



Notes on the proposed new s 46

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1 Introduction

1 The Draft Report of the Competition Policy Review has proposed that s 46 be re-framed to prohibit a corporation that has a substantial degree of power in a market from engaging in conduct if the proposed conduct has the purpose, or would have or be likely to have the effect, of substantially lessening competition in that or any other market.

2 However, it proposes that this primary prohibition should not apply if the conduct in question:

- a. would be a rational business decision or strategy by a corporation that did not have a substantial degree of power in the market; and
- b. would have the effect or likely effect of the conduct of benefiting the long-term interests of consumers.

3 This paper will examine both the proposed primary prohibition and the defence in the light of the criteria adopted by the Review.

4 The Draft Report states that, in guiding its consideration of whether the CCA is fit for purpose, the Panel has asked the following questions:

- a. Does the law focus on enhancing consumer welfare over the long term?
- b. Does the law protect competition rather than individual competitors?
- c. Is the law as simple as it can be consistent with its purpose?
- d. Does the law strike the right balance between prohibiting anti-competitive conduct and allowing pro-competitive conduct?¹

5 In addition to these criteria, the Panel also states that ‘the language of the law should be clear to market participants and enforceable by regulators and the courts’.² In my opinion, this objective is unattainable. The statutory language of the law relating to misuse of market power in the United States and Europe is very vague. But its meaning has been developed by the courts over decades of decisions. The same thing has happened in Australia. We should be very careful that, in seeking clarity in the statute, we produce a provision that does not achieve the underlying aim of the provision.

¹ Draft Report, p 38.

² Page 187.

2 The proposed primary prohibition

6 The proposed primary prohibition stands up well against the first criterion adopted by the Panel: it focuses on enhancing consumer welfare over the long term and it protects competition rather than individual competitors.

7 The fundamental purpose of laws concerning monopolisation is to prevent businesses gaining a competitive advantage by enhancing their market power. The law should allow large businesses to gain a competitive advantage based on their efficiency; but they should not be able to gain by enhancing their market power.

8 A useful screening mechanism to achieve this purpose is to restrict the focus of the law to businesses that already have substantial market power – because these are the businesses that are most likely to be able to gain through enhancing their market power. Consistent with the law concerning abuse of market power in the United States and Europe, the proposed primary prohibition restricts its focus to businesses that have substantial market power.

9 The proposed primary prohibition states that such a business should not engage in conduct if the proposed conduct has the purpose, or would have or be likely to have the effect, of substantially lessening competition in that or any other market. In my opinion, this suggested prohibition also satisfies the first two criteria proposed by the Panel.

10 The proposal has two principal changes from the current prohibition. In the first place, it adds effect or likely effect to the purpose of the conduct. In my opinion, this change is of no great moment. The Courts have had little difficulty in finding purpose under the current s 46; and one reason for this is that they are ready to infer purpose from the effect or likely effect of the conduct.

11 The second principal change is that the purpose, effect or likely effect is directed at the substantial lessening of competition rather than the current list of proscribed purposes which are:

- a. eliminating or substantially damaging a competitor or the corporation or of a body corporate that is related to the corporation in that or any other market;
- b. preventing the entry of a person into that or any other market; or
- c. deterring or preventing a person from engaging in competitive conduct in that or any other market.

12 This change is consistent with the Panel's criterion of protecting competition rather than individual competitors. Although the current proscribed purposes (b) and (c) focus on competition rather than individual competitors, the first of the current proscribed purposes seems to focus on protecting individual competitors

rather than protecting competition. For this reason, the proposed change from the list of proscribed purposes has some merit.

13 Whether it has sufficient merit to justify a change in the wording of the section is a matter of fine judgment.

14 I turn to the proposed defence.

3 The proposed defence

15 Under the proposal, a corporation can defend itself providing it can establish that the conduct in question:

- a. would be a rational business decision or strategy by a corporation that did not have a substantial degree of power in the market; and
- b. would have the effect or likely effect of benefiting the long-term interests of consumers.

16 In my opinion, the proposed defence performs badly against the criterion of striking the right balance between prohibiting anti-competitive conduct and allowing pro-competitive conduct.

17 As in the United States and under the current provision in Australia, a business can defend itself against a charge of abuse of market power if it can prove to the court that there is a legitimate business rationale for the conduct. Although legitimate business rationale is not framed as a defence under the current Australian provision, in practice (providing it has substantial market power) the defendant has to propose a legitimate business rationale for its conduct; and the plaintiff has then to try to discredit that rationale. The proposal of the Panel to frame legitimate business rationale as a defence merely codifies the current position.

18 However, the proposal requires that, to succeed, the defendant must prove a legitimate business rationale in a particular way: it must establish that the conduct would have the effect or likely effect of benefiting the long-term interests of consumers. In the language of an economist, this means that the defendant must prove that the conduct promotes economic efficiency.³

19 As I explained in a recent paper,⁴ proving that conduct promotes economic efficiency is merely one way in which a defendant might prove that conduct has a legitimate business rationale. However, the defence proposed by the Panel restricts the defendant to only one way of proving a legitimate business rationale – it has to prove that the conduct has the effect or likely effect of benefiting the

³ The Australian Competition Tribunal has considered the meaning of this phrase on a number of occasions. See, for example, *Seven Networks Limited (No 4) 92005* ATPR 42-056, paras 119-138.

⁴ Philip L Williams, “The counterfactual test in s 46”, *Australian Business Law Review*, 41 (2013) 93.

- long-term interests of consumers, that is, it has to prove that the conduct promotes economic efficiency.
- 20 There are certain circumstances in which this defence may result in the prohibition of conduct that is not anti-competitive.
- 21 Consider a refusal to deal by a corporation that has substantial market power. *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd*⁵ provides an example. In that case, Melway was able to prove its legitimate business rationale by pointing to natural experiments – circumstances in which it undertook similar conduct in markets in which it did not have substantial market power. That is, it could prove a legitimate business rationale by proving the first element of the proposed defence without needing to prove that the conduct promoted economic efficiency. Under the new proposal, in order to defend itself, Melway would also have to prove its exclusive distribution system promoted economic efficiency. In my opinion, this would make litigation more complex than is consistent with the underlying purpose of the provision; and it would raise the danger that innocent conduct could not be defended.
- 22 Corporations might refuse to deal for other legitimate reasons that would be difficult to justify under the proposed defence. Consider a corporation with substantial market power that refused to deal with an untrustworthy person. The corporation might refuse to deal because it believed that the applicant would create endless disputes if it were accepted as a business partner. In my opinion, this would be a legitimate business rationale; but it would not be available as a defence under the proposal of the Panel.
- 23 Other cases in which the proposed defence seems to be in danger of condemning legitimate business conduct are those involving predatory pricing. Consider cases such as *Carter Holt Harvey Building Products Group Ltd v The Commerce Commission (New Zealand)* [2004] UKPC 37 (14 July 2004) or *ACCC v Boral Ltd*⁶. Both of these cases involved a firm with market power (it may well have been found to have been substantial in the case of *Boral*) that was faced with a new entrant that was pricing aggressively. The incumbent attempted to stay in the market by pricing below avoidable cost for a period. Suppose that a court had to apply the proposed new provision to the facts in these cases. In both cases, a court may well have found that the incumbent had substantial market power and that its conduct resulted in a substantial lessening of competition – because competitors exited the market during the price war.
- 24 If findings such as these were made, in my opinion the incumbents should be given the opportunity to proffer a business rationale for their conduct so that the court can decide whether that business rationale is legitimate. However, the

⁵ (2001) 205 CLR 1; ATPR 41-805.

⁶ (1999) ATPR 41-715.

proposed defence requires that the business rationale has to be that the effect or likely effect of the conduct is to benefit the long-term interests of consumers. In my opinion, that requirement would be almost impossible to discharge in a predatory pricing case in which low prices for a short period of time forced a competitor out of the market. I am not seeking to debate the conduct of Carter Holt Harvey or Boral in these cases, I am merely attempting to illustrate that the proposed defence is very restrictive in its drafting by restricting any legitimate business rationale to one which promotes the long-term interests of consumers.

4 Conclusion

25 The restructuring of the provision has some merit – although I doubt whether changing the words of the statute will do much to increase the clarity of the law.

26 My concern with the proposed new provision is with the second limb of the defence. In my opinion, this will restrict defendants to a particular kind of legitimate business rationale – that the conduct promotes economic efficiency. This will remove from the business other sources of legitimate business rationales that should be allowed. The danger is that this will lead to finding contraventions where conduct does not lessen competition.

27 I suggest that, if the section is to be redrafted in the form proposed by the Panel, the second limb of the proposed defence be deleted.

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Conclusion

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