010 and is now known as *Competition and Consumer Act 2010* (Cth) (CCA).[27] The substantive changes made to the Act at this time related to the consumer provisions, not the conduct prohibitions.

Section 3: Part IV of the TPA/CCA and Treatment of Agreements

3.1 Overview

Part IV of the TPA (retained in the CCA) prohibited various types of business conduct, but for the present purpose it is the treatment of anti-competitive contracts, arrangements and understandings (collectively 'agreements') that is the focus. The first thing to note is that the legislation specifically referred not simply to contracts or arrangements but also to understandings. We return to this distinction in the next part of this article when considering how the courts have dealt with the

[21] See *Trade Practices Amendment Act 1977* (Cth). See also Trade Practices Act Review Committee, Report to the Minister for Business and Consumer Affairs (1976) (Swanson Committee) (available at: http://www.australiancompetitionlaw.org/reports/pdf/swanson1976.pdf).
[22] See *Trade Practices Revision Act 1986* (Cth).
[23] National Competition Policy Review, Report by the Independent Committee of Inquiry (1993) (Hilmer Review) (available at: http://ncp.ncc.gov.au/docs/National%20Competition%20Policy%20Review%20report,%20The%20Hilmer%20Report,%20August%201993.pdf).
[24] *Trade Practices Amendment (Cartel Conduct and Other Measures) Act 2009* (Cth).
[25] Review of the Competition Provisions of the Trade Practices Act (2003) (Dawson Review) (available at: http://tpareview.treasury.gov.au/content/report/downloads/PDF/Preliminaries.pdf).
[26] Section 45 (which prohibits anti-competitive agreements and collective boycotts by competitors) will continue to catch cartel activity where agreements between competitors include an exclusionary provision (see s 4D) or a provision that has the purpose, effect or likely effect of substantially lessening competition).
[27] See Schedule 5 of the *Trade Practices Amendment (Australian Consumer Law) Act 2010* (which was effective 1 January 2011).

legislation. Second, agreements were not treated in a single section of the Act but were divided between several sections. Thirdly, some agreements were deemed to be anti-competitive and hence illegal, others were to be illegal only if they could be shown to substantially lessen competition (or to have been reached for that purpose). Finally, exemption was, or later became, available for all types of agreements. These four aspects are inter- related and are discussed below.

At the time when the TPA was being formulated, the Chicago School of legal and economic thought, represented by judges such as Posner and Bork and economists such as Stigler, was in the ascendency. The Chicago School held that markets were responsive and adapted to produce efficient outcomes and so should not be subject to government intervention. The exception was where horizontal agreements or conspiracies existed. This approach later prompted Baker to draw an analogy between George Orwell's "Animal Farm" and the antitrust approach to agreements. In Orwell's tale the post revolution farmyard rules were too complex for the animals to remember and so the rules were gradually reduced to "four legs good, two legs bad" (referring first to the animals and second to the farmer). Baker likens this to the simplification of the approach to agreements: vertical good, horizontal bad.[28]

3.2 Separate sections regulating horizontal and vertical agreements

The more relaxed view of exclusive dealing influenced the structure of Part IV of the Act. This structure recognises the potential for any agreement to be anti-competitive but then treats some agreements as more likely to be so. Leaving aside the per se provisions for the moment, this approach identified not just vertical agreements as being less likely to be anti-competitive but within this group, exclusive dealing was treated differently from other vertical agreements essentially because exclusive dealing arrangements were likely to be efficiency-enhancing.

Exclusive dealing agreements were excised from section 45, to be addressed in section 47. Although the Second Reading speech for the 1974 Bill provides not real clues as to why exclusive dealing was separated out, a careful reading of at least one of Professor Brunt's essays does.[29] She explains that treatment of vertical agreements under Australian competition law was responsive to first the early pattern of restrictive practices and second to the smallness of the Australian economy.

[28] Jonathan B. Baker, 'Vertical Restraints with Horizontal Consequences: Competitive Effects of "Most-Favored-Nation" Clauses' (1996) 64(3) *Antitrust Law Journal* 517, 517.
[29] Maureen Brunt, 'The Australian Antitrust Law after 20 Years – A Stocktake' in Maureen Brunt, 'Economic Essays on Australian and New Zealand Competition Law' (Kluwer, 2003), 297, 336-339.

She goes on to suggest that market power may be created or added to via exclusivity agreements, even though those agreements could be efficiency-enhancing. It is worth noting that unlike the US laws on which the TPA drew, the TPA/CCA does not contain a provision that bans unilateral acts of monopolization unless they are engaged in by a business that already has substantial market power.[30] The decision to deal with exclusive dealing by way of a separate prohibition, rather than leaving it to be dealt with by a general prohibition against agreements, may have been intended to overcome this gap.

Nevertheless, leaving aside per se prohibitions, agreements caught by sections 45 and 47 are subject to the same competition test irrespective of their nature – they are prohibited where they have the purpose, effect or likely effect of substantially lessening competition. However, given the view that exclusive dealing is generally efficiency-enhancing, legal action taken in relation to section 47 could be expected to be more likely to relate to effect than purpose.

3.3 Exemption processes

As noted above, the TPA eventually allowed for the Australian Competition and Consumer Commission (ACCC) to grant exemption to all forms of agreements. Although the basis for immunity, net public benefit, is essentially the same for exclusive dealing as it is for other agreements, different processes are available when it comes to seeking exemption from the exclusive dealing prohibition. For horizontal arrangements and RPM, the only way to seek an exemption is to apply for authorisation.[31] Authorisation is also available for both forms of exclusive dealing as well as an additional exemption process, notification, which was introduced in 1977.[32] Whereas an application for authorisation required the applicant to establish that conduct generated a net public benefit, as well as pay an application fee, notification reversed the onus and the application fee was significantly lower.[33] Further, as a general rule parties are able to implement

[30] See *Boral Besser Masonry Ltd v Australian Competition and Consumer Commission* (2005) 215 CLR 374.
[31] It was not until 1995 that it became possible to seek authorization for RPM conduct: see s 88(8A) added by the *Competition Policy Reform Act 1995* (Cth).
[32] Prior to 1977 exclusive dealing agreements were also treated differently to other forms of agreements. Businesses were able to seek clearance from the ACCC. They were also able to seek clearance for merger activity, presumably because of concerns about curbing these forms of conduct that were often pro-competitive. Clearance, perhaps a hangover from the notification approach adopted under the TPA65, would be granted if the Commission reached the conclusion that the exclusive dealing agreement under consideration was not likely to substantially lessen competition. The clearance process for exclusive dealing was abolished in 1977 and replaced with notification, following a recommendation of the Swanson Committee: *Trade Practices Amendment Act 1977* (Cth). See John Duns, Authorisations and Notifications, in Ray Steinwall et al, 'Butterworths Australian Competition Law' (Butterworths, 2000), 422. Notification also became available for collective bargaining in 2006.
[33] At the time fees were mandated and the TPC/ACCC had no discretion to wave or reduce them.

their agreements more quickly under the notification process as immunity generally commences, at the latest, 14 days after the parties to the agreement notify the Commission.[34]

Today, it is generally accepted that the notification process was included in acknowledgment of the fact that exclusive dealing agreements are far less likely to be anti-competitive than horizontal agreements. For example in the latest edition of his leading textbook Corones puts the matter very simply: 'Exclusive dealing is generally pro-competitive. Notification is intended to provide a quick and more flexible means of obtaining immunity than authorisation'.[35] Although the Explanatory Memorandum accompanying the Act that introduced the notification scheme does not make this point directly, the fact that the exclusive dealing prohibition was singled out as the intended beneficiary of this quicker and cheaper exemption process is consistent with the view that the CCA is underpinned by the notion that exclusive dealing is quite often pro-competitive and efficiency enhancing. This is consistent with observations in the Swanson Report that led to the 1977 amendment that stressed the importance of alleviating the 'guilty until innocence can be proved' presumption which applies under the authorisations procedure[36] and the confinement of these concerns to exclusive dealing. Further, the desire to provide a different process for exemption in relation to exclusive dealing rather than for all potentially anti-competitive agreements seems to explain why exclusive dealing was excised from s.45.

3.4 Per se prohibitions

Two forms of vertical agreements are deemed to be anti-competitive - RPM and third line forcing.[37] An RPM agreement is a vertical agreement between a firm and its customers or vice versa in relation to the minimum price at which product can be sold at the retail level.[38] It is a particular form of vertical restraint which is dealt with not in section 47 but in section 48. It is difficult to explain this approach except in terms of the rampant nature of RPM prior to the introduction of the resale price maintenance prohibition in 1971,[39] and the general overriding concern about pricing

[34] Immunity is immediate if the notified conduct relates to a form of exclusive dealing that is competition tested. With respect to third line forcing, the conduct is immune 14 days after lodgment unless the ACCC issues a draft notice during this time, in which case immunity is suspended until the ACCC decides not to issue a final notice revoking immunity.
[35] Stephen G. Corones, 'Competition Law in Australia' (LawBook, 5th ed, 2010), 193.
[36] Swanson Committee, above n 24, [4.121].
[37] It should also be noted that other forms of conduct that do not involve the reaching of an agreement (such as inducing customers to charge the RRP and withholding supply from those that undercut the RRP) also breach the resale price maintenance prohibition (see s 96(3)). Further, a party can be guilty of third line forcing if they offer to enter into a third line forcing agreement or refuse to enter into an agreement because the would-be customer will not accept the third line forcing requirement (see s 47(7)).
[38] More precisely this is referred to as minimum RPM, as agreements could relate to maximum RPM. Australian law does not address maximum RPM as it is assumed to be in the interests of consumers.
[39] *Trade Practices Act 1971* (Cth). See also Karmel and Brunt, note 14, 95-96. With the arrival of bulk discount stores in Australia in the late 1960s, full service stores faced a free-riding problem. Consumers would obtain product

agreements that prevailed at the time: [40] RPM was regarded as a vertical price fix. Yet horizontal price fixing, at least until relatively recently, while a per se offence, was embedded in section 45.

Over the years since 1971, the treatment of RPM as per se illegal has attracted little criticism, possibly because where the purpose of RPM is not anti-competitive the objective can generally be achieved in other ways. However, in 2007 in the ***Leegin case*** a majority of judges in the United States Supreme Court decided that RPM would in future be assessed using a competition test.[41] This seems to have produced little reaction in Australia. In ***Jurlique***[42] Spender J discussed the potential for RPM to be efficient and to benefit consumers but only in passing, and these comments did not spark a general debate about introducing a competition test for RPM.

The position is radically different in relation to third line forcing. There appears to be no rational explanation for this particular form of exclusive dealing being deemed anti-competitive. Indeed, the ACCC and its predecessor the Trade Practices Commission (TPC) has received more notifications for such conduct than for other conduct, and more than for authorisation. Further, the success rate for notifications is far higher than for other exemption applications. Again the explanation for the treatment of third line forcing seems to come from experience around the time the legislation was being developed. For example, in the late 1960s and early 1970s banks required those seeking home loans also to take out life assurance as a condition for the loan in order to guarantee it. At the time banks were unable to offer insurance services. However, a practice developed where banks would offer loans that were conditional upon the customer taking out insurance with a nominated provider. The nominated agent was either related to the bank or was given some form of commission by the bank. The per se treatment of third line forcing may have been motivated by a desire to stamp out this practice, although it should be noted that there may have been more general concerns about this type of conduct, as evidenced by the Swanson Committee's observation in 1976 that 'the practice will, in virtually all cases, have an anti-competitive effect'.[43] However, by the time the Blunt

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information from the latter, then buy at cheaper prices from the former. In attempting to address this it was not unusual for the manufacturer, who wanted the full service store to promote its products, to impose minimum retail prices in order to ensure that retailers received a sufficient return to supply the required service.

[40] The fact that these concerns existed is further demonstrated by the fact that RPM was the only form of conduct that could not be granted immunity by the ACCC. This remained the case until 1995: *Competition Policy Reform Act 1995* (Cth).

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

[42] *ACCC v Jurlique International Pty Ltd* [2007] FCA 79.

[43] Swanson Committee, above n 24, [4.103].

Review report was issued in 1979, the harsher statutory treatment of third line forcing was already being questioned.[44]

The treatment of third line forcing is inconsistent with other forms of exclusive dealing such as full line forcing which is competition tested. Arguably both limit consumer choice and so may damage competition. For example, would the competitive effect be different if the banks bundled loan and insurance products or if they offered loans on condition that the customer deal with a nominated insurance company? At the time of most of the inquiries into the TPA, numerous submissions called for third line forcing to be competition tested, including as recently as the Dawson Inquiry in 2003.[45] With the exception of Swanson Committee and the Blunt Review, these inquiries recommended change but the government has not adopted the recommendation.[46]

3.5 Concluding remarks

There appears to be little substance to the view that exclusive dealing should be separated from other agreements simply because such agreements are often intended to enhance efficiency. The test embedded in section 47 (and section 45) is a competition test, not an efficiency test. Another argument against separating exclusive dealing from other types of agreements is the need to categorise such agreements in order to determine which section they fall under. [47] This may add cost and complexity to litigation as illustrated by the Visy case which went through an appeal to the Full Court, then on to the High Court.[48] Categorisation is inefficient if it is not required to achieve the objective of the legislation. It risks failing to apprehend some anti-competitive conduct simply because such conduct was not recognised at the time the legislation was developed.

The categorisation concern can also be illustrated in relation to section 48. While recommended retail prices (RRP) are not included in the definition of RPM,[49] the courts have clearly accepted that '[t]he fact that the specification of a price is couched in terms of recommendation does not prevent it from being a price specified'[50] where the supplier pressures the customer to charge the RRP or

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[44] Trade Practices Consultative Committee, *Small Business and the Trade Practices Act* (December 1979) [7.11] (Blunt Committee).
[45] See http://tpareview.treasury.gov.au/content/home.asp.
[46] In 1979 the Blunt Review (above n 48) noted that third line forcing was 'an area of the law which we would hope to review soon. The Hilmer Review (above n 26) recommended that the practice be subject to a competition test (see recommendation 3.3) as did the Dawson Review (above n 28), see recommendation 8.3.
[47] This is done at some length in s 47(2) – (9).
[48] *Visy Paper Pty Ltd v Australian Competition and Consumer Commission* (2003) 216 CLR 1.
[49] See section 97.
[50] *Trade Practices Commission v Bata Shoe Company of Australia Pty Ltd* (1980) ATPR ¶40-161, 42266.

attempt to get them to agree to do so.[51] However, uncertainty remains about the point at which pressure from a supplier to charge the RRP becomes RPM. Why should uncertainty about where the line should be drawn mean that if RRP has an anti-competitive effect it is not deemed anti-competitive but is competition tested under a different prohibition?

In addition, categorisation may encourage a 'rule-based' approach to competition analysis. In the US, in cases involving ties, for example, the approach in court seems to involve identifying the type of conduct, then considering whether there is a legitimate business rationale to explain it – if the conduct could be efficiency-enhancing, then it is unlikely to be found to contravene the antitrust provisions.[52] Most types of business conduct can be pro- or anti- competitive depending on the circumstances, and this is especially true of exclusive dealing. It is important, therefore, that a careful competition assessment not be supplanted by the arbitrary application of decision-rules.

Section 4: Consequences of abandoning the exclusive dealing 'carve out'?

In the previous section we concluded that, in principle, anti-competitive agreements (whether horizontal or vertical) should be regulated under a single prohibition. However, before recommending the combination of sections 47 and 45, it is necessary to consider two major consequences of such a decision. First, the role of notifications would need to be considered. Second, given the limited reach of the prohibition against unilateral anti-competitive behaviour,[53] we would need to be confident that anti-competitive refusals to deal are adequately regulated by s 46.

4.1 Notifications

As consequence of a decision to abandon the carve-out of exclusive dealing is the need to reconsider the role of notifications. The availability of the notification process has two benefits - it reduces the financial burden on small business,[54] and it increases efficiency when dealing with applications covering conduct likely to have little or no anti-competitive effect (especially third line

[51] See *Festival Stores v Mikasa (NSW) Pty Ltd* (1971) 18 FLR 260; *Mikasa (NSW) Pty Ltd v Festival Stores* (1972) 127 CLR 617; *Heating Centre Pty Ltd v Trade Practices Commission* (1986) 9 FCR 153, *Trade Practices Commission v Sony (Australia) Pty Ltd* (1990) ATPR 41-031 and most recently *Australian Competition and Consumer Commission v Dermalogica Pty Ltd* [2005] FCA 152.

[52] It should be noted that this approach is applied in circumstances where no exemption process (authorisation/notification) is available.

[53] See text accompanying n 33 above.

[54] This is illustrated by the extension of the provision to notify to small businesses wishing to engage in collective bargaining following a recommendation by the Dawson Inquiry.

forcing). If notification were to be retained for exclusive dealing, then exclusive dealing would still need to be defined and identified. However given there are alternate ways of delivering the benefits brought about by the notification scheme, it is hard to justify the retention of s 47 solely to identify conduct which can be notified as opposed to authorised. Given the ACCC's ability to exercise discretion in relation to the fees charged for authorisation applications and as to the depth of inquiry, it could be considered that there is no longer a strong case for notification as an alternative avenue to authorisation.[55] Other options, such as allowing small businesses to engage in conduct the subject of an authorisation application unless and until the ACCC refuses authorisation could also be explored.

4.2 Unilateral Market Power

A potentially graver concern is that a combined prohibition may not extend to all conduct currently caught by section 47. Assuming that the threshold 'agreement' requirement is retained, certain forms of conduct currently caught by s. 47 would only be regulated under the prohibition against the misuse of market power contained in s. 46. In its current form, s. 47 catches not only exclusive dealing agreements but also offers to enter into exclusive dealing arrangements[56] and refusals to supply a potential customer because that potential customer has not accepted or agreed to accept conditions that are attached to supply (negative exclusive dealing).[57] As noted earlier, one of the reasons the prohibitions on vertical and horizontal restraints may have been separated is because of a concern that market power may be created or strengthened by exclusive dealing conduct. Thus, before a recommendation can be made to merge sections 45 and 47, it is necessary to consider the case law to determine whether there are examples of negative exclusive dealing that may go unregulated because they are not caught by s 46.

The main reason that negative exclusive dealing may go unregulated is that section 46 only applies to businesses that have substantial market power at the time they engage in the negative exclusive dealing conduct. Perhaps we need not be too concerned about this. After all, a business that lacks

[55] The origin of the exemption or immunity provisions is the 1965 Act. These provisions did not distinguish between types of agreements or the method by which immunity was sought – all registered agreements were to be examined on a case by case basis. Initially the 1974 Act provided two processes for immunity or exemption. The first was a clearance if the Commission decided that the conduct was not anti-competitive; the second required assessment of public benefit under an authorization process. In 1977, following the Swanson Review (above n 24), clearance as such was removed as an option and notification was introduced. It was available for exclusive dealing other than third line forcing. [At this time the test for authorisation became the net public benefit test]. In 1995 as part of the Hilmer reforms, notification became available for third line forcing.

[56] See sections 47(2), (4), (6), (8).

[57] See sections 47(3), (5), (7) and (9).

substantial market power may not be able to bring about a lessening of competition by engaging in exclusive dealing conduct. Further, if the refusing business does not have substantial market power, this is likely to mean that would- be customers/suppliers have other options for supply/distribution. Finally, it could be argued that the offers or refusals under consideration are less likely to harm competition as they does not result in supply or distribution channels being tied up by contractual devices. However a refusal to supply goods or acquire and distribute them may have foreclosure effects and so the potential anti-competitive effects of such conduct cannot be ignored.

We reviewed all section 47 in which negative exclusive dealing was alleged with a view to determining whether conflating sections 47 and 45 would create a gap in the law. We found no cases based solely on an offer to enter into an exclusive dealing arrangement. However, we found several cases in which refusals to supply were challenged under section 47.[58] Many of these cases involved allegations of negative third line forcing. Section 46 was not raised in most of the third line forcing cases, suggesting that applicants appreciated that the respondent did not have market power and that a section 46 case would fail.[59] In one case section 46 was raised and the respondent was found guilty of negative third-line forcing while the section 46 case failed (because the applicant failed to make out a relevant market).[60] As third line forcing is not inherently anti-competitive, this does not necessarily highlight a gap in the law. Arguably, in circumstances where third line forcing threatens competition (namely when a firm with substantial market power engages in anti-competitive conduct designed to harm competition) section 46 will be adequate. We found two cases in which the applicant alleged that the respondent had engaged in negative downstream restrictions other than third line forcing but did not allege a breach of section 46.[61] In each of these cases, the conduct in question was caught by the definition of exclusive dealing but the claim under section failed because the conduct was not intended to, nor did it have the effect of, substantially lessening competition. The competition finding is consistent with the applicants' decision not to run a section 46 case.[62]

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[58] Where a trial decision was appealed, the trial judgment has been ignored and the appeal judgment analysed.
[59] *Brisbane Broncos Leagues Club Ltd v Alleasing Finance Australia Pty Ltd* (2011) 280 ALR 497; *Australian Automotive Repairers' Association (Political Action Committee) Inc (In liquidation) v Insurance Australia Ltd* [2006] FCAFC 33; *Joseph v La Trobe University* [2004] FCA 746; *Arrowcrest Group Pty Ltd v Ford Motor Co of Australia Ltd* [2002] FCA 1450; *Australian Competition & Consumers Commission v Health Partners Incorporated* (1997) 151 ALR 662 (Section 46 was originally raised but then abandoned); *Kam Nominees Pty Ltd v Australian Guarantee Corporation Ltd* (1994) 123 ALR 711; *Castlemaine Tooheys Ltd v Williams & Hodgson Transport Pty Ltd* (1985) 64 ALR 536.
[60] *Hospitality Group Pty Ltd v Australian Rugby Union Ltd* (2001) 110 FCR 157.
[61] Section 47(3).
[62] *Dandy Power Equipment Pty Ltd v Mercury Marine Pty Ltd* (1982) 44 ALR 173; *Outboard Marine Australia Pty Ltd v Hecar Investments No 6 Pty Ltd* (1982) 44 ALR 667.

Another category of case involved cases where section 46 and non-third line forcing section 47 claims were raised. In two of these cases both the section 46 and section 47 claims failed.[63] In another case, which demonstrates the categorisation problem, discussed earlier, the section 46 case was successful but the section 47 case failed.[64]

We were only able to find one case (other than those involving third line forcing) where the outcome would have differed if section 47 did not have independent existence. In *Universal Music Australia Pty Ltd v ACCC*[65] the respondents were found to have breached section 47 but not section 46. The section 46 case failed because the respondents did not have the requisite degree of market power. Consistent with earlier observations, the court also found that the negative exclusive dealing conduct in question could not be said to have had, or be likely to have, an anti-competitive effect. However the respondents were held to have breached section 47 because they had the purpose of substantially lessening competition. Given the findings that competition was not lessened, we should not be concerned that the outcome in this case would have been different unless one favours a moralistic approach to competition law rather than a welfarist approach.

In summary, we do not believe it would be problematic if negative exclusive dealing were only regulated under section 46. This would create a gap in the law in the sense that a firm without substantial market power, but perhaps with significant financial resources, could engage in anti-competitive conduct designed to develop market power with impunity. However, the likelihood that such conduct would cause significant harm to markets is sufficiently low that it does not justify a separate exclusive dealing prohibition which introduces the problems of categorisation. Further, the appropriate way to deal with such concerns is to bring them within the scope of section 46, a provision designed to deal with unilateral anti-competitive conduct. If desired, this could easily be achieved by prohibiting acts of monopolisation (attempts to gain market power through anti-competitive means) along the lines of the equivalent US provision.

Section 5: The courts' take on 'agreements'

Separate from the issue of simplifying the treatment of agreements by combining sections 45 and 47, there may also be a difficulty arising from the principles used by the court to establish the

[63] *Monroe Topple & Associates Pty Ltd v Institute of Chartered Accountants (Australia)* (2001) ATPR (Digest) 46-212; *Kernel Holdings Pty Ltd v Rothmans of Pall Mall (Australia)* (1991) 217 ALR 171
[64] *Australian Competition and Consumer Commission v Australian Safeway Stores Pty Ltd* (2003) 129 FCR 339.
[65] (2003) 131 FCR 529.

existence of an agreement. Identifying a contract poses the least problem, assuming one overlooks the potential application of the common law doctrine of illegality, an approach sanctioned in *Leahy*.[66] However, cases based on establishing the existence of an arrangement or an understanding pose greater problems

5.1 British Basic Slag and the meaning of 'agreement'

The decision by the Court of Appeal in ***British Basic Slag*** provides the basis for establishing the existence of an agreement,[67] even though the legislation under consideration in that case (the ***Restrictive Trade Practices Act 1956*** (UK)) referred to agreements and arrangements and made no reference to understandings. This case concerned eight steel producers each of whom held shares in British Basic Slag. Each company had agreed independently to supply all of its slag (the waste material resulting from processing iron ore in a blast furnace to make steel) to British Basic Slag under identical terms and not to supply it to any other party without the agreement of British Basic Slag. Despite having met and discussed drafts of the agreements, the steel producers claimed that there was no agreement between them. The court therefore had to decide what constituted an agreement. Diplock L.J. stated that an agreement involves a ***meeting of the minds*** and ***mutuality*** such that each party would consider itself under a legal or moral obligation to conduct themselves in a particular way.[68] Further, an agreement requires that 'parties to it should have communicated with one another, and that as a result of the communication each has intentionally aroused in the other an expectation that he will act in a certain way'.[69]

To put this into context, the UK Restrictive Practices Act applied to agreements "between two or more persons" "under which restrictions are ***accepted*** by two or more parties" [emphasis added]. Only the former is required under the Australian Act. Despite this, Australian courts have followed the approach of ***British Basic Slag*** when assessing whether or not an agreement exists.

5.2 Application of British Basic Slag in Australia

[66] Which is exactly what Gray J suggested should happened in ***Australian Competition and Consumer Commission v Leahy Petroleum Pty Ltd*** (2007) 160 FCR 321, [25].
[67] ***British Basic Slag Ltd v Registrar of Restrictive Trading Agreements*** [1963] 2 All ER 807.
[68] Ibid, 819.
[69] Ibid, 809

In 1975 in *Top Performance Motors,*[70] a case brought under ss.45 and 46 of the TPA in the Australian Industrial Court, Top Performance Motors needed to establish the existence of an arrangement or understanding between itself and its dealer. Smithers J adopted the approach used in British Basic Slag. He stated:

> [T]he existence of an arrangement…is conditional upon a meeting of the minds of the parties to the arrangement in which one of them is understood … as undertaking, in the role of a reasonable man, to regard himself as being in some degree under a duty, moral or legal, to conduct himself in some particular way…[and] …an understanding must involve the meeting or two or more minds. Where the minds of the parties are at one that a proposed transaction between them proceeds on the basis of the maintenance of a particular state of affairs or the adoption of a particular course of conduct, it would seem that there would be an understanding within the meaning of the Act.' [71]

Similarly, in 1979 in *Nicholas Enterprises*[72], consistent with Willmer LJ in *British Basic Slag*, Fisher J stated that what was necessary for establishing the existence of an agreement was for 'each of the parties to have communicated with the other, for each to have raised an expectation in the mind of the other, and for each to have accepted an obligation qua the other'.[73] He found that an understanding had been reached between the Morphett Arms Hotel and Nicholas Enterprises. However, on appeal (*Morphett Arms 1980*) while the Full Court agreed with Fisher J. that an arrangement involved mutual obligation, it did not consider that mutuality of obligation was required in order for there to be an understanding.[74]

5.3 Requirement for Communication

Going forward, the courts have generally required communication between the parties and acceptance of mutual obligations by the parties. In 1980 Lockhart J. delivered judgement in the *Email* case[75] Email and Warburton Franki were the only Australian suppliers of electricity transformers at the time. Email was recognised as the market leader, while the circumstances of Warburton Franki were such that it had no choice but to follow Email. The practice had grown up

[70] *Top Performance Motors Pty Ltd v Ira Berk (Queensland) Pty Ltd* (1975) 5 ALR 465.
[71] Ibid, 469.
[72] *Trade Practices Commission v Nicholas Enterprises Pty Ltd (No 2)* (1979) 26 ALR 609.
[73] Ibid 629.
[74] *Morphett Arms Hotel Pty Ltd v Trade Practices Commission* (1980) 30 ALR 88.
[75] *Trade Practices Commission v Email Ltd* (1980) 31 ALR 53.

of the two companies exchanging their price lists. The TPC alleged that this amounted to a price fixing agreement.

Despite the exchange of price lists (communication) Lockhart J. declined to find an arrangement or understanding. He found that 'Email did not believe that Warburton Franki would be in breach of an obligation…if it did not send price lists to Email or tender in accordance with its own price lists'[76] That is, there was a lack of mutuality or obligation in the conduct. Thus, based on ***British Basic Slag,*** and not withstanding the views expressed by the Full Court in ***Morphett Arms,*** Lockhart J stated that:

> there is a fundamental distinction between a hope or prediction of future behaviour on the one hand and the expectation of certain behaviour on the other; that is, behaviour which, as a result of communication between the parties, the party restricted is at least morally bound to adopt.[77]

Instead His Honour concluded that the sending of price lists was undertaken unilaterally and for sound commercial reasons – indeed, it tended to improve the operating efficiency of the market.[78]

Later in ***Geelong Petrol***, Gray J, rejecting suggestions that an arrangement can be tacit, stated:

> The ordinary understanding of what amounts to an 'arrangement' makes it difficult to envisage that an arrangement could come about without express negotiations between the parties… At the very least, there must be some express communication between the parties… even if the acceptance by one party of what the other has communicated is implicit in some act, rather than expressed in words. [79]

5.4 Evidence

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[76] Ibid, 69.
[77] Ibid, 66. See also *Stationers Supply Pty Ltd v Victorian Authorised Newsagents Association Ltd* (1993) 44 FCR 35.
[78] Again in *Radio 2UE Sydney Pty Ltd v Stereo FM Pty Ltd* (1982) 44 ALR 557, Lockhart J stated: 'There can be no arrangement without each of the parties communicating with each other and raising an expectation in the mind of the other. Otherwise there is no requisite meeting of the minds. There must be a consensus as to what is to be done and not just a mere hope as to what might be done or happen. Independently held beliefs are not enough' (at 566). As this matter involved a contract to produce a combined rate card to attract advertising whether an agreement existed was not an issue. Re Radio 2ue Sydney Pty Limited v Stereo FM Pty Limited (1982) and 2 Day-Fm Limited [1982] FCA 206; (1982) 62 FLR 437 (15 October 1982).
[79] Gray J, *Australian Competition and Consumer Commission v Leahy Petroleum Pty Ltd* (2007) 160 FCR 321, [26].

Having generally adopted the requirements of communication and mutual obligation as the essential features of an arrangement or understanding, the issue becomes an evidentiary one. Of course, this is not a problem where there is a written contract or agreement.[80] However, where no written record exists, and not withstanding the ability of the court to make an inference from the circumstances (see below), if oral exchanges are disputed, the court is likely to find that mutual obligation is lacking, especially where economic theory can be drawn upon to explain away parallel conduct.[81] This is somewhat spectacularly illustrated in *Geelong Petrol,* a case that provides insight into the evidentiary difficulties in establishing the existence of an arrangement or understanding. In his judgement in this matter Gray J stated:

> [T]he ACCC placed much emphasis on the proposition that what was being passed in the communications between competitors was advance notice of prices to be adopted, as distinct from notice by means of price boards of prices already being charged… [P]rivate communication of intended price increases, without communication of the intention to potential purchasers… does not constitute price-fixing, in contravention of s 45(2) of the Trade Practices Act, without more. Advance notice of the proposed implementation of a decision already made to increase prices would provide a competitor with the advantage of more time, but cannot itself be indicative of the existence of an arrangement or understanding containing a provision to fix prices. There are additional elements that need to be established before a finding can be made that an arrangement or understanding exists, or that effect is being given to it."[82]

The ACCC relied on direct evidence, circumstantial evidence, and admissions to establish the alleged arrangements or understandings. For various reasons the evidence presented was found wanting. Gray J observed:

> One curious feature of the case is that… [c]ounsel for the ACCC did not invite any witness to give evidence of his own state of mind on receiving information about a prospective price increase, as to whether he felt constrained to act on the information, or about whether he

[80]For example, in *Rural Press* the evidence put to the court was the minutes of a meeting, which recorded that Bridge Printing and Waikerie Printing had entered into a non-compete agreementHowever, he court seems to have based its findings on correspondence between the parties.
Australian Competition and Consumer Commission v Rural Press Ltd [2001] FCA 116 [2001].
[81] See, eg, George Hay, 'Practices that Facilitate Co-operation' in J Kwoka and L White (ed), *The Antitrust Revolution* (Foresman 1989).
[82] (2007) 160 FCR 321, [924] – [925].

> regarded the person providing the information as constrained to act on it… These subjects were left to those cross-examining.[83]
>
> The ACCC invited me to draw the inference from the circumstantial evidence that, in fact, such a commitment or obligation did exist in the case of each alleged arrangement or understanding. For numerous reasons …the circumstantial evidence does not point to this conclusion. Even if it did, it would not do so with sufficient strength to cause me to disbelieve the oral evidence on this issue. The situation was that each party to each alleged arrangement or understanding was free to do as it wished on every occasion when information about a prospective price increase was passed to it.[84]

5.5 Inferring the existence of an agreement

The difficulty of proving the existence of an agreement is somewhat mitigated in that courts may be prepared to infer the existence of an agreement. In ***Email*** (discussed above) it was accepted that '[p]arallel conduct may constitute circumstantial evidence from which an arrangement or understanding may be inferred … [but] when a credible explanation is given by the defendant it may be sufficient to negate the inference of an arrangement or understanding'.[85] In that case the court refused to infer the existence of an agreement. The forwarding of the price lists, and the parallel conduct that followed, were explained by the nature of the particular market in question.

The courts have also been prepared to infer the existence of an agreement between competitors from the fact that they have all knowingly entered into identical vertical agreements. For example, in ***News Ltd v Australian Rugby League Ltd (No. 2)***[86] the Court of Appeal inferred the existence of an arrangement. In response to rumours that a new rugby league competition might be introduced by News Ltd (Super League), the Australian Rugby League (ARL) required currently admitted clubs to sign commitment agreements obliging them to play in the ARL for five years. The court was prepared to infer the existence of agreement because '[e]ach club signed and returned its Loyalty Agreement in the knowledge and expectation that every other club would do the same'[87]

[83] Ibid [940].
[84] [948].
[85] (1980) 31 ALR 53, 56.
[86] (1996) 64 FCR 410.
[87] Ibid, 559.

and did so as a means of 'achieving unity and showing each other commitment and loyalty'.[88] Essentially the court viewed the ARL as coordinating the horizontal agreement between the clubs – a hub and spoke arrangement.

The *News Limited* decision contrasts with the *Newsagents Association* decision.[89] Although it was established that there were identical vertical agreements between various newsagents individually and Newspower Victoria, and that acceptance of the individual agreements would not be forthcoming if it were regarded as unlikely that other newsagents would join, Ryan J refused to infer from this a horizontal arrangement or understanding. He stated:

> Clearly, there must have been an expectation that other newsagents would participate in the "Newspower" arrangements. However, an expectation of that kind does not carry with it an understanding, arrived at between newsagents, to enter into membership agreements. The applicant must go further and establish an understanding between newsagents because Newspower Victoria and newsagents are not, as between themselves, competitors in any market.[90]

5.6 What about understandings?

The prohibition against anti-competitive understandings was introduced in 1977,[91] when the notion of combinations and conspiracies was replaced with arrangements or understandings. However the Explanatory Memorandum accompanying the 1977 amendments provide no guidance as to how understandings were intended to differ from arrangements. It is clear that contracts, arrangements and understandings as referred to in the TPA were seen as existing along a continuum of formality.[92] Further it is worth noting that contracts and arrangements are said to be made whereas understandings are said to be arrived at. However, the consequence of adopting the approach used in British Basic Slag in effect has been to convert "arrangements" into unenforceable contracts and to leave little independent role at all for 'understandings".

[88] Ibid, 564.
[89] *Stationers Supply Pty Ltd v Victorian Authorised Newsagents Association Ltd* (1993) 44 FCR 35.
[90] Ibid, 61.
[91] *Trade Practices Amendment Act 1977* (Cth).
[92] For a discussion of this see Caron Beaton Wells and Brent Fisse, 'Broadening the Definition of Collusion: A Call for Caution' (2010) 38 *Federal Law Review* 71.

In *AMA WA*, the ACCC alleged that the Australian Medical Association of Western Australi**a** Branch Inc arrived at an understanding with Mayne Nickless Limited (Health Care of Australia), to fix the prices for the supply of certain medical services to public patients at the Joondalup Health Campus.[93] In his judgement in this matter, Carr J opined:

" The authorities to date do not explain what difference (if any) there is between an understanding or an arrangement. It may be that the evidence required to establish an understanding is somewhat less than that required to prove an arrangement. Perhaps an understanding is a less formal, looser concept than an arrangement."[94]

The ACCC's failure to draw a distinction between an arrangement and an understanding relieved Carr J of the need to consider the evidentiary implications of the distinction further. However, his observation is not entirely accurate. For example, in 1980 Bowen C.J. in *Morphett Arms Hotel* was of the view that:

> [O]ne could have an understanding between two or more parties restricted to the conduct which one of them will pursue without any element of mutual obligation, insofar as the other party or parties to the understanding are concerned.[95]

Bowen CJ's comments are consistent with Lockhart J's observation in *Service Station* that 'the proposition that a relevant agreement must involve positive and clearly reciprocal obligations … is clearly erroneous'[96] and Lindgren J's review of the relevant authorities in *ACCC v CC (NSW) Pty Ltd* that led his Honour to conclude that '[t]he cases require that at least one party 'assume an obligation' or give an 'assurance' or 'undertaking' that it will act in a particular way'.[97] His Honour's observation was cited with approval by the Full Federal Court in *Rural Press.* [98]

Further, albeit in a decision handed down after *AMA WA*, in *Leahy*, Gray J highlighted one further difference between understandings and arrangements:

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[93] *Australian Competition and Consumer Commission v The Australian Medical Association Western Australia Branch Inc* [2003] FCA 686, [8].
[94] Ibid, [186]. His Honour quoted Franki J in *Trade Practices Commission v TNT Management Pty Ltd* (1985) 6 FCR 1 who stated: ' I would not necessarily reject a proposition that the requirements for entering into an understanding may be somewhat different and more easily satisfied than the requirements for making an arrangement', 25.
[95] (1980) 30 ALR 88,
[96] (1993) 44 FCR 35, [92]
[97] Ibid, [141].
[98] *Rural Press Ltd v Australian Competition and Consumer Commission* (2002) 118 FCR 236, [79].

"However broad and flexible an understanding might be, for the purposes of s 45(2)(a) of the Trade Practices Act it must be a consensual dealing between parties. ..Unlike an arrangement, it can be tacit, in the sense that it can be arrived at by each party, either by words or acts, signifying an intention to act in a particular way in relation to a matter of concern to another party. In order to be a consensual dealing, however, an understanding must involve a meeting of minds. [99]

So, although some attempts have been made to distinguish arrangements from understandings (namely that the latter can be established without proving that all parties have accepted commitments and without leading evidence of express communication between the parties), the most problematic evidential issue, the need to establish that one or more of the parties has made a commitment to act in a particular fashion, remains.[100] If an understanding must be shown to involve a meeting of minds, cases where the applicant has claimed the existence of an understanding, are likely to fail. The issue is one of evidence – a wink and a nod may pass between the parties but they are probably not observed by anyone else while the 'acts' to which Gray J refers often have alternative interpretations unrelated to anti-competitive conduct.

Section 5: Tacit Collusion and Understandings

Section 5 makes it clear that the courts are wedded to the interpretation of agreements contained in *British Basic Slag.* In today's economy communication (or an understanding) may be the product oflong periods of coexistence within a market rather than a single interaction. This raises for consideration the difficulty of addressing tacit collusion. Thus, leaving aside the possibility of merging the prohibitions against vertical and horizontal agreements, the forthcoming root-and-branch review should devote serious attention to the issue of signalling. The prices and price movements of firms within a market may be correlated for various reasons. First, common cost or demand conditions may drive the prices of all of the firms in the market. Second, in oligopolistic markets firms take into account the strategies of their rivals and so price movements may be coordinated but as a result of independent decision-making – referred to as conscious parallelism. Third, prices and price movements may be correlated due to collusion between the firms in the market. This may be achieved through explicit collusion. Alternatively, in some circumstances, firms may be able to collude without explicit communication between them, that is, they collude

[99] (2007) 160 FCR 321 [28].
[100] Arguments, based on the interpretation given to the phrase 'understanding' in the context of taxation legislation, that it should not be necessary to prove commitment have been expressly rejected by the courts: (2007) 160 FCR 321, [33].

tacitly. The term tacit collusion combines a process component (tacit 'agreement') with an outcome (collusion).[101]

As Green, Marshall and Marx note:

> Each firm realizes that its profits depend not only on its own actions, but also on the actions of its rivals. It is possible that firms, each possessing this insight and understanding that its competitors all possess it, might be able to succeed in the implementation or even establishment of a collusive agreement without communication.[102]

Further:

> Tacit collusion can arise when firms interact repeatedly. They may then be able to maintain higher prices by tacitly agreeing that any deviation from the collusive path would trigger some retaliation. For being sustainable, retaliation must be sufficiently likely and costly to outweigh the short-term benefits from "cheating" on the collusive path. These short-term benefits, as well as the magnitude and likelihood of retaliation, depend in turn on the characteristics of the industry.[103]

While explicit collusion or cartel conduct is specifically prohibited and penalties for such conduct have increased significantly in recent years, tacit collusion associated with oligopolistic market structures remains largely unscathed by legal prohibitions.[104]

For collusion to occur, it is necessary to have means by which to initiate coordination and then to implement it. With explicit collusion this is achieved by communication which occurs at both stages.[105] But with tacit collusion coordination occurs in the absence of direct communication and hence without the reaching of any specific agreement. Green et al[106] distinguish between the legal requirements for tacit collusion – communication at the initiation stage but not at the

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[101] Nicolas Petit, 'The Oligopoly Problem in EU Competition Law' in Ioannis Lianos and Damien Geradin (eds), *Handbook on European Competition Law: Substantive Aspects* (Edward Elgar, 2013), 259.
[102] Edward J. Green, Robert C. Marshall, and Leslie M. Marx, Tacit Collusion in Oligopoly, August 2013, 2. Available at: https://faculty.fuqua.duke.edu/~marx/bio/papers/tacitcollusion.pdf .
[103] Marc Ivaldi, Bruno Jullien, Patrick Rey, Paul Seabright, Jean Tirole, The Economics of Tacit Collusion, March 2003,.5. Available at http://ec.europa.eu/competition/mergers/studies_reports/the_economics_of_tacit_collusion_en.pdf
[104] See also the signally prohibitions contained in Div 1A of the CCA, which at present only apply to the banking industry. The application of the signalling laws can be extended to other industries by way of regulation.
[105] Although tacit collusion may be said to exist even if there is no communication at the initial stage.
[106] Green et al, above n, 108.

implementation stage – and the economic approach which would define tacit collusion as coordination without explicit communication at either stage.

What is not agreed upon amongst economists is the conditions that are required to enable tacit collusion. Clearly, the conditions that are conducive to explicit collusion are also conducive to tacit collusion – few market participants and high entry barriers. However, more is required for tacit collusion to enable joint profit maximization without direct communication. This includes, but is not limited to, the need for repeated interactions between firms, transparent pricing, repeated and regular purchases by buyers who do not behave strategically, and stability in the market.[107] The circumstances that give rise to tacit collusion (or its absence) are often very specific and may be behavioural rather than structural. However, apart from establishing whether the basic conditions for collusion exist, structural aspects of the market will not enable a distinction to be drawn reliably between conscious parallelism and tacit collusion.

Although the mechanism or process by which coordination occurs is different for tacit collusion than for explicit collusion, the effect is the same – reduced welfare. Yet, because there is no arrangement, tacit collusion is not susceptible to Australian competition law, especially given the legal approach to understandings (see above). For economists collusion is identifiable not by looking for the existence of an agreement, but from its effect, that is, enabling prices above competitive levels. The problem with this approach is that this outcome is not unique to tacit collusion. As noted, under oligopolistic conditions, conscious parallelism or market leadership may produce similar outcomes. Thus, the legal position is rather different: 'there must be direct or circumstantial evidence that reasonably tends to prove that (the parties) had a conscious commitment to a common scheme designed to achieve an unlawful objective'.[108]

From a policy perspective, it is often argued that extending the reach of the law (assuming this is possible) to tacit collusion is inappropriate because of the high risk of over-reach in that it will strike down conscious parallelism which is simply a response to the market structure and firms should not be prevented from acting rationally, that is, in their own best interests. Further, it is also claimed that tacit collusion rarely occurs anyway. Petit[109] takes issue with each of these arguments. In relation to the first, he argues that like explicit collusion, tacit collusion results in significant

[107] The more complex selection of the best market strategy, the less likely it is that coordination can occur without some form of communication.
[108] *Monsanto Co. v. Spray-Rite Svc. Corp* 465 U.S. 752 (1984), [20].
[109] Petit, above n 107.

welfare losses and that in other circumstances where welfare losses occur, market intervention often occurs. Thus:

> [C]ompetition laws seek to catch rational market conduct that distorts competition and in turn yields allocative (price), productive (costs) and dynamic (innovation, investment, products) inefficiencies, regardless of its purpose."[110]

Most governments are unlikely to accept such an approach to policy and law that infers tacit collusion from anti-competitive price effects, given the prevalence of oligopolistic markets and hence the degree of market intervention that would be involved. But there is a way to distinguish between conscious parallelism and tacit collusion that could also be used to legally identify tacit collusion. Posner observed that tacit collusion is a strategy that oligopolists deliberately choose.[111] The difference between 'the oligopoly problem' (conscious parallelism) and tacit collusion is that there is a deliberateness or purpose associated with the latter which is absent from the former. Additional action is often taken to facilitate, adjust and/or protect a situation of tacit collusion.[112] Facilitating practices include information exchanges, signalling, both horizontal and vertical agreements, financial relationships and technology agreements.[113] To the extent that these practices involve agreements, they could be prosecuted under s.45 or s.47 of the CCA.

However, signalling is unilateral conduct which may result in an understanding but does not of itself involve the making of an agreement, as that term has been interpreted by the courts. Nor does signalling require the signaler to possess substantial market power so signalling is unlikely to contravene s.46 of the CCA even though it may have the requisite anti-competitive purpose. Concern about the ACCC's inability to prove its case in *Geelong Petrol,* together with concerns about parallel conduct in banking caused the government to amend the CCA specifically to address signalling conduct. The *Competition and Consumer Act Amendment Act (No1) 2011* (Cth) came into effect on 6 June 2012. First, it prohibits per se private disclosure of price-related information to a competitor. Second, it contains a general disclosure prohibition, whether public or private, concerning:

i. prices for goods or services to be acquired or supplied by the corporation;

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[110] Ibid, 19.
[111] Richard A. Posner, 'Oligopoly and the Antitrust Laws: A Suggested Approach' (1968) 21 *Stanford Law Review* 1562, 1969. Available at: http://heinonline.org/HOL/LandingPage?handle=hein.journals/jrepale1&div=36&id=&page=
[112] Petit, above n 107, 20.
[113] Petit refers to these in relation to Article 101 of the Treaty on the Functioning of the European Union.

ii. the capacity of the corporation to acquire or supply goods or services; or

iii. any relevant aspect of a corporation's commercial strategy (including discounts, credits, rebates etc),

where the disclosure has the *purpose* of substantially lessen competition. The amendment is another example of the increasingly conduct-specific nature of amendments. Its operation is limited to the banking industry in relation to the taking of money on deposit and making advances of money or loans.[114] What this amendment does do is simply to add a prohibition on a particular form of conduct presumably because that conduct does or may facilitate coordination. In order to avoid the need for specific signalling prohibitions and the other shortcomings of the signalling amendment, is it possible to specify criteria which, if satisfied, indicate with a sufficiently high probability of being correct, that an agreement or understanding should be inferred such that tacit collusion becomes susceptible to the CCA?[115]

The first requirement for identifying tacit collusion is that there has been interaction ('communication') between competitors or potential competitors such that an 'understanding'[116] has been established. 'Innocent' parallel conduct may result in information being available, including to competitors, but it does not involve a deliberate transfer of information to competitors and given this, the focus is on private rather than public transfers. Although this narrowing of scope may be necessary to avoid catching beneficial disclosure to customers, it will fail to catch some relevant anti-competitive conduct. For firms that have operated in the same market for a significant period, that have similar structures and are well-informed, including about competition regulation, signalling through public statements may be sufficient to enable co-ordination. However, this is only likely in a stable market. Further, only information about future price increases or that otherwise relates directly or indirectly to future prices will be relevant.

Second, it must be established that there was a consistent and predictable response to the communication between rivals. If rivals sometimes respond in the expected manner but often do not, a reasonable inference is that the recipient of the signal/communication is making a unilateral decision - one of the factors that most influenced Gray J in *Leahy* to conclude that the communication between the parties did not contravene the Act was that sometimes the service station operators raised prices after receiving a telephone call, but at other times they did not.

[114] There is provision for extension to other industries (Regulation 49).
[115] The following is based on Rhonda L. Smith, Arlen Duke and David K. Round, 'Signalling, Tacit Collusion and s.45 of the TPA' (2009) 17 *Competition and Consumer Law Journal* 22.
[116] As a 'wink and a nod', this is unlikely to satisfy the criteria from British Basic Slag.

Third, it must be shown that the disclosure would be against the firm's or firms' self-interest but for the expectation that rivals will engage in the same conduct and so prices will increase.

Section 6: Conclusions and recommendation

Consistent with its election promise to review competition policy if elected, the Minister for Small Business released draft terms of reference for the review in mid-December, 2013. The review provides an opportunity to consider whether the highly proscriptive nature of Australia's CCA hinders effective protection and promotion of competition. Given this, one area which it would be appropriate to consider is the fragmented treatment of agreements. There appears to be no compelling reason for treating exclusive dealing separately from other agreements. The approach is clearly different from the treatment of agreements in most other jurisdictions – for example, Section 1 of the Sherman Act relates generally to conspiracies likely to damage competition. It is fair to say, however, that the application of the law to vertical agreements has been treated more permissively by the courts in the United States. To the extent that they can be shown to be efficiency-enhancing such agreements are unlikely to be found to breach the antitrust provisions. Although the EU distinguishes between horizontal and vertical arrangements, it does not single out exclusive dealing from other vertical agreements.

A simpler and more comprehensible approach would be to conflate sections 45 and 47. Agreements deemed to be anti-competitive (primary boycotts and resale price maintenance) could also be included in the new general section rather than in separate sections. However, third line forcing should finally cease to be a per se offence. Given the relatively recent amendments to establish the cartel provisions, it seems appropriate that these should remain unaltered for the present but should be subject to review at a later date.

With regard to exemption processes, rather than notification being available for particular conduct, subject to third line forcing becoming competition tested, notification (or a modified version of authorization) could be made available only to small business and it could be made available for all but section 46 conduct. Alternatively, the two avenues for exemption could be replaced by a clearance procedure. Under this, the relevant conduct would be notified to the ACCC with high level identification of its detriments and public benefits. The ACCC would then determine what conduct would be allowed to stand without further investigation at that point, and what would be

subject to more detailed scrutiny. However, this may result in indiscriminate registration, subject to the amount of the registration fee.

Finally, the current provisions relating to signalling should be reviewed. By and large the courts have adopted an approach to identifying understandings that means that they are unlikely to be proven unless one or both parties concede that an arrangement or understanding exists. As discussed, Gray J in ***Leahy,*** in effect extended the concept of communication beyond words to acts in relation to tacit arrangements. Clearly this would include signalling but also other facilitating practices. 'Signalling' would be defined as the private transfer of information to competitors and should be deemed to be collusive if it substantially lessens competition. More generally,

"If communication can be proven, if it can be established that rivals consistently reacted to that communication, if it would be against their interests to act in such a way but for the strong belief that their rivals will responded in a similar manner, and if the effect of the conduct is or is likely to substantially lessen competition, then the court should be prepared to infer the existence of the requisite arrangement or understanding to bring the conduct under section 45."[117]

[117] Smith, Round and Duke, above n 121, 42.