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***Competition and Consumer Amendment (Misuse of Market Power) Bill 2016 –  
submission to the Economics Legislation Committee***

The Australian Competition and Consumer Commission (ACCC) welcomes the opportunity to make a submission to the Economics Legislation Committee's inquiry into the *Competition and Consumer Amendment (Misuse of Market Power) Bill 2016*.

The ACCC continues to strongly endorse the proposed, simplified reformulation of the misuse of market power provision of the *Competition and Consumer Act 2010* (CCA) (section 46). This submission focuses on several concerns raised by stakeholders during the public consultation on the Exposure Draft of Competition Law Amendments. It should be read in conjunction with the ACCC's October 2016 letter addressed to the Treasury as part of these consultations (which has been published on both the ACCC and Treasury websites).

The ACCC notes that as part of the Exposure Draft consultation process, stakeholders raised a number of objections to the adoption of a substantial lessening of competition (SLC) test in section 46 of the CCA. This opposition is based on claims that the introduction of an SLC test will prevent or deter competition and restrain large businesses from competing on their merits. Opponents to the reform have also asserted that an SLC test is a novel, and therefore uncertain, test in the context of section 46.

The ACCC also notes that the consultation process revealed little stakeholder support for the proposed mandatory factors in the reformulated section 46. The ACCC remains concerned about the potential impact of the mandatory factors. Our views on this issue are set out in section 6 below.

To assist the Committee, this submission responds to the concerns raised by stakeholders.

## 1. Arguments that section 46 adequately addresses anti-competitive unilateral conduct

The ACCC regards the current section 46 as deeply deficient. It contains elements which make it very difficult for the ACCC or private litigants to successfully take action against firms with market power that are engaging in anti-competitive conduct, and hence provides scope for such anti-competitive unilateral conduct to go unchecked.

This is primarily because the current section 46 contains a requirement that before a party can be found to have contravened the provision it must be established on the balance of probabilities that it has taken advantage of its substantial market power. The take advantage element has proven to be particularly problematic in securing successful court action under this legislation, due to the way in which it has been interpreted by the courts.

It must also be established that the party has engaged in conduct which is for a prohibited purpose (the **prohibited purpose element**). The prohibited purpose element misdirects the prohibition towards conduct intended to impact rivals, when this is part and parcel of competitive behaviour.

### *Take advantage*

The 'take advantage' element has the role of filtering harmful anti-competitive conduct from benign and pro-competitive conduct. Unfortunately, the take advantage element has developed into a deeply flawed filter that over-corrects the provision to the other extreme by permitting serious anti-competitive conduct.

In seeking to use the take advantage element as a filter, the Australian and New Zealand Courts have undertaken complex counterfactual analyses and as a consequence, a firm with substantial market power need only show that the conduct it engaged in is conduct that a small firm would also engage in, in order to avoid breaching the prohibition.

This is highly unsatisfactory as it ignores the very different consequences that flow from the conduct undertaken by a large firm compared to a small firm in same the market.<sup>1</sup>

The ACCC also notes the take advantage element can produce outcomes that do not accord with the application of misuse of market power laws in other nations. In the US for example, Microsoft was prevented from forcing Windows users to install other Microsoft products, and hence to exclude the use of alternative software. Lifting these restrictions has led to the development of many diverse software offerings. Under current Australian law, the take advantage test would very likely not have been satisfied because firms without market power can bundle products in the same way that Microsoft did.

### *Prohibited purpose*

Section 46 currently prohibits conduct by a firm with substantial market power that has the purpose of harming actual or potential rivals or otherwise limiting competitive conduct by those rivals. However, it is a natural consequence of robust competition that more efficient firms damage less efficient firms by attracting customers and increasing their market share. Striving to grow, succeed and acquire market share and potentially market power at the expense of one's rivals is what drives competition and innovation. In reality, many actions taken by dominant firms could be considered to have the purpose of harming rivals.

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<sup>1</sup> Stuck, Cross, Douglas Richards, Weber Waller, *Use of Dominance, Unlawful Conduct, and Causation Under Section 36 of the New Zealand Commerce Act: A U.S. Perspective*, (2012) 18NZBLQ, 'whether firms with or without market power would have engaged in that conduct does not necessarily preclude anticompetitive purpose or effect', noting the court in *Berkey Photo, Inc. v. Eastman Kodak Co* (603 F.2d 263, 275 (2nd Cir. 1979)), 'Such conduct is illegal when taken by a monopolist because it tends to destroy competition, although in the hands of a smaller market participant it might be considered harmless, or even "honestly industrial".' Note that section 36 of the New Zealand *Commerce Act* is relevantly identical to section 46 of the CCA.

Hence the current legislation imposes the further requirement that a firm must be shown to be taking advantage of its substantial market power.

**Attachment 1** provides examples of anti-competitive conduct that the current section 46 of the CCA may not be able to address.

## **2. Arguments that an SLC test is novel or uncertain**

An SLC test is neither novel nor uncertain. To the contrary, it is a well-established and well understood test that is applied in the majority of the other competition provisions of the CCA, including anti-competitive agreements, mergers and acquisitions. It has a demonstrated ability to effectively filter harmful anti-competitive conduct from benign or pro-competitive conduct. The introduction of an SLC test into section 46 will merely allow the ACCC and the Courts to apply this clear and effective test to a broader range of conduct than is the case at present.

The inclusion of an SLC test in section 46 will mean that dominant Australian businesses will be required assess their unilateral conduct in a similar way to that in which they already assess their contracts, covenants and acquisitions. Further, it is a test applied internationally to conduct and so will also be well understood by multinational firms carrying on business in Australia.

## **3. Arguments that adopting an SLC test will prevent or deter competition**

The adoption of an SLC test will not restrain large businesses from competing on their merits, reduce productivity, chill investment or lead to higher prices. The adoption of an SLC test will appropriately target anti-competitive conduct. Conduct that enhances competition or is benign, by definition, does not substantially lessen competition and will not be captured by the proposed SLC test.

Competition, by its very nature, is deliberate and ruthless. Advantages gained through research and development, innovation or economies of scale do not lessen competition, even if the conduct causes harm to competitors or forces them to exit a market.

- Investing in improved technology and lowering prices is a normal part of the competitive process that increases efficiency and will increase rather than lessen competition.
- Passing on lower prices to consumers arising from increased efficiency is a normal part of the competitive process and will increase rather than lessen competition. This is the case even where the prices are at a level that competitors find hard to sustainably match. Retailers adopt pricing strategies to promote their competitive position and increase their share of the contestable market; such strategies can include loss leading and national pricing where a chain retailer may offer a form of price guarantee. This conduct can be undertaken by firms with market power and those seeking to gain market share. In the majority of cases such pricing strategies stimulate competition and are pro-competitive. The proposed new section 46 with an SLC test will only capture pricing strategies undertaken by a firm with substantial market power where that strategy has damaged the competitive process.
- Expansion by a firm into a new geographic area or into a complementary market that, because of the efficiency or technical expertise of the entering firm, causes others to exit or decide not to enter, is a normal part of the competitive process and will increase, not lessen, competition.

All these examples highlight the ability of an SLC test to appropriately differentiate between harmful anti-competitive conduct, and benign or pro-competitive conduct.

#### **4. Arguments that an SLC test will remove the causal connection between market power and conduct**

The ACCC accepts that removal of the take advantage test and introduction of an SLC test would mean the law would no longer allow dominant firms to engage in conduct only on the basis that the conduct is of a kind that a non-dominant firm would theoretically engage in. Indeed, this is one of the key benefits of the proposed reform.

One of the reasons for unilateral conduct provisions is to take account of the very different competitive and consumer harms that result from anti-competitive conduct by firms with substantial market power as compared to those without. Therefore, it is undesirable that section 46 currently effectively provides a safe harbour for firms with market power to engage in anti-competitive conduct without regard to the consequences of the conduct on competition. A large firm can simply argue that the action it carried out could also be carried out by a small firm, and therefore fails the take advantage test, despite the very different consequences of similar actions undertaken by large and small firms.

#### **5. Arguments that amending section 46 would impose an unreasonable burden upon large business**

The ACCC accepts that amending section 46 to remove the take advantage element and insert an SLC test will expose a very small number of firms – those with substantial market power – to more scrutiny. This additional responsibility is imposed upon firms with substantial market power because of the significant competitive consequences that flow from anti-competitive unilateral conduct by a firm with substantial market power.

However, the conduct would only be restrained to the extent it crosses an internationally recognised threshold of anti-competitive conduct, being that the conduct has the purpose, effect, or likely effect of substantially lessening competition.

The ACCC anticipates that the removal of the current take advantage and prohibited purpose tests, and the substitution of an SLC test, would improve the efficacy of section 46, and therefore the efficiency and effectiveness of the Australian economy.

#### **6. Mandatory factors**

The draft legislation being considered by Parliament includes the addition of a number of “mandatory factors” that need to be considered as part of the process of deciding whether the actions of a firm are in breach of section 46.

One of these mandatory factors requires consideration of whether “*the conduct has the purpose of, or has or would be likely to have the effect of, increasing competition in that market, including by enhancing efficiency, innovation, product quality or price competitiveness*” in the relevant market.

The ACCC has previously expressed serious concerns with the proposed mandatory factors in an amended section 46.<sup>2</sup>

The ACCC notes that in submissions to Treasury on the exposure draft legislation, the proposed mandatory factors did not receive widespread support from stakeholders, including business stakeholders. For instance, the Business Council of Australia, drawing from an independent legal opinion, stated that the mandatory factors do not provide for additional clarity around how an SLC test should be applied.<sup>3</sup>

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<sup>2</sup> [ACCC letter to the Treasury on the Exposure Draft Consultation on Competition Law Amendments, p. 7, October 2016.](#)

<sup>3</sup> BCA Submission to Treasury on the Exposure Draft of the Competition and Consumer Amendment (Competition Policy Review) Bill 2016, p. 8: [https://consult.treasury.gov.au/market-and-competition-policy-division/ed\\_competition\\_law\\_amendments/consultation/view\\_respondent?uuld=79210900](https://consult.treasury.gov.au/market-and-competition-policy-division/ed_competition_law_amendments/consultation/view_respondent?uuld=79210900)

As the ACCC has previously stated, an SLC test is neither novel nor uncertain. Quite the reverse. It is a well-established test that already applies to other provisions within Part IV of the CCA, and businesses are already familiar with this test. Given this, the proposed mandatory factors are not necessary.

Further, the ACCC considers that the factor relating to efficiency and innovation, will impose additional complex elements to be applied in determining whether there has been a contravention of the section. This creates scope for judicial interpretation about the interaction between efficiencies and competition, and innovation and competition, that could lead to further uncertainty about the application of section 46. Efficiency and innovation are concepts which have not been the subject of judicial consideration in the context of competition law enforcement. Rather they are factors that may constitute a public benefit which are weighed against the detriment resulting from a lessening of competition in an authorisation context. The impact of introducing them into the section 46 test is uncertain and unclear. This factor may provide a potential loophole and will unnecessarily add complexity, making it more difficult for the ACCC, and private litigants, to establish a breach of the revised section 46.

Yours sincerely

Rod Sims  
Chairman

**Attachment 1 – examples of conduct that the current law may not appropriately address**

	<b>Conduct</b>	<b>Why current law unlikely to apply</b>	<b>Why an SLC test will help</b>
<b>A</b>	<p><b>Land banking</b>                      A retailer operates six out of eight retail fuel sites in a major town. The local planning authority has designated four other sites in the town as suitable for the establishment of new retail sites. The retailer buys the first option to purchase all four of the sites before this can occur.</p>	<p>Unlikely to be taking advantage of market power because a firm without substantial market power could also buy the option. In other words, conduct that is designed to protect market power but could be undertaken by a firm without substantial market power is unlikely to breach the current section 46 (<i>Rural Press</i>).</p> <p>There are likely to be legal difficulties with this conduct being captured as an ‘acquisition’ for the purposes of the merger provisions and with the acquisition having an SLC effect.</p>	<p>An SLC test would allow an assessment of whether the conduct has an anti-competitive purpose or effect in the relevant market, including by way of the higher barriers to entry that the conduct is likely to erect.</p> <p>Even if the conduct could be assessed using the ‘effect’ of SLC under the merger provisions, the revised section 46 would allow ‘purpose’ of SLC to also be assessed.</p>
<b>B</b>	<p><b>Locking up supplies</b>                      A firm with 60% total sales in a market enters into long term agreements to lock up 90% of all supplies of an essential ingredient in its production process.</p>	<p>Unlikely to be taking advantage of substantial market power as a firm without market power could enter into such agreements (see <i>Cement Australia</i>). In other words, conduct that is designed to protect market power but could be undertaken by a firm without substantial market power is unlikely to breach the current section 46 (<i>Rural Press</i>).</p>	<p>An SLC test would allow an assessment of whether the conduct has an anti-competitive effect (or purpose) in the relevant market, including by preventing competing producers from growing their production thereby competing with the firm.</p>
<b>C</b>	<p><b>Restricting supplies of essential materials</b>                      A vertically integrated firm with substantial market power refusing to supply downstream competitors</p>	<p>Depends very much on the details but likely to be caught by the current law, although there could be some difficulties in showing take advantage and / or purpose (see and compare <i>Queensland Wire</i> and <i>Melways</i>).</p>	<p>An SLC test would allow an assessment of whether the conduct has an anti-competitive effect, without the complicated use of a counterfactual test to assess whether the conduct constituted taking advantage of a firm’s market power.</p> <p>Assessing whether the conduct has the purpose or effect of substantially lessening competition (rather than whether it amounts to taking advantage of substantial market power) provides a clearer and more predictable test for</p>

			assessing whether the refusal to deal is based on genuine business concerns (such as the credit worthiness of the buyer) or being in engaged in to prevent rivalry.
<b>D</b>	<p><b>Retaliatory threats</b>                  A firm is the only distributor of newspapers to newsagents and convenience stores in town. A distributor of newspapers in a neighbouring town expands its distribution area to compete with the firm. The firm threatens to commence operating in the entrant's distribution area unless the entrant keeps to its own area.</p>	Unlikely to be taking advantage of market power as the firm is using its assets as a distributor to make a threat of retaliation credible, i.e. using its financial power rather than market power (see <i>Rural Press</i> ). Further, if the entrant does not accede to the threat, then there would be no section 45 agreement to assess under the SLC test.	An SLC test would allow an assessment of whether the conduct has an anti-competitive purpose or effect in the relevant market, including by eliminating the threat of entry from a neighbouring distributor (In <i>Rural Press</i> – an SLC was found but no breach of section 46).
<b>E</b>	<p><b>Joint marketing fee</b>                  A retailer with more than 60% of sales in a market asks its suppliers to pay it 20% of sales price in a joint marketing fee. It doesn't impose this requirement on suppliers of products it sells under its home brand.</p>	Unlikely to be taking advantage of market power as any retailer could ask suppliers to contribute to marketing expenses.	An SLC test would allow an assessment of whether the conduct has an anti-competitive purpose or effect in the relevant market, including by imposing considerable additional costs on suppliers that compete with home brand suppliers.
<b>F</b>	<p><b>Freezing out competing suppliers from retail display and demonstration opportunities</b>                  A retailer with more than 60% of sales in a market discriminates in favour of its own brand products in relation to in-store placement and promotions.</p>	There may be difficulties with showing taking advantage and / or purpose. Alternatively, an unconscionable conduct case where the targets of the conduct are large suppliers of proprietary brands would be challenging (and not available at all where the suppliers are listed companies).	An SLC test would allow an assessment of whether the conduct has an anti-competitive purpose or effect in the relevant market, including by making it more difficult for suppliers of proprietary brands to compete with home brand products.
<b>G</b>	<p><b>Targeted price discounting strategies by an incumbent, designed to dissuade new entrants in a region</b>                  Possible predatory pricing by a dominant firm.</p>	If truly predatory, i.e. below relevant costs of supply and targeted at potential competitors, this conduct would be picked up by the current law.	An SLC test would allow an assessment of whether the conduct has an anti-competitive purpose or effect, without the complexities of demonstrating below cost pricing. Assessing whether the conduct has the purpose or effect of substantially lessening competition (rather than whether it amounts to taking advantage of

			substantial market power) provides a clearer and more predictable test for assessing whether the price discounting is a genuine competitive response or being in engaged in to prevent rivalry.
H	<b>Tying up customers in long term contracts with anti-competitive rebates</b>	Depending on the detail this could fall within the current law.	<p>An SLC test would allow an assessment of the conduct through the prism of the SLC test.</p> <p>Assessing whether the conduct has the purpose or effect of substantially lessening competition (rather than whether it amounts to taking advantage of substantial market power) provides a clearer and more predictable test for assessing whether the use of rebates is competitive conduct or being in engaged in to prevent rivalry.</p>