



Australian
Competition &
Consumer
Commission

Reinvigorating Australia's Competition Policy

**Australian Competition & Consumer Commission
Submission to the Competition Policy Review**

25 June 2014

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1 Executive summary

The Australian Competition and Consumer Commission (ACCC) considers that the National Competition Policy (NCP) and related reforms have been critical to Australia's economic performance and rising living standards over the last two decades. The NCP reforms relating to infrastructure alone were estimated to have permanently increased Australia's GDP by 2.5 per cent.

While Australia can be proud of its past economic performance, there are challenges ahead, not least more recent declines in the nation's productivity as the public policy focus on competition and other incentives has declined. There is no better time, therefore, to build on the success of these earlier reforms and reinvigorate Australia's competition policy.

Reinvigorating Australia's competition policy involves removing regulatory barriers to competitive market structures and improving price signals, amending the *Competition and Consumer Act 2010* (Cth) (CCA) to create suitably balanced incentives for market participants, and ensuring that institutional settings sustain competitive processes across markets and governments and over time.

Context: Australia's modern economy

The key challenge facing the original National Competition Policy Review¹ (the Hilmer Review) in the early 1990s was how to spur greater efficiency in non-trade exposed industries. Since that time, many substantial reforms have occurred and the nature of Australia's economy has continued to evolve. As integration with the global economy grows, the structure of Australia's economy continues to shift away from traditional sectors such as manufacturing towards service based industries, with sectors such as agriculture and mining also playing a significant role.

Rapid advancement in technology, particularly digital technologies, is playing a large part in these structural shifts. Future economic growth will be closely connected with the digital age, as technological development lowers barriers to entry across a range of markets, exposing more sectors of the economy to domestic and international competition.

In service industries, online marketplaces are emerging to connect disparate buyers and sellers, in the process disrupting established businesses and expanding or creating new markets. Australian consumers are increasingly drawn to online services and, in many cases, individuals can participate as either consumers or suppliers, or as both, with trades facilitated by online reputation and ratings.

Technology, and the pervasiveness of digital platforms, also provides numerous opportunities in more traditional sectors of the Australian economy. The use of new technologies continues to drive reforms in sectors including roads and shipping (e.g. GPS or other tracking devices on trucks and shipping containers), energy (e.g. smart-grid applications) and health (e.g. remote monitoring to head off emergencies).

Effective competition policy creates incentives for firms to continually drive such innovation for the long term benefit of consumers, and for markets to evolve in response to changing consumer demands.

Microeconomic reform opportunities

The Competition Principles Agreement, agreed to by Australian governments in 1995 following the Hilmer Review, provided the foundation for competition reform in Australia for the ensuing decade.

¹ Independent Committee of Inquiry, *National Competition Policy* (25 August 1993).

Against this background, this submission identifies eight key principles that the ACCC considers are central to an effective and sustained competition policy. These are:

- **Review of regulatory barriers to competition:** Legislation and government policies should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs, and the objectives of the legislation can only be achieved by restricting competition.
- **Architecture necessary to facilitate markets:** In certain sectors (for example, possibly in road infrastructure), governments will need to create the architecture necessary to facilitate trade; for example, as occurred for the national electricity market, and water markets in the Murray-Darling Basin.
- **Structural separation:** Governments should structurally separate natural monopoly from potentially competitive activities, and further separate potentially competitive activities into a number of smaller, independent business units, unless the cost outweighs the benefit.
- **Government or private ownership:** Governments should not retain ownership of business enterprises unless there is a clearly stated public policy reason for doing so, and government ownership is the best way to meet this objective. Most importantly, privatisations should never be driven by budget goals at the expense of creating a competitive market structure.
- **Social and equity objectives:** Targeted social assistance policies are likely to remain necessary. However, governments should regularly review the merits of any community service obligations (CSOs) and the best means for funding and delivering any mandated CSOs.
- **Corporation and competitive neutrality:** If a business is to remain in government ownership despite being a contestable activity, government should establish a corporatised governance structure, and ensure that the business does not enjoy any net competitive advantage simply as a result of its government ownership.
- **Consumer participation:** Successful structural reform of a market may require measures designed to support effective consumer engagement in the market.
- **Economic regulation:** Regulation may be required where competition is not feasible. This may involve access regulation where access to a monopoly service is needed by businesses to compete in upstream or downstream markets, or price regulation where competitive pressures on a supplier of a good or service are not sufficient to achieve efficient prices and protect consumers.

It is, however, in their application that such principles deliver for Australian markets and consumers. In chapter 3 of this submission, the ACCC identifies, by way of example, ten areas where the application of these principles has the potential to drive productivity growth. The first two examples apply across sectors whereas the latter eight are more targeted reforms.

1. Privatisation

There are signs that in privatising assets, Australian governments are focusing overly on short term budget goals without sufficient regard to longer term competition. Governments should consider how the privatisation process can promote competition, for example by separating, rather than integrating, potentially competitive facilities. Governments should also avoid the temptation to boost asset values by privatising without appropriate price and access regulation in place. Such short term financial benefits to governments amount to a tax on future generations of Australians.

2. Regulation and productivity

There are still a number of areas across the economy where the policy purpose of regulation and its associated costs are disproportionate and regulation is limiting productivity. Examples include the ethanol mandate on petrol in NSW, the WA potato marketing corporation and a number of cases of government licensing requirements. Governments should ensure that regulations such as these are reviewed from a competition perspective.

3. Roads

While road reform began during the microeconomic reform agenda of the 1990s, it is far from fully implemented. With current road charging mechanisms and structural arrangements failing to promote efficient decisions by road users and funding bodies, Australia has an opportunity to engage in structural reform of road provision and charging, leading to considerable productivity benefits.

4. Congestion pricing

There are opportunities to enhance the productivity of certain key infrastructure assets such as roads, electricity, ports and airports by greater utilisation of congestion pricing.

5. Shipping

Approximately 99 per cent of Australian imports and exports are transported by sea. Policies currently exist which restrict competition in the shipping industry; they should be reviewed and abolished where appropriate.

6. Energy

While the energy sector has gone through an extensive reform program, the implementation of further reforms, such as privatising remaining government owned assets with the objective of promoting competition, and deregulating retail markets, would further enhance the efficiency of Australia's energy markets.

7. Water

The water sector has gone through a series of microeconomic reforms and water markets now exist in many areas throughout Australia. However, there is scope for further reforms to better define the types of rights available, and to extend the reach of water trading in a range of ways; for example, in more rural areas, between rural and urban regions, and between different water users.

8. Intellectual property

Intellectual property is of increasing importance to Australia's economy. The *extent* of any intellectual property rights should balance:

- on the one hand, the incentives for innovation in the creation of intellectual property; and
- on the other, the incentives that access to intellectual property material provides for efficient use of that intellectual property and for innovation from such use.

A review by the Productivity Commission would assist in this regard. Remaining restrictions on parallel imports should also be removed. The intellectual property related exemption in section 51(3) of the CCA should be repealed, and further consideration given to the effectiveness of current access mechanisms.

9. Human services

There is scope for greater competition in human services, the potential benefits of which may include lower prices, greater efficiency in service provision, greater innovation and improved consumer choice. Mechanisms by which this could be achieved include by facilitating competitive neutrality between private and public providers and also by promoting competition between 'public' providers.

10. Land use

Land use restrictions such as restrictions on the location of retail outlets may affect competition by unduly raising barriers to entry. While some land use restrictions can serve valuable social purposes, they are inappropriate where they are used for the purpose of protecting existing market participants from competition from new entrants.

Enhancing the effectiveness of the CCA

A key plank of effective competition policy is effective competition law. Such laws are critical for preserving the integrity of markets, so that businesses have the incentive to operate more efficiently, price competitively and offer better products to their customers. This in turn delivers benefits to the community through lower prices, innovation, and higher quality products.

Australia will only benefit from a market economy if it works within appropriate boundaries. Competition law must strike a balance between, on the one hand, preventing business activities that undermine the competitive process, and on the other not inhibiting healthy rivalrous behaviour that is part of the ordinary cut and thrust of robust competition. While the ACCC recognises this challenge, it should be stressed that there are large losses from exclusionary, collusive or coercive conduct if the competition law is too weak.

In preparing this submission, the ACCC has had regard to a number of principles that it considers provide a useful framework for assessing whether the competition law continues to promote the welfare of all Australians.

- **Efficient:** Competition law ensures that markets work in an efficient manner by prohibiting businesses from engaging in conduct which undermines the competitive process. The law should prohibit anti-competitive conduct but should also permit conduct which is pro-competitive or more efficient.
- **Universal:** Competition law should apply to all sectors of the Australian economy, other than where a more limited application has been found to provide a net benefit to the public.
- **Clear:** Setting the parameters regarding how businesses may behave to ensure the integrity of markets can give rise to some unavoidable complexities. It is important that the CCA strikes the right balance between complexity and clarity so that the laws remain comprehensible and workable.
- **Effective:** Prohibitions will not act as a deterrent or shape business behaviour where they cannot be readily enforced or where penalties do not act as an appropriate deterrent. To be effective, the prohibitions must be able to be efficiently enforced by the ACCC and private litigants, and penalties must outweigh the gains that businesses may obtain from anti-competitive conduct.
- **Proportionate:** Regulation should be imposed only when it can be shown to offer an overall net benefit. The prohibitions and statutory processes set out in the CCA should

strike a balance between providing a framework which promotes more efficient markets and the regulatory burden imposed upon business.

The ACCC considers that there are several areas where the CCA could be amended to better meet these principles.

Reforms to the competition provisions

Key areas for CCA reform

- Amend the section 46 misuse of market power prohibition to ensure that it is effective in prohibiting anti-competitive conduct by firms with substantial market power. The ACCC considers that this could be best achieved through the introduction of an effects test and amendments to overcome limitations with the application of 'take advantage'.
- Expand application of the 'price signalling' provisions prohibiting anti-competitive disclosure of information throughout the whole economy, not just the banking sector.
- To bring merger authorisation into line with other authorisation provisions, remove first instance merger authorisation by the Australian Competition Tribunal (the Tribunal), to be replaced with merger authorisation by the ACCC with a right of review by the Tribunal.
- Amend the third line forcing provisions to prohibit such conduct only where it has the purpose, effect or likely effect of substantially lessening competition in a market (subject to review and, if necessary, amendment of the Australian Consumer Law to ensure adequate consumer protections remain).
- There are a number of exemptions from the CCA that are no longer appropriate, and others that should be amended to better ensure that the restriction on competition is proportionate and results in a net benefit to the public.
- Amend the CCA to put beyond doubt that conduct which occurs overseas, but which has an anti-competitive effect in Australia, is caught by the CCA. This should include clarification of the circumstances in which an overseas corporation is considered to be 'carrying on business within Australia'.
- There are two key areas in which the ACCC considers greater clarity in the drafting and structure of the provisions would considerably improve the accessibility of the provisions and reduce the regulatory burden: cartel provisions; and the authorisation and notification provisions.

Reforms to the ACCC's investigative powers

The effectiveness of the CCA in discouraging anti-competitive conduct is directly linked to its enforceability. In turn, the investigative tools available to the ACCC are critically important for effective enforcement.

Several investigative tools in the CCA require amendment to ensure that they operate appropriately.

Key reforms to the ACCC's investigative powers

- The ACCC's compulsory information gathering powers under section 155 are of particular importance. Recommended changes include:
 - (i) increasing criminal penalties for non-compliance, and introducing civil penalties;
 - (ii) introducing civil provisions to compel compliance with a section 155 notice;
 - (iii) ensuring section 155 powers apply where appropriate; including in relation to:
 - particular investigative circumstances, such as multi-party investigations; and
 - other ACCC functions under the CCA, such as enforcement of section 87B undertakings, assessment of formal merger clearances and Part IIIA access undertakings.
- To support the ACCC in gathering evidence for investigations, and foster greater detection of anti-competitive conduct, greater protection for whistle-blowers or informants should be provided through:
 - (i) sanctions that better deter intimidation; and
 - (ii) the creation of a third party whistle-blower regime, modelled on the regime in the *Corporations Act 2001* (Cth) (Corporations Act).
- Several more suggested reforms to investigative tools are set out in Attachment A to the submission.

Reforms to assist small business

The ACCC, like all regulators, has a 'dual role'; it both enforces the provisions of the CCA and educates businesses about their rights and responsibilities. Given the particular needs of small businesses, the ACCC provides them with specific resources to address these requirements. The ACCC considers that there are a number of specific amendments to the CCA that would assist small businesses.

Key reforms to assist small businesses

- Extend the unfair contract term provisions in the Australian Consumer Law to contracts involving small businesses.
- Amend the collective bargaining / boycott notification regime to make it more accessible and to allow small business greater opportunities to undertake collective boycotts. The ACCC proposes a number of amendments which will make notifications more flexible and will allow for a greater number of arrangements to be put into effect.
- Amend all prescribed industry codes to improve their enforceability. The ACCC supports the introduction of civil pecuniary penalties, infringement notices and improvements to the audit provisions regarding industry codes.
- Implement a legally enforceable supermarket and grocery industry code of conduct that provides clear rights and obligations.
- Amend the Horticulture Code to improve its coverage.
- Amend the ACCC's educative and research role as provided for by the CCA to better reflect current practices and stakeholder expectations.

The ACCC's submission also outlines further information in relation to specific queries raised by the Issues Paper. The ACCC would be happy to provide the Competition Policy Review Panel with further information regarding any of its functions under the CCA.

Further information to assist the Competition Policy Review Panel

- In response to specific queries raised by the Issues Paper, the ACCC considers that:
 - (i) resale price maintenance should continue to be prohibited outright; and
 - (ii) the potentially negative effects on competition and consumers should be considered in relation to any proposed legislative response to international price discrimination.
- The ACCC has provided information regarding merger processes in Australia, the ACCC's approach to merger review and an overview of merger processes in the European Union and the United States to further inform the Competition Policy Review Panel's consideration of these issues.
- The ACCC has provided further explanatory information regarding the role of market definition in competition matters and other related factors that arise in relation to merger analysis.

Institutions and implementation

The ACCC notes that the framework implemented in the 1995 reforms has been used to guide competition reform in other countries, and could similarly provide the model for future competition reform in Australia.

That experience suggests that there are a number of components which contributed to its success:

1. The use of independent expert bodies to progress reform within the framework agreed to by governments.
2. A shared vision and commitment to a clear set of principles across all Australian governments (Commonwealth, state/territory and local) and across political parties.
3. The Productivity Commission to quantify expected net benefits from the proposed reforms, and impact on government budgets.
4. Where reform to be undertaken by the States/Territories is expected to result in an increase in Commonwealth tax revenue, some distribution by the Commonwealth to the States/Territories of that increase in revenue, subject to States/Territories implementing the reform.
5. A statutory body to undertake monitoring and transparent reporting on outcomes, including where commitments are not being delivered.
6. Tying the intergovernmental commitments to legislation.
7. Targeting social assistance and adjustment packages to facilitate adjustment to, instead of preventing, structural change.

The institutional structure arising from the 1995 reforms has been one of the core strengths of Australia's NCP. This includes the structure of the ACCC, combining competition enforcement, consumer protection and economic regulation into a single, economy-wide body with the single objective of making markets work to enhance the welfare of Australians. This amalgamation of functions is consistent with recent international trends.

One issue consistently raised in Organisation for Economic Co-operation and Development (OECD) assessments of Australia's competition policy framework is that the ACCC, unlike most comparator jurisdictions overseas, does not use market studies to supplement its enforcement function.

The ACCC considers that a broader market study function is needed for the ACCC to assess whether, in particular sectors, competition problems exist or not, and to support better targeted action by the ACCC or others in response.

Market studies

- In 2012, the International Competition Network found that 40 member authorities including, for example, the United States, the UK, European Commission, Japan and Republic of Korea, conduct market studies, and that the number continues to grow.
- Market studies overseas are used:
 - (i) as a lead-in to enforcement action when anti-competitive behaviour is expected but the exact nature and source of the problem is unknown;
 - (ii) to identify a systemic market failure and to better target a response; and
 - (iii) to address public interest or concern about markets not functioning in a competitive way. The market study could either confirm these concerns, and propose some solutions, or find them to be unfounded.

The Hilmer Review significantly improved Australia's productivity and international competitiveness, stimulating job creation and improved living standards for Australians. The ACCC likewise expects the same outcomes from the current Competition Policy Review.

2 Reinvigorating Australia's Competition Policy

The legacy of the Hilmer Review was a competition policy that helped drive the improvement in Australian living standards over the last two decades. However, Australia's productivity growth and its commitment to competition policy have stalled and need to be reinvigorated. In this context, the current Competition Policy Review provides a timely opportunity to refocus on Australia's competition policy agenda. This submission draws upon the ACCC's experience in implementing the 1995 National Competition Policy Reforms to suggest areas for the current Review to explore.

2.1 Objective of the current Competition Policy Review: Improving productivity

In the 1980s and 1990s, financial deregulation and the reduction in trade barriers increased the exposure of many sectors of the Australian economy to international competition. The challenge facing the Hilmer Review was how to spur improvements in efficiency in non-trade exposed industries.

Since this time, the structure of the Australian economy has increasingly shifted away from agriculture and manufacturing towards services, with the mining industry also growing in importance.² Particularly in the service industries, structural change has in part been driven by new technology. As discussed in chapter 3 of this submission, the increasing use of the internet and associated technologies has both exposed Australian businesses to international competition, and opened up new opportunities and markets.³

The four key issues identified by Treasury as confronting Australia in the decade ahead are:⁴

- Australia's deteriorating productivity performance;
- our record, but now falling, terms of trade;
- the ageing of our population; and
- Australia's fiscal position.

Although Treasury also notes that rapid development throughout the Asia-Pacific provides an opportunity.

The Productivity Commission reports that Australia's productivity has stalled since the mid-2000s, with multi-factor productivity declining between 2003-04 and 2012-13.⁵ Australia's productivity performance has been worse than most other developed countries over this period. The improvement in Australia's terms of trade since 2004 has insulated our per capita income from the effect of this decline in productivity.⁶ However, as Australia's terms of trade fall, and our participation rate declines as baby boomers retire, it is only through

² Ellis Connolly and Christine Lewis, *Structural Change in the Australian Economy* (Reserve Bank Bulletin, September Quarter 2010).

³ Peter Downes and Andy Stoeckel, Centre for International Economics, *Drivers of Structural Change in the Australian Economy* (December 2006).

⁴ Dr Martin Parkinson PSM, Secretary to the Treasury, *Fiscal Sustainability & Living Standards - The Decade Ahead* (Speech, The Sydney Institute, 2 April 2014).

⁵ Multifactor productivity is the efficiency of producers based on their use of both labour and capital. While some of this decline in productivity has been attributed to cyclical factors (the increase in investment during the mining boom) and economic shocks (such as drought), some of the decline remains unexplained: Productivity Commission, *Productivity Update* (April 2014). See also Gary Banks, *Productivity Policies: The To Do List* (Economic and Social Outlook Conference, 'Securing the Future', November 2012).

⁶ The length and magnitude of the terms of trade boom (the increase in export prices relative to import prices) is unprecedented in Australia's history: Reserve Bank of Australia, 'Australia after the Terms of Trade Boom', *Bulletin* (March Quarter 2014).

productivity growth that Australia will be able to maintain or grow the 'size of the pie'. Achieving productivity growth is therefore critical to Australian living standards – stimulating job creation and growth in real wages.

2.2 Productivity: Role of competition policy

Economy-wide productivity depends on the productivity results achieved by individual firms. This in turn will depend upon both incentives and enablers such as infrastructure and education.⁷ The key message from the Hilmer Review and subsequent government reviews was that:

- competition provides an *incentive* for firms to improve economic efficiency – to:
 - produce goods and services at least cost (technical or productive efficiency)
 - allocate resources to their highest valued use (allocative efficiency); and
 - innovate to create new products and production processes (dynamic efficiency);
- economic efficiency plays a vital role in enhancing community welfare;
- competition policy is not about the pursuit of competition for its own sake. Rather, it seeks to facilitate effective competition to promote efficiency and economic growth while accommodating situations where competition does not achieve efficiency or conflicts with other social objectives.⁸

Research since the 1990s affirms that these principles should remain at the core of Australia's competition policy.⁹ In particular:

- the Productivity Commission estimated in 2005 that the productivity improvements and price changes in six infrastructure areas, to which the NCP reform was an important contributor, generated a permanent increase of 2.5 per cent in Australia's GDP;¹⁰
- a 2011 study by the Productivity Commission and Australian Bureau of Statistics, using data from the Business Longitudinal Database, found that firms are more likely to innovate if they face stronger competition, and that innovation is associated with better productivity outcomes;¹¹ and
- more broadly, the empirical evidence collated by the OECD across economies shows a positive correlation between product market competition, innovation and economic growth.¹²

⁷ Fred Hilmer, *What's Wrong with Microeconomic Reform Today?* (Sydney Institute, 31 August 2010).

⁸ Hilmer Review pp. xvi & 6. This is reflected in Treasury's wellbeing framework which recognises that wellbeing of Australians goes beyond GDP (the level of goods and services that can be consumed): Treasury, *Treasury Strategic Framework* (2011).

⁹ Alternative economic theories have also emerged such as the 'zero growth theory' (which challenges the equation of economic growth with progress) and 'post scarcity economics' (which challenges the assumption of scarce resources, and thus the role of competitive markets as a mechanism for allocating resources). However, the link between competition, economic efficiency and Australian welfare remains valid.

¹⁰ Productivity Commission, *Review of National Competition Policy Reforms* (Inquiry Report No. 33, 2005). See also ACCC, *Evaluating Infrastructure Reforms and Regulation: A Review of Methods* (ACCC/AER Working Paper Series, Working Paper No 2, August 2010) & *Evaluation of Australian Infrastructure Reforms: An Assessment of Research Possibilities* (Working Paper No 5, December 2011).

¹¹ Productivity Commission and Australian Bureau of Statistics, *Competition, Innovation and Productivity in Australian Businesses* (Research Paper, ABS Catalogue No 1351.0.55.035, 2011). See also Juan Correa and Carmine Ornaghi, 'Competition & Innovation: Evidence from U.S. Patent and Productivity Data' (June 2014) 62(2) *The Journal of Industrial Economic* 258.

¹² Sanghoon Ahn, *Competition, Innovation and Productivity Growth: A Review of Theory and Evidence* (Economics Department Working Papers No. 317, OECD, 2002); Secretariat, Working Party No. 2 on

Policy design can be improved by insights about the drivers of human behaviour including the cost of complexity.¹³ However, the core principle remains that when customers can choose between different providers, they benefit and so does the economy as a whole. In general, insulating firms from the incentive provided by international or domestic competition is a poor public policy for Australia.

2.3 ACCC submission

This submission was prepared by the ACCC in conjunction with the Australian Energy Regulator (AER) in respect of the sections relevant to energy.

The submission is divided into three chapters:

- microeconomic reform (chapter 3);
- CCA reform (chapter 4); and
- institutions and implementation (chapter 5).

Chapters 3 and 4 address two key facets of competition policy.

Microeconomic reform focuses on the role of *government* in promoting competitive market structures and price signals, and the role of economic regulation where competition is not feasible. Chapter 3 sets out principles for promoting competitive market structures in the Australian economy. These principles largely derive from the Hilmer Review but need to be reinvigorated by the current Competition Policy Review. The chapter then identifies, by way of example, ten areas where there is the potential for competition reform to drive productivity growth.

The CCA focuses on rules applying to *private firms* to prevent conduct that insulates a firm from the incentive of competition. Chapter 4 examines principles that may provide a useful framework for assessing whether the existing competition law continues to promote competition for the welfare of all Australians. It then discusses the key areas where the CCA requires reform or improvement in order to ensure that it continues to drive efficient outcomes for Australian consumers and businesses, as well as further information that may assist the Review Panel.

Successful competition reform also depends upon institutional design. Chapter 5 covers lessons that have been learnt since the 1990s on how to ensure necessary competition reforms are implemented, and institutional arrangements including the role and functions of the ACCC.

Rather than attempting to provide the answer to every microeconomic or CCA issue, this submission seeks to identify – based on the ACCC’s experience and observations – some key reforms that will promote the objective of making markets work for the benefit of Australians. The ACCC would be happy to provide further detail on any of the issues raised in this submission, and to respond to issues of interest to the Review Panel.

Competition and Regulation, Competition Committee, Directorate for Financial and Enterprise Affairs, Organisation for Economic Co-operation and Development, *Factsheet on Competition and Growth* (DAF/COMP/WP2(2013)11, 28 October 2013).

¹³ Richard H. Thaler and Cass R. Sunstein, *Nudge: Improving Decisions about Health, Wealth, and Happiness* (Yale University Press, 2008).

3 Microeconomic reform

3.1 Introduction

The Competition Principles Agreement (CP Agreement),¹⁴ agreed to by Australian governments in 1995 following the Hilmer Review, provided the foundation for competition reform in Australia for the ensuing decade.

An important, if not determinative, factor in the success of the CP Agreement was the mechanism that provided for payments by the Commonwealth to the states/territories for implementation of the agreed reforms.¹⁵ The payments recognised the revenue benefits to the Commonwealth from the reforms and were intended to share the benefits with the states/territories.

However, cessation of the payments in 2006 coincided with a noticeable decrease in commitment to the principles in the CP Agreement. Given Australia's declining productivity growth, it is important that Australian governments re-commit to the implementation of principles to foster competitive markets.

Section 3.2 identifies some key principles that the ACCC considers should form part of the intergovernmental commitment to competition. These principles cover:

- Review of regulatory barriers to competition
- Architecture necessary to facilitate markets
- Structural separation
- Government or private ownership
- Social and equity objectives
- Corporatisation and competitive neutrality
- Consumer participation
- Economic regulation

Section 3.3 then identifies, by way of example, ten areas where the application of these principles has the potential to drive productivity growth. The first two examples apply across sectors whereas the latter eight are more targeted reforms.

1. **Privatisation:** There are signs that, in privatising assets, Australian governments are focusing overly on short term budget goals without sufficient regard to longer term competition. Governments should consider how the privatisation process can promote competition, for example by separating, rather than integrating, potentially competitive facilities. Governments should also avoid the temptation to boost asset values by privatising without appropriate price and access regulation in place. Such short term financial benefits to governments amount to a tax on future generations of Australians.
2. **Regulation and productivity:** There are still a number of areas across the economy where the policy purpose of regulation and its associated costs are disproportionate and regulation is limiting productivity. Examples include the ethanol mandate on petrol in NSW, the WA potato marketing corporation and a number of cases of

¹⁴ The CP Agreement covered: oversight of GBEs; competitive neutrality; structural reform of public monopolies; legislation review; access to services provided by means of significant infrastructure facilities; application of the principles to local government; and the operation of the NCC.

¹⁵ Agreement to Implement the National Competition Policy and Related Reforms 1995.

government licensing requirements. Governments should ensure that regulations such as these are reviewed from a competition perspective.

3. **Roads:** While road reform began during the microeconomic reform agenda of the 1990s, it is far from fully implemented. With current road charging mechanisms and structural arrangements failing to promote efficient decisions by road users and funding bodies, Australia has an opportunity to engage in structural reform of road provision and charging, leading to considerable productivity benefits.
4. **Congestion pricing:** There are opportunities to enhance the productivity of certain key infrastructure assets such as roads, electricity, ports and airports by greater utilisation of congestion pricing.
5. **Shipping:** Approximately 99 per cent of Australian imports and exports are transported by sea. Policies currently exist which restrict competition in the shipping industry; they should be reviewed and abolished where appropriate.
6. **Energy:** While the energy sector has gone through an extensive reform program, the implementation of further reforms, such as privatising remaining government owned assets with the objective of promoting competition, and deregulating retail markets, would further enhance the efficiency of Australia's energy markets.
7. **Water:** The water sector has gone through a series of microeconomic reforms and water markets now exist in many areas throughout Australia. However, there is scope for further reforms to better define the types of rights available, and to extend the reach of water trading in a range of ways; for example, in more rural areas, between rural and urban regions, and between different water users.
8. **Intellectual property:** Intellectual property is of increasing importance to Australia's economy. The *extent* of any intellectual property rights should balance:
 - on the one hand, the incentives for innovation in the creation of intellectual property; and
 - on the other, the incentives that access to intellectual property material provides for efficient use of that intellectual property and for innovation from such use.

A review by the Productivity Commission would assist in this regard. Remaining restrictions on parallel imports should also be removed. The intellectual property related exemption in section 51(3) of the CCA should be repealed, and further consideration given to the effectiveness of current access mechanisms.

9. **Human services:** There is scope for greater competition in human services, the potential benefits of which may include lower prices, greater efficiency in service provision, greater innovation and improved consumer choice. Mechanisms by which this could be achieved include by facilitating competitive neutrality between private and public providers and also by promoting competition between 'public' providers.
10. **Land use:** Land use restrictions such as restrictions on the location of retail outlets may affect competition by unduly raising barriers to entry. While some land use restrictions can serve valuable social purposes, they are inappropriate where they are used for the purpose of protecting existing market participants from competition from new entrants.

3.2 Competition principles

The purpose of the CP Agreement was to provide a framework for promoting competitive market structures and behaviour of entities in the Australian economy (competition policy in turn formed part of broader reforms including trade, labour and fiscal policies). The table below summarises the competition principles that should be reinvigorated and taken forward by the current Competition Policy Review. The table uses the electricity sector as an example. While the energy sector in Australia currently faces major challenges from a range of relatively recent events, the creation of Australia's national electricity market (NEM) shows how the competition principles work together to reform a market.

Competition Principle	Example – Electricity sector reform¹⁶
<p>1. Review of regulatory barriers to competition Legislation and government policies should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs, and the objectives of the legislation can only be achieved by restricting competition.</p>	<p>The Australian NEM commenced in 1998. The rules governing the market provide for non-discriminatory entry for new participants in generation and retail supply (see the National Electricity Code (NEC) and the National Electricity Rules (NER) which replaced the NEC in 2005).</p>
<p>2. Architecture necessary to facilitate markets In certain sectors (for example, possibly in road infrastructure), governments will need to create the architecture necessary to facilitate trade; for example, as occurred for the NEM, and water markets in the Murray-Darling Basin.</p>	<p>In 1996, governments established the National Electricity Market Management Company (NEMMCO) to operate the physical dispatch process across the NEM, perform pool settlements and co-ordinate and plan for power system security.</p>
<p>3. Structural separation Governments should structurally separate natural monopoly from potentially competitive activities, and further separate potentially competitive activities into a number of smaller, independent business units, unless the cost outweighs the benefit.</p>	<p>The starting point for most jurisdictions was an integrated electricity utility providing generation, transmission, distribution and retail services. From the early to mid-1990s, jurisdictions implemented a similar set of reforms to: break up generation into several businesses; establish one or more transmission businesses; and establish several retail/distribution businesses, with ring-fencing between the distribution and retail functions. Subsequent developments have varied. In some jurisdictions: retail businesses separated from networks and integrated with generation; and concentration in ownership increased. However, the natural monopoly networks remain structurally separate from more competitive activities.</p>

¹⁶ AER, *State of the Energy Market Report (2007) Part 1 Essay A*; AEMC & KPMG, *National Electricity Market: A Case Study in Microeconomic Reform (2013)*.

4. Government or private ownership
Governments should not retain ownership of business enterprises unless there is a clearly stated public policy reason for doing so, and government ownership is the best way to meet this objective. Most importantly, privatisations should never be driven by budget goals at the expense of creating a competitive market structure.

5. Social and equity objectives
Targeted social assistance policies are likely to remain necessary. However, governments should regularly review the merits of any CSOs and the best means for funding and delivering any mandated CSOs.

6. Corporatisation and competitive neutrality
If a business is to remain in government ownership despite being a contestable activity, government should establish a corporatised governance structure, and ensure that the business does not enjoy any net competitive advantage simply as a result of its government ownership.

7. Consumer participation
Successful structural reform of a market may require measures designed to support effective consumer engagement in the market.

8. Economic regulation
Regulation may be required where competition is not feasible. This may involve access regulation where access to a monopoly service is needed by businesses to compete in upstream or

Victoria separated its State Energy Commission into generation, transmission and distribution/retail companies prior to selling these businesses from 1996 to 1999. The Victorian privatisation process is widely regarded as a well-designed reform.¹⁷ (The broader issue of privatisation in the electricity sector is discussed later in this chapter).

Each jurisdiction undertook an analysis of the electricity CSOs. For example, in Victoria, the review of electricity CSOs prior to the sale of electricity utilities found some non-commercial activities which did not fulfil the criteria for CSOs. Activities that satisfied the criteria were designated as conditions in the retail and distribution licences.¹⁸

The need for competitive neutrality varied across jurisdictions depending on the role of the public sector in the electricity industry. All government businesses in generation, network and retail were corporatised, and all governments set up competitive neutrality complaints units.

The ACCC and the AER, as the bodies responsible for enforcing the Australian Consumer Law and the National Energy Retail Law, have a shared responsibility for protecting consumers so that they have confidence in the energy market. For example, in 2012, under the National Energy Retail Law, the AER developed an online price comparator website to assist small energy customers to compare the electricity and gas offers available to them. In 2011 and 2014, the ACCC authorised an industry code of practice for face-to-face energy sales by electricity and gas retailers (e.g. door-to-door sales).

From commencement, the NEC provided for non-discriminatory access to the interconnected electricity transmission and distribution networks. Retail price regulation was also warranted as an interim step whilst competition in the

¹⁷ See, for example, Graeme Hodge, Valarie Sands, David Hayward and David Scott (eds), *Power Progress: An Audit of Australia's Electricity Reform Experiment* (2004).

¹⁸ Industry Commission, *Community Service Obligations: Policies and Practices of Australian Governments* (Information Paper, February 1997).

downstream markets, or price regulation where competitive pressures on a supplier of a good or service are not sufficient to achieve efficient prices and protect consumers. Principles for the design of economic regulation include:

- (i) *Nationally consistent principles:*
Governments should apply consistent principles to economic regulation. Cooperative regimes may be needed where there is a national integrated market.
- (ii) *Objective of economic regulation:*
The overall object of economic regulation should be to promote the long term interests of Australian consumers.
- (iii) *Emerging competition:*
An essential component of a regime is a mechanism for winding back economic regulation if effective competition develops. Governments also need to address issues arising where substitute services are emerging, resulting in a decline in demand for the regulated service, but there remain captive customers.
- (iv) *Ensuring regulation is fit for purpose:*
The CP Agreement recognises that regulatory regimes may range from monitoring and information gathering to negotiation and arbitration, to upfront determination of terms and conditions.

market evolved to the point where jurisdictions could transition to full retail contestability. (Energy price deregulation is discussed later in this chapter).

Each jurisdiction participating in the NEM enacted legislation to give effect to the National Electricity Law (NEL) including the NEC.

The original list of objectives in the NEC was replaced by a single national electricity objective in the NEL in 2005. The new objective focuses on an efficient national electricity market for the long term interests of consumers.

The NEL and NER provide for certain network service providers to be exempt from the economic regulation requirements in the NER. For those services subject to economic regulation, the NEL sets out two categories: direct control services (subject to price or revenue regulation) and negotiated services. In essence, the form of regulation depends upon the extent of market power. The NEL and NER also set out mechanisms for reclassifying a network service; broadly, through a rule change in the case of transmission services, and through an AER determination in the case of distribution services.

(The issue of declining demand for network services is discussed later in this chapter).

The categorisation in the NEL and NER of unregulated, direct control and negotiated network services¹⁹ allows the form of regulation to be tailored to the extent of the network's market power. In respect of direct control services, the NER was amended in 2012 to allow regulatory determinations to accommodate changing circumstances, and the different characteristics of network service providers.²⁰

¹⁹ In respect of electricity transmission services, the NER defines two categories of regulated services: prescribed transmission services and negotiated transmission. In respect of distribution, the NER provides for the AER to classify a distribution service as a: direct control service (which in turn is divided into two subclasses: standard control services and alternative control services); or a negotiated distribution service.

²⁰ AEMC, *Economic Regulation of Network Service Providers, and Price and Revenue Regulation of Gas Services* (Final Position Paper, 29 November 2012).

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| <p>(v) <i>Pricing principles:</i>
Regulated prices should provide the right incentives to drive economic efficiency.</p> | <p>The NEL sets out revenue and pricing principles which, in essence, focus on promoting economic efficiency in respect of direct control network services. (The issue of the structure of regulated prices is discussed later in this chapter).</p> |
| <p>(vi) <i>Process:</i>
The regulatory process should ensure all interests are represented.</p> | <p>As part of the Better Regulation Program, the AER issued a consumer engagement guideline to ensure that networks identify consumer preferences, and that this drives network decisions. In 2013, the Consumer Challenge Panel was established by the AER to provide an independent consumer perspective to challenge the AER and network service providers during determination processes. Governments have also agreed to create a new, funded, consumer advocacy body, Energy Consumers Australia, which will incorporate the Consumer Advocacy Panel.</p> |

The remainder of this section provides case studies illustrating the significance of these principles to economic outcomes in Australia.

3.2.1 Review of regulatory barriers to competition

A critical competition principle is to ensure that government policies and regulation do not restrict competition unless the benefits to the community outweigh the costs.

The mechanism by which the Hilmer Review intended this to be achieved was the ongoing review by the National Competition Council (NCC) of reform progress. However, as noted above, once the competition payments to the states/territories ceased in 2006, the impetus for this review slowed considerably. There are a number of examples, such as the one below, which show the importance of reviewing markets as they develop, to ensure that regulation does not unnecessarily restrict competition and innovation.

Case study – electricity metering

To date, regulated network businesses have exclusively provided, maintained and owned the majority of electricity meters installed on residential premises. Most electricity metering services have involved basic tasks of installing and maintaining assets, and manually relaying basic consumption data to reconcile market systems.

As highlighted in the Australian Energy Market Commission’s (AEMC) *Power of Choice* review, advances in metering technologies have the potential to fundamentally change the traditional role of metering in the market and expand the range of products and services available to consumers. For example, advanced metering with communication capability (smart meters) are capable of recording consumption on a near real time basis, and differentiating consumption at different times of the day. This can provide consumers with better information about their consumption and more control over how they manage their use. In so doing, advanced metering can support greater consumer participation and choice in the market. Better consumption information can also help consumers weigh up competing retail price offers.

However, the rules around the provision of metering services have not kept pace with these advances in metering technologies. There is currently a degree of exclusivity in who can provide metering services in the NEM. The NER still mandate that regulated networks are exclusively responsible for provision of certain metering services (these are the types 5 and 6 meters, manual interval and accumulation, respectively) which represent the meters that the majority of residential customers have on their premises. The NER also mandates that only retailers can be responsible for provision of other meter services such as types 4 meters (smart meters). Until recently, the NEL and NER have also allowed jurisdictional governments the ability to mandate regulated roll outs of meters, which has created investment uncertainty for commercial businesses looking to enter the metering market.

While these were intended to be transitional measures, largely to ensure that small electricity consumers had effective metering services at the commencement of full retail competition, they still remain. This exclusivity limits competition and innovation in metering services.

The AEMC is currently considering proposed changes to the NER which would allow competition in the provision of metering services. It is expected that these changes will promote greater consumer participation and choice, thereby allowing the potential benefits of advanced metering to be realised.

The ACCC considers that a renewed commitment to legislation and policy review is required by governments at all levels. This should be made in accordance with the principles adopted by Council of Australian Government (COAG) in 2007 as part of its *Principles of Best Practice Regulation*.²¹ This would require governments to:

- identify all regulatory barriers to competition
- establish a case for action before addressing a problem; in particular, a case for action may be established where the market is unable to deliver the desired economic efficiency goal due to, for example, imperfect competition, externalities, public goods, imperfect or costly information or a social or equity goal
- adopt the option that generates the greatest net benefit for the community
- take action that is effective and proportional to the issue being addressed.

The future Australian economic landscape will be closely aligned with the digital age, where the use of new technologies will drive reforms and innovation, at times very rapidly. It would be of concern if Australian government regulation at a commonwealth, state/territory or local government level impeded competition in these markets without an analysis of whether the benefits of regulation outweigh the costs.

The case study below, regarding mobile apps supporting new passenger transportation services, provides an example of where a cost/benefit review in relation to regulation restricting competition would be warranted.

Case study – mobile apps supporting new passenger transportation services

As noted in chapter 2, the use of new technology is a key determinant of Australia's productivity. Mobile apps supporting new passenger transportation services are an example of where a cost/benefit competition review is needed.

The supply of traditional taxi services in countries across North and South America, Europe, the Middle East and the Asia-Pacific (including Australia) has been radically shaken up in recent years. The innovation of mobile apps providing services linking passengers with transportation service providers has provided much needed competition to many of the world's traditional taxi service markets.

²¹ Council of Australian Governments, *Best Practice Regulation: A Guide for Ministerial Councils and National Standard Setting Bodies* (October 2007).

One of the benefits of such services is that they appear to be responsive to passenger needs (making it easier for consumers to locate, arrange and pay for transportation services) and allow provision of services (reliability, cleanliness etc.) to meet unmet consumer demand.

Owners of mobile apps such as that operated by technology firm, Uber Technologies, have been subject to heavy criticism by taxi lobby groups worldwide concerned that the new models could threaten the profitability of traditional taxi services.²² In some countries, Uber and its drivers have been found to be breaching local regulations,²³ and in others it has been effectively banned.²⁴

Competition regulators across the world have expressed concern at measures taken to ban or deter the entry of such firms. The Vice-President of the European Commission noted that a decision by a Brussels court to ban Uber 'is not about protecting or helping passengers – it's about protecting a taxi cartel'.²⁵ The Federal Trade Commission has raised concerns about legislation proposed by Chicago City Council imposing license fees and other restrictions upon operators of mobile apps such as Uber, noting that 'any restrictions on competition that are implemented should be no broader than necessary to address legitimate subjects of regulation, such as safety and consumer protection, and narrowly crafted to minimize any potential anticompetitive impact'.²⁶

3.2.2 Creating architecture necessary to facilitate markets

In some instances, governments may need to not only remove regulatory barriers to competition, but to also undertake reforms to create the architecture necessary to facilitate trade. For example, the mechanisms that were put in place under the NCP umbrella for trade in wholesale electricity, gas and rural water in the Murray-Darling Basin. This could involve definition and allocation of new forms of property rights, corporatisation of aspects of programs traditionally delivered by governments, and/or making certain activities subject to competitive tendering processes.

In essence, the aim is to use the features of a market (such as price and quality, and the threat of competition) to drive more efficient outcomes (such as better investment decisions by governments or private firms, better use of available capacity and better outcomes for users). In the long term, if markets are created in the appropriate way, it is likely that government involvement in the sector will decrease. As discussed in chapter 5, the current Competition Policy Review provides a way forward to identify sectors requiring microeconomic reform.

The structural reform of Australia's road markets is an example of an area where market architecture could be introduced to enhance Australia's productivity. This is discussed below at section 3.3.3.

3.2.3 Structural separation

One of the lessons learnt since the implementation of the Hilmer reforms is that failure to structurally separate natural monopoly functions from competitive activities prior to privatisation by governments can result in significant detriment to consumers and the Australian economy as a whole.

²² For example, taxi drivers have been protesting and striking in Milan, Italy, in protest against Uber. N. O'Leary and I. Binnie, 'Milan Taxi Drivers March Against Silicon Valley Ride-app Uber', *Reuters* (20 March 2014).

²³ *Ibid.* In July 2013, a town council in Milan ordered Uber cars to return to company headquarters between each ride, irrespective of the location of their next passenger. This was later suspended by a regional court that said the rule was 'irrational' given the advent of mobile phones.

²⁴ N. Kroes, *Crazy Court Decision to Ban Uber in Brussels* (15 April 2014) available at ec.europa.eu.

²⁵ *Ibid.*

²⁶ Letter from Federal Trade Commission to City of Chicago dated 15 April 2014, available at www.ftc.gov.

Case study – structural reform in telecommunications

Telstra is in a unique position in the Australian fixed-line telecommunications sector. As an extensively vertically and horizontally integrated provider, Telstra operates at all levels of the supply chain and competes with many of the businesses that it supplies. This structure was established while Telstra was still in government ownership, with no major structural reforms occurring prior to its (eventually completed) full privatisation in 2006. This has given rise to long standing competition concerns around Telstra's ability and incentive to favour its retail business over other service providers accessing its network, to the detriment of consumers.

As an example, Telstra's pricing decisions for its wholesale access services and its own retail services regularly led to concerns that access seekers cannot profitably compete with Telstra in downstream markets (vertical price squeeze conduct). There have also been concerns that Telstra favoured its retail business on performance metrics such as activating services or fixing faults. Further, Telstra's vertical integration created a lack of transparency that made it difficult for the ACCC to effectively enforce competition regulations.

In response to these longstanding concerns regarding the vertical integration in the telecommunications industry, the Australian Government determined that the National Broadband Network (NBN) should operate as a wholesale-only, open access network. Consistent with this objective, legislation was also introduced which provided a framework for the voluntary structural separation of Telstra. Under this framework, the ACCC accepted a Structural Separation Undertaking (SSU) from Telstra in February 2012. The SSU provides for the structural separation of Telstra via the progressive migration of end users from the copper and hybrid-fibre coaxial (HFC) networks as the NBN is rolled out across Australia.

This structural reform, which is currently being implemented, is intended to address many of the long-standing competition concerns. Ensuring a competitive industry structure for telecommunications services is important to promoting efficiency, and ultimately the long term interests of end users. Related issues associated with structural reform in telecommunications are currently being considered by the *Independent Cost-Benefit Analysis and Review of Regulation*, chaired by Dr Michael Vertigan and due to report in June 2014.

The Hilmer Review recommended a presumption in favour of separation at the ownership or control level.²⁷ However, under the CP Agreement, each government merely agreed to review the merits of separation.²⁸

The ACCC considers that governments should structurally separate natural monopoly from potentially competitive activities unless the cost outweighs the benefit.

The Hilmer Review also recommended that governments review the merits of structurally separating potentially competitive activities into a number of smaller, independent business units to facilitate new market entry and competition where there is none.²⁹ This principle is reflected in the CP Agreement.³⁰ The Victorian electricity privatisation process (under which electricity generators were sold individually rather than as a package³¹) provides an example. A further example is the decision by the Commonwealth government, as part of the 1991 telecommunications reforms, to separate the satellite service (AUSSAT Pty Ltd) from Telstra (created by merging Telecom and the Overseas Telecommunications Commission), and to sell AUSSAT to Optus.

²⁷ Recommendation R10.2.

²⁸ Clause 4(c)(2).

²⁹ Hilmer Review p. 222.

³⁰ Clause 4(c)(3).

³¹ See box in section 3.3.1 for more information on this example.

3.2.4 Government or private ownership

The Hilmer Review noted that there is evidence that privatisation may increase the efficiency of many businesses, which is consistent with the overall goals of competition policy.³² More recently, the Productivity Commission also found that the evidence suggests that government owned enterprises are less efficient than their private sector peers.³³ Through competition for capital, private ownership improves a firm's productivity incentive. Privately owned firms have greater incentive and ability to be cost efficient and innovative compared to government owned enterprises.

The Productivity Commission, in its review of electricity networks, sets out a framework for making coherent choices about ownership.³⁴ The strongest rationale for government ownership is where governments find it difficult to write good contracts with private businesses or to regulate them effectively and where those contractual problems can be effectively overcome through government ownership.

The ACCC considers that governments should not retain ownership of business enterprises unless there is a clearly stated public policy reason for doing so, and government ownership is the best way to meet this goal. Section 3.3.6 of this submission provides the example of electricity networks where, as the Productivity Commission states, the rationale for government ownership no longer holds.

However, privatisations should never be driven by budget goals at the expense of creating a competitive market structure or putting in place appropriate access or price regulation. This issue is further discussed in section 3.3.1.

3.2.5 Social and equity objectives

As discussed in chapters 2 and 5 of this submission, competition is a means to achieving economic efficiency. However, governments may have objectives other than economic efficiency. CSOs can play an important role in delivering social and equity protections.

The key is to ensure, as set out in the CP Agreement,³⁵ that social and equity objectives are met in such a way as to minimise the impact on competition and the incentive to improve productivity. For example, CSOs can be funded in a variety of ways including cross-subsidisation (which requires a government business enterprise (GBE) to charge higher prices to some users to recover the losses incurred by supplying the CSO to other users). This distortion of relative prices is likely to result in production and consumption inefficiencies, and requires barriers to entry to prevent competitors entering the high margin markets and undercutting the regulated business. Supporting regulatory measures that restrict entry in these higher margin markets may lead to further inefficiencies.³⁶

Competition policy is not intended to reduce the commitment of governments to effective delivery of CSOs. Instead, it is intended to facilitate a more systematic identification and implementation of these requirements. The ACCC considers that governments should regularly review the merits of any mandated CSOs and the best means of funding and delivering them to minimise the impact on prices signals and competition.

³² Hilmer Review p. 226.

³³ Productivity Commission, *Electricity Networks Regulatory Framework* (Inquiry Report No. 69, April 2013).

³⁴ Productivity Commission, *Electricity Networks Regulatory Framework* (Inquiry Report No. 69, April 2013).

³⁵ Clause 4(c)(6).

³⁶ Industry Commission, *Community Service Obligations: Policies and Practices of Australian Governments* (Information Paper, February 1997).

Case study – Australia Post

Australia Post is facing significant cost pressure in complying with its existing CSOs which are specified in government regulations but are not directly funded by government (except in its capacity as shareholder). In 2012-13, Australia Post estimated the cost of its compliance with CSOs at \$177.5 million. As further discussed below, there may be merit in reviewing the CSOs applying to Australia Post e.g. the requirement for Monday-Friday delivery of letters.

3.2.6 Corporatisation and competitive neutrality

If a business is to remain in government ownership despite it being a contestable activity, it should not enjoy any net competitive advantage simply as a result of its government ownership.³⁷

In the 1980s, Australian governments embarked on a GBE reform program that sought to make GBEs more independent from government, responsive to consumer needs and efficient, including by 'corporatisation'.³⁸ In many cases, corporatisation was also a transitional step towards privatisation.

In 1996, following the CP Agreement, Australian governments published competitive neutrality policy statements outlining their implementation programs, including the application of this principle to local governments. Each government also created specific bodies to receive, investigate, and make recommendations about complaints. When the various bodies investigate a complaint, its findings are published and provided to government. Where changes to competitive neutrality arrangements are recommended, the governments concerned are not, however, obliged to accept that advice.

Since 2005, there has not been significant reporting on competitive neutrality compliance across jurisdictions.³⁹ Consequently, it is difficult to assess fully the effectiveness of competitive neutrality across the country. The ACCC also notes that since 2006 there has been a significant decline in the number of completed competitive neutrality complaint investigations.⁴⁰

The ACCC considers that Australian governments should review their competitive neutrality policies and related mechanisms. A review into, among other things, the timeliness and transparency of complaints handling and the implementation of recommendations, could promote a more effective regime.

3.2.7 Consumer participation

The effective operation of a market depends upon the demand side as well as the supply side. As discussed in section 5.2 of this submission, empowered consumers who are able to exercise the choice provided by competition are necessary for a level playing field for businesses, which in turn promotes economic efficiency and productivity growth.

As noted in section 2.2, policy design has been improved by insights about the drivers of consumer behaviour including the cost of complexity.⁴¹ The complexity that can come with competition may be a barrier to consumers taking full advantage of the benefits of competition. One of the insights gained since the Hilmer Review is that successful structural

³⁷ CP Agreement clause 3.

³⁸ Corporatisation involved transferring the business functions from departments to corporate entities owned by government. See ACCC/AER Working Paper No.1, *Evolution of Infrastructure Regulation in Australia* (July 2009).

³⁹ The NCC previously considered competitive neutrality implementation across jurisdictions as part of its annual progress assessments on NCP. This ceased in 2005.

⁴⁰ Victorian Competition and Efficiency Commission (VCEC), *Competitive Neutrality Inter-jurisdictional Comparison Paper* (2013).

⁴¹ Richard H. Thaler and Cass R. Sunstein, *Nudge: Improving Decisions about Health, Wealth, and Happiness* (Yale University Press, 2008).

reform of a market may require specific measures designed to support consumer participation.

Case study – energy

A competitive retail energy market relies on confident consumers exercising informed choice. Some consumers find energy markets complex and may be deterred from engaging fully in the market by lack of access to clear, easy-to-understand information about their current energy contracts and alternative contracts available to them.

Of particular importance in informing and empowering consumers is the AER's energy price comparison website, Energy Made Easy (www.energymadeeasy.gov.au). Energy Made Easy helps consumers to compare available energy contracts.

The National Energy Retail Law and the Retail Rules include other roles for the AER in prescribing how retailers present their pricing information to customers. The AER has developed a Retail Pricing Information Guideline which, among other things, requires retailers to use a standardised energy price fact sheet to communicate prices and other key product information. Access to clear, easy to understand information on their energy contract and alternative contracts can assist consumers to make an informed choice.

The AER's role in energy retail is supported by the ACCC. For example, in June 2014, the ACCC reauthorised an industry code of practice for face-to-face energy sales conducted by electricity and gas retailers.

Case study – telecommunications

The rapidly evolving telecommunications landscape has also increased complexity for many consumers and contributed to information asymmetries in relation to products and pricing models for different products.

The establishment and funding by the Commonwealth government of the Australian Communications Consumer Action Network (ACCAN) in 2009 has played a key role in ensuring that consumer interests are represented in this sector.⁴² ACCAN has identified a number of emerging issues, helped the ACCC understand how these impact on consumers, responded to ACCC regulatory decisions, published research on consumer behaviour and contributed to ACCC consumer information strategies. ACCAN has also facilitated discussions with a broad range of stakeholders about policy issues, such as telecommunication challenges in remote and rural areas, which have helped inform broader debate.

3.2.8 Economic regulation

Economic regulation is where the government intervenes in market decisions such as price, rate of return and output.⁴³ It may be required where a market is unable to deliver the desired economic efficiency goal due to the supplier's market power. Economic regulation may involve:

- access regulation – where access to a monopoly service is needed by businesses to compete in upstream or downstream markets; or
- price regulation – where competitive pressures on a supplier of a good or service are not sufficient to achieve efficient prices and protect consumers.

⁴² Department of Broadband, Communications and the Digital Economy, *Mid-term Review of the Australian Communications Consumer Action Network (ACCAN)* (April 2012).

⁴³ See ACCC/AER Working Paper No.1, *Evolution of Infrastructure Regulation in Australia* (July 2009).

As the Productivity Commission noted in its 2012 *National Access Regime* inquiry:⁴⁴

Where an infrastructure service provider is not constrained from using its market power, denial of access or monopoly pricing can lead to allocative inefficiencies that impose costs on the community. Access regulation can address these allocative inefficiencies, and facilitate lower prices for consumers.

The ACCC considers that competition principles relating to economic regulation should include the following six elements:

- **Nationally consistent principles:** Governments should apply consistent principles to economic regulation. Cooperative regimes may be needed where there is a national integrated market.
- **Objective of economic regulation:** The overall object of economic regulation should be to promote the long term interests of Australian consumers.
- **Emerging competition:** An essential component of a regime is a mechanism for winding back economic regulation if effective competition develops. Governments also need to address issues arising where substitute services are emerging, resulting in a decline in demand for the regulated service, but there remain captive customers.
- **Ensuring regulation is fit for purpose:** The CP Agreement recognises that regulatory regimes may range from monitoring and information gathering to negotiation and arbitration to upfront determination of terms and conditions.
- **Pricing principles:** Regulated prices should provide the right incentives to drive economic efficiency.
- **Process:** The regulatory process should ensure all interests are represented.

Nationally consistent principles

The Hilmer Review and CP Agreement recognised that consistent principles for economic regulation should be applied across the economy.⁴⁵

In respect of economic infrastructure, convergence between infrastructure services is occurring at four levels:

- At a technical level, network facilities are converging; for example, the physical and administrative structure of electricity transmission and distribution companies is generally suited to erecting and operating telecommunications transmission links.
- At a market level, the services provided by infrastructure may be substitutable which facilitates competition and the winding back of regulation; for example, road, rail, shipping and aviation may compete, to some extent, for the same customers.
- At a corporate level, firms are operating across different markets; for example, electricity distributors and telecommunications carriers or carriage service providers are forming joint ventures; and electricity suppliers are entering the gas market to provide 'dual fuel' options including joint meter reading visits, combined bills and single payment schemes.
- At a financial level, firms compete for debt and equity finance or funding by government.

Where industries converge, regulation by reference to a technological definition is 'an impossible mission'.⁴⁶ As the Hilmer Review noted, the increasing national orientation of

⁴⁴ Productivity Commission, *Inquiry Report: National Access Regime* (2012).

⁴⁵ Hilmer Review p. vii; CP Agreement clauses 2, 4 & 6.

commercial life needs to be recognised by Australian governments applying consistent principles for economic regulation. In the case of certain markets, governments need to go further by adopting uniform legislation; for example, as occurred for the NEM and Murray-Darling Basin. The ACCC considers that the path to a consistent economy-wide approach to economic regulation of significant infrastructure has been slow and requires renewed commitment from all levels of Australian government. The following case study is an example of the regulatory burden that arises where different rules apply to a market.

Case study – inconsistencies in rail regulation

The Hunter Valley Coal Network (HVCN) in NSW comprises approximately 700 kilometres of track. It connects coal mines in the Hunter Valley and Gunnedah Basin regions to the Port of Newcastle. The HVCN is leased from the NSW government by the Australian Rail Track Corporation (ARTC) under a 60-year lease. ARTC manages the HVCN, except for five sections of track which are owned and operated by RailCorp.

For sections of the HVCN that are managed by ARTC, third parties negotiate terms and conditions of access according to the 2011 Hunter Valley Access Undertaking (HVAU), accepted by the ACCC under Part IIIA of the CCA. In contrast, for the five sections of the HVCN that are managed by RailCorp, third parties negotiate terms and conditions pursuant to the NSW Rail Access Undertaking (NSWRAU) overseen by the Independent Pricing and Regulatory Tribunal of NSW (IPART).

Although the NSWRAU and the HVAU have sought to reflect the objects of Part IIIA of the CCA and COAG has agreed to consistent rail regulation,⁴⁷ the implementation of the two access undertakings has meant that there are now different regulatory arrangements applying to the HVCN. These differences may impact upon the efficiency of the Hunter Valley coal supply chain, given there is an inconsistency in the terms and conditions of access.

For example, the HVAU incorporates a tri-partite contracting structure under which coal producers may contract directly with ARTC, and exercise their access rights via an above rail operator. Under the NSWRAU, however, contracts for rail access are negotiated between RailCorp and above rail operators, on behalf of coal producers. This misalignment in contracting structure means that coal producers are required to negotiate with multiple parties to obtain rail access for the one train journey, increasing their costs.

Objective of economic regulation

The objects clause in a regime is critical as decisions made under a regime must take account of, and promote, the objective.

In 2007, the CP Agreement was amended to include the following objects clause for access regimes:

promote the economically efficient use of, operation and investment in, significant infrastructure thereby promoting effective competition in upstream or downstream markets.

However, there is no reference in this clause to the long term interests of end users. This contrasts to the objective of the telecommunications access regime in Part XIC of the CCA⁴⁸ and the 2005 objective in the NEL. For example, the NEL objective is to:

promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to—

⁴⁶ Bill Childs, 'Regulation of Convergence' (1993) 1(8) *Telecommunications Law & Policy Review* 99. See also Rodney Shogren, 'Convergence of General Competition Law with Telecommunications Specific Regulation – the Australian Experience' (March 1998) 1(9) *TeleMedia* 153.

⁴⁷ Council of Australian Governments' Meeting, 10 February 2006.

⁴⁸ CCA s. 152AB.

- (a) price, quality, safety, reliability and security of supply of electricity; and
- (b) the reliability, safety and security of the national electricity system.

The Expert Panel established to review the energy merits review regime, described the NEL objective as ‘well crafted, and ... at the cutting edge of international best practice’.⁴⁹ The Expert Panel emphasised that the ends (consumer interests) should not be displaced by the means to those ends (economic efficiency). The UK Department for Business Innovation and Skills similarly recognises that the objective of economic regulation is to:⁵⁰

create a system of incentives and penalties that aim to replicate the outcomes of competition in terms of consumer prices, quality and investment and puts the protection of consumers’ interests at its heart.

The ACCC considers that the overall object of economic regulation should be to promote the long term interests of Australian consumers.

Emerging competition

The emergence of a substitute service will usually enhance competition, promoting economic efficiency.⁵¹ An essential part of the CP Agreement is the principle for determining when a service should cease to be subject to economic regulation or the form of regulation should be changed.⁵² This is likely to become of increasing importance as new technology leads to the development of substitute services.

Case study – telecommunications

Under the telecommunications access regime in Part XIC of the CCA, the ACCC may declare a service if it is satisfied that it will promote the long term interests of end users.

The Domestic Transmission Capacity Service (DTCS) is a high capacity transmission service that enables service providers to provide downstream wholesale and retail services to end users. The DTCS was deemed to be a declared service in 1997 because it was recognised to be an essential input for other services. However, the ACCC has progressively removed regulation in areas that have been found to be competitive.

In March 2014, the ACCC varied the DTCS declaration to exclude an additional 112 metropolitan Exchange Serving Areas and eight regional routes. The ACCC’s competition assessment found that these DTCS routes are sufficiently competitive and should be removed from regulation.

However, there is an emerging issue, which could be addressed in the current Competition Policy Review, where substitute services are developing (resulting in a decline in demand for the regulated service) but certain customers remain captive⁵³ to the regulated service. There is a question as to who should bear the cost if this risk eventuates.

Businesses that are subject to economic regulation usually exhibit increasing returns-to-scale. A decline in demand results in a decline in revenue which is larger than the reduction in costs. In the short to medium run, the decline in cash flow can be borne by some combination of:

- the owners of the regulated firm;

⁴⁹ Professor George Yarrow, The Hon Michael Egan and Dr John Tamblyn, *Review of the Limited Merits Review Regime: Stage Two Report* (30 September 2012).

⁵⁰ UK Department for Business Innovation and Skills, *Principles for Economic Regulation* (April 2011).

⁵¹ Competition Committee, Directorate for Financial and Enterprise Affairs, OECD, *The Impact of Substitute Services on Regulation* DAF/COMP(2006)18 (23 June 2006).

⁵² CP Agreement cl 6(1) & (3).

⁵³ E.g. businesses that have made sunk investments on the basis of the regulated service; households who have entered into long term contracts; or low-income households with less capacity to take up new technology.

- the customers whose demand is not declining, or other services provided by the regulated firm where demand is not declining;
- the customers whose demand is declining; or
- the government (tax payers).

In the long run, it is generally not possible to insulate customers from a change in demand. Eventually the service is likely to be terminated or the impact of the lower demand passed through to the remaining customers.

Ideally, the existing regulatory regime/contract would set out a reasonable allocation of the risk of declining demand from commencement. There are no hard-and-fast rules as to what constitutes a reasonable allocation of risk. However, there are arguments for:

- the service provider to bear some risk so as to retain incentives for efficient investment and operation;
- the customer whose demand is falling to bear some risk e.g. in the form of take-or-pay arrangements or exit fees;
- captive customers to largely be insulated from the risk in the short to medium term; and
- government to provide compensation where the decline in demand is the direct result of a change in government policy.⁵⁴

Where a decline in demand occurs, policy options include:

- reviewing government regulation that impacts on demand for the old service e.g. restructuring regulated prices, or government subsidies for the new service;
- removing price control regulation of the old service – but if there remain captive customers, this could result in the cost being borne by these customers rather than the service provider;
- applying the existing regime or amending the regime to deal with the allocation of the cost in the short to medium term – but the focus also needs to be on how to transition to a sustainable service model. This may require a review of government regulation such as CSOs.

Better outcomes could be achieved if governments agree to guiding principles to deal with this issue of declining demand – including that, where possible, regulatory regimes should identify in advance the risk of changes in demand, and the mechanism by which this risk should be allocated. In general, such a mechanism should protect the interests of captive customers.

Case study – declining demand in post, electricity and fixed-line telecommunications

Australia Post

Before increasing the price of certain letter services, Australia Post is required to notify the ACCC under Part VIIA of the CCA.⁵⁵ The Minister may disapprove the price under the *Australian Postal Corporation Act 1989*. However, electronic communication technology is making letter postal services increasingly obsolete, and increasing the unit cost of sustaining current service levels.

⁵⁴ Infrastructure Australia's National Public Private Partnership Policy and Guidelines provides that, in respect of economic infrastructure, governments should provide relief or compensation for changes in law which specifically (and only) affect the project or other similar projects: Infrastructure Australia, *National Public Private Partnership Guidelines Volume 7: Commercial Principles for Economic Infrastructure* (February 2011) Principle 19.

⁵⁵ The current declaration expires in 2016.

While Australia Post has implemented some price increases in response, it has raised an issue of the ongoing economic viability of the service given the decline in demand for traditional mail services. This necessitates a broader government review of this service beyond simply prices.

A key question is whether there remain any captive customers or captive services which must make use of the Australia Post letter delivery service. If the government decides that the service should continue, the focus should be on how to rationalise the service to reduce the cost, and how to increase transparency of government funding for it.

Electricity

In the electricity sector, there has been a recent reduction in demand for electricity network services, in part attributable to regulated tariff structures.⁵⁶

It is common for distribution networks to have a low fixed charge and a high variable charge. But (at least at uncongested times) the marginal cost of using the electricity network is low, so a high variable charge creates incentives for customers to artificially reduce their consumption at these times. Similarly, the cost savings available to users create excessive incentives to invest in appliances and devices which also reduce consumption at uncongested times. This contributes to a reduction in revenue for electricity network businesses with little or no impact on the network costs. There is therefore an overriding need for a review of regulated price structures. Reforms of this kind are currently being progressed.⁵⁷

Communications

Telstra is facing a decline in demand for its traditional fixed-line voice telephony services as customers switch to mobile services or voice-over-IP broadband services. This raises the question of the impact of this decline in demand for the regulation and pricing of the declared fixed-line services. The ACCC is currently conducting a public inquiry into making final access determinations for these services that will consider how the impacts of declining demand should be addressed.

Ensuring regulation is fit for purpose

Economic regulation can encompass a variety of instruments such as legislation, administrative decisions pursuant to legislation, public ownership, information campaigns, negotiation and moral persuasion. As part of the NCP reforms, Australia has shifted towards transparent economic regulatory regimes based in legislation. Explicit and enforceable rules are particularly critical to ensuring that privatisation achieves the regime objective.

However, the form of economic regulation also needs to be 'fit for purpose', that is, effective and efficient (or proportionate to the problem being addressed). The CP Agreement recognised that there is a broad spectrum of possible regulatory tools including:

- monitoring and information gathering: which can be a useful tool to provide information to governments, regulators and the wider community about the

⁵⁶ Government incentives for household solar generation also played a role in reducing demand for network services. This does not suggest that government should respond to a decline in demand by removing policies designed to reduce pollution externalities. The key point is to ensure that correct network price signals are provided to users; e.g. such that pollution is reduced by the lowest cost means.

⁵⁷ See the AER submission to the Energy White Paper (12 February 2014) which supports the AEMC *Power of Choice* (November 2012) recommendations (in particular, the restructuring of network prices, regulatory arrangements that are 'robust to future changes in technology' and contestability of services where competition is viable). The issue was raised at the SCER / COAG Energy Council on 13 December 2013 and 1 May 2014. AEMC is also currently considering rule changes to amend the way by which distribution network prices are set and structured (to be finalised in November 2014) and to promote competition in metering services (to be finalised in 2015).

transitional impact of deregulation and other reforms on price levels in particular industries;

- negotiation and arbitration: e.g. where access is required to a structurally separated monopoly service in order to compete in an upstream or downstream market; and
- ex ante (upfront) determination of term and conditions: e.g. where access is required to a vertically integrated monopoly service, or case-by-case negotiation is impractical (as in an interconnected electricity network).

The ACCC considers that competition principles relating to economic regulation should include a requirement that the form of regulation be ‘fit for purpose’.

Case study – milk monitoring program

The milk monitoring program is an example of the monitoring tool providing information on the transitional impact of a deregulation reform.

As part of the implementation of NCP, Australian governments agreed to abolish regulated farm gate price controls for market (drinking) milk from 1 July 2000.

The ACCC’s milk monitoring program was undertaken chiefly to monitor the effects of deregulation on farmgate prices for milk. In particular there was significant public concern that deregulation would lead to increased milk prices and that the benefits of restructuring would flow to milk processors and retailers rather than to farmers and consumers.

The monitoring was undertaken based on Ministerial direction (under provisions now contained in Part VIIA of the CCA) and involved monitoring the effects of deregulation of farmgate prices for milk over a six month period commencing on 1 July 2000.

The ACCC’s major finding from its monitoring (contained in an April 2001 monitoring report *Impact of Farmgate Deregulation on the Australian Milk Industry*) was that consumers benefited overall from reduced milk prices as a result of deregulation.

Case study – reducing regulation at Newcastle wheat terminal

The Newcastle wheat terminal is an example of how the form of regulation should be adjusted in response to changing market circumstances.

In 2014, the ACCC consented to an application by GrainCorp (a wheat port terminal operator and exporter) to decrease the level of economic regulation applied at its terminal at Newcastle.

GrainCorp argued that regulation should be reduced because its Newcastle terminal now faces competition from two other bulk wheat export facilities, neither of which are subject to access regulation. The ACCC agreed that there was sufficient competition such that regulation could appropriately be reduced, and that allowing GrainCorp’s Newcastle terminal to be subject to minimal regulation would provide GrainCorp with greater flexibility to compete against the two bulk wheat export operations at the Port of Newcastle.

The ACCC noted that, where there is sufficient competition, minimal or no regulation is required. However, where wheat ports have significant market power or are a monopoly and are owned by a wheat marketer in competition with others upstream, then regulation is required to ensure farmers can sell their grain into a competitive market.

Case study – telecommunications arbitrations

The operation of the 1997 telecommunications regime shows the impact of a regime that was not fit for purpose. The telecommunications-specific access regime inserted into the *Trade Practices Act 1974* (Cth) (Trade Practices Act) in 1997 was based on the declare-negotiate-arbitrate model set out in Part IIIA. Like Part IIIA, access to services begins with a declaration process. Failing agreement (and in the absence of an undertaking), the terms and conditions of access were determined by the ACCC acting as arbitrator.

However, there are two primary determinants of the probability of a negotiated outcome: the extent of the access provider's market power (one determinant of which is the access seeker's countervailing power); and whether the access provider is vertically integrated. By June 2009, the ACCC had received 157 access dispute notifications under Part XIC. In contrast, by the same time the ACCC had received only 2 access dispute notifications under Part IIIA. Further, telecommunications arbitrations proved to be lengthy and resource intensive processes requiring duplication of similar disputes between multiple access seekers.

In 2011, the arbitration model was replaced by upfront access determinations. The ACCC has recently submitted to the government's *Independent Cost-Benefit Analysis and Review of Regulation* that, since the 2011 reforms, 'Part XIC is fit-for-purpose and generally working well to provide effective access regulation for telecommunications services'.

Pricing principles

Price signals are central to achieving good economic outcomes in all sectors, and are a key element of economic regulation. Price provides the information needed for efficient demand and supply.

In 2007, the CP Agreement was amended to include the following principles for regulated access prices:⁵⁸

Regulated access prices should be set so as to:

- 1. generate expected revenue for a regulated service or services that is at least sufficient to meet the efficient costs of providing access to the regulated service or services and include a return on investment commensurate with the regulatory and commercial risks involved;*
- 2. allow multi-part pricing and price discrimination when it aids efficiency;*
- 3. not allow a vertically integrated access provider to set terms and conditions that discriminate in favour of its downstream operations, except to the extent that the cost of providing access to other operators is higher; and*
- 4. provide incentives to reduce costs or otherwise improve productivity.*

However, more broadly, efficient price signals should be a core feature of market structural reform. Section 3.3 provides the examples of congestion pricing at ports and airports, and the AEMC's 2012 review of demand side participation and management in electricity including the efficiency of price signals in the NEM.⁵⁹

Process

The representation of all interests in a regulatory process is important to achieving the objective of economic regulation. Lack of participation by an interest group such as consumers or end users may:

- impact on outcomes that result from the regulatory process;
- reduce the legitimacy of the regulatory outcome; and
- preclude the negotiation needed within a regulatory process to identify win-win outcomes e.g. customer preferences may support a lower price in exchange for a reduced quality of service.

The table at the commencement of this section 3.2 provides the example of the AER's consumer engagement guideline for regulated electricity and gas networks⁶⁰ and the establishment of the Consumer Challenge Panel in 2013⁶¹. This follows work undertaken

⁵⁸ Clause 6(f)(2).

⁵⁹ See also Productivity Commission, *Electricity Network Regulatory Frameworks* (Inquiry Report No. 62, 2013).

⁶⁰ To ensure that networks identify consumer preferences, and that this drives network decisions.

⁶¹ To provide an independent consumer perspective to challenge the AER and network service providers during determination processes.

successfully by regulators in the UK including Ofgem (energy regulator) and Ofwat (water regulator for England and Wales). It also reflects one of the key principles set out by the World Bank in its handbook on infrastructure regulation, concerning transparency and public participation.⁶²

The ACCC considers that competition principles relating to economic regulation should include the need to address barriers to participation by interest groups in the regulatory process, including funding where necessary.

3.3 Identifying key areas for reform

By reaffirming the principles developed in the Hilmer Review and incorporating the lessons learnt over the last two decades, a new competition framework for Australia can assist in boosting productivity and living standards, promoting a strong and innovative business sector and achieving better outcomes for consumers. However, to achieve these benefits, governments need to identify and agree upon key areas of the economy for microeconomic reform. The process by which this could be done is discussed in chapter 5 of this submission. The following sections of this chapter provide ten examples of areas for reform.

3.3.1 Privatisation

Key points

- There are signs that, in privatising assets, Australian governments are focusing overly on short term budget goals without sufficient regard to longer term competition. Governments should consider how the privatisation process can promote competition, for example by separating, rather than integrating, potentially competitive facilities.
- Governments should also avoid the temptation to boost asset values by privatising without appropriate price and access regulation in place. Such short term financial benefits to government amount to a tax on future generations of Australians.
- It is also important that the merits of structural separation are considered prior to privatisation.

A number of Australian governments have foreshadowed significant asset sale programs over the next few years, which could significantly impact on the structure of key infrastructure markets in Australia. The types of assets that could be sold include ports, electricity generators and transmission and distribution assets as well as possibly railway and post assets.

This impetus towards privatisation is likely to be enhanced by the Commonwealth government's proposed asset recycling scheme. If passed into legislation, the Commonwealth will provide incentive payments to the states and territories to privatise assets and reinvest proceeds into new infrastructure.⁶³

A key concern of the Hilmer Review was that privatisation may be driven primarily by budget goals, at a cost to competition. For example, businesses with a substantial degree of market power are likely to attract premiums on sale, relative to the case where they are structured in such a way as to maximise competition. This was recognised in the CP Agreement which included the requirement that:

4(c) *Before a Party introduces competition to a market traditionally supplied by a public monopoly, and before a Party privatises a public monopoly, it will undertake a review into: ..*

⁶² World Bank, *Handbook for Evaluating Infrastructure Regulatory Systems* (2006).

⁶³ Asset Recycling Fund Bill 2014 (Cth) Explanatory Memorandum.

2. *the merits of separating any natural monopoly elements from potentially competitive elements of the public monopoly;*
3. *the merits of separating potentially competitive elements of the public monopoly;*
7. *the price and service regulations to be applied to the industry.*

Experience with government privatisations over recent decades has shown that acting in accordance with these principles promotes competitive outcomes. In the electricity sector, for example, during the development of the NEM in the 1990s, getting the market structures right was key to the development of effective competition. It was during this time that natural monopoly transmission and distribution networks were generally vertically separated from potentially competitive generation and retail functions.

Further, at the generation and retail levels, there was, in most states, horizontal separation into a number of competing generation and retail businesses. In the states that chose to privatise electricity assets, this market structure was put in place prior to sale.

Case study – Victorian electricity generation privatisation

In the early 1990s, the Victorian government owned a major portfolio of generation assets. It owned four major brown coal generators, as well as some gas and hydro generators. From the mid–late 1990s, the Victorian government disaggregated and privatised its generation portfolio. It sold four generators based on the individual coal fired plants (Loy Yang A, Loy Yang B, Yallourn and Hazelwood) as well as separate gas (Ecogen) and hydro (Southern Hydro) generation companies. While the creation of six competing players attracted considerable opposition at the time, this market structure set a strong foundation for the commencement of generation competition. Notwithstanding some recent aggregation, the subsequent experience has seen a relatively competitive electricity generation sector.

However, there are concerning signs that, increasingly, Australian governments are privatising assets with a view to maximising proceeds of sale at the expense of competition.

Case study – Sydney Airport privatisation

When Sydney Airport was sold for \$5.6 billion in June 2002, the Commonwealth government provided the acquirer the valuable right of first refusal to operate a second Sydney airport (recently announced to be located at Badgery’s Creek). The National Audit Office has found that the sale price for Sydney Airport was higher than a number of possible valuation benchmarks, including the government’s own estimate of the sale price in the 2001-02 budget.

The ACCC considers that the higher sale price was likely a reflection of a valuation premium associated with the right of first refusal option. The right of first refusal confers on Sydney Airport a monopoly over the supply of aeronautical services for international and most domestic flights in the Sydney Basin, and forecloses the potential for competition between Sydney Airport and an independent operator of a second airport. Inclusion of this right of first refusal increased the sale price but is likely to have had an anti-competitive impact on the aviation sector.

Another key issue is the nature of the regulatory settings that apply to monopoly assets when privatised by governments. Governments should avoid the temptation to attempt to maximise sale revenue by privatising without appropriate price and access regulation in place. While this may attract a financial benefit upfront, loss of competition effectively imposes a tax on future generations of Australians.

The ACCC has concerns that, at times, governments are not establishing appropriate access mechanisms prior to the sale of such assets, instead relying on contractual arrangements with the new owner.

Where the sale would otherwise be likely to result in a substantial lessening of competition in breach of section 50 of the CCA, the ACCC may be able to deal with infrastructure access issues via remedies accepted from infrastructure buyers to address those competition concerns. Merger remedies accepted by the ACCC are court-enforceable undertakings, accepted pursuant to section 87B of the CCA.

However, the ACCC considers that reliance on the merger process is generally an inadequate means of dealing with complex issues of access to significant monopoly infrastructure. Section 50 remedies can only address competition concerns arising from an acquisition and therefore cannot extend to addressing competition issues arising from the monopoly characteristics of the infrastructure. In other words, where privatisation represents a bare transfer of the monopoly asset from the government to the private sector, the sale is unlikely to lead to a substantial lessening of competition in a market, and therefore merger remedies would not be available.

By contrast, in some asset privatisations, a particular purchaser might raise competition issues because the purchaser holds an interest in competing assets (horizontal aggregation) and/or businesses at other levels of the supply chain (vertical integration). It is in this circumstance that merger remedies may be an available mechanism to deal with section 50 concerns.⁶⁴

However, even in such cases it is not clear that section 50 remedies represent the most effective mechanism for ensuring appropriate terms and conditions of access to monopoly infrastructure. In contrast to a section 87B undertaking, a regulated access regime allows proposed arrangements to be effectively reviewed, amended or renewed. Adopting section 50 remedies for infrastructure involving long term leases would generally involve long term behavioural undertakings which are not preferred by the ACCC due to the inherent risks in terms of ensuring their effectiveness and compliance with the remedy over such a long time horizon.

The compressed nature of merger processes is also far less suited to establishing terms and conditions of access as compared to regulatory processes under which such matters are worked through over a significant period of time. For example, the sale process adopted by the NSW government for the Port of Newcastle resulted in bidders notifying the ACCC of their proposed bids six weeks before final bids were due. While the date for final bids was extended by a short period, it did not provide sufficient time for ACCC assessment and clearance (which was a requirement for conforming bids). In certain reviews involving sale of government-owned infrastructure, the ACCC received considerable criticism from stakeholders that not enough time was provided to comment on proposed undertakings.

Furthermore, the ACCC has limited information gathering powers to ensure ongoing compliance with the provisions of a section 87B undertaking (see section 4.4 of this submission). This can be contrasted with the legislative frameworks established for ACCC regulation of natural monopoly infrastructure, such as the national electricity regime, and Part XIC of the CCA.

Case study – privatisation of Australia’s container ports

The largest container port in Australia is the Port of Melbourne, followed by Port Botany, the Port of Brisbane, the Port of Fremantle and Port Adelaide. Three of these ports have been privatised to date – Port Botany, Port of Brisbane and Port Adelaide. The Port of Fremantle and the Port of Melbourne are currently government owned, although the Victorian government has announced plans to lease the Port of Melbourne.

⁶⁴ These remedies could involve divestment of other assets owned by the acquirer or, particularly in the case of transactions that raise concerns regarding vertical integration, a behavioural undertaking from the acquirer that provides third parties with access to bottleneck infrastructure on efficient terms.

Privatisation of port assets can raise issues of efficiency where monopoly rights are conferred by state governments, with no consideration to the prospect for competition and/or the need for economic regulation. This has the potential to result in lost efficiencies and/or higher charges which may be hard to remedy after assets are sold.

In March 2014, it was suggested that ‘there’s a way you can add value [to the Port of Melbourne sale] because by giving rights or options to develop Hastings, you are effectively conferring almost a monopoly’. It was also stated: ‘There’s nothing wrong with [conferring almost a monopoly] because port charges are actually regulated by the Essential Services Commission’. The ACCC notes that the Port of Melbourne is subject to price monitoring by the Essential Services Commission (ESC). This does not, however, provide for the ESC to set or control the Port of Melbourne’s charges. In the ACCC’s experience, price monitoring does not provide an effective constraint on monopoly pricing behaviour.

The announcement by the Victorian government in May 2014 that it intends to offer a medium term lease over the Port of Melbourne does not suggest that rights to the Port of Hastings will be included in the Port of Melbourne lease. However, the ACCC remains concerned over arrangements designed to maximise proceeds received by a government by reducing the prospect of competitive provision of port services. Another example relates to Port Botany and the Port of Newcastle. An article in the Newcastle Herald on 11 May 2014 stated: ‘The government has confirmed it leased Botany with a clause that prevented Newcastle from competing against it with a container terminal. And the Newcastle lease is believed to contain a similar undertaking’.

One final point should be noted. Where a government monopoly asset is to be privatised, there should be no presumption that any regulation applying at that time will remain ‘fit for purpose’ once the asset is sold. In particular, governments should carefully consider the incentives any purchaser will have – even if it has no interests upstream or downstream at the time of sale – to vertically integrate into related markets at a later time. Regulatory settings that apply to monopoly assets when privatised may therefore need to be adaptable to possible changes to industry structure, including that a private firm may seek vertical (re)integration.

By leveraging such market power into otherwise competitive parts of the supply chain or related industries, a private firm’s conduct in such circumstances may provide poor outcomes for competition and efficiency. The legislative and regulatory arrangements that apply to such firms are likely to be important factors in determining the nature and scope of competition in the affected markets for many years into the future.

While this submission cautions against imposing unnecessary restrictions on firms’ abilities to participate in markets, the ACCC also suggests that where the sale of an asset is likely to confer enduring market power, governments should carefully consider whether legislative restrictions on vertical (re)integration might be warranted.

Case Study – National Broadband Network

While NBN Co is currently publicly owned, the stated government intent is to privatise in the future. There are legislative measures applied to NBN Co that address issues of vertical integration in the telecommunications industry, such as wholesale only restrictions and provision for ownership restrictions.⁶⁵ Having these restrictions in legislation ensures that structural separation should not be subverted in the future by allowing NBN Co to directly supply services to retail customers, or entering into ownership arrangements with retailers and other carriers.

⁶⁵ See *National Broadband Network Companies Act 2011* ss. 9 & 69-74.

3.3.2 Regulation and productivity

Key points

- The post-Hilmer NCP contained a co-ordinated review of a range of regulation and its impact on competition.
- Although much progress was made, there remain cases where the policy purpose of regulation and its associated costs are disproportionate and regulation is limiting productivity.
- A reinvigorated competition policy should include a process for legislative review of regulatory 'red tape' from a competition perspective.

Introduction

To provide context for the above recommendations, this section articulates a framework under which regulation that restricts competition might be considered. Specific examples are cited, where appropriate, to provide guidance to the Review Panel on the types of regulatory impediments that could be removed. The examples given here are drawn from the ACCC's experience in administering the CCA in a wide range of markets.

Unnecessary regulation can reduce economic productivity. Regulation that restricts competition should be no more burdensome than needed to achieve a policy objective and should be proportionate, transparent, and accountable. While regulation may address important policy aims, such regulation should also be the most effective method of achieving policy aims to justify the costs of that regulation.

This is consistent with the CP Agreement where governments agreed that legislation should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs, and the objectives of the legislation can only be achieved by restricting competition. The ACCC is therefore proposing that the Review Panel consider a reinvigoration of this process to ensure that outstanding restrictions continue to be considered on this basis. There will be challenges associated with removing regulatory impediments and some potential structural adjustment issues to consider.

Purpose of regulation

The Review Panel has noted that a range of restrictions contained in a 'multitude of federal, state and territory and local government instruments' may affect competition and that these instruments may not have competition as a focus.⁶⁶ However, competition policy should accommodate situations where competition does not achieve efficiency or conflicts with other social objectives. Some of those issues are considered below.

Information asymmetries

One type of regulation is that which is directed at addressing 'information asymmetries' – where suppliers have information about products or services that consumers do not. Information asymmetries can therefore lead to poorly informed consumers and inefficient market outcomes.

Regulatory oversight may be required in order to correct this market failure. For example in health, a key concern is how consumers can assess whether their health professional is providing appropriate advice. Regulations governing the accreditation of health professionals are a means of assuring service quality does not fall below minimum acceptable standards.

⁶⁶ *Competition Policy Review: Issues Paper* (14 April 2014) p. 12.

Externalities

In some cases, free markets will not produce efficient outcomes because production or consumption decisions impose costs on others that are not taken into account by the decision maker. Externalities are costs (or benefits) which result from the decisions of one party but which are borne (or received) by others. The policy purpose of some regulations is to control for potential negative externalities, in general by seeking to restrict outputs generating the negative effects closer to the 'socially optimal' level.

While this type of regulation may appropriately address this type of market failure, it is important that it is no more burdensome or intrusive than required to address that failure.

No clear market failure

In some cases, regulation may operate primarily to protect the interests of particular market participants but to the detriment of consumers, other businesses (including upstream or downstream), potential new entrants, and Australia's economy as a whole. Some of these regulations have been in place for some time and changes may significantly affect the value of investments made by parties in a particular market sector. Consequently, such regulations are often supported by powerful interest groups.

Costs of regulation on productivity

Economic efficiency can enhance community welfare and competition provides the *incentive* for firms to improve economic efficiency. Therefore, all regulation that limits competition imposes costs on the community. Those costs must be considered against the benefits of the regulation. In some cases, the costs of regulation may be to the detriment of productivity and, furthermore, may not deliver the desired benefits.

Case study – ethanol

In October 2007, the New South Wales government mandated that a certain proportion of petrol sold in the state should be ethanol, and that this proportion would steadily increase over time. The intention of the mandate was to develop a secure market for ethanol producers, and create a viable biofuels industry.⁶⁷

However, not only have these goals not been met (the ethanol mandate is not being met and there are only three producers in Australia), the policy has had a number of negative consequences. These include that the mandate has affected the competitive dynamic among retailers by reducing the availability of regular unleaded petrol from many retail sites.

Further, it has reduced consumer choice because some motorists who cannot use ethanol in their vehicles (or choose not to) have, because of the reduced availability of regular unleaded petrol, decided to use premium unleaded petrol. This is reflected in the fact that demand for premium unleaded petrol in NSW over the last five years has doubled (which is a significantly higher growth rate than in other states).

Furthermore, as premium unleaded petrol retails at a higher price than regular unleaded petrol, it has meant that these motorists have been paying higher prices than if they had continued to purchase regular unleaded petrol. A recent study estimated this cost to be \$12.3 million per month in 2013.⁶⁸

Given the above, it is clear that government regulation which was primarily designed to provide industry assistance to local ethanol producers has effectively resulted in less choice and higher fuel prices for many motorists in NSW.

⁶⁷ Independent Pricing and Regulatory Tribunal, *Ethanol Supply and Demand in NSW – Other Industries – Final Report* (March 2012) p. 10.

⁶⁸ Michael D. Noel and Travis Roach, *Regulated and Unregulated Almost-Perfect Substitutes: Aversion Effects from a Selective Ethanol Mandate* (31 March 2014) p. 30.

Proportionate regulation

Where objectives can *only* be met through regulation, then the overall benefits must outweigh the overall costs. The costs and benefits can be considered broadly to take into account impacts on upstream and downstream markets, impacts on investment, and benefits to consumers.

In weighing the costs and benefits of legislation it is important to consider the costs and benefits of these to the community as a whole. Particular interest groups may have a vested interest in maintaining regulation, and this may be a barrier to effective regulatory roll-back. However, where regulation imposes high costs on the community as a whole it should not be maintained in the interests of particular groups.

Case study – Western Australian Potato Marketing Corporation

The *Marketing of Potatoes Act 1946* (WA) restricts the production of potatoes for human consumption without a licence from the Potato Marketing Corporation. The Corporation operates to protect returns to potato growers.

The Economic Regulation Authority (ERA) in Western Australia has recently concluded that ‘the restrictions on potato marketing have raised the incomes of potato growers in Western Australia. However, this has been at the cost of Western Australian consumers who pay higher prices than otherwise, have limited choices of potato varieties and endure poor product quality’.⁶⁹

In some cases, there may be a clear policy rationale for regulation and/or the regulation may have the potential to address issues of concern to the broad community. However, regulation should still be fit for purpose and no more burdensome than required to achieve the policy aim.

Applying the principle of proportionate regulation is critically important, but can be difficult in practice. The often important policy rationale of the legislation can mean that the competition costs are considered secondary, and ways to achieve the policy purpose at a lower cost are not fully considered. The below case study of government licensing is intended to demonstrate the ways the principle of proportionate regulation may be applied to different types of legislation.

Case study – government licensing

Government licensing can include licences to undertake a particular type of activity, for example: taxi licences, gambling licences, vehicle licences, fishing licences, forestry licences, water rights licences, chemical handling licences, and radio frequency spectrum licences.

Different types of licences may be directed at achieving different sorts of policy objectives, including efficiently allocating a finite stock of scarce goods, taking into account ecological sustainability concerns, limiting the potential anti-social effects of certain activities, and ensuring quality or safety standards are met. These are important policy objectives which can be promoted by licensing regimes.

However, some licence regimes may have potential anti-competitive consequences that should also be considered.

In particular, special considerations arise where licensing can act to limit supply. Some licences do not significantly limit supply at all and are granted to anybody who meets the criteria e.g. certain trade licences. However, other licences allocate a resource for which supply is unable to be increased in response to changes in demand. That is, the scarcity or limitation in supply is inherent to the right granted by the licence.

⁶⁹ Economic Regulation Authority (Western Australia), *Inquiry into Microeconomic Reform in Western Australia*, (11 April 2014) p. 265.

Examples include wild fishery or forestry licences. By contrast, some licences may impose an 'artificial' limitation on supply. That is, the legal requirement for the licence and a cap on the number of licences that can be granted itself creates the scarcity; e.g. taxi licensing.

Where goods are inherently scarce, providing or auctioning licences may provide an efficient way to allocate those scarce resources. However, where the scarcity is created by the licence regime itself the benefits of the regime must be balanced against the costs of limiting supply. A consequence of limiting supply may be to reduce competitive pressure and increase prices. A review of licencing regimes should focus on whether the policy benefits associated with the licensing regime can be achieved without limiting supply given this potential consumer detriment.

For example, where the purpose of licensing is to take into account externalities, such as environmental costs, limiting supply may serve an important policy purpose. However, where the purpose of limiting supply is to benefit only certain market participants (such as current licence holders) or to preserve value of licences in secondary markets this may be to the detriment of consumers generally. In such cases, allocating licences to anyone who meets minimum standards would be more appropriate.

Where licences are allocating genuinely scarce resources, it is important to ensure that the process for granting licences is fair and transparent and promotes efficient markets. If licences for scarce goods or services are granted to relatively inefficient providers, then this results in a productivity loss compared to if the service had been provided by a more efficient provider. This cost is borne by consumers. Competitive tendering processes are important in this context.

The charges imposed for licences are likely to be directly or indirectly borne by consumers. As noted above, a licensing regime may be considered as imposing a relatively low regulatory burden to achieve regulatory oversight e.g. quality or safety standards. However, where licence charges are significantly beyond the direct costs associated with the licensing regime and are designed to raise state revenue this increases the regulatory burden and has the potential to distort markets by imposing additional costs on certain activities. That said, in some cases, such as where the licence relates to a scarce good as discussed above, the pricing mechanism may be a means of efficiently allocating licences.

While there are very good policy reasons for many government licensing schemes, the ACCC considers that they should be included in any legislative review seeking to identify the potential for productivity gains. While the exact recommendations for reform will depend on the licensing regime under consideration, the above general principles should apply.

Regulation should also be periodically revised and assessed. As further discussed in chapter 5, supporting institutional arrangements can ensure that the general competition principles that should apply to regulation are applied in practice.

3.3.3 Roads

Key points

- While road reform began during the microeconomic reform agenda of the 1990s, it is far from fully implemented.
- Current road charging mechanisms and structural arrangements are failing to promote efficient decisions by road users and funding bodies.
- The ACCC considers that structural reform of those functions of government responsible for road provision and charging would lead to more efficient investment in roads and alternative transport infrastructure, better informed decisions by road users, and consequently, major productivity gains across the economy as a whole.

Introduction

Australian roads – together, an asset with an estimated replacement cost of approximately \$150 billion⁷⁰ – are a major plank of Australia's infrastructure, and as an input into transport services are key enablers of efficiency in a range of other sectors. Given this, efficient use of, and investment in, Australia's road infrastructure is critical to ensuring Australia's ongoing competitiveness.

Despite their key role, roads have not been subject to the level of microeconomic reform that has occurred in other industries since the 1990s. In part this reflects the relative difficulty of the reforms, including roads being regarded as open access, non-excludable goods. It also reflects that until recently, charging road users directly for their use of public roads was prohibitively expensive except at specific locations such as toll bridges or tunnels.

It is, however, now timely to reassess how microeconomic reforms that have been applied in other areas (such as electricity and telecommunications) might be applied to roads, particularly as technological advances in measuring road use further develop. The ACCC recognises, though, that public confidence and support will be important to the success of implementing reforms. Phasing in of reform, commencing with heavy vehicles, may provide a pathway to transforming the sector.

The problem: Impediments to efficiency

The ACCC considers that the structures underpinning Australia's current road transport services including the charging mechanisms, are inefficient. Three main disconnects can be identified in the current system:

1. Prices faced by road users do not reflect the economic costs of using roads.

The charges currently applied to vehicles for their use of roads are indirect, and averaged across location and road type. They are recovered from road users through fixed annual registration charges and fuel-based road user charges (i.e., fuel excise). Charges for heavy vehicles are set through a cost recovery model based on historic expenditure on road services (through the pay-as-you-go or PAYGO model) managed by the National Transport Commission (NTC). The NTC recommends charges, which are determined by the Transport and Infrastructure Council (a COAG body).

Consequently, a particular road user faces the same financial costs of road use regardless of which roads are used and regardless of the time at which roads are used.⁷¹ The highly averaged charges do not convey suitable signals about the cost of using certain roads or groups of roads, and therefore do not efficiently influence drivers' choice of routes. Nor do they provide appropriate incentives for road users to shift their use from peak to off-peak times where feasible, or to consider alternative transport modes at times of congestion.

The pricing regime for roads likely distorts competition between road and rail users. This is because rail prices are generally more cost-reflective and subject to less averaging than road prices. The ACCC considers that the more that costs and prices can be specifically identified with location, the better signals for usage across both road and rail networks.

2. There is no direct link between the prices charged to road users and the revenues received by road providers.

The bodies making decisions about future road funding are:

- local governments in respect of local roads (80% by length)
- state road agencies providing arterial roads

⁷⁰ Infrastructure Australia, *National Road Asset Reporting Pilot* (2013) p. 6.

⁷¹ The one exception to this is toll roads; however, given these amount to a relatively small component of the national network of roads this is unlikely to make a material difference to the analysis.

- state and Commonwealth governments providing nationally significant transport corridors (the National Land Transport Network).

Funding for these entities' investment in, and maintenance of, roads comes from a variety of sources including local rates, state general revenues and Commonwealth revenues.

In contrast, funds raised from vehicle registration and fuel excise do not go directly to those entities. Consequently, the road owner's revenue does not vary commensurately with the usage of the roads it maintains.

This has a range of implications. As the road owner does not necessarily receive additional revenue for doing so, the road owner:

- has no ability or incentive to change its pricing structures to encourage drivers off congested roads and onto roads with spare capacity;
- has no ability or incentive to change its pricing structures to encourage drivers to change their travel plans from peak to off-peak times; and
- does not have strong incentives to invest in increased road capacity even where there may be strong demand for the roads it manages.

This is likely to result in sub-optimal decisions to invest in and maintain certain roads or groups of roads. Furthermore, investment decisions in infrastructure for alternative modes of transport such as rail will also be less than optimal.

3. Decisions about funding for investment in roads are often made via political processes rather than by an independent assessment of the relative costs and benefits of a proposed investment. Decisions about road funding made by political processes can lack accountability and transparency.

The ACCC considers that the process by which decisions are made may lead to investment not being directed to those projects that have the highest economic value, leading to inefficient freight flows where roads may not be designed to support higher productivity heavy vehicles. This can lead to higher maintenance costs and, overall, higher transport costs as roads deteriorate and are replaced rather than maintained.

Road reform: The way forward

To date, reforms in the road sector have focused on pricing (the demand side) with limited change to how roads are provided (the supply side). To some extent this reflects the fact that, until recently, there have not been obvious ways for measuring and charging for an individual vehicle's use of the road system. However, technological advances are making such options increasingly feasible, and they will likely become more so in future.⁷² The scope for more substantive reform in the provision of roads is greater now than ever before.

The ACCC considers that a priority area for microeconomic reform is to establish the necessary architecture for functioning road markets. This will necessitate supply side reform opportunities as well as reform of user charging arrangements. Initial reform could focus on charges for heavy vehicles and the major road freight corridors as part of a longer term reform agenda.

Supply side reforms

Supply side reforms should ensure that new roads are being, and are seen to be, built where they are most needed. Changes to current institutional and governance arrangements are necessary to change the incentives of the road providers to ensure road provision is on an economically efficient basis. This will involve establishing some level of independence of those making investment decisions from government, including, possibly, the corporatisation

⁷² Productivity Commission, *Public Infrastructure* (Draft Report, 2014) Volume 1 pp. 132-3.

or competitive tendering of aspects of road provision and charging. Promoting greater commercialisation into the sector is also likely to facilitate the making of rational pricing decisions to maximise efficiency of the road system. In the longer term, as markets develop, consideration could turn to appropriate ownership arrangements and government involvement in the sector could lessen.

Supply side reforms have the potential to confer substantial benefits across the road system. Even in the partial market involving freight, where reforms have progressed furthest, the following benefits have been identified:

- Supply side reforms are likely to go some way to addressing what is known as the 'last mile' problem – the issue that the final leg of a supply chain is usually the least efficient sector of transportation. By better linking road pricing to funding road providers are likely to face incentives to make targeted investments which may, if efficient, ease restrictions to access for high productivity vehicles at key locations.
- Funding from heavy vehicle charges could be dedicated to roads and, further, directed to the specific roads or categories of roads that are valued most by that vehicle class so that appropriate levels of funding are allocated to road corridors servicing key supply chains.
- During the process of reform, while governments remain involved in the sector, supply side reforms are likely to facilitate greater competition for the supply of roads by allowing private providers and government providers to access road funding from vehicle charges on equal terms.
- Such reforms would also encourage widespread adoption of best practice contracting models by all levels of government. This includes, but is not limited to, focussing on minimising long term costs rather than short term costs, and encouraging investment in appropriate levels of road quality.
- Structural reform has the potential to establish monopoly service providers, as occurred in the reforms to the energy market. To ensure investment and pricing outcomes are consistent with principles of efficiency, there may be a need for economic regulation. An independent regulator could be required to establish or oversee pricing and related terms and conditions.
- CSOs imposed on road providers by governments – such as in relation to local roads, roads in rural and remote areas and particularly dangerous roads – should be transparent.

Reform of user charges

On the demand side, reform of user pricing is an important element of any market framework. As outlined above, road user prices currently do not reflect the cost of, or demand for, using the road, leading to inefficient decisions by road users and providers. It is also likely to distort competition between road and rail users.

A considerable amount of work has been carried out to date on road pricing, particularly in relation to user charges for heavy vehicles. In summary:

- In April 2007, COAG set up the COAG Road Reform Plan (CRRP) to conduct a review of current heavy vehicle user charges and to investigate the viability of alternative charging models for heavy vehicles.
- CRRP then conducted a Feasibility Study into other charging and funding arrangements for heavy vehicles. The study found that reform was feasible if charges were directly linked to road funding and investment changes. It recommended that new direct charging arrangements be developed for COAG consideration by December 2012.

- In July 2012, COAG noted the recommendations of the Feasibility Study, giving support for reform planning. The 2014-15 Budget confirms the Australian Government's ongoing support for heavy vehicle charging and investment reform.⁷³

The ACCC considers that the work undertaken to date by industry and government should be continued to determine the appropriate structure and level of road user charges including implementation arrangements. The supply side reforms identified above should also provide some impetus for demand side reform by better aligning the road providers' interests with the choices made by road users.

3.3.4 Congestion pricing

Key points

- Congestion pricing can be an effective mechanism to enhance the efficiency of infrastructure networks.
- In addition to roads, utilisation of congestion pricing could be an effective tool in relation to electricity networks, ports and airports where congestion externalities exist.

Introduction

Consideration of road pricing often includes consideration of congestion charges. Congestion pricing is a form of pricing which recognises that the monopoly infrastructure has limited capacity and that on occasion demand for the services of the monopoly infrastructure may exceed its ability to supply. At such times the price for the monopoly service may have to increase to efficiently balance supply and demand. This requires prices which vary dynamically according to the supply and demand conditions in the market. Congestion may also give rise to a negative externality, in that a user of a utility does not pay the full cost that its usage imposes on other users of that utility. For example, in heavy traffic a particular road user's decision to use that road at that time contributes to the congestion and thereby imposes a cost which is borne by all the other users of the road.

If unaddressed, congestion can result in two main kinds of inefficiencies. First, there is the possibility of a misallocation of available capacity, where non-price rationing (e.g. queuing) could result in users with a relatively low value of their use being satisfied in preference to users who value the utility more highly. Second, high levels of demand can result in a level of service quality which is too low because the private costs of use are less than the social costs, leading to excessive use.

At peak times congestion pricing will result in prices which efficiently ration access to the scarce infrastructure capacity. Only those customers who value the service the most highly will choose to use the infrastructure at those times. Congestion charges ideally account for the congestion externality cost in the usage price, meaning users pay for their contribution to the social cost. A party not willing to pay the social cost of their contribution to congestion would choose not to use the utility. While not all congestion will necessarily be eliminated at this price, marginal usage which costs more than it is worth will be avoided. Further, users with the highest willingness to pay will be given preference over those who do not value the utility as highly, improving allocative efficiency.

Case study – trucks accessing container terminals

Growth in container trade is expected to result in a doubling of Australia's freight task over the next twenty years. This will require targeted investments to increase capacity as well as ongoing productivity improvements in the sector.

⁷³ Australian Government, *Portfolio Budget Statement 2014-15*, Infrastructure and Regional Development, p. 247.

Despite most container terminals offering 24 hours per day and 7 day per week operations, weekday truck access is still the most intensely used, with around 50 per cent of truck activity occurring on weekdays between 6am and 6pm. With most container ports located in high urban density areas, building more roads is often not a feasible option to reduce congestion. The ACCC considers that the utilisation of peak period pricing models could be a more efficient way of shifting demand away from peak to off-peak times.

Peak period pricing models for trucks have been recommended in the past. In 2007, IPART recommended that an auction system for vehicle booking slots be implemented at the Port Botany container terminals. This was not, however, accepted by the NSW government which opted for a performance management system to improve truck turnaround times (this was implemented in February 2011). While it has been successful in improving turnaround times, it does not address more fundamental challenges of shifting terminal access from peak to off-peak times. This will be critical as container numbers escalate in coming years.

Case study – electricity

Electricity networks have obligations to meet power quality and reliability standards including at times of peak demand.

To meet these standards, networks must either:

- invest in network infrastructure to meet peak customer demand; or
- have access to options that deliver load reductions during times of peak customer demand.

Demand management can make greater use of existing networks and reduce the need for investment in network augmentation to cater for periods of high demand, thereby reducing the overall cost of the network.

A range of initiatives have been introduced by networks to encourage efficient demand side management options including direct load control where electricity distributors remotely control electric devices in a home or a business and turn on and off appliances such as air-conditioners and pool pumps for short intervals. However, further reforms are needed for more efficient peak pricing mechanisms in this sector including critical peak demand tariffs where customers are encouraged to reduce electricity consumption during peak demand periods.

Incentives to price congestion

An unregulated infrastructure owner generally has an incentive to increase price in response to congestion. However, where an infrastructure owner is subject to economic regulation under a 'revenue-cap' methodology, it may lack the incentive to engage in congestion pricing because under this approach the total revenue of the infrastructure owner is predetermined regardless of the volumes. Accordingly, in some circumstances, it may be necessary for governments to review the rules by which regulated prices are set.

Other industries

The ACCC considers there could be merit in utilising the approach of congestion pricing to address congestion in other infrastructure sectors such as ports (outlined above) and airports.

In relation to airports, there have recently been signs of increasing congestion at Australia's major airports (Sydney, Melbourne, Brisbane and Perth). Rapidly increasing passenger numbers, in part driven by the surge in demand for fly-in and fly-out services in the resources rich states of Queensland and Western Australia, appear to be placing pressure on aeronautical and landside infrastructure at these airports.

In terms of mechanisms to deal with congestion, there has been a preference in Australia, to date, to use administrative solutions to allocate airline slots instead of economic solutions such as peak-load pricing or the sale of slots by auction.

The administrative system relies heavily on the practice of ‘grandfathering’ slots – that is, the incumbent airlines retain the slots they have historically had access to provided they meet minimum usage requirements set out in airports’ use-or-lose guidelines.⁷⁴ Congestion and peak-period prices (or clarification of property and tradeable rights in slots) might be used, however, to better ration excess demand and also provide better signals for new investment in capacity.

The ACCC considers that, on balance, economic solutions to rationing airline slots are likely to lead to more efficient outcomes than administrative solutions. That said, it is important to take into account the sunk investments that have been made by airlines in relation to their slots and recognise the benefits that administrative allocation of airline slots can have in relation to issues such as scheduling.⁷⁵

There are few examples of true congestion pricing and peak-period pricing used at airports. In Australia, Brisbane and Perth airports have introduced minimum peak-period charges designed to discourage runway demand by smaller aircraft, typically providing regional services, during peak-periods.

The ACCC considers that there would be benefits to the consideration of whether economic solutions to the allocation of airline slots can be greater utilised in Australia.

3.3.5 Shipping

Key points

- Given the importance of shipping to the Australian economy, principles of competition and efficiency should be applied to ensure industry structures promote signals for efficient investment and use.
- For international shipping, cartel immunity to certain international shipping lines registered under Part X of the CCA should no longer be automatically available. Instead, a higher threshold for immunity should apply, such as that which applies to all other industry sectors through the authorisation provisions of the CCA. Cooperative arrangements between competitors can be authorised by the ACCC if they deliver net public benefits to the Australian community.
- In the domestic shipping sector, there are a number of legislative restrictions on competition that should be reviewed to ensure the costs do not outweigh the benefits of regulation; namely onerous procedural requirements relating to the granting of temporary licences for foreign shipping lines and the imposition of Australian labour standards which add to costs and ultimately higher freight costs for Australia businesses. Measures should be taken to ensure coastal shipping regulations (including cabotage) do not impede competition.

Introduction

Shipping is vital to the Australian economy given that 99 per cent of Australian imports and exports by volume are transported by sea. In addition, a proportion of Australia’s domestic freight also depends on coastal shipping. That said, of Australia’s domestic freight task, most freight is carried by rail. In 2011-12, rail had a 48.5 per cent share of the task, with road carrying 34.6 per cent and coastal shipping carrying 16.8 per cent of total domestic freight

⁷⁴ Most airports adhere to international guidelines on demand management set out by IATA, see: <http://www.iata.org/policy/slots/Pages/slot-guidelines.aspx>.

⁷⁵ Darryl Biggar, ‘Why Regulate Airports: A Re-examination of the Rationale for Airport Regulation’ (September 2012) 46(3) *Journal of Transport Economics and Policy* 367-380.

volumes. Coastal shipping can be an alternative to road and rail services, but may not always be available or competitive for Australian domestic routes or certain products.

Over the next 20 years, the nation's freight task is expected to double. It will therefore be critical to improve freight flows by promoting competitive industry structures that provide signals for efficient use of existing resources and investment in future capacity.

Regulatory restrictions on competition in the shipping industry

The ACCC is concerned that there are a number of regulatory restrictions on competition where it is not clear that the benefits of the regulation outweigh the costs to competition.

The ACCC considers that there are two particular areas where reform could lead to productivity benefits to the Australian shipping industry and the industries that rely on them. These are outlined below.

Cartel immunity to certain international shipping lines

The ACCC considers that Part X of the CCA – which provides cartel immunity to registered international shipping lines to enable them to cooperate with each other – is out-dated and unnecessary. Current administrative arrangements and the unique status afforded by Part X to international liner shipping result in a lack of transparency, and there is limited analysis suggesting that such anti-competitive agreements deliver net public benefits to Australia. This is in contrast to the existing net public benefit test applied to all other industries, under the existing authorisation provisions pursuant to Part VII of the CCA, where immunity can be granted to competitors who seek to enter into cooperative agreements.

It is also relevant to note that Part X extends conditional exemptions to declared inland terminals. This could limit transparency and competition where shipping lines provide a full and inclusive freight rate service that includes land transport to and from sea ports to inland terminals.

Part X was included in the CCA to address a concern that Australia, being geographically remote from many of its trading partners, was not an attractive region for international shipping lines to service. It was considered that international shipping lines would be more likely to service Australian markets if they were given exemption from anti-competitive conduct prohibitions to engage in discussions about scheduling and other matters (e.g. capacity and price). This was intended to provide Australian shippers with access to regular international shipping services and potential cost savings by bolstering the negotiating power of shippers. However, the increase of non-conference shipping services over time has resulted in Australian shippers having access to vessel capacity and competitive freight rates outside of the shipping services covered by registered Part X agreements. In 2004 the Productivity Commission recommended that Part X be revoked, but this recommendation was not implemented by government.⁷⁶ The ACCC's view is that the revocation of Part X is long overdue.

Domestic coastal shipping (cabotage) restrictions

In terms of domestic shipping, the ACCC is of the view that changes in recent years to Australia's coastal shipping regulations have impeded foreign shipping lines from competing with Australian vessels for domestic trade and add to freight costs for Australian businesses.

Cabotage is the restriction on the transport of goods or passengers between two locations in the same country by a vessel or aircraft registered in another country. Australian shipping is subject to a number of regulations whereby vessels are required to register and obtain licences to operate along Australia's coastline. For vessels registered in overseas countries to carry domestic (Australian) cargo when operating along Australia's coastline, they must

⁷⁶ Productivity Commission, *International Liner Cargo Shipping: Review of Part X of the Trade Practices Act 1974* (Report No. 32, March 2005).

adhere to the *Coastal Trading (Revitalising Australian Shipping) Act 2012* (Cth) and the *Fair Work Act 2009* (Cth). Foreign shipping lines are required to operate under a system of temporary licences (with trade restricted to a period of no more than 12 months) and pay their foreign crews Australian wages and conditions for the duration of their Australian voyage.

These requirements on foreign shipping lines are adding to administrative complexity and cost of providing a domestic shipping service and resulting in higher freight costs for Australian businesses. This is particularly concerning for a nation like Australia which is so dependent on freight systems for its national economic welfare. Additional costs imposed on foreign lines may affect whether such lines compete in the market for Australian coastal shipping. Where domestic trade represents an international shipping line's incidental business, any additional costs or onerous procedural requirements to carry domestic cargo could act as a general disincentive to entering the domestic shipping market.

The ACCC is also concerned that current regulatory arrangements can interfere with market forces by restricting the ability of foreign lines to compete with Australian vessels for coastal trade. For example, under the current licencing arrangements, Australian vessels can lodge a 'notice in response' to a foreign line's application for a temporary licence, claiming it is equipped with available capacity to carry the nominated cargo. While the licence assessment process provides for some discretion in granting a temporary licence, the ACCC considers the current administrative arrangements act as potential artificial impediments to new entry and competition resulting in higher freight costs for Australian businesses.

The case for whether or not coastal shipping should be regulated in its current form is an issue about the justification of ongoing industry protection. In most cases, restrictions on competition drive higher prices for customers – in this case, Australian businesses and consumers, in the form of higher freight rates. The Competition Policy Review should consider whether the benefits of current protections outweigh the costs they impose on Australian businesses and the wider community. A more detailed analysis of these issues is contained in the ACCC's submission to the government review of coastal shipping.⁷⁷

3.3.6 Energy

Key points

- While the energy sector has gone through an extensive reform program, the implementation of further reforms would enhance the efficiency of Australia's energy markets. Previous energy market reviews have highlighted the potential efficiency gains that could be realised by privatising remaining government owned energy assets with the objective of promoting competition, and deregulating retail markets.
- Other reforms may be required in the future to accommodate the significant technical change that the energy sector is facing. The energy market governance arrangements appear capable of identifying and responding to these issues as they emerge.

Energy sector reform

The energy sector in Australia has undergone significant reform over the past two decades.

Up to the early 1990s, in each Australian state there was generally a government owned, integrated electricity authority responsible for each step in the electricity supply chain – for the generation of electricity, for the transporting of electricity across transmission and distribution networks, and for supplying electricity to end use customers. There was no ability

⁷⁷ ACCC, *ACCC Submission to Government's Options Paper: Approaches to Regulating Coastal Shipping in Australia* (May 2014) available at www.infrastructure.gov.au (by following the links to the Review of Coastal Trading).

for consumers to choose their electricity supplier and there was no interstate trading of electricity.

From the early 1990s, Australian governments embarked on a series of reforms to establish a more efficient and competitive energy sector. The first step in the reform process was structural reform – both vertical and horizontal. The natural monopoly transmission and distribution networks were vertically separated from the potentially competitive generation and retail functions. The revenues of these network businesses were then subject to revenue regulation by an independent regulator. At the generation and retail levels, in each state there was generally horizontal separation into a number of competing generation and retail businesses.

The reforms also involved the development of a wholesale market to allow the trading of electricity. The NEM began operating in December 1998 and today covers six jurisdictions – Queensland, New South Wales, the Australian Capital Territory, Victoria, South Australia and Tasmania – that are physically linked by an interconnected transmission network. Western Australia and the Northern Territory are not in the NEM, largely because of the vast distances involved.

To date these market arrangements have successfully brought forward required generation investment. From the inception of the national market in 1998, over 13,000MW of generation capacity has been commissioned – more than a quarter of total capacity in the market. This has ensured that the generation capacity required to reliably supply customers has continued to be met – without the need for any central authority to purchase capacity.

While these reforms have been significant, rising energy prices have focused considerable recent attention on the performance of the energy sector. The key driver of the electricity price increases in most jurisdictions has been higher network costs. Some increases in network costs were necessary to replace ageing assets and meet increased peak demand. However, weaknesses in the framework for setting prices for energy network businesses, including significant restrictions on the ability of the regulator to reject excessive forecasts, meant that consumers were paying more than necessary for a reliable energy supply. Recent changes to the rules for setting these prices for energy network businesses have addressed these problems. Incentives for household solar PV also played a significant role in increasing retail electricity costs. Governments have subsequently revised the level of these incentives.

In gas, higher network costs were a key driver of price increases. However, the rise in wholesale prices to reflect export prices has also been a factor.

Further reform opportunities

There are further reforms that could be pursued to further enhance the efficiency of Australia's energy markets. Some of these reforms are 'unfinished business' from the initial reform program, while others may be required to ensure that the market deals appropriately with rapidly changing market conditions.

Privatisation

Despite recent privatisation in most states, there is still significant government ownership of electricity generation and electricity networks, particularly in Queensland, New South Wales, Tasmania and Western Australia.

A consistent theme of energy sector reviews over the past 15 years has concerned the potential benefits of privatisation of government owned generation and network assets.⁷⁸

⁷⁸ See Council of Australian Governments Energy Market Review, *Towards a Truly National and Efficient Energy Market* (2002); Energy Reform Implementation Group, *Energy Reform – The Way Forward for Australia* (2007); and Productivity Commission, *Electricity Network Regulatory Frameworks* (Inquiry Report No. 62, 2013).

The reviews have highlighted that under government ownership, businesses may have conflicting objectives. While these businesses may have incentives to become more efficient and profitable, their decision making may also be influenced by political factors or state development concerns. These conflicting objectives can create problems in both the network and generation sectors.

In networks, the regulatory regime is based on 'incentive regulation' where profit maximising incentives are designed to act as an impetus for businesses to pursue cost reductions and quality improvements. Network businesses that have conflicting objectives may not be as responsive to incentive based regulation. Privatisation of networks may help align the objectives of these network businesses with those of the incentive based regulatory framework.

In generation, previous reviews have highlighted that private sector players were reticent to enter markets where they would compete against government owned generators.⁷⁹ Private sector players believed that government owned players may not always act commercially, which created risk issues for the private sector players and discouraged entry. Privatisation of generation removes this key barrier to ongoing private investment.

Generation privatisation, however, will only provide long term benefits to consumers if a market structure is established which supports competition. This requires that sufficient competing players (number and size) are active in the market. Generation privatisation that is primarily motivated by the objective of maximising sale revenues will not be compatible with effective ongoing generation competition. Selling generators with substantial market power is likely to attract sale premiums, as is a sale which establishes an entity that will then be in a position to exert market power. However, these privatisations also create the potential for ongoing market power concerns. These considerations are particularly important given that there are large government owned generation portfolios in some states.

Retail price deregulation

Another major element of the energy reforms involved the introduction of competition in retail electricity markets. With the introduction of retail contestability for household customers in Tasmania from 1 July 2014, all customers in the NEM will be eligible to choose their electricity retailer.

While full retail competition has been introduced, there are still regulated retail prices in most states. Under the amended Australian Energy Market Agreement 2006 (AEM Agreement), COAG agreed to phase out energy price regulation in jurisdictions where competition is effective. Victoria phased out regulated retail prices on 1 January 2009, with South Australia and New South Wales following more recently. In other states, there is still a regulated retail price for consumers who do not take up an offer from a competing retailer.

There are a number of risks of continuing with retail price regulation where a market is competitive. If regulated prices are set too high, consumers who remain on the regulated retail price will pay too much for energy. If prices are set too low, competition will be affected as retailers will be discouraged from entering and competing in retail markets. Prices that are too high or too low also distort economic activity away from the level that would occur if the price was set correctly.

Consistent with the AEM Agreement, retail price deregulation offers the greatest potential to deliver retail energy markets characterised by strong competition that offer innovative products and services to the benefit of consumers.

Effective competition, however, does rely on informed consumers actively seeking out the best deal and finding the best prices. By providing customers with the tools to more

⁷⁹ See in particular Energy Reform Implementation Group, *Energy Reform – The Way Forward for Australia* (2007).

effectively compare retailers' energy offers, uniform adoption of the National Energy Customer Framework (NECF) will play an important role to play in supporting retail price deregulation. Adoption of the NECF is also expected to facilitate an increase in retail competition by reducing regulatory complexity and lowering barriers for energy retailers to enter into the market across participating states and territories. The full benefit of a national retail market will be realised when a uniform NECF is adopted in all jurisdictions.

Framework for considering further reforms

While these reforms are well understood, there is potentially a range of other reforms that may be required in future.

At present, the Australian energy sector is currently going through a period of significant technical change. There has been significant growth in small-scale local generation, particularly rooftop solar PV which has been installed by over a million households. Further, the IT and communication revolutions have opened up the scope for a host of new devices and appliances, allowing small-scale consumers for the first time to respond to local electricity market conditions.

These changes involve a significant shift in the way electricity is produced and consumed, and create a far more active role for consumers in the market; for example, by at times acting as net producers of electricity through their solar PV systems. The challenge is to ensure that any required amendments to market rules can be implemented to respond to changes in market conditions. In dealing with these emerging issues, competition should be relied upon to drive better outcomes for consumers. Market rules and regulation should not restrict competition unless the benefits to the community outweigh the costs.

The current governance arrangements provide an established process for progressing required changes to deal with emerging market issues. High level policy direction is set by the COAG Energy Council, which is made up of the energy ministers of the Commonwealth and state governments. This Council progresses key reform priorities in the energy sector. There is also an independent agency, the AEMC, responsible for approving amendments to the energy rules. Proposed changes are considered by the AEMC through an open, transparent consultation process.

While the pace of reform can sometimes be slow, these mechanisms are able to progress required energy sector reforms. As highlighted earlier, there was previously a range of significant weaknesses in the rules for setting prices for energy network businesses. In 2011, the AER submitted a rule change proposal to the AEMC to address these weaknesses, and reforms which significantly improve these rules were finalised by the AEMC in 2012.

Further, the AEMC's 2012 *Power of Choice* review recognised the changes the Australian energy sector is facing and recommended an integrated package of reforms to facilitate efficient demand side participation in the NEM. These reforms are designed to increase the responsiveness of the demand side to evolving market, technological developments and changing consumer interests over the next 15 to 20 years. While it has taken some time, these reforms are now in the process of being implemented.

This experience suggests that the market governance arrangements will be able to identify emerging issues in future and put in place arrangements to promote ongoing efficient investment and innovation. It does not appear that any significant changes to the institutional framework will be required to progress energy reforms in future.

There are aspects of these arrangements, however, that could be improved.

The pace of reform can sometimes be slow, particularly where the same issue is considered in separate market review and rule change processes. As highlighted above, changes to the rules resulting from the AEMC's 2012 *Power of Choice* review are only now being considered.

Further, there have been examples where individual initiatives were progressed that conflicted with broader reform priorities. As an example, in recent years there has been a range of reforms designed to deliver a secure but more affordable energy supply, such as reforms to network regulation rules and appeal processes. At the same time, however, there were other initiatives, such as incentives for household solar PVs. While these initiatives met broader environmental objectives, they placed upward pressure on electricity prices, as the costs of electricity purchased under feed in tariffs were reflected in electricity bills. In future reform, it will be important to ensure that proposed changes to the rules are considered holistically, and that the overall impact of individual initiatives which impact on energy costs are carefully considered. The national energy objective of promoting the long term interests of energy consumers provides a strong framework not only to consider changes to the rules, but also to consider the impact of other initiatives and reforms.

3.3.7 Water

Key points

- Extending the application of Water Act rules to address barriers to water trade outside the Murray-Darling Basin has the potential to increase water users' access to markets and enable water to reach higher value uses.
- The removal of remaining institutional or legislative impediments to rural-urban trade should be pursued, and structural reforms to facilitate competition in the supply of bulk water to urban areas, should be actively considered.
- States and territories should consider further 'unbundling' their water access rights into their component parts, with separate clearly defined and tradeable rights to storage, carryover and delivery where appropriate.
- Restrictions on the use and trade of water according to the identity of the water access right holder, or the purpose for which the water is used, should be critically assessed as they are inimical to the efficient allocation of water resources and operation of water markets.

Introduction

Water markets exist in many areas throughout Australia and enable the trade of statutory water access rights between users and locations. Where trade is well developed, water markets are an efficient and effective means of allocating scarce water resources between competing uses.

Most water trading in Australia occurs in the Murray-Darling Basin, particularly in the southern connected system around the River Murray, the Murrumbidgee River and the Lower Darling River. This trade has only been made possible by concerted reforms by governments at both the state and, more recently, Commonwealth level. However, further reforms have the potential to improve existing markets and to apply the lessons and experiences from reforms in the Murray-Darling Basin to other parts of the country.

Remove barriers to water trade imposed by irrigation infrastructure operators outside the Murray-Darling Basin

Significant progress has been made in reducing barriers to trade imposed by irrigation infrastructure operators (IIOs) in the Murray-Darling Basin. The benefits of these reforms should be extended beyond the Murray-Darling Basin to improve access to water markets and the opportunities for trade.

In rural areas, water taken from natural water courses is often delivered to irrigators and other water users by IIOs. These water users generally have a right of access to the IIO's

irrigation network – represented by their ‘water delivery right’ – and are required to pay fixed and/or variable charges to the IIO.

Where an IIO customer wishes to terminate their right of access – typically because they wish to permanently trade their water to an area outside of the IIO’s irrigation network – they are generally liable to pay a termination fee to the IIO.⁸⁰ While there are legitimate economic arguments for some level of termination fees, the fees and conditions imposed by an IIO can represent a significant barrier to the trade of water by their customer. Similarly, some IIOs hold a statutory water access entitlement on behalf of their customers, who in turn hold an ‘irrigation right’ against the IIO. In these situations, the IIO’s consent is required to trade water for use outside of the IIO’s irrigation network.

IIOs have an incentive to prevent the trade of water outside of their irrigation networks, primarily because this will reduce their revenue from variable charges. To prevent trade, IIOs can either withhold their consent for such trades (where they hold the statutory water access entitlement on behalf of their customers) or impose prohibitive termination fees. Such actions can effectively ‘lock’ water into a particular geographical area, preventing it from reaching higher value uses.

In the Murray-Darling Basin, the Water Charge (Termination Fees) Rules 2009 regulate the circumstances in which a termination fee can be imposed, and cap the maximum amount of the fee. The Water Market Rules 2009 prevent IIOs from preventing or unreasonably delaying the transformation of a customer’s irrigation right into a separate statutory water access right that can be traded free of IIO restrictions.

Extending the application of these rules to areas outside the Murray-Darling Basin has the potential to increase irrigators’ and other water users’ access to markets, providing them with greater flexibility in managing their water and delivery needs, and enabling water to reach higher value uses.

Case study – assessing the impact of reforms in the Murray-Darling Basin

Under the *Water Act 2007* (Cth), the ACCC prepares an annual water monitoring report. The most recent report, relating to the 2012-13 financial year, considered the impact of transformation (of irrigation rights) and terminations (of water delivery rights) on operators since the commencement of the water market and charge rules.

The report found that the impact of the rules on IIOs has been manageable to date. Most transforming irrigators are maintaining their access to the IIO’s irrigation network. In 2012-13, 82 per cent of transforming irrigators did not terminate any water delivery right, and nearly two thirds of transforming irrigators transformed less than half of their irrigation rights.

The introduction of the rules also saw a significant reduction in the termination fees imposed by most IIOs, and corresponded with significant increases in the volume of water allocation trade in the Murray-Darling Basin.

Facilitating competition in bulk water supply to major urban areas

Water is typically supplied to major Australian cities by a monopoly bulk water supplier owned by the relevant state or territory government. The bulk water business may also incorporate distribution and/or retail functions.

In these circumstances, there is little or no scope for the competitive provision of bulk water services to urban customers and the incentives for efficient supply augmentation will be dampened.

State and territory governments should actively consider the separation of bulk water supply activities from the distribution / retail functions of urban water businesses in circumstances

⁸⁰ Previously, ‘exit fees’ were imposed by IIOs when water was traded for use outside of their irrigation network. Termination fees are imposed when water delivery rights are terminated, rather than when water is traded.

where these functions are currently combined. Competition could be further advanced by the horizontal separation of existing bulk water supply activities into stand-alone businesses, each responsible for one or more bulk water sources such as a dam, desalination plant or water recycling plant. Each new bulk water supplier would also be subject to competition from new entrants / supply sources, including those from the private sector.⁸¹

The ACCC acknowledges that structural reforms like those outlined above are not without costs and care must be taken to ensure that the resulting market structure is sustainable in the longer term. However, the ACCC also believes that if managed properly, such reforms can produce significant benefits.

For example, while water trading between urban and rural uses already occurs within many systems in the Murray-Darling Basin, trade to or from major urban supply areas is less common. Such trade⁸² can allow urban distributors / retailers to increase supply more cheaply than alternative augmentation options and would provide a competitive constraint on the price of existing bulk water supply options.

Rural to urban trade would also provide rural water holders with an additional source of funds and access to expanded markets. Where water was sourced from within an irrigation network, revenue from termination fees or ongoing fixed annual access fees would continue to pay for the upkeep of infrastructure.

The ACCC considers that removal of remaining institutional or legislative impediments to rural-urban trade should be pursued even if structural reforms in urban areas are not pursued.⁸³

Clarify property rights for rural water storage and delivery

States and territories have separated water access rights from land in many of their water systems. However, the resulting water access right often still encompasses a right to store the water in dams, a right to carry over water from one season to the next and a right to have the water delivered to, or made available at, a location in a natural water course.⁸⁴

This means that water access right holders cannot independently adjust their access to storage, carryover or delivery without also adjusting their right to a share of available water resources.

States and territories should consider further 'unbundling' their water access rights into their component parts, with separate and clearly defined rights to storage, carryover and delivery.⁸⁵ Where appropriate, these separate rights should be clearly defined and made tradeable, to enable a more efficient utilisation of water service infrastructure.⁸⁶

⁸¹ The ACCC notes that these, and other, structural options have previously been considered by the Productivity Commission. See Productivity Commission, *Australia's Urban Water Sector* (Inquiry Report, 31 August 2011) chapter 12.

⁸² This assumes that hydrological connections and water supply considerations would make such trades possible.

⁸³ From 1 July 2014, a trade of a water access right from the Murray-Darling Basin can no longer be restricted because water extracted under that right may be transported or used outside the Murray-Darling Basin, due to the operation of section 12.10 of the Basin Plan. While this provision will address certain legislative barriers to rural-urban trade, it will not address any institutional impediments that may exist preventing or deterring urban water authorities from pursuing such trade.

⁸⁴ As noted at the beginning of the section, after water has been extracted into an IIO's irrigation network, separately defined water delivery rights govern where the water can be delivered *within* that irrigation network.

⁸⁵ The ACCC acknowledges that a right to storage is only applicable in regulated systems. Also, water access rights in some areas may encompass other characteristics amenable to being separately specified, such as a right to operate works, a right to use water on land.

⁸⁶ Water delivery rights within the irrigation network of an irrigation infrastructure operator (IIO) in the Murray-Darling Basin are often able to be traded. From 1 July 2014, the Basin Plan will prevent IIO's from unreasonably restricting the trade of water delivery rights.

Case Study – The Barmah Choke

The Barmah Choke is a narrow stretch of the Murray River between Cobram and Echuca. When the flow of the Murray reaches about 8500 ML per day (measured downstream of Picnic Point) the surrounding Barmah-Millewa forest floods. This limits the amount of water that can be delivered downstream in times of high flow. The constraint has led to restrictions on the trade of water access rights from areas upstream to downstream of the Choke.

This is because water access rights have an implied right to have water delivered to, or made available in, a particular location or zone. Approving the trade of a water access right from above to below the Choke effectively moves the obligation to deliver the water from above to below the Choke. Because there can be a significant delay between when a water allocation is traded and when it is ordered/used, water trading rules must take a relatively conservative approach to managing delivery constraints – restrictions on trading through the Choke apply even at times where it is not constrained.

Trades from below to above the Choke are generally always permitted as they do not increase the potential demand for Choke capacity. While such trades free up capacity in the Choke, this benefit is not captured by the seller of the water access right.

If the implied right to delivery is separated out from water access rights and made tradeable, there would be scope for mutually beneficial trade of such rights between water users. Furthermore, if this right was further clarified to relate to delivery at particular times of the year, then Choke capacity would be more efficiently utilised, and more water could be traded to higher value uses.

Ensure neutrality between different water users and uses

While the majority of water use in rural areas is for irrigation, other water users and uses are becoming more common. In particular, an increasing volume of available water access rights are held by environmental water holders, who use their water on wetlands, to supplement or replace natural flow regimes, to flush salt from systems or for other environmental purposes. Other water users, such as the mining industry, urban water authorities and forestry plantations are increasingly engaging in water markets.

The value placed on water use will differ between users and over time. The allocation of government issued water access rights through free and efficient markets is therefore the best means of ensuring that scarce water resources are used where they are most highly valued.

However, restrictions on the use and trade of water according to the identity of the water access right holder, or the purpose for which the water is used, remain widespread.⁸⁷ Restrictions of this type include restrictions on the ability to trade for non-land owners, for environmental water holders or urban water authorities. Similarly, states and territories may also make the holding of a water access right conditional on the water accruing to the right only being used for a particular purpose. These restrictions are inimical to the efficient allocation of water resources and operation of water markets.

Trading restrictions which apply to some users and not others (e.g. government owned water) undermines the efficiency of water markets by placing some participants at a competitive disadvantage. Where governments seek to expand opportunities for water trade, these opportunities should be made available to all water users.⁸⁸

⁸⁷ Part 2 of the Basin Plan water trading rules will address many of these restrictions from 1 July 2014, but only in the Murray-Darling Basin, and the rules contain a number of exemptions.

⁸⁸ See also the ACCC submission to the Murray-Darling Basin Authority's draft Constraints Management Strategy, available at: <http://www.mdba.gov.au/sites/default/files/cms-feedback/Australian-Competition-and-Consumer-Commission-Submission.pdf>.

3.3.8 Intellectual property

Key points

- On the *extent* of any intellectual property rights, relevant legislation and related institutions should balance:
 - (i) on the one hand, the incentives for innovation in the creation of intellectual property; and
 - (ii) on the other, the incentives that access to intellectual property material provides for efficient use of that intellectual property and for innovation from such use.
- On the *use* of intellectual property rights, the CCA should apply in the ordinary way. The ACCC recommends that section 51(3) of the CCA should be repealed and that, in general, there is no reason to treat intellectual property any differently to other services in relation to access. In future, access to intellectual property may be of increasing significance and effective access regimes may become more important.
- The ACCC considers that there is no reason to justify a blanket legislative restriction on parallel imports. Rather, any distribution arrangements that require a balance to be struck between the benefits of addressing a ‘free rider’ problem and any detriments to competition should be subject to the general competition provisions, where authorisation is available if the arrangements can be shown to be in the public interest.
- The ACCC recommends that the Productivity Commission be asked to inquire into whether the right balance is struck between the extent of intellectual property rights and their use.

Intellectual property (IP) is a form of intangible property right for the creation of something new or original. It grants an exclusive right of use (which may then be traded) to the rights holder, and includes copyright over literary, musical and artistic works; patents over inventions and new processes; trade marks; designs; and trade secrets and confidential information. Such rights are often of significant value to firms across a broad range of industries, and their ability to compete effectively can be significantly affected by their holdings of, or access to, particular rights.

The ACCC recognises there is a clear market failure which the establishment of IP rights is designed to address. It is possible, however, that the extent of such rights and subsequent use can have negative impacts on competition. It is important that:

- The *extent* of any IP rights should balance:
 - (i) on the one hand, the incentives for innovation in the creation of IP; and
 - (ii) on the other, the incentives that access to IP material provides for efficient use of that IP and for innovation from such use.
- The *use* of any IP rights should be subject to the CCA.

IP materials have the characteristics of a public good; that is, it is difficult to exclude parties from using it (non-excludable), and/or its use by one party has no effect on the extent to which it is available for others (non-rivalrous).⁸⁹

Creators of IP incur fixed and often high creation costs. Creators would be unwilling to incur these costs unless the expected risk-adjusted return equalled or exceeded them. However, once the IP is created it can be copied and utilised at very low, and often zero marginal cost. Absent IP laws that grant exclusive rights, the price of IP would tend to zero which would make no contribution to recovering fixed creation costs. That is, users would be generally unwilling to pay for a good as they could otherwise obtain it for free. As a result, expected

⁸⁹ A non-excludable product means that once the product has been made available, users who have not paid for it cannot easily be prevented from consuming it. Non-rivalry in consumption refers to the situation where one person’s consumption of a good does not reduce the consumption of the good available to others.

returns to the creator would be insufficient to provide appropriate incentives for efficient investment in IP material to the detriment of welfare.

IP regulation is one way to overcome this 'free-riding' problem as IP laws grant exclusive statutory property rights to IP rights holders and penalise unauthorised use of IP. By doing so, a positive price of using IP is able to be maintained, thus improving the incentives for its creation. However, the resulting ability to exclude may limit access to IP which has implications for its efficient use, including generating further innovation. Thus it is necessary for IP law to provide an appropriate balance between providing incentives for the *creation* of IP material and for the efficient *use* of that material.

Maintaining an appropriate balance may be of increasing importance in the future, as technology increasingly underpins the activities of all corners of the economy.

Extent of IP rights

The ACCC acknowledges that it is difficult to precisely define the extent of IP rights required to ensure that an appropriate balance is struck. In some cases, IP regulation may resolve the free-riding problem whilst creating or exacerbating other types of market failure.

A potential concern is that certain IP rights can lead to market power and competition issues. The ACCC considers that in the vast majority of cases the mere grant of an IP right will not raise significant competition concerns. The ACCC notes that rights holders are entitled to legitimately acquire market power by developing a superior product to their rivals, and pursuant to the policy purpose of IP regulation, the temporary market power from an IP right provides the very incentive to invest in the production of new IP. Such innovation is also a key goal of competition law. In this respect, IP and the competition law are for the most part complementary, both being directed towards improving economic welfare.

However, in particular cases, the use of exclusive IPs rights will raise a conflict between the two underlying policies. This might occur where IP owners are in a position to exert substantial market power or engage in anti-competitive conduct to seek to extend the scope of the right beyond that intended by the IP statute.⁹⁰

A relevant example is the ACCC's current action against the pharmaceutical company Pfizer.

Case study – Pfizer exclusive dealing conduct in supply of atorvastatin

The ACCC has instituted proceedings in the Federal Court⁹¹ against Pfizer Australia Pty Ltd (Pfizer) for alleged misuse of market power and exclusive dealing, in contravention of the CCA, in relation to its supply of atorvastatin to pharmacies.

Atorvastatin is a pharmaceutical product used to lower cholesterol. Pfizer's originator brand of atorvastatin, Lipitor, was for a number of years the highest selling prescription medicine under the Pharmaceutical Benefits Scheme. Prior to loss of patent protection in May 2012, Lipitor was prescribed to over one million Australians with annual sales exceeding \$700m.

The ACCC alleges that Pfizer offered significant discounts and the payment of rebates previously accrued on sales of Pfizer's Lipitor, conditional on pharmacies acquiring a minimum volume of up to 12 months' supply of Pfizer's generic atorvastatin product.

The offers were made prior to Pfizer's loss of patent protection for the Atorvastatin molecule, when other suppliers of generic medicines were prevented from making competing offers to supply a generic atorvastatin product to pharmacies.

⁹⁰ The OECD is holding a Roundtable on Generic Pharmaceuticals on 18-19 June 2014 that will focus on competition between originator and generic pharmaceutical companies, and the practices used by originators to reduce competition to the detriment of consumers. The Roundtable will consider a number of unilateral practices and anti-competitive agreements, including pay for delay agreements, which are of global concern to regulators.

⁹¹ *ACCC v Pfizer Australia Pty Ltd* (NSD 146/2014).

The ACCC alleges that Pfizer engaged in this conduct for the purpose of deterring or preventing competitors in the market for atorvastatin from engaging in competitive conduct as well as for the purpose of substantially lessening competition.

The case raises an important competition issue regarding the conduct of a patent holder nearing the expiry of the patent and what constitutes permissible competitive conduct.

In the ACCC's view, the extent of IP rights should be determined within a cost-benefit framework. For example, in relation to the duration of certain IP rights, the ACCC notes that careful consideration should be given to the effect of granting excessively long rights may have on innovation and in turn competition.

Other aspects of legislation may also define the extent of IP rights. For example, in the recent Australian Law Reform Commission's (ALRC) review of copyright and the digital economy (Copyright Review), the ACCC supported the introduction of a flexible 'fair use' exception in the *Copyright Act 1968* (Cth) (Copyright Act). Such an exception would limit the scope of copyright by allowing certain forms of use without payment to the copyright owner. The ACCC considers that such an exception has the ability to provide a desirable degree of flexibility that will enable the law to accommodate and foster technological advances and innovations that might otherwise be curtailed by prescriptive and/or narrow exceptions in the Copyright Act.

In contrast, legislation that limits so-called parallel importing can extend the application of IP rights beyond what is necessary to support innovation. This is discussed further below.

Parallel importing

Parallel imports are products that have been legally supplied in one country but are imported into another country without the permission of the owner of the IP rights in the importing country. A range of businesses that sell goods may be interested in parallel imports. For example, supermarkets may seek alternative overseas sources of groceries or other retailers may seek to source their products overseas. Incentives for parallel importing are likely to arise where a supplier or manufacturer seeks to segment its distribution into geographic markets and charge different prices (price discriminate⁹²) based on differences in consumers' willingness to pay across those markets rather than differences in the cost of supplying the different markets.

Parallel importation may circumvent such international price discrimination by allowing consumers to access goods sold at lower prices in non-Australian markets. Parallel importation provides an alternative source of goods, which can promote competition and potentially provide consumers with lower cost products and improve the international competitiveness of user industries.

Parallel imports of certain forms of IP are currently restricted by legislation, although the nature and extent of the restrictions varies according to the type of IP. Such restrictions effectively provide an import monopoly to the domestic distributor and protect owners of the local IP rights from competition. The restrictions may also enable copyright owners to practice international price discrimination to the detriment of Australian consumers.

For trade marks, use of a trade mark in relation to goods or services will not infringe the *Trade Marks Act 1995* (Cth) (Trade Marks Act) provided that the registered mark has been applied to the goods or services by, or with the consent of, the owner of the mark.⁹³ The Trade Marks Act therefore appears to allow parallel imports. However, recent cases in Australia (see case study below) have found that section 123 of the Trade Marks Act, as a defence to infringement, does not exclude any limit or condition on the grant of a trade mark. As a result, a trade mark owner may be able to prevent parallel imports into Australia if the

⁹² Price discrimination is discussed in further detail in chapter 4.

⁹³ Trade Marks Act s. 123.

use of the trade mark is for specific territories. Prospective importers will therefore need to not only be satisfied that their goods are legitimate, but also, whether there are any territorial or other conditions that apply which may limit their ability to import goods to Australia. In many cases this may be difficult to determine, especially where the good has been through a number of transactions (see *Paul's Retail Pty Ltd v Lonsdale Australia* below).

Case study – Sporte Leisure Pty Ltd v Paul's Warehouse International Pty Ltd and Paul's Retail Pty Ltd v Lonsdale Australia Ltd

Two recent cases, *Sporte Leisure Pty Ltd v Paul's Warehouse International Pty Ltd (No. 3)* [2010] FCA 1162 (Sporte Leisure Case) and *Paul's Retail Pty Ltd v Lonsdale Australia Ltd* [2012] FCAFC 130 (Lonsdale Case) considered the application of section 123 of the Trade Marks Act as a defence to infringement of a registered trade mark. Section 123 provides that 'a person who uses a registered trade mark in relation to goods that are similar to goods in respect of which the trade mark is registered does not infringe the trade mark if the trade mark has been applied to, or in relation to, the goods by, or with the consent of, the registered owner of the trade mark'.

Sporte Leisure case

This case involved trade marked clothing products imported into Australia by the retailer Pauls Warehouse. The trade marked clothing was imported from India. The Indian manufacturer had obtained a licence from the Australian trade mark licensor to use the trade mark, but had agreed to not supply the goods outside of India.

The Federal Court held that even though the clothing products had been manufactured overseas with the consent of the Australian licensor, the unauthorised importation and sale of those goods in Australia may infringe the registered trade mark.

Lonsdale case

Similar to the *Sporte Leisure* case, this case also involved the importation of trade marked clothing into Australia. Here, a United Kingdom company, Lonsdale Sports Limited (LSL) granted a German company, Punch, a licence to promote, distribute and sell goods bearing the Lonsdale trade mark within a defined territory in Europe. Pursuant to this licence, Punch sold Lonsdale branded clothing to a subsequent company in Europe. Ultimately, the Lonsdale branded clothing reached Paul's Retail who offered and sold the trade marked clothing in Australia. Lonsdale Australia, the Australian trade mark owner commenced action for infringement.

The Full Federal Court considered the application of section 123 of the Trade Marks Act. The court found that there was no consent by Lonsdale Australia as the use was outside the scope of the original licence, between LSL and Punch, which was to sell the trade marked products within the specified territory.

For some copyright products, including books, the Copyright Act grants copyright holders the right to restrict parallel imports, extending copyright protection into the sphere of distribution.⁹⁴ The appropriateness of an importation right under IP laws has been subject to considerable scrutiny and debate over several decades, both in Australia and overseas. In particular, the so-called importation provisions of the Copyright Act were subject to several inquiries, including several into sound recordings, books and computer software by the Prices Surveillance Authority (PSA). In each inquiry, the PSA found that the importation

⁹⁴ Under section 37 of the Copyright Act, it is generally an infringement of copyright to import a literary work, among other works, into Australia for commercial purposes without the copyright owner's consent, where the importer knew, or ought reasonably to have known, that if the literary work had been made by the importer in Australia it would have infringed copyright. Under section 38 of the Copyright Act, it is generally an infringement to sell an imported literary work if the seller knew that if the work had been made in Australia by the importer, it would have infringed copyright. Sections 102 and 103 of the Copyright Act extend importation protection to subject matter other than works. Essentially, in relation to books, these provisions protect the published edition of a book.

provisions enabled copyright holders to practice international price discrimination to the detriment of Australian consumers and recommended that the importation provisions of the Copyright Act be removed. In 2000, these recommendations were reiterated by the Intellectual Property Competition Review Committee.⁹⁵ In 2009, the Productivity Commission recommended that the parallel importation provisions be removed as they apply to books.⁹⁶

An outcome of the Australian debate is that the general prohibition regarding parallel imports was removed for sound recordings (in 1998) and computer software (in 2003). Also excluded from parallel import control are works and other subject matter that are accessories. There is a separate regime for books that allows limited parallel importation to address issues of availability.⁹⁷ However, the general prohibition against parallel importing still applies to literary works (other than books), dramatic, musical and artistic works, broadcasts and cinematographic films.

Individuals have always had the ability to import books from overseas for their own personal use. Thus on an individual basis, consumers are able to take advantage of lower prices offered by international online suppliers such as Amazon and Book Depository. These own-use exemptions benefit Australian consumers but may create an uneven playing field for Australian businesses (including small businesses) that are not able to parallel import on a commercial scale.

The ACCC has consistently held the view that parallel importation restrictions (via legislation) extend rights to copyright owners beyond what is necessary to address 'free riding' on the creation of IP (the economic rationale for establishing copyright in the first instance).⁹⁸ The ACCC considers that there is no further economic reason to justify a blanket legislative restriction on parallel imports. Rather, any arrangements that seek to address a 'free rider' problem in distribution⁹⁹ are not unique to IP, and should be subject to the general competition provisions, under which authorisation is available if the arrangements can be shown to be in the public interest.

Use of IP right: Competition law should clearly apply

Where there are significant competition concerns it is imperative that the use of IP rights is subject to the CCA in the same way as any other property right. In particular, the ACCC considers that the 'exception' in section 51(3) of the CCA should be repealed.

Part IV of the CCA prohibits anti-competitive agreements, mergers and other practices that substantially lessen, prevent or hinder competition. As the holders of IP rights may engage in arrangements with users of the material or with other IP rights holders, in some circumstances these arrangements may risk breaching the competition provisions of the CCA. The CCA contains per se prohibitions that prohibit certain conduct outright as well as general prohibitions against anti-competitive behaviour. The ACCC notes that in certain circumstances, parties can, via an application for authorisation or by lodging a notification, seek protection from legal action for conduct that risks breaching the Part IV provisions of the CCA (with the exception of misuse of market power). The ACCC may grant

⁹⁵ Intellectual Property and Competition Review Committee, *Final Report* (September 2000).

⁹⁶ Productivity Commission, *Restrictions on the Parallel Importation of Books* (Research Report, 2009).

⁹⁷ The Copyright Act was amended in 1991 to allow parallel imports of books in limited circumstances. The amendments mainly address the availability of books, rather than international price differences. If a book is not published in Australia within 30 days of overseas publication, protection from parallel imports is forfeited permanently. For other books, if a publisher does not respond to a written order within 7 days, or is unable to fill that written order within 90 days, booksellers can import enough copies to satisfy their reasonable requirements until the publisher restores availability. Booksellers are also able to import to fill verifiable orders by individuals and libraries. Individuals retain their ability to import for own-use.

⁹⁸ ACCC, *Submission to the ALRC Copyright and the Digital Economy Issues Paper* (November 2012); ACCC, *Submission to the Productivity Commission's Study into Copyright Restrictions on the Parallel Importation of Books* (January 2009).

⁹⁹ Note that 'free riding' in distribution is not necessarily an issue relevant to all forms of IP.

authorisation, broadly speaking, if it is satisfied that the likely public benefits of the conduct outweigh the likely public detriment.

Case study – the cost-benefit framework of collective copyright licensing

The ACCC has an ongoing interest and role in IP issues and in copyright more specifically. These arise from a number of sources, including the intersection of competition policy and IP policy, and from provisions in the CCA and the Copyright Act.

Similar to other forms of IP, copyright legislation seeks to overcome the free-rider problem by providing creators of copyright material with protections that allow them to exclude others from the use of their material within a framework of certain exceptions. In addition to this, collective management of licensing arrangements by copyright collecting societies is proffered as a solution to the high transaction costs of licensing copyright material. For many who seek access to copyright materials, a collecting society may be the only point of access.

There are benefits and efficiencies in the existence of collecting societies e.g. to provide a single point of access to copyright material for users with unpredictable usage requirements. However, the existence of collecting societies also raises some potential competition issues. Specifically, collective licensing is done by collecting societies who represent copyright owners, who might otherwise be in competition with one another, to act collectively rather than individually. This may raise concerns about the potential creation and exercise of market power. For example, a collecting society may negotiate fees that are higher than necessary to provide adequate incentives for investment in copyright materials, and may restrict competition that may otherwise be feasible, for instance from other collecting societies and from direct and source licensing.

The ACCC considers that the trade-off between costs and benefits of collective licensing should be balanced in pursuit of economic efficiency, with measures to control the potential exercise of market power by collecting societies if necessary to achieve an appropriate balance. The ACCC has an active role in two of these measures, the Copyright Tribunal of Australia (Copyright Tribunal) and the CCA.

Under section 157B of the Copyright Act, the ACCC can join cases brought by businesses before the Copyright Tribunal regarding the price for material licensed by copyright collecting societies. The ACCC has been a party to two proceedings before the Copyright Tribunal.

In proceedings concerning voluntary licenses and licence schemes, the Copyright Tribunal must, if requested by a party to the proceeding, consider relevant guidelines made by the ACCC.¹⁰⁰

The ACCC also has a role, through the authorisation provisions of the CCA, of ensuring the arrangements that collecting societies have in place with their members, licensees and other collecting societies, deliver net public benefits. In this regard, the ACCC has authorised the input, output, distribution and overseas licensing arrangements of the Australasian Performing Right Association (APRA) several times since 1999. On each occasion, the ACCC has recognised the arrangements deliver a number of public benefits. However, these benefits must be balanced with the public detriment resulting from the loss of competition between copyright holders. The ACCC has therefore imposed a number of conditions in each authorisation to mitigate the potential harm from APRA's market power and promote competition from source licensing where this is feasible.¹⁰¹

Currently, section 51(3) of the CCA provides a limited exception for certain IP licence conditions from the competition provisions of the CCA (misuse of market power and resale price maintenance are not excepted). The ACCC has a long standing view that section 51(3) of the CCA should be repealed. The ACCC considers that a blanket exception on certain IP

¹⁰⁰ Copyright Act s. 157A.

¹⁰¹ The most recent conditional re-authorisation of APRA's licensing arrangements was on 6 June 2014 for five years until 28 June 2019.

arrangements is not justified and the repeal of the section would prevent IP rights holders from imposing anti-competitive licence or assignment conditions. As noted above, the CCA contains provisions that allow the ACCC to grant protection from legal action to parties for conduct that risks breaching Part IV if it is satisfied that the likely public benefit (which predominantly relates to efficiency considerations) from the conduct outweighs any likely public detriment.

Section 51(3) of the CCA has been reviewed on a number of occasions and various recommendations to amend it have been made.¹⁰² More recently, in 2013, the Standing Committee on Infrastructure and Communication's final report from its inquiry into the pricing of information technology (IT) recommended the repeal of section 51(3) of the CCA.¹⁰³ A similar recommendation was also made in the ALRC's Copyright Review final report.¹⁰⁴

While the ACCC maintains that IP rights should be subject to the CCA in the same way as other property rights, it is important to recognise the inherent limitations in the competition law when considering other reforms to IP regulation. The ACCC notes that Part IV of the CCA covers specific types of anti-competitive conduct and as such may not be applicable to certain conduct in IP markets. For example, there may be no general competition law remedy for conduct that simply reflects an exercise of unilateral market power, such as monopoly pricing or poor service.

In this respect, if access to particular IP becomes more restricted in the future due to the pace of technological advancement, there may be a need to consider the effectiveness of existing access mechanisms.

Currently, access regimes for certain types of IP (e.g. the compulsory licensing regime for patents and the power of the Copyright Tribunal to determine charges and conditions for use of copyright materials) exist to provide an avenue for access to IP as well as a deterrent for unreasonable refusal to licence. Such provisions exist in recognition of the potential for excessive harm to competition from the withholding of supply by a rights-holder. In practice, they are utilised relatively infrequently; for example, there have been only three applications for compulsory licensing of patents.

In the event that existing frameworks prove not to be effective in ensuring efficient access in the future, some legislative change to access regimes may require further consideration. In its submission to the *Intellectual Property and Competition Review Committee* in 1999, the ACCC noted that there is no reason to treat IP any differently to other services in relation to access.¹⁰⁵ The ACCC reiterates this view, and notes that one way of achieving this might be to remove the IP exclusion from Part IIIA of the CCA.¹⁰⁶ The ACCC notes that were this option to be further pursued, additional ancillary changes to Part IIIA may also be required to clarify its application for this purpose. However, many features of the Part, such as the national significance test, would appear to provide appropriate thresholds for its application in this context.

Future challenges

The ACCC considers that IP regulation should be regularly reviewed within a cost-benefit framework and updated to ensure ongoing relevance. This is particularly important to ensure IP regulation does not restrict productivity gains arising from growth in the digital economy.

¹⁰² The NCC's review of sections 51(2) and 51(3) of the Trade Practices Act (March 1999); and the *Review of Intellectual Property Regulation* by the Intellectual Property and Competition Review Committee (September 2000).

¹⁰³ See Recommendation 8 in Standing Committee on Infrastructure and Communications, *At What Cost? IT Pricing and the Australia Tax* (2013) available at: http://www.aph.gov.au/parliamentary_business/committees/house_of_representatives_committees?url=ic/itpricing/report.htm.

¹⁰⁴ See ALRC, *Copyright and the Digital Economy Final Report* (February 2014) pp. 74-75, 196.

¹⁰⁵ ACCC, *Submission to the Intellectual Property and Competition Review Committee* (1999).

¹⁰⁶ Section 44B(E).

In addition to the need for the competition law to apply to IP rights, as discussed above, as technology becomes increasingly integrated into all aspects of economic activity, a number of challenges may arise in the attempt to achieve an appropriate balance for the regulation of IP.

First, the ACCC notes that IP regulation can become quickly obsolete as the manner in which IP material is used changes. This is particularly the case where the manner in which IP material is protected is highly dependent on the use of technology. For example, a key consumer service that has emerged in the digital economy is cloud computing. The now discontinued Optus TV Now service is an example of a cloud service that was unable to operate due to Australia's current copyright laws. While controversial, this may be an example of certain IP regulations not reflecting current consumer practices, lagging behind advances in technology or not being reflective of the manner in which IP is used.

The ACCC also notes that the growth in digital technology has resulted in calls for changes to IP regulation. For example, the ACCC's submission to the ALRC Copyright Review noted that the existing provisions in the Copyright Act may be inhibiting the growth of new services and competition made possible from developments in the digital economy.¹⁰⁷ One reason for this is because digital technologies are largely based on copying, so copyright law applies; however existing laws were not designed for the digital economy and may therefore achieve inefficient outcomes. This view was adopted by the ALRC in its final report.¹⁰⁸ As noted above, the ACCC also supports the introduction of a flexible 'fair use' exception in the Copyright Act.

Secondly, the ACCC considers that caution should be exercised when entering international treaties or agreements that may have the effect of significantly limiting the ability of the Australian Government to make substantial and effective reforms to IP regulation. Australia is a party to and/or in the process of (re)negotiating a number of international treaties and agreements. The obligations arising under these agreements may have significant consequences for the granting and use of IP (and consequently for competition) over many years, or even decades. Pursuant to the Agreement on Trade-Related Aspects of Intellectual Property Rights, to which Australia is a signatory, efforts have been made in recent years to further harmonise patent systems. While there may be benefits to harmonisation, the balance between a national competition law and IP objectives will differ internationally, and therefore, Australia should be highly mindful of the impacts on competition and the Australian economy in approaching future negotiations.

The ACCC considers that intervention in markets should only be triggered in the event of market failure. In the absence of market failure, open and competitive markets will generally ensure resources are directed to produce the goods and services that consumers want at the lowest possible cost. However, as discussed in section 3.2, as a general principle regulation should be proportionate and no more restrictive of competition than necessary. In the context of IP, intervention to address one issue may create or exacerbate other issues and any intervention must be carefully balanced. Although it may be debatable where the appropriate balance lies between protecting IP rights (thereby encouraging innovation) and ensuring access to IP, it is essential that the outcome delivers a net benefit to society (as opposed to particular interested parties or groups). Such an outcome would be consistent with an overriding objective of promoting efficiency and welfare.

The ACCC recommends that the Productivity Commission consider within a cost-benefit framework the extent of IP protections under the various relevant laws in Australia. Such a

¹⁰⁷ See discussion on third party use of copyright material in ACCC, *Submission to the ALRC Copyright and the Digital Economy Discussion Paper* (31 July 2013) pp.10-12, available at: <http://acc.gov.au/regulated-infrastructure/communications/intellectual-property/alrc-review-of-copyright-the-digital-economy/discussion-paper-submission>.

¹⁰⁸ See in particular ALRC discussion relating to fair use and third parties in the ALRC, *Copyright and the Digital Economy Final Report* (February 2014) available at: <http://www.alrc.gov.au/publications/copyright-report-122>.

review should examine whether these laws maintain an appropriate balance between on the one hand creating and maintaining incentives for innovation in the creation of IP and, on the other, maintaining incentives for its efficient use.

3.3.9 Human services

Key points

- The ACCC considers that there is likely to be the prospect for greater competition in human services, the potential benefits of which may include lower prices, greater efficiency in service provision, greater innovation and improved consumer choice.
- Mechanisms by which this could be achieved include by facilitating competitive neutrality between private and public providers and also by promoting competition between public providers.
- It is important to note that the CCA applies to human services and that the ACCC will continue to apply the CCA to safeguard competitive outcomes.
- Changes to introduce competition must take into account the need for regulatory oversight in a sector characterised by market failures with inter-related policy issues around equity, welfare and access.

What are human services

Human services – which include health, education, child care, aged care and disability care and support – have historically been areas of considerable government involvement via both funding and direct service provision. This section considers the prospects for greater competition in those sectors, and whether competition would be likely to bring productivity gains and benefits for consumers, with a focus on health and education.

Human services receive substantial government funding and are seen by many as an essential function of government. As an example, total expenditure (recurrent and capital) on health care services in Australia was estimated to be \$140.2 billion in 2011-12. This was estimated to account for 9.5% of gross domestic product in 2011-12, up from 7.8% in 2002-03.¹⁰⁹ In relation to education, national education expenditure was \$94 billion in 2010-2011. This was estimated to account for 7.1% of gross domestic product in 2010-11, up from 5.3% in 2006-2007.¹¹⁰

Human services markets in Australia

Market failures and regulation in human services

From an economic viewpoint, there would appear to be a number of market failures that characterise human service markets.

- 'Information deficiencies' may arise and as human services are often essential services upon which consumers rely, regulation is often required to provide sufficient assurance of quality and standards. Examples include regulatory oversight to accredit university courses and a regulatory framework to oversee aged care facilities.
- Some human services have an external benefit (positive externality). When a positive externality exists in an unregulated market, the price is unlikely to take into account the external benefits, and, as a result, the quantity produced is likely to be less than the socially efficient outcome. In health, for example, the community at large may

¹⁰⁹ SCRGSP (Steering Committee for the Review of Government Service Provision), *Report on Government Services 2014*, (2014) Vol. E, Productivity Commission, Canberra.

¹¹⁰ Australian Bureau of Statistics, *Year Book 2012* (Cat No 1301.0) (2013).

benefit from immunisation programs or basic public health initiatives. In education, public benefits may arise from universal basic education (providing a literate and educated population) and higher education may also contribute to economic productivity and growth.

- Economies of scale may limit competition making it uneconomic to service certain consumers – such as consumers in remote areas. This may raise equity and social policy issues, for example in relation to universal access to basic education and health services.
- There is a potential ‘agency problem’, particularly in health, because the patient is heavily reliant on advice from the health professional to make decisions. Because the health professional might have different incentives to the patient (for example, a healthcare professional may not always have regard to the price of different treatment options), there is an increased risk of gold plating and over servicing.

Given the above, it is unsurprising that human services are highly regulated sectors. While the private sector may provide certain services in these fields, regulation is designed to address market failures to ensure services are provided at a level consistent with society’s interests. As noted earlier, as a general competition principle, regulation should be proportionate to the market failure it is seeking to address and the impact on competition taken into account. However, the substantial market failures in human services provides context for the level of regulation of the sector.

Funding Mix

Governments provide substantial funding for human services. For example, Australian governments funded 69.7% of total health expenditure during 2011-12, an increase from 69.1% in 2010-11.¹¹¹ As well as funding ‘public’ providers, governments may also fund ‘private providers’ such as private schools.

The funding mix for human services is a matter of government policy and may change over time. While there may be both ‘public’ and ‘private’ providers, in some cases a provider may receive a mix of public and private funding.¹¹² In a budget-constrained environment there may be questions as to the appropriate mix of private and public funding and the appropriate scope of governmental involvement. The ACCC considers these are primarily policy questions that are distinct from the question as to what role competition can play in these markets.

Competition in human services

The Review Panel has asked whether greater competition among providers will serve the interests of consumers of health, education and other services. While noting the policy issues around equity, welfare and access, facilitating greater competition in the human sectors would likely have the same benefits as competition brings to any other sector. The potential benefits include lower prices, greater efficiency in service provision, greater innovation and improved consumer choice.

¹¹¹ Australian Institute of Health and Welfare, *Health expenditure Australia 2011-12* (AIHW Canberra, 2013). This report notes that the largest contributor to the spending in 2011-21 was on public hospitals (\$42.0 billion or 31.8% of recurrent expenditure. Expenditure on medical services (\$23.9 billion, or 18.1%) and medications (\$18.8 billion or 14.2%) were other major contributors.

¹¹² For example, public universities receive both Commonwealth funding and fee-based funding from student contributions. Similarly, private schools may rely on the fees paid by parents but also receive public funding. Health services in Australia are also delivered by a variety of government and non-government providers in a range of service settings. In the case of public hospitals, for example, the Australian Government and the states and territories together provide the majority of the funding. A small amount of other funding comes from private health insurers and from individuals who choose to be treated as private patients and pay hospital fees.

Specifically, benefits to consumers could arise from:

- Facilitating greater competition in the already deregulated aspects of the human services sector i.e. between private providers;
- Ensuring competitive neutrality between 'public' and 'private' providers; and
- Encouraging competition between 'public' providers e.g. using competition to promote innovation and efficiency within the public sector.

A degree of competition already exists

Despite the historical role of government in providing human services, a degree of competition already exists in many human services markets. This includes competition between private hospitals, doctors, secondary schools and vocational training providers, to name but a few examples. Given the development of substantial private markets in some human service industries, the ACCC plays a role in protecting or promoting competition in those markets through the general application of the CCA. The ACCC receives complaints about competition in human services such as the health sector¹¹³ and has applied the CCA to promote competition in the human services sector.

Case study – enforcement action in professional health services

As an example of how the CCA can apply to health services, in 2007 the ACCC instituted proceedings alleging that two Adelaide cardiothoracic surgeons engaged in anti-competitive conduct over the provision of cardiothoracic surgical services to private patients in or near South Australia.

The Federal Court made declarations including that the two doctors sought to reach a non-compete arrangement with other doctors to withdraw services from particular hospitals. Further, that the two doctors made an arrangement that they would hinder or prevent a newly qualified surgeon from entering or supplying his services in the market before he had undertaken further surgical training, notwithstanding that he was legally qualified to practice as a cardiothoracic surgeon. The doctors gave effect to that arrangement by advising either hospitals at which the surgeon sought to operate, or cardiothoracic surgeons who had been asked to support the surgeon's applications to operate at those hospitals, that the surgeon was insufficiently trained, or had not completed his training, and should not be allowed to operate at those hospitals.

The court ordered each of the doctors to pay a pecuniary penalty of \$55,000.

The ACCC has taken enforcement action in a number of other cases in relation to conduct relating to where doctors or other health professions (e.g. orthodontists and radiologists) acted together to withdraw services, prevent competition from other providers, induce boycotts, fix the price of health services, or impose referral policies that restricted supply.

¹¹³ In 2013, the ACCC received 65 contacts about competition health-related issues. The types of issues raised include anti-competitive rostering and accreditation issues, boycotts impacting competitors, preferential referrals or exclusive arrangements, pricing issues including fee setting, private health ancillary services, merger, authorisation and notification issues; and issues relating to government funding or policy.

Case study – private hospital mergers

In the context of private hospitals, the ACCC recently assessed the proposed acquisition of Brunswick Private Hospital in Melbourne by Healthscope Limited. The ACCC released a statement of issues on 27 March 2014 noting that the ACCC was concerned that the proposed acquisition was likely to result in a substantial lessening of competition in the market for the supply of private rehabilitation services to patients in northern Melbourne. On 12 June 2014 the ACCC announced its decision to oppose the acquisition. The ACCC has also assessed other private hospital mergers including Health Care's proposed acquisition of Brisbane Waters Private Hospital at Woy Woy on the New South Wales Central Coast and St John of God Health Care Inc's proposal to acquire the Mercy Hospital at Mount Lawley in Perth.

The CCA applies to the human services sector as it does any other industry. The ACCC will continue to apply the CCA to those substantial areas of the human services industry that are already subject to competition, in order to safeguard competitive outcomes.

Competitive neutrality

The ACCC supports the promotion of competitive neutrality to ensure that government businesses do not have a competitive advantage simply by virtue of their public sector ownership. In terms of human services, the role of private providers is significant. Competition between 'public' and 'private' providers may mean that consumers of 'public' services have access to a generally lower cost but less differentiated 'public' product. Conversely, the availability of private alternatives may provide an option for those dissatisfied with the public system. Therefore, the public and private competition process could include, for example, parents withdrawing their children from public schools to attend private schools or using a public hospital even where insured for private health cover.

As discussed above at section 3.2, the ACCC considers that Australian governments should review their competitive neutrality policies and related mechanisms. A review into, among other things, the timeliness and transparency of complaints handling and the implementation of recommendations, could promote more effective regimes.

Case study – Cyclopharm and PETNET competitive neutrality

In 2011 a manufacturer of nuclear pharmaceuticals called Cyclopharm complained to the Australian Government Competitive Neutrality Complaints Office (AGCNCO), that it was unable to compete with a government owned competitor, PETNET Australia, who priced a product below cost and did not apply commercial interest rates on borrowings.

The AGCNCO found that the business plan of PETNET would put it in breach of competitive neutrality requirements, noting that the 'revenue and expenditure forecasts over 10 and 15 years demonstrate that PETNET Australia's commercial operations are unlikely to achieve a commercial rate of return on the equity invested over either time period'.

The ACCC understands that the recommendation of AGCNCO in relation to PETNET was not actioned further by government. The ACCC further understands that in the absence of specific action, in June 2012 Cyclopharm instituted proceedings in the Federal Court against PETNET for alleged contraventions of section 46 of the CCA and section 18 of the Australian Consumer Law. This case has not yet concluded.

Encouraging competition between 'public' providers

Even where services are funded in whole or part by the government and there are 'public' providers, there is potential for competition between those public providers. For example, there may be some restrictions on the ability of consumers to choose a public provider e.g. school zoning. These restrictions on competition are generally directed at ensuring scarce public resources are allocated efficiently, but by limiting substitution may dull incentives for

innovation and quality amongst public providers. The prospect for greater choice between public providers may therefore be worth further consideration in the overall context of health and education policy.

3.3.10 Land use

Key points

- Land use restrictions may affect competition by raising barriers to entry. Drawing on the experience of the Productivity Commission, there is evidence that some restrictions are not proportionate – i.e. they may be not be of benefit to the community as a whole.
- Many land use restrictions are applied at a sub-national basis leading to a diversity of approaches that may make these restrictions difficult to review.
- The ACCC recommends that competition analysis should be incorporated into planning decisions in a manner that considers the benefits to consumers from competition.

Land use restrictions must be proportionate

Planning and zoning regulations address how land can be used and by whom. Such regulations can be intended to ensure that land is allocated for high-value uses, having regard to the impact of certain uses on others in the community. This may include environmental and social amenity considerations.

Regulation that is *disproportionate* can restrict valuable development by increasing the cost of starting new businesses, creating delays in the opening of new businesses, or restricting the total supply of a service/good. As a general principle legislation should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs and the objectives of the legislation can only be achieved by restricting competition. Land use restrictions may therefore involve considering environmental or social amenity considerations, while taking into account competition.

Internationally, the OECD Competition Committee has articulated how this general principle of proportionality may apply and the intersection between land use restrictions and competition policy:¹¹⁴

Land use restrictions often serve valuable social purposes. The benefits of particular policies for land use must be balanced against the costs though ... More careful integration of policy on land use restrictions with competition policy could benefit consumers and many entrepreneurs and reduce the likelihood that public or private restrictions will lead to scarcity.

The ACCC considers that there are planning, zoning, or other development regulatory restrictions that could exert an adverse impact on competition and recommends that reinvigorating competition policy reform should include consideration of land use laws.

Case study – retail locations

Retailing regulations may require planning approval for businesses to retail in particular locations. The Productivity Commission found that retailing location restrictions are extremely complicated, prescriptive, and exclusionary and may act to restrict market entry.¹¹⁵ By imposing increased 'red tape' these processes may act to deter new market entrants, including small businesses, or increase the costs of market entry.

¹¹⁴ OECD, *Policy Roundtables: Land Use Restrictions as Barriers to Entry* (2008). Available at <http://www.oecd.org/daf/competition/sectors/41763060.pdf>.

¹¹⁵ Productivity Commission, *Performance Benchmarking of Australian Business Regulation: Planning, Zoning and Development Assessments* (2011) and Productivity Commission, *Economic Structure and Performance of the Australian Retailing Industry* (2011).

Barriers to entry

Land use regulation can explicitly or implicitly operate to limit new entrants by taking into account impacts on established businesses, such as how incumbent businesses may be negatively affected by competition by new entrants. For example, processes that require consideration of whether there is 'unmet demand' for a proposal explicitly limit competition from new entrants. Other regulation may implicitly have this effect. For example, a Productivity Commission survey found that 3% of Australian councils considered protecting local businesses a *top five* priority of council planning; in Tasmania the figure was 17%.¹¹⁶

Whether explicit or implicit, the form of these regulations may operate to protect existing market participants, at a cost to the community as a whole including potential new entrants and consumers. The ACCC does not consider that it is ever appropriate for planning processes to be used for the purpose of protecting existing market participants from competition from new entrants. This is because competition provides the *incentive* for greater efficiency and innovation, to the benefit of consumers.

Gaming of appeals processes

Planning and zoning rules which have a strong policy rationale on social amenity grounds may still be manipulated for anti-competitive purposes and policy makers should be conscious of this potential. This may include 'gaming' of appeals processes and procedures by incumbents to neutralise competitive threats by objecting to deter competition or delay competitive entry.

Case study – ACCC v Liquorland (Australia) Pty Ltd

An economic justification for liquor licensing is that it ensures the social costs of liquor are taken into account when establishing the number of, and location of, liquor outlets as well as their trading hours. However, there may be concerns where appeal processes allow existing liquor licence holders to prevent or delay new entrants to the detriment of competition and, in particular, where those processes are subject to gaming by incumbents.

As a case study of how licensing regimes may be used with anti-competitive effect is *ACCC v Liquorland (Australia) Pty Ltd* (2005) ATPR 42-070. The ACCC alleged that the conduct arose in circumstances where Liquorland objected to certain liquor licence applications and then proposed restrictive agreements in return for withdrawing their objections. The Federal Court ordered Liquorland to pay penalties of \$4.75 million in total.

Case study – grocery inquiry

In the 2008 grocery inquiry the ACCC found that planning and zoning laws can act as a barrier to the establishment of new supermarkets.¹¹⁷ The ACCC also received specific and credible evidence of incumbent supermarkets using planning objection processes to deter new entry in circumstances where the incumbent supermarket had no legitimate planning concerns.

Competition policy, land use and local government

Many planning and zoning regulations are applied at a sub-national basis, at the state or local council level. This means that there is a great variation in the type and amount of regulation. As discussed in chapter 5, reinvigorating competition policy requires a coordinated approach led by appropriate institutions to ensure the principle of proportionate regulation is implemented effectively.

¹¹⁶ Productivity Commission, *Performance Benchmarking of Australian Business Regulation: Planning, Zoning and Development Assessments* (2011) p. 39.

¹¹⁷ ACCC, *Report of the ACCC Inquiry into the Competitiveness of Retail Prices for Standard Groceries* (July 2008) p. xix.

3.4 Conclusion

As the Hilmer Review observed, while competition rules have many benefits, more is required if Australia is to build a more competitive economy.¹¹⁸ This chapter has set out eight key principles that the ACCC considers should form part of the intergovernmental commitment to competition. These are largely based on the principles coming out of the Hilmer Reforms, but reinvigorated to take into account the lessons learnt since the adoption of the CP Agreement in 1995. This chapter identifies, by way of example, ten areas where there is potential to drive productivity growth by applying these principles. If Australia is to prosper, and to generate sustainable jobs in an era of globalisation, Australia needs a renewed commitment to these competition principles.

¹¹⁸ Hilmer Review p. xxviii.

4 Competition and consumer law in Australia

4.1 The role of competition and consumer protection law

4.1.1 Making markets work for consumers and businesses now and in the future

The objective of the CCA is to enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection.¹¹⁹ Most relevant to this chapter it does this by:

- setting the boundaries for what anti-competitive conduct is prohibited, where businesses act either unilaterally or in collusion (Part IV);
- prohibiting unfair practices, primarily through the Australian Consumer Law provisions prohibiting misleading conduct, unconscionable conduct and unfair contract terms; and
- providing for consumer protection, including through the provisions in the Australian Consumer Law relating to product safety.

This chapter focusses on the competition provisions of the CCA, which include provisions prohibiting anti-competitive agreements, misuse of market power, anti-competitive vertical restraints and mergers or acquisitions which substantially lessen competition.

Competition law is critical for preserving the integrity of markets, so that businesses have the incentive to operate more efficiently, price competitively and offer better products to their customers. This in turn delivers benefits to the community through lower prices, innovation, and higher quality products.

Australia will only benefit from a market economy if it works within appropriate boundaries. Competition law must strike a balance between, on the one hand, preventing business activities that undermine the competitive process and, on the other, not inhibiting healthy rivalrous behaviour that is part of the ordinary cut and thrust of robust competition. While the ACCC recognises this challenge, it should be stressed that there are large losses from exclusionary, collusive or coercive conduct if competition law is too weak.

Protection of the competitive process does not equate to protection for individual competitors. Effective competition is a vigorous process, where businesses which are less efficient or which no longer provide a compelling offer to consumers are replaced by more efficient or innovative businesses.

Where competition does not promote efficiency, the CCA provides a range of mechanisms for businesses to receive legal protection for engaging in anti-competitive conduct if it will result in a net benefit to the public.

Whilst the Australian Consumer Law is not a focus of this review, the ACCC considers it important to note that the consumer protection provisions play a crucial and complementary role to the competition rules in ensuring that markets work for Australian consumers. Where a business engages in misleading or deceptive conduct, uses pressure sales tactics or acts unconscionably to take advantage of its customers, consumers are unable to make well-informed decisions regarding their purchases and an uneven playing field is created for other businesses that compete fairly.

This undermines one of the fundamental requirements for the efficient operation of markets – that consumers are well informed and able to act in their own self-interest to purchase goods and services that best meet their needs.

¹¹⁹ CCA s. 2.

4.1.2 Assessing Australia's competition law

The competition law should regularly be reviewed to ensure that it remains effective in prohibiting conduct which is anti-competitive whilst not prohibiting conduct that may be welfare enhancing. The law must also be tested to ensure that it is flexible enough to be applied in new markets and to evolving business practices. Where the competition law is inadequate in preventing anti-competitive behaviour, Australian consumers, and the economy, suffer detriment through higher prices, inefficient allocation of resources and lack of innovation.

In preparing this submission the ACCC has had regard to a number of principles that may provide a useful framework for assessing whether the competition law continues to promote competition for the welfare of all Australians.

- **Efficient:** Competition law ensures that markets work in an efficient manner by prohibiting businesses from engaging in conduct which undermines the competitive process. The law should prohibit anti-competitive conduct but should also permit conduct which is pro-competitive or more efficient.
- **Universal:** Competition law should apply to all sectors of the Australian economy, other than where a more limited application has been found to provide a net benefit to the public.
- **Clear:** Setting the parameters regarding how businesses may behave to ensure the integrity of markets can give rise to some unavoidable complexities. It is important that the CCA strikes the right balance between complexity and clarity so that the laws remain comprehensible and workable.
- **Effective:** Prohibitions will not act as a deterrent or shape business behaviour where they cannot be readily enforced or where penalties do not act as an appropriate deterrent. To be effective, the prohibitions must be able to be efficiently enforced by the ACCC and private litigants, and penalties must outweigh the gains that businesses may obtain from anti-competitive conduct.
- **Proportionate:** Regulation should be imposed only when it can be shown to offer an overall net benefit. The prohibitions and statutory processes set out in the CCA should strike a balance between providing a framework which promotes more efficient markets and the regulatory burden imposed upon business.

In addition to the principles outlined above, Australia's competition law should have regard to developments in other jurisdictions and the challenges faced in applying local laws to global economies. International jurisdictions provide useful guidance regarding alternative approaches to competition policy. However, any comparison must have regard to the broader legislative, social, political and historical context within which those international policies apply.

4.1.3 ACCC submission regarding the CCA

The ACCC's submission addresses the following topics:

- Key areas where the CCA requires reform to ensure that it continues to deliver efficient outcomes for Australian consumers (see section 4.2).
- Provisions within the CCA where the policy settings are correct but the provisions are unwieldy and overly complicated. The ACCC recommends areas where these provisions could be reviewed to provide greater clarity (see section 4.3).
- Improvements to the ACCC's investigative tools to ensure that the ACCC is able to effectively enforce the prohibitions (see section 4.4).

- The ACCC's role in relation to small business and specific reforms to the CCA that are likely to assist small businesses (see section 4.5).
- Further information to assist the Review Panel in relation to topics raised by the *Competition Policy Review: Issues Paper*¹²⁰ (see section 4.6).

In preparing this submission, the ACCC has not provided information in relation to all of the questions posed by the Issues Paper, or all of its functions under the CCA. The ACCC has also not sought to restate its detailed submissions provided to the *Independent Cost-Benefit Analysis and Review of Regulation* (also referred to as the 'Vertigan Review')¹²¹ and the Productivity Commission *Inquiry into the National Access Regime*¹²². The ACCC would be happy to provide further information should it assist the Review Panel.

4.2 Reforms to the CCA to ensure that it continues to drive efficient outcomes

Key points

The ACCC considers that there are several areas where the CCA could be amended to better meet the principles identified above. Key areas for improvement include:

- Amend the section 46 misuse of market power prohibition to ensure that it is effective in prohibiting anti-competitive conduct by firms with substantial market power. The ACCC considers that this could be best achieved through the introduction of an effects test and amendments to overcome limitations with the application of 'take advantage'.
- Expand application of the 'price signalling' provisions prohibiting anti-competitive disclosure of information throughout the whole economy, not just the banking sector.
- To bring merger authorisation into line with other authorisation provisions, remove first instance merger authorisation by the Australian Competition Tribunal, to be replaced with merger authorisation by the ACCC with a right of review by the Tribunal.
- Amend the third line forcing provisions to prohibit such conduct only where it has the purpose, effect or likely effect of substantially lessening competition in a market (subject to review and, if necessary amendment, of the Australian Consumer Law to ensure adequate consumer protections remain).
- There are a number of exemptions from the CCA that are no longer appropriate, and others that should be amended to better ensure that the restriction on competition is proportionate and results in a net benefit to the public.
- Amend the CCA to put beyond doubt that conduct which occurs overseas, but which has an anti-competitive effect in Australia, is caught by the CCA. This should include clarification to the circumstances in which an overseas corporation is considered to be 'carrying on business within Australia'.

¹²⁰ Issued by the Review on 14 April 2014.

¹²¹ The ACCC's submissions to this review are available at the review homepage (http://www.communications.gov.au/broadband/national_broadband_network/cost-benefit_analysis_and_review_of_regulation) or on the ACCC [website](#).

¹²² ACCC, Productivity Commission Review of the National Access Regime - ACCC Submission to Issues Paper, February 2013 available at www.pc.gov.au by following the links to the submissions to the inquiry into the National Access Regime (2013).

4.2.1 Misuse of market power prohibition requires reform to be fully effective

The ACCC considers that the effectiveness of section 46 is hindered by the form of its current drafting and the unduly narrow interpretation of the words of the statute adopted by the courts.

The ACCC supports amendments to section 46 to overcome limitations on the application of ‘take advantage’ and the lack of an effects test.

Current provision – not effective in capturing anti-competitive unilateral conduct

Section 46 of the CCA, which contains the prohibition against misuse of substantial market power, is a crucial component of Australia’s competition law. It provides that a firm with a substantial degree of power in a market shall not take advantage of that power for certain proscribed purposes. The High Court has described the object of section 46 as being to protect the interests of consumers and that competition is a means to that end.¹²³

U.S. economist and judge Richard Posner has written that most truly exclusionary conduct is engaged in by what he termed the ‘fragile monopolist’ whose substantial market power is under threat from actual or potential competition.¹²⁴ Encouraging new entrants or ‘challenger firms’ is extremely important for the proper functioning of our market economy.

Section 46 focusses specific attention upon firms that have substantial market power. This was emphasised by the High Court in *Melway Publishing Pty Ltd v Robert Hicks Pty Limited*¹²⁵ at [29] where the majority quoted from Scalia J of the Supreme Court of the United States (*Eastman Kodak Co v Image Technical Services Inc* 504 US 451 at 488 (1992)):

Where a defendant maintains substantial market power, his activities are examined through a special lens: Behaviour that might otherwise not be of concern to the antitrust laws – or that might even be viewed as procompetitive – can take on exclusionary connotations when practised by a monopolist.

The types of unilateral conduct that the prohibition aims to capture include refusals to supply, price-based exclusionary conduct (predatory pricing, loyalty rebates, bundling and price squeezes), conduct which raises the costs of rivals, vertical restraints and leveraging of market power across markets. However, such conduct is only prohibited by section 46 if the firm possesses a substantial degree of market power and has taken advantage of that power for the purpose of:

- eliminating or substantially damaging a competitor;
- preventing the entry of a person into a market; or
- deterring or preventing a person from engaging in competitive conduct.

Section 46 has been the subject of significant discussion, numerous reviews¹²⁶ and legislative amendments which have attempted to codify its interpretation.¹²⁷

The ACCC considers that, as currently drafted and interpreted, the provision is of limited utility in prohibiting conduct by firms with substantial market power which has a detrimental impact on competition.

¹²³ *Queensland Wire Industries v Broken Hill Pty Ltd* (1989) 167 CLR 177 at 191 per Mason CJ and Wilson J (‘*Queensland Wire*’).

¹²⁴ Richard A. Posner, ‘Keynote Address: Vertical Restrictions and “Fragile” Monopoly’ (2005) 50(3) *The Antitrust Bulletin* 499.

¹²⁵ (2001) 205 CLR 1 (‘*Melway*’).

¹²⁶ For example, chapter 4 of the Hilmer Review; chapter 3 of the Dawson Report.

¹²⁷ For example, several subsections were introduced in 2007 to clarify the interpretation of a substantial degree of market power: *Trade Practices Legislation Amendment Act (No 1) 2007* (Cth) sch 2; similarly, section 46 (1AAA) and (6A) were introduced in 2008 to clarify *inter alia* the interpretation of take advantage and selling below cost: *Trade Practices Legislation Amendment Act 2008* (Cth) sch 1, 2.

The ACCC considers that the provision is deficient in two respects: first, due to its failure to capture unilateral conduct which has a deleterious *effect* on competition; and second, due to the way in which the *'take advantage'* limb of the test is currently being applied.

Capturing anti-competitive unilateral conduct – an 'effects' test

In its current form, section 46 does not capture unilateral conduct by a firm which has the effect or likely effect of substantially lessening competition, unless it can be shown to have one of the proscribed purposes.

The ACCC has long argued that the failure of section 46 to consider the effect of conduct by a firm with substantial market power is a gap in the law.¹²⁸

While the ACCC has not lost a section 46 case in the courts on the basis that it has failed to establish an anti-competitive purpose, the impact of the purpose requirement often arises at the earlier, investigative, stage. There have been occasions where the ACCC has investigated serious complaints from market participants alleging an anti-competitive effect as the result of unilateral conduct by a dominant firm, but the ACCC has formed the view, based on the documents and evidence available, that despite the anti-competitive effect it would be unable to establish that the conduct had been engaged in for a proscribed purpose. In those circumstances, the ACCC has been unable to commence proceedings against the dominant firm under section 46. Accordingly, simply observing the outcome of, and reasoning deployed in, decided cases on section 46 will not adequately capture this deficiency. This experience also suggests that, as currently drafted, Part IV of the CCA does not effectively capture all forms of anti-competitive unilateral conduct and fails to recognise that economic harm can arise from unilateral conduct which has the effect of substantially lessening competition but is not engaged in for an anti-competitive purpose.

The omission of an 'effects' test is also inconsistent with trends internationally¹²⁹ as well as with other provisions of Part IV which are framed in terms of both purpose and effect (sections 45 and 47). It is also inconsistent with Part XIB which includes a prohibition against misuse of substantial market power by a telecommunications provider which has the effect, or likely effect, of substantially lessening competition in a telecommunications market: see sections 151AK and 151AJ. This latter provision was originally introduced in 1997, over 15 years ago, in recognition of the difficulties that may arise in obtaining evidence of a firm's purpose and the concern that "reliance on a 'purpose test' alone risks a focus on the perceived morality of conduct rather than its economic effect".¹³⁰

The ACCC recognises that sections 45 and 47 do capture some kinds of unilateral conduct that may be engaged in by a firm with market power with the effect of substantially lessening competition. However, the other requirements of these provisions mean that they do not adequately cover the gap in the law created by the current drafting of section 46. For example, a refusal to deal with a potential competitor (such as was the case in *Queensland Wire*) would fall outside of both section 45 (as there would be no contract, arrangement or understanding) and section 47 (as there would be no refusal to supply for one of the reasons identified in section 47(3)).

Accordingly, the ACCC considers that section 46 should be amended to capture unilateral conduct by a firm with substantial market power that has, or is likely to have, the effect of substantially lessening competition in a market.

¹²⁸ See, for example, the ACCC submission to the Dawson Review. ACCC, *Submission to the Trade Practices Act Review* (2002) at <http://tpareview.treasury.gov.au/submissions.asp>.

¹²⁹ Andrew I. Gavil, 'Imagining a Counterfactual Section 36: Rebalancing New Zealand's Competition Law Framework, working draft paper (2013).

¹³⁰ Explanatory Memorandum, *Trade Practices Amendment (Telecommunications) Bill 1996* (Cth) 10.

Sections 45 and 47 each apply to conduct that ‘has the purpose, or has or is likely to have the effect, of substantially lessening competition’.¹³¹ If an effects test is added to section 46, consistent with prohibitions within sections 45 and 47, the scope of conduct within the provision should also include purpose. Such a provision would be consistent with the broader approach to anti-competitive conduct found across the CCA and enable it to address anti-competitive conduct more effectively.

The ‘take advantage’ limb

The specific formulation of section 46 prohibits a firm with substantial market power taking advantage of that power for the purpose of harming actual or potential rivals or otherwise limiting competitive conduct. As the very objective of the competitive process is to win business at the expense of rivals (including through efficient conduct such as innovative products or lower costs), the ‘take advantage’ limb of the provision was seen as the key filter to distinguish conduct that is pro-competitive (or benign) from anti-competitive conduct.

However, as jurisprudence regarding section 46 has developed over time, it has become apparent that the ‘take advantage’ limb of section 46 is now an unsatisfactory mechanism for making this distinction. Specifically, the ACCC considers that the interpretation of the section has moved away from the original intent that section 46 be construed in the final analysis as a single provision,¹³² with the elements of substantial market power, take advantage and purpose being dealt with in a holistic way, as the High Court did in the early case of *Queensland Wire*.

Mason CJ and Wilson J observed in that case that:¹³³

[T]he question is simply whether a firm with a substantial degree of market power has used that power for a purpose proscribed in the section, thereby undermining competition....

Dealing with the ‘take advantage’ element, those judges found that:¹³⁴

[I]n effectively refusing to supply Y-bar to the appellant, BHP is taking advantage of its substantial market power. It is only by virtue of its control of the market and the absence of other suppliers that BHP can afford, in a commercial sense, to withhold Y-bar from the appellant. If BHP lacked that market power - in other words, if it were operating in a competitive market - it is highly unlikely that it would stand by, without any effort to compete, and allow the appellant to secure its supply of Y-bar from a competitor.

Similarly, Deane J analysed the facts as follows:¹³⁵

Its refusal to supply Y-bar to Q.W.I. otherwise than at an unrealistic price was for the purpose of preventing Q.W.I. from becoming a manufacturer or wholesaler of star pickets. That purpose could only be, and has only been, achieved by such a refusal of supply by virtue of B.H.P.’s substantial power in all sections of the Australian steel market as the dominant supplier of steel and steel products. In refusing supply in order to achieve that purpose, B.H.P. has clearly taken advantage of that substantial power in that market. If that purpose be one of those specified in s.46(1) of the Act, B.H.P.’s conduct constituted a contravention of that sub-section.

¹³¹ This is with the exception of section 45(1)(a) and the per se prohibitions for third line forcing. Otherwise, section 45(1)(b) and section 47(10)(a) each use the phrase ‘has the purpose, or has or is likely to have the effect, of substantially lessening competition’. Such effect is taken to be an effect in a relevant market: sections 45(3) and 47(13).

¹³² Explanatory Memorandum, *Trade Practices Revision Bill 1986* (Cth) at [36]. The Explanatory Memorandum also emphasised that the provisions of section 46 enable the court to consider whether the corporation *would* have been likely to engage in the conduct in a competitive market, not just whether they *could* have done so.

¹³³ (1989) 167 CLR 177 at 191.

¹³⁴ (1989) 167 CLR 177 at 192.

¹³⁵ (1989) 167 CLR 177 at 197-198.

In *Melway*, the High Court again emphasised the need to treat the take advantage and purpose elements of section 46 as inter-related:¹³⁶

Although there are two aspects of that prohibition, they are inter-related.

Despite the High Court's approach in *Queensland Wire* and *Melway*, later decisions have adopted a more disembodied approach to assessing the elements of section 46. In seeking to distinguish between conduct driven by pro-competitive economic efficiency, and that which is proscribed, the courts have been drawn into complex 'counterfactual' analyses, without sufficiently coupling the use of the market power with the purpose sought to be achieved.

Further, it is particularly difficult to apply such analyses when considering conduct outside of an outright 'refusal to deal', which was the conduct in question in *Queensland Wire* and *NT Power Generation Pty Ltd v Power and Water Authority*.¹³⁷ At its most extreme, as in the New Zealand '0867' case,¹³⁸ this complex, disaggregated form of analysis can focus on the standard of proof of the possible behaviour of a firm in a hypothetical world in which it does not enjoy market power, in a manner that is divorced from the economic rationale for the conduct by the firm in question and which is at the heart of the prohibition.

Even where a firm with substantial market power engages in conduct which has a clear, documented anti-competitive purpose and a significant anti-competitive effect, as the recent *ACCC v Cement Australia Pty Ltd* decision¹³⁹ shows, the technical requirements of section 46 as currently interpreted by the courts make it difficult to establish a misuse of market power. The ACCC considers that *Rural Press Limited v ACCC*¹⁴⁰ and *Cement Australia* best exemplify the narrow interpretation of 'take advantage' that has been taken by the courts: in both cases the conduct of a firm with substantial market power, despite being found by the Court to have been engaged in for a substantial anti-competitive purpose and having the effect of substantially lessening competition, was not found to constitute a 'taking advantage' of the firms' market power. Accordingly, no contravention of section 46 was made out in either case.

Case study – Rural Press and Cement Australia

In *Rural Press*, the majority of the High Court found that Rural Press had not taken advantage of its substantial market power because the conduct engaged in – a threat to enter Waikerie's Riverland market if Waikerie did not stop distributing its newspaper in competition with Rural Press in Murray Bridge – *could* have been engaged in by a firm without market power (at [52]). Further, the Court found that Rural Press' conduct was not *materially facilitated* by its market power because what gave the threats significance was its 'material and organisational assets' rather than its market power (at [53]). In other words, the conduct was found to constitute a use of financial power rather than market power.

In *Cement Australia*, Greenwood J articulated the test of whether a corporation has taken advantage of its market power as whether a profit maximising firm operating in a workably competitive market could, in a commercial sense, profitably engage in the conduct (at [1899]), or put another way, whether a firm profitably *could* have engaged in the conduct in question in the absence of a substantial degree of power in the relevant market (at [1902]). The Federal Court found that a substantial purpose of the decisions by Cement Australia to enter into and renew contracts to obtain additional flyash was to foreclose a rival from entering into the South East Queensland concrete grade flyash market (at [2413], [2682]).

However, because other commercial factors existed which suggested that a profit maximising firm confronting the circumstances faced by Cement Australia could, absent a

¹³⁶ (2001) 205 CLR 1 at [25] per Gleeson CJ, Gummow, Hayne and Callinan JJ.

¹³⁷ (2004) 219 CLR 90.

¹³⁸ *The Commerce Commission v Telecom Corporation of New Zealand Limited* [2010] NZSC 111.

¹³⁹ [2013] FCA 909 ('*Cement Australia*').

¹⁴⁰ (2003) 216 CLR 53 ('*Rural Press*').

substantial degree of market power, have made a decision to act as Cement Australia did, the Court found the conduct did not constitute a taking advantage of market power. The ACCC notes that this case is still before the Court.

The amendments in 2008 to section 46(6A) introduced a list of factors that courts may have regard to in considering whether a firm has taken advantage of its market power.

While the conduct in *Rural Press* and *Cement Australia* pre-dated the introduction of section 46(6A) (and so the Court was not required to consider the possible application of the section to the facts), it is not clear that these cases would have been decided differently if section 46(6A) had applied.

Options for reform

There are a number of potential options for reform to section 46 that may address the concerns outlined above.

First, the absence of an effects test could be addressed by an amendment modelled upon the telecommunications regime in section 151AJ. The ACCC considers that the concerns articulated by the Dawson Report that such a test would discourage legitimate competitive practices and therefore have a ‘chilling’ effect upon efficient, pro-competitive conduct are unfounded and have not been demonstrated in the telecommunications sector.

Such an amendment would better target unilateral conduct which has the effect of substantially lessening competition in a market as a whole (rather than an effect on individual competitors). However, this approach, without further amendments to the section, would not address the ACCC’s concerns about the limitations of the take advantage limb.

The concerns arising from the interpretation of the take advantage limb might be addressed by:

- an amendment to define more prescriptively the application of the take advantage limb; or
- a reformulation of the test to remove the take advantage limb and replace it with a substantial lessening of competition test.

In relation to amendments to remove or further define the reference to ‘take advantage’, there are a number of possibilities. For example, it may be desirable to define ‘take advantage’ in a more prescriptive manner to ensure that the counterfactual enquiry focusses on the question: ‘what exclusionary advantage does a firm with substantial market power get from the conduct that a firm without such market power would not?’¹⁴¹ In essence, this is consistent with the approach in *Queensland Wire*.

As for a potential reformulation of the test, the existing section 46(1) (inclusive of the reference to ‘take advantage’ for certain proscribed purposes) might be retained, but augmented with a provision which provides that:

A corporation that has a substantial degree of power in a market shall not engage in conduct that has the purpose or has, or is likely to have, the effect of substantially lessening competition in that or any other market.

A further alternative step would be to replace the entirety of section 46 with a simplified provision along the lines of the above clause.

The ACCC recognises that each option for reform has advantages and disadvantages. However, the ACCC considers that the body of case law on section 46 and, in particular, on the interpretation of the ‘take advantage’ limb, results in a misuse of substantial market power provision of limited utility. Reform to the provision is important, and the ACCC considers that reform could be implemented in a way which overcomes any concerns regarding over-reach. The CCA is an economic statute and this will guide the court’s

¹⁴¹ Gavil, above n 127.

interpretation of any amendment. In particular, amending or removing the ‘take advantage’ limb, so long as such a change is combined with the key filter of a substantial lessening of competition test, will not capture pro-competitive conduct. It would also have the advantage of making Part IV more uniform as a substantial lessening of competition test is a familiar filter that is already relied upon and regularly applied in sections 45, 47 and 50.

Finally, consistent with the ACCC’s recommendations in section 4.3, any reform in this area should avoid being overly prescriptive and employing legalistic drafting. Depending on the ultimate reform to section 46, there may be scope to remove other parts of the provision to the extent there is overlap.

4.2.2 Anti-competitive disclosure of information provisions should be extended to the whole economy

The ACCC recommends that anti-competitive disclosure of information provisions should apply across the economy. This is consistent with the universality principle that anti-competitive conduct should be prohibited regardless of the sector of the economy in which it occurs.

Current prohibition – limited to banking sector

The communication of competitively sensitive information can interfere with independent rivalry between firms as it eliminates strategic uncertainty and facilitates coordination between competitors.

In Australia, this interference with the competitive process will only be prohibited if it:

- takes place as part of a contract, arrangement or understanding (which involves a cartel agreement, an exclusionary provision or which has the purpose, effect or likely effect of substantial lessening competition in a market) or an attempt to reach such a contract, arrangement or understanding;
- is a misuse of market power, and meets the technical requirements of section 46; or
- involves banking services and is caught by the pricing disclosure provisions in Division 1A of Part IV of the CCA.

The provisions in Division 1A currently prohibit the following types of conduct in relation to particular types of banking services:

- The private disclosure of pricing information to a competitor, where it is not in the ordinary course of business.
- The public or private disclosure of information relating to price, capacity or commercial strategy for the purpose of substantially lessening competition in a market.

The prohibitions can be extended to other types of goods and services by regulation by the Minister.

At the time of introducing the laws, the government noted that most comparable jurisdictions had laws that are capable of dealing with anti-competitive price signalling and information disclosures and that the provisions would close a gap in Australia’s competition law.¹⁴²

¹⁴² Commonwealth, Parliamentary Debates, House of Representatives, 24 March 2011, Wayne Swan, Treasurer and Deputy Prime Minister, p. 3133.

Anti-competitive disclosures can be just as harmful as hard core cartels and are recognised as such in international best practice

Horizontal arrangements between competitors can range from hard core cartel conduct (such as an agreement between competitors to fix prices) to parallel conduct (where competitors price uniformly but with no communication between them).

Arrangements along this continuum may produce similar anti-competitive effects – coordinated conduct between competitors which leads to a loss of efficiency as firms are not competing by offering lower prices or higher quality services to consumers. However, the culpability of the firms for that anti-competitive outcome differs significantly depending upon how the coordinated conduct has come about.

The disclosure of sensitive pricing information between competitors and the public disclosure of competitively sensitive information for the purpose of substantially lessening competition is not behaviour that should be permitted by the law. It is, as some commentators have described it, a 'deliberate attempt to overcome structural impediments to coordination and subvert the competitive functioning of the market, while having no offsetting business rationale'.¹⁴³

Further, as international cartel enforcement continues to be successful in identifying and penalising hard core cartels, more sophisticated firms will find other ways to engage in practices to avoid true competition. An extension of the prohibition against anti-competitive disclosures would go some way toward aligning Australia's competition law with international best practice.

European Commission competition law, for example, applies to all sectors of the economy *unless* an exemption is created. Further, anti-competitive disclosures are prohibited where their object or effect is to prevent, restrict or distort competition, whether they are part of a fully formed agreement or reflect a 'concerted practice'.¹⁴⁴

Where the disclosure of future prices takes place using public channels, this is only likely to be illegal after receiving rigorous testing under a competition test.

Anti-competitive conduct should be prohibited universally throughout the economy

The current gap in the CCA in relation to anti-competitive disclosures, other than in relation to banking, enables businesses to engage in anti-competitive practices without any countervailing benefit arising from such conduct. In the same way that cartel conduct can occur anywhere across the economy, so too can practices that facilitate cartel like outcomes, such as the disclosure of competitively sensitive information between competitors.

Consistent with the principle of universality, competition law should address anti-competitive behaviour wherever it occurs in the economy. The ACCC therefore recommends that the limitation on Division 1A (to only apply to sectors of the economy prescribed by regulation) be removed.

¹⁴³ Caron Beaton-Wells and Brent Fisse, *Submission: Meaning of 'Understanding' in the Trade Practices Act 1974* (7 April 2009) 10 (available at: <http://www.law.unimelb.edu.au/files/dmfile/BeatonWellsandFisseSubmissionMeaningofUnderstandingintheTradePracticesAct0704091.pdf>), citing GA Hay, 'Facilitating Practices', in ABA Section of Antitrust Law, *Issues in Competition Law and Policy Vol II* (ABA Book Publishing, Chicago, 2008) ch. 50, p. 1189.

¹⁴⁴ Article 101(1) of the European Community Treaty.

4.2.3 Merger authorisations should be determined by the ACCC with rights for merits review by the Tribunal

The ACCC considers that to ensure an efficient and effective merger authorisation process the ACCC should be the first instance decision maker with rights of merits review to the Tribunal. The current process which requires applications to be made direct to the Tribunal increases costs to applicants and the ACCC, as well as deterring participation by third parties.

The ACCC considers that these changes could be implemented without increasing the current maximum statutory time period of six months for the determination of a merger authorisation, by allowing the ACCC and the Tribunal each a maximum of three months to make their respective determinations. To support the achievement of these timeframes, further consideration should be given to the information gathering powers that would be available to the ACCC at first instance.

Current process for merger authorisation

The CCA provides that merger parties may seek authorisation of a proposed acquisition. Following reforms introduced in 2007, such applications are made directly to the Tribunal.¹⁴⁵

To grant authorisation, the Tribunal must be satisfied in all the circumstances that the proposed acquisition would result, or be likely to result, in such a benefit to the public that the acquisition should be allowed to occur.¹⁴⁶ This is quite a different test to that of formal or informal merger clearance by the ACCC, which assesses whether a proposed merger or acquisition will contravene section 50 of the CCA (i.e. whether the proposed acquisition would have the effect or be likely to have the effect of substantially lessening competition in a market).

The CCA provides that the Tribunal must make a decision on a merger authorisation application within three months. The Tribunal may extend this period for up to an additional three months.

The ability of merger parties to seek authorisation of a proposed acquisition is an important mechanism for ensuring that acquisitions that are in the public interest can occur. Merger authorisations are relatively infrequent. For the ten year period prior to 2007, when merger authorisation was undertaken by the ACCC, there were nine applications for merger authorisation decided by the ACCC. Since the regime was amended in 2007, two applications for authorisation have been made to the Tribunal. An outline of the two applications made to the Tribunal to date – one by Murray Goulburn Co-operative Co Limited (Murray Goulburn) in respect of its proposed acquisition of Warrnambool Cheese and Butter (WCB) and the other by AGL Energy Limited (AGL) in respect of its proposed acquisition of the assets of Macquarie Generation in NSW – is provided below.

Murray Goulburn application to the Tribunal for authorisation to acquire WCB (ACT 4 of 2013)

Murray Goulburn filed its application for authorisation to acquire WCB with the Tribunal on 29 November 2013. This was the first merger authorisation application made to the Tribunal

Before the Tribunal had heard the application, control of WCB was acquired by rival bidder Saputo, leading to Murray Goulburn withdrawing its application from the Tribunal on 23 January 2014.

¹⁴⁵ CCA s. 95AT.

¹⁴⁶ Section 95AZH(1) provides that the Tribunal must not grant authorisation unless it is so satisfied.

AGL application to the Tribunal for authorisation to acquire the assets of Macquarie Generation in NSW (ACT 1 of 2014)

On 24 March 2014, AGL filed an application with the Tribunal for authorisation to acquire the assets of Macquarie Generation. Macquarie Generation is a NSW state-owned corporation which was being offered for sale as part of the broader privatisation of NSW electricity generation assets by the NSW government. The hearing to consider the application for authorisation by the Tribunal commenced on 2 June 2014.

AGL's application for authorisation to the Tribunal followed an announcement by the ACCC on 4 March 2014 that it would oppose the proposed acquisition pursuant to section 50, on the basis that it was likely to have the effect of substantially lessening competition. This followed a three month informal review by the ACCC.

The Tribunal is a merits review body, not a first instance investigative body

The ACCC considers that the current merger authorisation process has consequences that were not envisaged when the legislation was amended to enable applicants to apply directly to the Tribunal for merger authorisation.

The Tribunal is a highly regarded and experienced merits review body. The Tribunal hears applications for review of determinations of the ACCC granting or revoking non-merger authorisations, revocations of notifications and certain decisions in access matters.

A review by the Tribunal is in most cases a re-hearing or a re-consideration of a matter (albeit on limited material for some reviews). The Tribunal may perform all the functions and exercise all the powers of the original decision-maker for the purposes of undertaking its review. It can affirm, set aside, or in some cases vary, the original determination, notice or declaration.

The ACCC has a statutory role of assisting the Tribunal in relation to these applications. This makes sense in relation to the above functions as the ACCC, due to its prior investigation or review of a particular matter, will have already gathered information relating to the industry, the parties, other market participants and the issues raised by the proposed conduct, and will have had a sufficient opportunity to consider those issues.

In the context of merger authorisations, however, the Tribunal has the role as the *first instance* decision maker. The primary investigative functions that form part of authorisation analysis at first instance are, however, very different to the inquiries made by a review body. In the ACCC's view, this function is not a natural fit for a review body such as the Tribunal. The Tribunal does not conduct detailed market inquiries itself, and does not have the resources to do so.

Under the current merger authorisation process, the ACCC performs two roles. First, it acts as an investigative body conducting market inquiries and gathering information from market participants (and preparing a report for the Tribunal in relation to any matters specified by the presiding member of the Tribunal, and in relation to any matter the ACCC considers relevant to the application). Secondly, it assists the Tribunal by preparing the above-mentioned report which must be requested by the Tribunal, calling witnesses, reporting on statements of fact, examining or cross examining witnesses and making submissions to the Tribunal on issues relevant to the application.

Based on recent experience, the ACCC is of the view that it is not efficient or effective for it to undertake these two functions concurrently. In particular, the ACCC's ability to effectively investigate and conduct market enquiries to test the issues which arise from the proposed acquisition (including public benefit claims, which are not considered in informal merger reviews) is limited due to the statutory timeframe. Once an application has been filed the ACCC must provide assistance to the Tribunal by filing evidence and submissions in

preparation for the hearing of the application and, in parallel, prepare a detailed report for the Tribunal.

As a result, in the ACCC's view it would be more efficient and cost effective for the ACCC to investigate and determine applications for merger authorisation, using its significant experience in both merger review and the application of the net benefits test in the context of authorisation determinations. This would leave the Tribunal to do what it does best: merits review on appeal from the ACCC's determination.

Other issues with current merger authorisation process

It is the ACCC's experience that the direct to Tribunal merger authorisation process results in significantly higher costs, and less participation by industry participants with the related risk of less reliable information on which to base a decision, than would be the case if the ACCC was responsible for making the initial merger authorisation determination.

The current process may also result in potential inconsistency where authorisation is sought for related non-merger conduct, and denies applicants the right to seek merits review from a merger authorisation determination.

To elaborate on the above:

- *Significant resource costs.* It is the ACCC's experience that the costs of a Tribunal hearing incurred by the ACCC, the applicant, and third parties are significant and largely unavoidable. For example, for third party market participants these costs include retaining lawyers to assist with responding to information requests, dealing with confidentiality concerns and preparing sworn statements for filing with the Tribunal, in addition to the significant time and costs involved for the particular witnesses preparing for and giving evidence before the Tribunal at a hearing. These costs are far greater than those incurred (if at all) in non-merger authorisation applications of equivalent commercial complexity. The ACCC considers the overall cost to applicants, third parties and the ACCC would be significantly reduced if the ACCC was responsible for determining merger authorisation applications. The ACCC would be happy to provide a confidential submission expanding upon these matters if it would assist the Review Panel.
- *Market participants reluctant to participate.* Although the CCA requires the Tribunal proceedings to be conducted with as little technicality and formality as possible,¹⁴⁷ in the ACCC's experience many parties who are prepared to provide submissions to the ACCC on a confidential basis are not willing, or are very reluctant to, provide submissions or other evidence (such as witness statements and affidavits) during the Tribunal process. Some market participants with potentially relevant information do not want to be involved in the Tribunal's public, court-like process and setting. It is also the case that some market participants do not wish to disclose commercially and competitively sensitive information in the context of a Tribunal hearing, even where strict confidentiality regimes are in place, particularly where they have ongoing commercial arrangements in place with the applicant.
- *Combining merger and non-merger authorisation.* Under the current processes, businesses which seek authorisation for both an acquisition as well as related non-merger conduct (such as tolling or other transitional arrangements with the vendor) would be required to make two applications, one to be determined by the Tribunal and the other to be determined by the ACCC. As an example, if the 2003 Qantas/Air New Zealand alliance authorisation applications were considered now, separate applications would need to be made: one to the Tribunal for the partial acquisition, and one to the ACCC for the collaborative arrangement/cooperation agreements. This is clearly

¹⁴⁷ See CCA s. 103.

inefficient and unduly costly. More substantively, it also leads to potentially conflicting or inconsistent decisions.

- *No merits review.* The current merger authorisation process denies the applicant the ability to seek merits review of an adverse decision. This is inconsistent with the right of applicants adversely affected by a decision of the ACCC in relation to non-merger authorisations.

Merger authorisation process reform

The ACCC considers that reforming the merger authorisation process so that merger authorisation applications are made to the ACCC would mean that many applications would be determined without the need for Tribunal review. Those applications that require Tribunal review would benefit from the investigation already undertaken by the ACCC, potentially reducing the cost and timeframe for Tribunal determination and ensuring that adequate information can be put before the Tribunal to enable it to reach a sound decision.

The current process (where parties apply directly to the Tribunal) was introduced partly because of the concern that applicants were discouraged by the length of time a review could take if it involved consideration by the ACCC with an appeal to the Tribunal. The ACCC suggests that this concern can be addressed by providing the ACCC and the Tribunal with a maximum period of three months each for reaching a decision. This would mean the maximum time period for merger authorisation would be no greater than the maximum six month time period allowed by the current Tribunal merger authorisation process. To support the achievement of these timeframes, further consideration should be given to the information gathering powers that would be available to the ACCC in its decision at first instance including section 155. This is discussed further at 4.4.3 below.

4.2.4 Third line forcing conduct should only be prohibited if it has a significant impact on competition or consumers

The ACCC considers that third line forcing conduct should only be prohibited if it has the purpose, effect or likely effect of substantially lessening competition. The ACCC notes, however, that circumstances may arise where third line forcing conduct which does not substantially lessen competition nevertheless results in significant consumer detriment. The Australian Consumer Law should be reviewed (and, if necessary, amended) to ensure that consumers remain adequately protected in these circumstances.

Current provision – captures benign and procompetitive conduct and imposes unnecessary regulatory burden

Third line forcing occurs where a firm supplies goods or services (or goods or services at a particular price) but only if the customer also purchases goods or services from another unrelated firm.¹⁴⁸ Unlike other types of exclusive dealing which are prohibited by the CCA only when they have the purpose, effect or likely effect of substantially lessening competition,¹⁴⁹ third line forcing is prohibited outright ('per se') without regard to the purpose of the conduct or its effect on competition.

There are legitimate reasons why a business may only supply goods or services if a customer also acquires goods or services from another party. The forced tie may:

- ensure the optimal, safe or proper functioning of the goods or services that the firm provides (for example, a higher quality third party product may be required for a consumer to access or properly enjoy the primary goods or services);

¹⁴⁸ CCA ss 47(6) & (7).

¹⁴⁹ CCA s 47(1).

- allow businesses to work together to provide a differentiated offer to attract customers (e.g. credit card loyalty schemes where a restaurant provides a benefit to consumers on condition that they use a particular brand of credit card); or
- support the ordinary commercial operation of a distribution model (for example, the sale of mobile phones by third parties on condition that the mobile services are acquired from a particular telecommunications company).

In recognition that there will be many instances of third line forcing where the conduct may be benign or procompetitive, a notification process was introduced to enable firms to simply and inexpensively¹⁵⁰ lodge notifications with the ACCC (see section 4.3.3 for further information).

The ACCC receives a significant number of notifications of third line forcing conduct; it received over 750 such notifications in the 2012-13 financial year. In the vast majority of cases, the ACCC takes no further action in relation to these notifications. In some instances the ACCC will make further inquiries including initiating a public consultation. In very few instances, this may result in the notification being withdrawn by the applicant, the ACCC taking steps to remove the protection provided by the notification or the ACCC accepting an undertaking from the applicant.

The streamlined notification process provides a relatively simple mechanism for businesses to obtain immunity from legal action. However, given the large number of notifications that do not raise competition concerns (or which are even procompetitive), the process imposes an unnecessary regulatory burden on business and the ACCC.

Third line forcing should be prohibited where it causes significant competition or consumer detriment

Previous reviews have recommended that the prohibition against third line forcing should be amended to make it also subject to a competition test, as is the case for the other vertical arrangements proscribed under section 47.¹⁵¹ To date, these reforms have not been adopted.

The ACCC considers that the per se prohibition against third line forcing is inefficient and that such conduct should only be prohibited under competition law if it has the purpose, effect or likely effect of substantially lessening competition in a market.

Third line forcing may have a distortionary effect on the demand for forced goods and services as it can undermine one of the fundamental requirements for the efficient operation of markets – that consumers are well informed and able to act in their own self-interest to purchase goods and services that best meet their needs. As a result, consumers may be required, or induced, to purchase goods or services which are undesirable, for example due to their poor quality or high price.

This harm is most likely to occur where the primary seller has significant market power or otherwise has a compelling offer, or where consumers are confused as to the conditions associated with the offer or do not fully take them into account when making the purchase. The potential for consumer detriment may be particularly high where consumers do not or cannot (for example, because the price is unknown) take into account the full cost of purchasing the forced product when purchasing the primary product. This harm is particularly likely to be significant where consumers are locked into purchasing the forced product over an extended period of time or where consumers are misinformed.

Where the primary seller has significant market power, it is likely that its third line forcing conduct would foreclose competing suppliers of the forced good or service and would

¹⁵⁰ The fee for lodging a third line forcing notification is \$100.

¹⁵¹ Hilmer Review and Dawson Report.

substantially lessen competition. This would still contravene a third line forcing provision which incorporated the proposed “competition” requirement.

There may be some circumstances where conduct does not have the purpose or effect of substantially lessening competition in a market, but the third line force may still cause significant consumer detriment. Detriment may arise as the result of unacceptable business practices similar to unfair contract terms or misleading representations. A further example is where companies engage in third line forcing due to financial incentives provided to the primary seller by the seller of the forced goods or services. These financial benefits are often not disclosed to consumers and can raise similar concerns to any other type of secret commission or ‘kickback’.

To the extent that significant consumer detriment arises from these types of business practices, the ACCC is concerned to ensure that consumers remain effectively protected. The ACCC considers that this would be best achieved through provisions in the Australian Consumer Law that specifically address this concern rather than through an outright prohibition against third line forcing. For these reasons, the ACCC considers that the Australian Consumer Law should be reviewed (and, if necessary, amended) in order to ensure that third line forcing conduct, which is not likely to substantially lessen competition but which is likely to cause significant consumer harm, is prohibited.

Case study – Jasmin Solar – Notifications – N96232 & N96653 (2014)

Jasmin Solar lodged a notification regarding the provision of discounted solar panels to customers (generally to low income and elderly consumers) on condition that they entered into long term contracts for their energy needs with another party. If the customer exited the energy contract (for example, because prices were excessive), they would need to pay damages under the primary contract with Jasmin Solar.

Given the competitiveness of the markets for the provision of solar panels and electricity retailing, the ACCC did not consider that the arrangements would be likely to significantly distort competition in either the retail supply of electricity or the retail supply and installation of solar panels.

However, the ACCC was concerned that the arrangements could give rise to public detriments as customers would be locked into long term energy contracts which could expose them to being charged excessive prices by the electricity retailer and may be exposed to excessive termination fees. As the price of electricity could increase over time by an unknown amount, even fully rational consumers would be unable to properly calculate the cost of the electricity contract they would be required to enter into in order to receive the discounted solar panel.

The ACCC accepted a section 87B undertaking from Jasmin Solar and Diamond Energy which mitigated these concerns. As a result, the ACCC was satisfied that the likely public benefits would outweigh the likely public detriments.

4.2.5 Exemptions from competition law should be regularly reviewed and transparent

Exemptions by Commonwealth, state or territory statutes should be time limited

The ACCC recommends that any exemption by the Commonwealth, state or territory governments to exclude conduct from the CCA should be time limited.

Current provision – government restrictions on competition

Where a government wishes to directly authorise anti-competitive conduct between firms that may otherwise breach Part IV, it may rely upon section 51(1), the general exemption in

the CCA. Conduct which is specifically authorised by federal, state or territorial legislation which meets the requirements prescribed by section 51 is specifically exempted from the prohibitions in Part IV of the CCA.

Separately, legislation may restrict competition in other ways; for example, where a government prohibits firms from selling goods at a price other than that determined by a statutory body this restricts price competition but would not breach the competition provisions (see sections 3.2.1 and 3.3.2).¹⁵² In these circumstances, the legislation does not need to specifically invoke section 51(1).

Regular review of exemptions would ensure that restrictions continue to be appropriate

As a broad principle, the ACCC considers that statutory exemptions for anti-competitive conduct may undermine the important principle that competition policy should be implemented in a uniform manner across the economy. The ACCC notes the recommendations from the Hilmer Review (which were not adopted) that the states and territories should not have the ability to grant exemptions through statute or regulation, and that the Commonwealth should only be able to grant exemptions through statutes, rather than regulation.

The concern raised in the Hilmer Review regarding the proliferation of anti-competitive regulation was addressed through the NCP reform agenda, where governments committed to only maintain or introduce legislation which restricts competition if it can be demonstrated that the benefits outweigh the costs and that the objectives of the legislation can only be achieved through such restrictions.¹⁵³ Governments also committed to extensive transparent reviews of existing legislation and the introduction of mechanisms to ensure that new legislation, including legislation which invokes section 51(1), met these principles.

As is noted in section 3.3.2, the ACCC considers that a renewed commitment to legislation and policy review is required.

To support any new commitments regarding regular legislative review, the ACCC considers that section 51(1) should be amended to provide a sunset clause for exemptions legislated by Commonwealth, state and territory governments (such as that which exists for exemptions by regulation). This would ensure that the restrictions on competition are regularly reviewed through a transparent and accountable process prior to being renewed (e.g. through the passage of new legislation). Restrictions that no longer satisfy a net public benefit assessment would then automatically no longer apply if governments choose not to renew them, rather than needing to be specifically repealed.

Exemption for export cartels

The ACCC recommends that the exemption for export cartels be repealed subject to appropriate transitional arrangements being established.

If the provision is not repealed, the ACCC recommends that greater transparency be provided regarding export cartels which are exempted from the CCA. This could include a requirement that the arrangements be time limited and included on a public register.

Current provision – a broad exemption for cartel conduct

Section 51(2)(g) exempts export cartels from a number of Part IV prohibitions. In light of international and national developments, particularly the policy changes to criminalise cartel behaviour, the ACCC considers that the appropriateness of this exemption requires reassessment.

¹⁵² For further elaboration on this point see Hilmer Review p. xxvi and chapter 5.

¹⁵³ See CP Agreement clause 5.

In principle, the ACCC considers that a blanket exemption for cartel activity which affects overseas markets is inappropriate and inconsistent with the strong stance that Australia has taken in relation to domestic cartel arrangements. The ACCC also has concerns in relation to the potential 'spill over' effects that these arrangements may have on domestic markets.¹⁵⁴

It is also worth noting that, irrespective of these laws, export cartels may be breaching the domestic cartel laws of the countries to which they are exporting.

The ACCC has received 23 notifications of export cartels in the past five years.

Examples of arrangements that may constitute an export cartel

The following are examples of arrangements that may constitute an export cartel and which would be able to be notified to the ACCC under the current exemption. *Australian producers set a minimum price for goods sold internationally*

A group of Australian producers that market their goods overseas coordinate an agreement whereby all member producers meet regularly before and during export negotiations to compare information on market conditions in the target market overseas and assess supply volumes from Australia and other countries. At each meeting, the producers agree to set a minimum price for their products for export from Australia to the target market agree and that each member will endeavour to sell their products at or above this price.

Arrangements which facilitate entry into export markets

A small producer wishes to start selling its product into overseas markets for the first time and contracts with a larger producer that has been exporting for some time and has an established presence in a number of overseas markets. The large producer markets and sells the small producer's goods overseas effectively on consignment, within a band of acceptable prices agreed with the small producer.

Export cartels should be subject to transparency and a public benefit test

As noted above, the ACCC considers that the exemption should be repealed. Repeal of this provision would mean that to the extent that some of these arrangements may have demonstrated public benefits that outweigh the anti-competitive detriments, the parties may seek authorisation from the ACCC. These export cartels would then be subject to the same public assessment process as other conduct which may breach Part IV.

Any repeal would need to include appropriate transitional arrangements to allow parties who wish to continue with arrangements that may risk breaching the competition provisions of the CCA to seek authorisation, where appropriate.

An alternative mechanism to the authorisation provisions could be to modify the notification process to allow arrangements to be revoked if they do not result in a net public benefit. This would be similar to the notification process for exclusive dealing conduct where parties may receive deemed immunity for conduct by lodging a notification with the ACCC, yet the ACCC retains a power to remove that immunity if the public detriments outweigh the public benefits.

The ACCC also considers that if these changes are not made, greater transparency should be provided regarding the arrangements which benefit from the exemption. This could include a requirement that the ACCC maintain a public register where some details of the arrangements are made public. The benefit of the exemption should also be time limited.¹⁵⁵

¹⁵⁴ ACCC submission, *NCC Review of Sections 51(2) and 51(3) of the Trade Practices Act 1974* (27 August 1998) Attachment, p. 2.

¹⁵⁵ Under the existing process, the ACCC is often not provided with information that would enable it to determine the expiry of particular arrangements.

4.2.6 Overseas conduct having an anti-competitive effect in Australia

The CCA should be amended to put beyond doubt that conduct which occurs overseas, but which has an anti-competitive effect in Australia, is caught by the CCA. This should include clarification of the circumstances in which an overseas corporation is considered to be ‘carrying on business within Australia’.

Current provision – potential ambiguities in relation to overseas conduct

The CCA generally only applies to anti-competitive conduct that occurred within Australia. The application of the CCA is specifically extended to anti-competitive conduct outside Australia (such as an acquisition between firms in another country or a meeting in another country where a cartel is formed) to the extent the conduct was engaged in by a corporation that is incorporated in Australia or carrying on business within Australia.¹⁵⁶

In recent years, the ACCC has considered a number of global mergers where the conduct occurs overseas and the merger parties are foreign corporations (i.e. two companies merge the parent companies of their global businesses, both of which are located outside of Australia). In some instances, these mergers raise potentially significant competition concerns in a market in Australia despite the merger parties not being incorporated in Australia or where the parties have asserted that they are not ‘carrying on business within Australia’ pursuant to section 5(1) of the CCA. The phrase ‘carrying on business within Australia’ is not defined in the CCA, and there has been only limited consideration of the phrase in a competition law context by the courts.¹⁵⁷

Where global mergers raise significant competition concerns in Australia, foreign merger parties generally submit to the jurisdiction of the CCA and offer undertakings pursuant to section 87B where appropriate to remedy any competition concerns raised by the ACCC.¹⁵⁸ However, this is not always the case.

A similar issue has arisen in relation to international cartels where the primary cartel agreement may be reached overseas but is given effect to in various places, including Australia. The conduct in Australia (which in a bid rigging case, for example, may comprise the Australian subsidiary bidding at an artificially high price) may be conduct engaged in by a local subsidiary that has little or no knowledge of the cartel arrangements and is in this case simply following instructions from the parent. However, that subsidiary may otherwise have sufficient independence from the parent company to not be treated as its agent. In other words, both the making of, and giving effect to, the cartel agreement may only be caught by the CCA if it can be said that the foreign corporation carried on business within Australia, either directly or through the subsidiary acting as its agent.

The ACCC considers that if a foreign corporation is supplying goods or services to Australian consumers, either directly or through a subsidiary or agent, that the corporation is thereby carrying on business in Australia. However, there have been cases where parties have asserted that this is not the case. For example, issues may arise where:

- due to the legal structures of global conglomerates, the parent company (which was the subject of the acquisition or engaged in the anti-competitive conduct) may argue

¹⁵⁶ CCA s. 5.

¹⁵⁷ See, e.g., *Bray v F Hoffman-La Roche Ltd* [2002] FCA 243; *Trade Practices Commission v Australian Iron & Steel Pty Ltd* (1990) 22 FCR 305.

¹⁵⁸ Where section 50 does not apply to an overseas merger, section 50A may apply. This provision was introduced to bring some overseas mergers between foreign companies with subsidiaries in Australia within the jurisdiction of the CCA. If the Tribunal makes a declaration that an acquisition would have the effect of substantially lessening competition in a market and would not result in net public benefits, then the remedy requires the acquirer to cease carrying on business in the relevant market within six months. This provision is cumbersome and has never been used. In any event, the remedy may not assist in relation to improving competition outcomes.

that it is not ‘carrying on business within Australia’ through a subsidiary that may be many layers removed in the corporate hierarchy; or

- overseas businesses are selling and delivering increasingly significant amounts of goods and services to Australian consumers without a locally incorporated entity (such as via the internet or a distribution agreement with another company).

Proposed reform – clarification of ‘carrying on business within Australia’

In order to more effectively capture conduct that occurs overseas but impacts Australia, section 5 of the CCA could be amended to include a non-exhaustive list of matters that constitute ‘carrying on business within Australia’. For example, a corporation could be considered to be ‘carrying on business within Australia’ if it supplies goods to Australian consumers. It may also be useful to specify the nature of the conduct of subsidiaries in Australia that would constitute carrying on business by the foreign parent corporation.

Such clarification would enable the ACCC to unambiguously respond to conduct with anti-competitive effects in Australia.

4.3 Bringing greater clarity to the CCA

Key points

There are two key areas in which the ACCC considers greater clarity in the drafting and structure of the provisions would considerably improve the accessibility of the provisions and reduce the regulatory burden:

- the cartel provisions; and
- the authorisation and notification provisions.

4.3.1 Clarity in the CCA

Australia’s competition law is often criticised for its prescriptive drafting style which is in stark contrast to the approach adopted in other jurisdictions such as the United States.¹⁵⁹ Such criticism particularly focuses upon the more recent additions to the CCA, such as the cartel provisions and the various amendments to the section 46 prohibition against misuse of market power, which have sought to prescriptively codify the application of the law.¹⁶⁰

The ACCC considers that the drafting of the CCA could be improved to remove unnecessary complexity, provide greater clarity, flexibility and, potentially, enhanced enforceability of the prohibitions. In this submission, the ACCC has focused on those areas of the CCA which would benefit most from such refinement.

4.3.2 Provisions relating to cartel behaviour could be improved

The ACCC considers that the policy settings in Australia relating to cartels are appropriate. The ACCC would support a review of the cartel provisions to ensure that they are clear and suitably capture conduct which they are intended to prohibit. Any changes to the law should support and strengthen the current cartel policy. Policy settings regarding cartel conduct are appropriate.

Cartels harm consumers, businesses and the economy by increasing prices, reducing choice or distorting the ordinary competitive processes leading to innovation and product

¹⁵⁹ See: Hilmer Review p. 30 (referencing the Trade Practices Commission submission regarding simplification of the competitive conduct rules).

¹⁶⁰ See, for example: Justice Steven Rares, *Competition, Fairness and the Courts* (Competition Law Conference, 24 May 2014) (available at: <http://www.fedcourt.gov.au/publications/judges-speeches/justice-raises/raises-j-20140524>).

development. They adversely affect domestic and international competitiveness and ultimately result in reduced employment opportunities for Australians.

Cartels continue to be an enduring enforcement priority for the ACCC and a key component of its competition work. The important reformulation of the cartel provisions in 2009 introduced specific criminal offences for price-fixing, bid rigging, output restrictions, market sharing and customer allocation. These forms of conduct are recognised as ‘hard-core’ cartel behaviour which is recognised by the OECD as being the most egregious violation of competition law.¹⁶¹

The introduction of criminal sanctions for cartel conduct was strongly advocated by the ACCC, including in its submission to the Dawson Review. The ACCC continues to hold the view that criminal sanctions for executives found guilty of engaging in cartel behaviour provide an appropriate sanction for hard-core cartel conduct.

Hard-core cartel conduct is a form of theft which is comparable to fraud and little different from classes of corporate crime that also attract criminal sentences. The ACCC considers that civil remedies fail to deter the most flagrant and harmful collusive agreements, where competitors, usually in secret, agree to fix prices, rig bids, limit output or share markets or customers. Cartel conduct is highly profitable and so difficult to detect that civil pecuniary penalties are not a sufficient deterrent for firms and individuals to comply with the law.

Cartel provisions are overly complex and could be simplified

The ACCC has instituted proceedings for civil breaches of the reformulated cartel provisions that were introduced along with criminal sanctions but a criminal prosecution is yet to be commenced. No contested proceedings under the new provisions have been concluded,¹⁶² although there has been one private action.¹⁶³ The interpretation of the new provisions is therefore yet to be fully tested by the courts.

Despite this limited experience, the cartel provisions have been widely criticised, including by members of the judiciary, practitioners and academics, for the complexity of their drafting. Concerns include the potential difficulty in achieving a successful prosecution (especially criminally, where a jury must be directed on complex matters) and the ‘lawful’ escape routes that may be available as a result of the exceptions.¹⁶⁴

The process of prescribing the cartel offences with the necessary degree of specificity required of a criminal offence has resulted in drafting that is complex and which may not provide appropriate certainty.

The ACCC would support a review of the cartel provisions to ensure that they are clear and suitably capture conduct which they are intended to prohibit. Any changes to the law should support and strengthen the current cartel policy.

¹⁶¹ See OECD, *Recommendation Concerning Effective Action Against Hard Core Cartels* (25 March 1998).

¹⁶² *ACCC v Koyo Australia Pty Ltd* [2013] FCA 1051 and *ACCC v NSK Australia Pty Ltd* [2014] FCA 453, where orders were made by consent.

¹⁶³ *Norcast SARL v Bradken* [2013] FCA 235.

¹⁶⁴ Brent Fisse, *Avoidance and Denial of Liability for Cartel Conduct Proactive Lawful Escape Routes Left Open by the Cartel Legislation* (Competition Law Conference, 23 May 2009) (available at: http://www.brentfisse.com/images/Fisse_Avoidance_&_Denial_of_Liability_for_Cartel_Offences_230509.pdf); Justice Steven Rares, *Competition, Fairness and the Courts* (Competition Law Conference, 24 May 2014) (available at: <http://www.fedcourt.gov.au/publications/judges-speeches/justice-raises/raises-j-20140524>).

4.3.3 Simplifying the authorisation and notification regimes to promote accessibility for business

The authorisation and notification provisions should be reviewed to ensure that they strike the right balance between effective regulation and the regulatory burden imposed.

The authorisation and notification provisions and the associated application forms should be reviewed to consolidate and/or simplify where appropriate.

Authorisation provides statutory protection from legal action under the competition provisions of the CCA, other than section 46 (misuse of market power). Statutory protection for exclusive dealing conduct, collective bargaining and/or collective boycott arrangements and certain information disclosures can also be sought by lodging a notification with the ACCC.

The authorisation and notification provisions of the CCA recognise that in certain circumstances, allowing conduct that might restrict competition in order to enhance efficiency and welfare may be in the public interest. While open and unrestricted competition in markets is generally viewed as the best way to allocate resources and drive efficiency, where there is a market failure or market imperfection, it may be the case that restrictions on competition could achieve a more efficient outcome.

The authorisation and notification process involves a trade-off between the public benefits from the proposed conduct for which authorisation is sought, against the public detriments arising from that conduct. This trade-off can also be seen as an assessment of the benefits of addressing the source of market failure or market imperfection and the costs of restricting competition. This

Divisions 1 and 2 of Part VII of the CCA provide for the granting of authorisation and the issuing of an objection notice in response to a notification.

There are a number of procedural differences between authorisation and notification. For example, the statutory protection provided by a notification comes into force automatically (either immediately or after 14 days depending on the type of notification lodged). By contrast, the authorisation provisions of the CCA broadly require the ACCC to engage in public consultation and publish a draft determination before a final determination granting or denying statutory protection is made. Authorisation and notification are transparent processes. The ACCC maintains internet based public registers for all such applications made to it.

The ACCC has published a number of guidelines explaining the authorisation and notification processes and its approach to assessing requests for statutory protection. These publications are available from the ACCC website. It is not proposed to deal with them in any detail for the purposes of this submission.

The ACCC receives approximately 30 authorisation projects (involving a greater number of applications) a year. For the 2012-13 financial year the ACCC received 65 authorisation applications (spanning 33 projects), 78 notifications of collective bargaining (spanning 6 projects) and over 750 notifications of exclusive dealing conduct. The ACCC did not receive any notifications of collective boycott or notifications of price disclosure.

Authorisation is a highly effective mechanism that has consistently been used by the business community to assist in responding to a diverse range of market failures.

Examples of the types of conduct or arrangements where authorisation has been sought include non-prescribed voluntary industry codes of conduct, industry levies, certain types of joint ventures or alliances, and collective bargaining.

Case study – examples of authorisation matters

Providing for industry self-regulation

In 2014, the ACCC authorised an industry code of practice to be adopted by marketing companies who provide face-to-face sales on behalf of electricity and gas retailers.

Assisting in the transition from a regulated environment to a deregulated environment

In 2010, the ERA undertook a review of the *Chicken Meat Industry Act (WA) 1977* (the CMI Act). This review broadly recommended that the CMI Act should be allowed to expire and that the industry should move to a deregulated environment in which grower contracts are developed through a process of collective bargaining. In 2011 the Western Australian Broiler Growers' Association sought and was granted authorisation to allow growers to engage in collective bargaining.

Assisting vulnerable consumers

In 2012, the ACCC granted authorisation to allow a number of financial institutions to provide fee free balances and withdrawals to their customers from existing selected ATMs located in very remote Indigenous communities. This proposal was in response to the ATM Taskforce report which found that people in very remote Indigenous communities pay relatively high levels of total ATM fees.

Addressing coordination problems in major infrastructure projects

In 2010, the ACCC authorised a capacity framework, enabling industry to implement a long term solution to the ongoing capacity constraints in the Hunter Valley coal chain.

Current provisions - the authorisation and notification provisions must strike the right balance

Authorisation is a highly effective, and in the main, efficient mechanism for addressing market failures or imperfections. As noted above, it allows industry to develop solutions that best fit their circumstances and for these arrangements to be permitted where they deliver an overriding benefit to the public.

The ACCC considers, however, that both the authorisation and the notification provisions, and associated forms, would benefit from simplification and, where appropriate, consolidation.

The authorisation and notification provisions have not been holistically reviewed since their introduction in 1974. While there have been a number of amendments since this time, these amendments have addressed specific issues rather than providing a considered review of the overall effectiveness of the provisions in contributing to the objective of the CCA. The current Competition Policy Review provides an important opportunity to undertake such an analysis.

The complexity of provisions risks impeding accessibility by business

The ACCC is concerned that the complexity of the authorisation and notification provisions may make the process less accessible for business, especially small businesses. The risk is that some prospective applicants may be deterred from making an application or feel compelled to seek professional assistance, the cost of which may also act as a deterrent in some cases.

In particular the ACCC notes that the provisions impose technical 'red tape' burdens on applicants, for example one 'arrangement' can involve the completion of multiple complex forms and the need to satisfactorily address technical variations of the public benefit test.

In the ACCC's experience, applicants and their advisers can find it confusing to identify the correct application form(s) and public benefit test(s) that will be applied to their specific

proposal. To add to this complexity, an application providing the correct information but lodged on the incorrect form is invalid under section 89(1) of the CCA.

While guidance materials and consultation with ACCC staff can assist, ultimately the process is more complicated than it may otherwise need to be, giving rise to higher compliance costs.

The inflexibility of provisions can prevent common sense outcomes

The ACCC also considers that some provisions can be seen as inflexible. For example, an applicant who requires an extension to the 6 month time frame for an ACCC determination in order to provide additional information in support of their proposal is ultimately 'book ended' by the operation of subsections 90 (10) and (10A). These provisions were introduced to provide timely decisions for applicants but they have acted as an unintended impediment on occasion. The ACCC notes that greater flexibility would be provided by allowing an applicant to request that the timeframe for the ACCC's consideration of its application be extended. Such an amendment would address this inflexibility while preserving the general timeliness of the authorisation process.

Working within these complexities

The ACCC takes a practical approach to performing its authorisation and notification functions in order to reduce the red tape burden that can be experienced by applicants. As part of this, the ACCC has a range of user friendly authorisation and notification guidelines, including guidelines specifically targeting small business. The ACCC also provides examples of completed application forms which applicants can use to better understand the types of information they need to provide to support their application. While such materials are useful for applicants, there are limits to what the ACCC can do. Ultimately the ACCC must work within the framework provided by the CCA and it is clear that more could be done to improve the statutory framework.

The ACCC considers that there is a strong case for reducing the regulatory red tape in this area and further considers that it can be done without the loss of regulatory safeguards and jurisprudence.

The authorisation and notification provisions provide an important counterbalance to the competition provisions of the CCA. They ensure that arrangements which result in an overriding public benefit can occur, even when there are potential competition concerns. Reforms to improve the effectiveness and efficiency of the authorisation and notification provisions, while not currently high profile considerations, are important in the ongoing refinement of competition law. The Competition Policy Review provides an opportunity for such reforms to be considered further.

4.4 Improving the effectiveness of the ACCC's investigative tools

Key points

- The effectiveness of the CCA in discouraging anti-competitive conduct is directly linked to its enforceability. In turn, the investigative tools available to the ACCC are critically important for effective enforcement.
- Several investigative tools in the CCA require amendment to ensure that they operate appropriately.
- The ACCC's compulsory information gathering powers under section 155 are of particular importance. Recommended changes include:
 - (i) increasing criminal penalties for non-compliance, and introducing civil penalties;
 - (ii) introducing civil provisions to compel compliance with a section 155 notice;
 - (iii) ensuring section 155 powers apply where appropriate; including in relation to:
 - particular investigative circumstances, such as multi-party investigations; and
 - other ACCC functions under the CCA, such as enforcement of section 87B undertakings, assessment of formal merger clearances and Part IIIA access undertakings.
- To support the ACCC in gathering evidence for investigations, and to foster increased detection of anti-competitive conduct, greater protection for whistle-blowers or informants should be provided through:
 - (i) sanctions that better deter intimidation; and
 - (ii) the creation of a third party whistle-blower regime, modelled on the regime in the Corporations Act.
- Several more suggested reforms to investigative tools are set out in Attachment A to this submission.

4.4.1 The ACCC's investigative tools are critical to the effective enforcement of the CCA

*'Law cannot reach where enforcement cannot follow.'*¹⁶⁵

The effectiveness of the CCA in discouraging anti-competitive conduct is directly linked to its enforceability – both perceived and actual. The enforceability of the CCA is directly affected by the drafting of its provisions and the ACCC's ability to identify and investigate alleged breaches of such provisions. Accordingly, the effectiveness of the investigatory powers available to the ACCC is of critical importance. These investigative powers are not available to private litigants, and as a result the ACCC will often be uniquely placed to pursue matters involving significant competitive and consumer harm.

Investigations by the ACCC necessarily centre on the search for evidence that determines whether a breach of the CCA is likely to have occurred, regardless of whether subsequent action involves litigation or some alternative enforcement strategy.

There are a number of tools available to the ACCC to assist it in obtaining such evidence, including:

- the ability to issue a notice under section 155 to require information and documents to be provided, or to require attendance at an examination, in relation to an investigation;

¹⁶⁵ Nicholas Goodison, 'Fraud - Add Action to the Act', *The Times* (16 January 1986).

- search and seizure powers under warrants;
- substantiation notices (which are available in certain consumer protection matters); and
- sharing information and liaising with other Commonwealth and state regulatory authorities who are able to obtain additional information through broader warrant powers.

These tools are complementary to the ACCC's ability to obtain evidence voluntarily from traders and complainants. The ACCC may also obtain information from international regulatory agencies, although there are limitations to the scope of the information that can be obtained.

The compulsory information gathering powers conferred by section 155 are crucial to the ACCC's ability to effectively carry out its enforcement role.¹⁶⁶ Section 155 compels the production of evidence to the ACCC and removes reliance upon voluntary evidence gathering processes. It is particularly important in the investigation of covert behaviour.

Section 155 is broadly similar to the investigatory powers of other Australian law enforcement agencies, including the Australian Taxation Office and the Australian Securities and Investments Commission (ASIC).

The decision to issue a section 155 notice is not taken lightly. The ACCC does not consider it appropriate to use its powers under section 155 to conduct a 'fishing expedition' for information, documents or evidence. It does not, and cannot, under section 155(1), issue a notice unless the Commission, the Chairperson or the Deputy Chairperson has the requisite 'reason to believe'¹⁶⁷ relating to the matter. In addition to these legislative requirements, the ACCC follows rigorous internal processes for assessing whether a section 155 notice may be issued and will also have regard to the potential burden and cost of compliance for a recipient.

The ACCC considers that there are a number of reforms to section 155 and other investigative provisions of the CCA which would significantly assist the ACCC's investigative processes. These are outlined below. A further important subset of suggested reforms to the investigative provisions is outlined for completeness at **Attachment A** to this submission.

4.4.2 Current penalties and enforcement regime for non-compliance with section 155 notices are inadequate

Provisions addressing matters of non-compliance with section 155 notices require amendment to ensure that the CCA provides effective and efficient deterrence for those parties seeking to obstruct investigations and so that the ACCC can efficiently pursue non-compliance, including through civil orders, when it arises.

As has been noted, the information powers conferred by section 155 are a critically important element of the ACCC's investigative, and ultimately enforcement, activities. Non-compliance with a validly issued section 155 notice inevitably interferes with ACCC investigations and in many cases prevents the ACCC taking action to address harm. It is therefore very important that non-compliance is strongly deterred.

Under the current provisions, a refusal or failure to comply with a section 155 notice by the specified due date or knowingly furnishing information or giving evidence that is false or misleading, is a criminal offence. At present, this offence attracts a fine of up to \$3,400 and/or 12 months imprisonment for individuals, and up to \$17,000 for companies.

In circumstances where a custodial sentence for non-compliance with section 155 notices may be ordered for individuals, it is important that commensurate financial penalties are set

¹⁶⁶ In the 2012-2013 financial year, 358 notices were issued under section 155.

¹⁶⁷ Section 155 provides that a notice can only be issued where the Commission, the Chairperson or Deputy Chairperson has reason to believe that a person is capable of furnishing information, producing documents or giving evidence relating to a matter that contravenes, or may contravene, the CCA.

for companies. The ACCC considers that the current financial penalties are woefully inadequate and fail to reflect the seriousness and criminality of this conduct. Particularly so when the non-compliance could be seeking to avoid revealing a contravention of the CCA that could attract a corporate penalty of \$10 million or more.

Further, the prosecution of non-compliance with section 155, being an offence, requires the preparation of a brief of evidence by the ACCC and referral of the matter to the Commonwealth Director of Public Prosecutions for consideration of prosecution action. This is a time consuming and resource intensive process that does not address the primary issue; namely, non-compliance with the legal requirement to provide information or documents or give truthful evidence relevant to the underlying ACCC investigation. Even if successful, a prosecution cannot compel provision to the ACCC of the information, documents or evidence it seeks to pursue for its investigation.

Section 155 should therefore be amended to allow the ACCC to seek civil court orders compelling compliance with a notice and, when appropriate, civil pecuniary penalties of sufficient quantum to deter non-compliance. This would improve the ACCC's capacity to deal with non-compliance in a timely manner.

The existence of a dual criminal and civil regime for non-compliance would give the ACCC the ability to more appropriately characterise and address obstructionist conduct by recipients of notices. A civil regime would allow the ACCC to efficiently pursue interim orders to obtain the information and documents it needs in a timely manner without unduly halting the progress of an investigation. An improved, co-existing criminal regime would allow the ACCC to address more serious levels of obstructionist behaviour which require a higher level of deterrence and penalty.

4.4.3 The ACCC should be able to use section 155 in more circumstances

The ACCC considers that section 155 should be available in a broader range of circumstances including:

- **after the commencement of proceedings seeking injunctive relief, multi-party investigations and staggered litigation;**
- **when investigating breaches of the ancillary liability provisions; and**
- **in respect of other broader ACCC powers and functions including in relation to section 87B undertakings, formal merger clearances and Part IIIA access codes and undertakings.**

The ACCC considers that the drafting of section 155 limits its scope and application in several circumstances which impacts upon the effectiveness of evidence gathering by the ACCC.

Use of section 155 notices after the commencement of proceedings seeking injunctive relief

A number of Federal Court decisions addressing section 155 have found that the power is to be used only for the performance of the administrative function of determining whether proceedings should be instituted.¹⁶⁸ Accordingly, the ACCC is generally unable to use these investigative powers to gather evidence once an investigation is concluded and proceedings commenced in respect of that investigation.

Section 155(4) was intended to provide a narrow exception to this for circumstances where the ACCC needed to seek urgent interim injunctive relief to prevent serious contravening

¹⁶⁸ *Brambles Holdings Ltd v TPC (No 2)* (1980) 32 ALR 328; *Pioneer Concrete v TPC* (1982) 152 CLR 460; *Kotan Holdings v TPC* (1991) 30 FCR 511; *Korean Airlines v ACCC (No 3)* [2008] FCA 701.

conduct from continuing soon after becoming aware of it but, where the investigation was continuing and the use of section 155 powers remained necessary.¹⁶⁹

One interpretation of this provision is that it is applicable only where the ACCC seeks injunctive relief (whether interim or final) with no other orders. However, the ACCC invariably seeks injunctive relief as part of a proceeding for a broader suite of remedies, including declarations and penalties. If the provision is interpreted in this narrow way, its intended application will be significantly curtailed.

The ACCC is unable to test this interpretation before the Courts because to do so would place the ACCC Chairman, as the issuer of the notice, at risk of a finding of contempt.

Accordingly, the ACCC considers that amendment to section 155(4) is appropriate to clarify that notices may be issued in circumstances where the ACCC has sought urgent interim injunctive relief as part of a proceeding for a broader range of remedies.¹⁷⁰

Use of section 155 notices after the commencement of multi-party investigations and staggered litigation

Section 155 is predicated upon the ACCC conducting an investigation into 'a matter that constitutes, or may constitute, a contravention'. As noted above, a number of the Federal Court cases dealing with section 155 have found that the ACCC cannot use its investigative powers to gather evidence once proceedings have commenced in respect of that investigation.

The ACCC considers that the combination of these cases and the terminology used in section 155 has the potential to cause additional difficulties in multi-party investigations where proceedings have commenced in respect of some parties subject to the ACCC's investigation and not others. This difficulty is highlighted by the particular wording in section 155(4), namely 'the Commission commences proceedings in relation to the matter'.

In such circumstances, the language of the section draws into question whether the relevant 'matter' is the fact of the contravention or the conduct of the particular recipient of a notice. For example, where cartel conduct is engaged in by three traders and proceedings have only been instituted against two of these traders, there is doubt as to whether the ACCC can issue a notice to the third trader (who remains under investigation) owing to the fact that proceedings have been commenced in respect of that contravention.

The ACCC considers that amendment to section 155(4) is appropriate to clarify that the relevant 'matter' should be limited to the conduct of the recipient of a notice, to avoid any unnecessary ambiguity that could stifle the scope of obtaining evidence in relation to multiple parties and where staggered litigation is necessary.

Section 155 should be available for investigations of possible breaches of the ancillary liability provisions

The present wording of section 155 confines its operation to investigation of 'a matter that constitutes, or may constitute, a contravention' of the CCA or other specified legislation.

The ACCC considers that the provision should be amended to put beyond doubt the ACCC's current interpretation that conduct which may only be able to be characterised as an attempt to contravene, an attempt to induce a contravention, aiding and abetting or being knowingly

¹⁶⁹ The Explanatory Memorandum for the introduction of section 155(4) makes reference to the concerns of the ACCC that it 'has been significantly hindered by its inability to fully investigate matters through the use of section 155 after it has applied for an interim injunction' and states that the introduction of subsection (4) was to avoid the 'CCC's ability to investigate suspected contraventions of the law... [from being] frustrated': Explanatory Memorandum, *Trade Practices Legislation Amendment Bill 2008* (Cth).

¹⁷⁰ For example, the need for a properly functioning section 155(4) is important in product safety matters where there is a need for urgent injunctive relief to halt the distribution and sale of dangerous products but where a full investigation is yet to take place.

concerned in a contravention, or conspiring to contravene, are all clearly captured by the terms of section 155.

Section 155 should be more broadly available in relation to other ACCC powers and functions

In addition to investigating potential contraventions of the CCA, the ACCC is able to use section 155 notices in relation to other powers and functions, such as those it has in relation to 'designated communications matters'.¹⁷¹ For example, the ACCC is able to use its section 155 powers to investigate potential breaches of Telstra's Structural Separation Undertaking or to gather information in relation to its decisions regarding the terms of access to telecommunications services.

There are a number of powers and functions that the ACCC may exercise in connection with matters set out in the CCA where it is not clear that the ACCC may use its compulsory information gathering powers under section 155. The ACCC considers that these deficiencies should be addressed to increase the effectiveness of the ACCC's functions.

The ACCC considers that section 155 notices should be available to compel information in relation to most of the ACCC's powers and functions related to the CCA, including.¹⁷²

- **Investigating potential breaches of section 87B undertakings:** The ACCC accepts undertakings from parties to resolve issues relating to potential breaches of the CCA, including as an alternative to court proceedings (e.g. where the ACCC has concerns that a breach has occurred, the party may provide an undertaking that they will cease the relevant behaviour and commit, for example, to a compliance program) or to remedy competition concerns that the ACCC may have in relation to a merger.

Particularly in the merger context, the remedies that may be provided by a party in a section 87B undertaking may be complex and require monitoring over an extended period of time to ensure that competitive detriment does not occur (see section 3.3.1). Whilst the obligations provided in these undertakings are court enforceable, it can be difficult for the ACCC to effectively monitor compliance and investigate suspected breaches. This affects the efficacy of section 87B undertakings as a flexible and timely process by which parties can remedy competition concerns.

- **Assessment of formal merger clearance applications:** Where a party makes an application for formal clearance of an acquisition, the ACCC may only 'request' additional information and documents. To ensure that the ACCC is provided with the necessary information to properly consider such an application in a timely way, the ACCC considers that compulsory information gathering powers would be appropriate. As is noted in section 4.2.3, in the event that the ACCC were to become the first instance decision maker in merger authorisation applications further regard would also need to be had to the compulsory information gathering powers that would be made available to it.
- **Investigating potential breaches of access undertakings and access codes under Part IIIA:** The ACCC is not able to use its compulsory information gathering powers to investigate potential breaches of access undertakings or access codes. The ACCC considers that it should be able to compel the provision of information in relation to compliance with undertakings and access codes under Part IIIA, consistent with the extension of the ACCC's section 155 powers to other regulatory matters (such as telecommunications undertakings).

¹⁷¹ CCA s 155(9).

¹⁷² While the Australian Consumer Law is outside of the scope of the current Review, the ACCC notes that section 155 also does not apply in respect of Unfair Contract Terms: refer to Attachment A of this submission.

4.4.4 Greater protection for whistle-blowers

Greater protection should be available for whistle-blowers, through sanctions that deter intimidation and the creation of a third party whistle-blower regime, modelled on the regime provided in the Corporations Act.

The success of ACCC investigations is heavily reliant upon the co-operation of individuals particularly, in respect of alleged contraventions which involve coercive, covert behaviour. Typically, there are three categories of such individuals: *immunity applicants* (who are involved in alleged conduct), *informants* (who have knowledge of the conduct but are not directly involved) and *complainants* (who have some limited knowledge of the conduct and wish to report the matter to the ACCC). All three categories of individuals will have unique concerns about the implications of their assistance in an ACCC investigation.

Of these, immunity applicants have the benefit of the protection of the ACCC's immunity and co-operation policies.¹⁷³ Similarly, informants have some protection afforded by section 162A of the CCA in respect of intimidation or other coercive conduct they may be subjected to as a result of co-operation with the ACCC. The information provided by complainants is kept confidential to the extent permitted by the law and is guided by the ACCC and AER information policy.¹⁷⁴

However, these protections do not adequately extend to circumstances outside of the ACCC's control which may flow as a consequence of assistance provided to the ACCC for example, contractual actions or other impacts to livelihood. The ACCC strongly supports consideration of reform to penalties for intimidation and other coercive conduct under section 162A as well as the introduction of a third party whistle-blower regime applicable to all informants and complainants (hereafter referred to as "third party whistle-blowers") outlined below.

Penalties for intimidation are inadequate

Parties may obstruct current or future ACCC investigations by seeking to intimidate persons who may otherwise assist the ACCC. Section 162A broadly prohibits persons from threatening, intimidating or coercing another or causing damage, loss or disadvantage to another, on account of that other person assisting the ACCC.

In the ACCC's experience, concerns over intimidation or harm in the context of assisting an ACCC investigation can pose a significant hurdle to obtaining crucial information and may halt the progress of an ACCC investigation indefinitely.

The ACCC notes that the same sanctions apply to contraventions of section 162A as in relation to matters of non-compliance with section 155; that is, a fine of up to \$3,400 and/or 12 months imprisonment for individuals, and up to \$17,000 for companies. The ACCC considers that the level of sanctions are inadequate and do not provide sufficient deterrence.

Further, section 162A should be reviewed to put beyond doubt the ACCC's interpretation that it captures both positive acts and failures to act (for example not renewing a contract).

The CCA should provide for an effective whistle-blower regime

The CCA, unlike the Corporations Act, does not provide for a formal third party 'whistle-blower' regime. The ACCC's immunity policy has been very successful in encouraging

¹⁷³ ACCC, *ACCC Immunity Policy for Cartel Conduct* (July 2009) available at <http://www.accc.gov.au/publications/accc-immunity-policy-for-cartel-conduct> ; ACCC, *ACCC Co-operation Policy for Enforcement Matters* (2002) available at <http://www.accc.gov.au/publications/accc-cooperation-policy-for-enforcement-matters>. These documents are currently under review, see <http://www.accc.gov.au/media-release/accc-releases-draft-cartel-immunity-and-cooperation-policy-for-comment>.

¹⁷⁴ ACCC, 'ACCC & AER information policy: collection and disclosure of information' (June 2014) <http://www.accc.gov.au/publications/accc-aer-information-policy-collection-and-disclosure-of-information>.

whistle-blowers involved in cartel conduct. This policy is augmented by the ACCC's co-operation policy for enforcement matters. However, the immunity policy is limited to conferring protection from ACCC legal action or a criminal prosecution. It only applies to persons engaged in the contravention and it does not protect third-party whistle-blowers from action that may be taken to punish them for assisting the ACCC.

The ACCC considers that protection for third party whistle-blowers is an important element of an effective competition policy and that such a regime should be introduced as an amendment to the CCA.

Corporations Act – response to whistle-blowers within a firm under investigation

The Corporations Act broadly provides that a third party whistle-blower can be protected from civil or criminal liability, as well as from liability or termination arising from enforcement of any other form of right or remedy, such as a contract.¹⁷⁵ The regime does not protect a whistle-blower from liability arising from conduct they engage in themselves.¹⁷⁶ Protection is afforded if the whistle-blower meets certain conditions - such as being an employee, officer or contractor of the company the subject of the disclosure; having made the disclosure to ASIC or other specified persons; having reasonable grounds for believing the law has been contravened; and having made the disclosure in good faith.¹⁷⁷ The whistle-blower also has a right to compensation if the protection afforded to them under the regime is breached in specified circumstances.¹⁷⁸

The ACCC would additionally support measures within any such third party whistle-blower regime that is introduced to make it harder for intimidation to occur and to increase the protections afforded to informants and complainants generally.

While the ACCC can and does seek to protect the identity of persons who come forward with information in relation to a possible contravention of the CCA, and while provisions exist in the CCA itself (s. 155AAA) and exemptions in other regimes (such as freedom of information or court processes) to resist production of confidential information or documents on public interest grounds, consideration could be given to specific protections to information or documents that disclose the identity of whistle-blowers within a whistle-blower regime.

Further, the ability for the ACCC to seek compensation on behalf of a witness who has suffered loss or damage as a result of giving evidence would help to deter unlawful intimidation, and so should also be considered as part of a whistle-blower regime.

¹⁷⁵ Corporations Act s. 1317AB.

¹⁷⁶ Corporations Act s. 1317AB(1).

¹⁷⁷ Corporations Act ss. 1317AA 1317AB.

¹⁷⁸ Corporations Act ss. 1317AC 1317AD.

4.5 Small business and the CCA

Key points

The ACCC, like all regulators, has a 'dual role' – it both enforces the provisions of the CCA and educates businesses about their rights and responsibilities. The ACCC recognises that the information needs and interests of small business, particularly those of micro businesses, are very different to those of large firms. Given the particular needs of small business, the ACCC provides specific resources to educate and support them.

The ACCC recommends the following reforms to assist small business:

- Extend the unfair contract term provisions in the Australian Consumer Law to contracts involving small businesses.
- Amend the collective bargaining / boycott notification regime to make it more accessible and to allow small business greater opportunities for to undertake collective boycotts. The ACCC proposes a number of amendments which will make notifications more flexible and will allow for a greater number of arrangements to be given put into effect.
- Amend all prescribed industry codes to improve their enforceability. The ACCC supports the introduction of civil pecuniary penalties, infringement notices and improvements to the audit provisions regarding industry codes.
- Amend the Horticulture Code to improve its coverage.
- Implement a legally enforceable supermarket and grocery industry code of conduct that provides clear rights and obligations.
- Amend the ACCC's educative and research role as provided for by the CCA to better reflect current practices and stakeholder expectations.

4.5.1 ACCC role in the small business sector

There are over two million businesses operating in Australia. While definitions for 'small business' differ, it is clear that the vast majority of these businesses are small, with over 97 per cent having less than 20 employees.¹⁷⁹ Small business plays a significant role in Australia's economy, contributing one third of Australia's productivity and accounting for almost half of Australia's private sector employment.¹⁸⁰

These statistics do not tell the full story though; the majority of small businesses are 'micro businesses', having less than five employees. Small businesses are more common in some sectors, for example services and agriculture, than in others, such as mining and manufacturing. Small businesses are located across metropolitan, regional and rural centres, with the majority of small businesses located in capital cities. The distribution however, is not equal, with over half of small businesses in Queensland and Tasmania being located in regional areas.

The ACCC, like all regulators, has a 'dual role' – it both enforces the provisions of the CCA and educates businesses about their rights and responsibilities. In carrying out its enforcement role, the ACCC's main goals are to:

- maintain and promote competition and remedy market failure, and
- protect the interests and safety of consumers and support fair trading in markets.

¹⁷⁹ Australian Bureau of Statistics, *8165.0 - Counts of Australian number Businesses, including Entries and Exits, Jun 2009 to Jun 2013* (2014).

¹⁸⁰ Department of Industry Innovation, Science, Research and Tertiary Education, *Australian Small Business Key Statistics and Analysis* (2012).

The ACCC takes the firm view that prevention of a breach of the CCA is always preferable to taking action after a breach has occurred. As part of this, the ACCC seeks to ensure that small businesses are fully aware of both their rights and responsibilities under the CCA.

The ACCC recognises that the information needs and interests of small business, particularly those of micro businesses, are very different to those of large firms. The ACCC uses a number of communication channels to reach small business – through its website, a dedicated small business hotline, targeted publications, apps, online education modules, webinars, video clips and DVDs, as well as through speaking engagements and presentations to key small business representatives.

The ACCC also has two consultative committees which are focussed on the small business sector - the Small Business Consultative Committee and the Franchising Consultative Committee. These committees provide a forum through which competition and consumer concerns relating to the small business sector and the franchising sector can be considered and addressed collaboratively. Members are drawn from a range of sectors, including Federal and state Small Business Commissioners, key small business associations, franchisees, franchisors, business advisors, government agencies, researchers and educators.

The ACCC also has a number of staff dedicated to undertaking liaison with small business and a dedicated Deputy Chair with extensive knowledge of and experience in small business.

In addition to its broader educative role, the ACCC also provides guidance to small business about their rights and obligations under the CCA. For example, ACCC staff work closely with small businesses to assist them in completing the lodgement process for applications for authorisation or notifications of collective bargaining.

The ACCC publishes *Small Business in Focus*¹⁸¹ on a bi-annual basis which provides information about the enquiries and complaints from small businesses received by the ACCC. This data shows that while the majority of queries relate to the Australian Consumer Law, in particular misleading conduct or deceptive, a significant number relate to competition issues. Common competition concerns for small business include exclusive dealing and allegations of misuse of market power by another business.

The ACCC has a number of enforcement priorities that are particularly relevant to small business:

- conduct resulting in a substantial consumer (including small business) detriment;
- unconscionable conduct, particularly involving large national companies or traders, which impacts on consumers and small business;
- conduct in concentrated markets which impacts on small business, consumers or suppliers;
- in conjunction with other agencies, disruption of scams that rely on building deceptive relationships and which cause severe and widespread consumer or small business detriment;
- complexity and unfairness in consumer or small business contracts; and
- credence claims, particularly those with the potential to adversely impact the competitive process and small business. Most complainants in relation to misleading credence claims are small businesses who are losing business due to the deception of others.

¹⁸¹ ACCC, *Small Business in Focus* (2014) (available at: <http://www.accc.gov.au/publications/small-business-in-focus/small-business-in-focus-1-july-2013-to-31-december-2013>).

The ACCC's enforcement activities are undertaken to make markets work for all Australians. This can mean that the ACCC deals with small businesses as complainants, affected competitors or as respondents.

In addition to its functions under the competition and consumer provisions of the CCA, the ACCC is also responsible for promoting compliance with a number of mandatory codes of conduct that are of direct relevance to small business: the Franchising Code of Conduct, the Horticulture Code of Conduct, the Oilcode and the Unit Pricing Code. Specific reforms to improve the effectiveness of the prescribed codes are discussed below.

In the ACCC's experience, of key importance to small business is a legal system which supports the principle that all businesses should be able to compete on their merits.

4.5.2 Provisions restricting unilateral conduct and prohibiting unconscionable conduct

The ACCC supports the Australian Government's proposed legislative amendments to extend the existing unfair contract term provisions to contracts involving small business.

A common concern raised with the ACCC by small business is that of unilateral changes to contracts by a larger business. From the small business' perspective, these unilateral changes are to the sole benefit of the larger counterparty, or have resulted in some detriment to their business without offsetting benefits. While many of these concerns raised with the ACCC by small business relate to contractual matters rather than competition matters, not all do.

The CCA provides a number of measures aimed at addressing particular forms of anti-competitive unilateral conduct and the ACCC has made specific recommendations regarding amendments to improve the section 46 prohibition relating to misuse of market power (see section 4.2.1). The Australian Government has also recently commenced a process of consultation to consider whether the current unfair contract term provisions of the Australian Consumer Law should be extended beyond consumers to small business.¹⁸² It is the ACCC's experience that in certain circumstances small businesses have characteristics in common with those of a consumer. This is particularly so when dealing with standard form contracts that are offered on a 'take it or leave it' basis. In these circumstances the scope for a small business to amend the contract to better suit its circumstances is limited.

The unconscionable conduct provisions also provide a mechanism through which unilateral conduct can be regulated. The ACCC recognises that unconscionable conduct is a complex area of the law. In September 2012, it published *Unconscionable Conduct: Business Snapshot*¹⁸³ which explains the principles and factors behind unconscionable conduct to assist businesses and consumers in understanding what such conduct is. The Snapshot also provides practical tips for businesses to minimise the risk of becoming a victim of unconscionable conduct, as well as to avoid engaging in such conduct towards other businesses or consumers. Unconscionable conduct remains a significant matter of concern for consumers and the business community, and the ACCC is currently undertaking ten in-depth investigations and is engaged in proceedings in the Federal Court in relation to five matters.

¹⁸² The Treasury, *Extending Unfair Contract Term Protections to Small Businesses* (23 May 2014) (available at: <http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2014/Small-Business-and-Unfair-Contract-Terms>).

¹⁸³ ACCC, *Unconscionable Conduct: Business Snapshot* (September 2012) (available at: <http://www.accc.gov.au/publications/business-snapshot/unconscionable-conduct>).

4.5.3 Small business issues relating to the supermarket and grocery industry

The ACCC considers that a legally enforceable supermarket and grocery industry code of conduct that provides clear rights and obligations should be implemented.

The ACCC has recently commenced action against Coles Supermarkets Australia Pty Ltd and Grocery Holdings Pty Ltd alleging unconscionable conduct in their dealings with suppliers.¹⁸⁴ This action is part of a broader investigation into claims made against the major supermarket chains about their dealings with suppliers. The broader investigations have focussed on whether there was evidence that the major supermarket chains were misusing their market power in breach of section 46 of the CCA and/or were engaging in unconscionable conduct in their dealings with suppliers in breach of sections 20, 21 and/or 22 of the Australian Consumer Law. The ACCC's investigations are continuing.

The ACCC notes that concerns about dealings between big businesses, such as retailers and food processors, and the small businesses who supply them are not a recent development, nor are they unique to Australia. In 2008, the ACCC undertook a Grocery Inquiry¹⁸⁵ which closely examined whether buyer power was leading to distortions in the grocery sector. More recently the OECD has published its report on the *Roundtable on Competition Issues in the Food Chain Industry*.¹⁸⁶ The roundtable was held by the Competition Committee in October 2013 and examined developments in the food chain across a range of countries and the regulatory responses that had been implemented. Australia, through the Treasury and the ACCC, participated in the roundtable and its submission is included in the OECD's report. The OECD report found that many nations have considered the food supply chain due to concerns of anti-competitive or unfair practices.

A supermarket and grocery industry working group which includes Coles, Woolworths and the Australian Food and Grocery Council, has developed the *Food and Grocery Prescribed Industry Code of Conduct* (Food and Grocery Code).¹⁸⁷ It is proposed that the Food and Grocery Code would regulate the supply relationship between retailer supermarkets and grocery suppliers and that it would be enforceable under the CCA.

The ACCC considers that a legally enforceable supermarket and grocery industry code of conduct that provides clear rights and obligations should be implemented. The ACCC does however have some concerns in respect of the current draft Food and Grocery Code, including the potential for gaps in its application (e.g. parties subject to the code would need to agree to be bound by it). The draft Food and Grocery Code also contemplates allowing supermarkets to contract out of certain obligations, and the ACCC considers this to be problematic given relationships in the supermarket supply chain are generally characterised by an imbalance in bargaining power. These factors, if not satisfactorily addressed, may impede the enforceability of the Food and Grocery Code.

¹⁸⁴ ACCC, *ACCC Takes Action Against Coles for Alleged Unconscionable Conduct Towards its Suppliers* (5 May 2014) (available at: <http://www.accc.gov.au/media-release/accc-takes-action-against-coles-for-alleged-unconscionable-conduct-towards-its-suppliers>).

¹⁸⁵ ACCC, *Report of the ACCC Inquiry into the Competitiveness of Retail Prices for Standard Groceries* (July 2008) (available at: <http://www.accc.gov.au/about-us/public-consultations/grocery-inquiry-2008>).

¹⁸⁶ OECD, *OECD Policy Roundtables – Competition Issues in the Food Chain* (14 May 2014) (available at: <http://www.oecd.org/daf/competition/CompetitionIssuesintheFoodChainIndustry.pdf>).

¹⁸⁷ Australian Food and Grocery Council, *Food and Grocery Industry Code of Conduct* (November 2013) (available at: <http://www.afgc.org.au/industry-affairs/food-and-grocery-code-of-conduct.html>).

4.5.4 Effective dispute resolution for small business

The ACCC considers that Small Business Commissioners provide an important avenue of flexible and effective dispute resolution for small business, and recommends that they continue to be utilised for the mediation of disputes which may fall outside the ambit of the CCA.

Not all unilateral conduct will contravene the CCA, and of the conduct that may contravene the CCA, the enforcement provisions of the CCA are not necessarily the most efficient mechanism for a small business seeking to address their concerns. In the ACCC is often approached by small businesses which are seeking guidance or assistance to have a dispute resolved in a timely and efficient manner, rather than looking to the ACCC to take enforcement action. This reflects the fact that for many small businesses an important outcome is to preserve the ongoing commercial relationship between the parties.

The ACCC considers that many of the commercial disputes between small and larger businesses could be addressed in an efficient and timely manner through the adoption of more flexible models for dispute resolution. Formal, highly structured processes as codified in the CCA are not particularly conducive to resolving small business disputes, largely because such processes and forums are often intimidating and/or inaccessible to small businesses (because of cost or other factors). The ACCC considers that Small Business Commissioners provide an important avenue for small businesses seeking accessible, timely and effective dispute resolution services and the ACCC already works closely with each of the Commissioners to cross-refer matters to the most suitable agency.

There are a number of other regulatory and industry bodies established to provide guidance, and in some cases dispute resolution services, to small businesses. In some circumstances the ACCC assists small business in identifying the most appropriate forum to address their concerns efficiently and effectively.

4.5.5 Improved processes for small business to notify collective bargaining and collective boycotts

The ACCC recommends that the collective bargaining and boycott provisions be reformed to allow greater use than at present of collective boycotts by small business:

- **the ACCC should be able to impose conditions to address competition concerns so that notified collective boycott arrangements can proceed;**
- **the timeframe for the ACCC to assess collective boycott notifications should be extended from 14 to 60 days;**
- **in exceptional circumstances where a collective boycott is causing imminent serious detriment to the public, the ACCC should have a limited 'stop power' to require collective boycott conduct to cease;**
- **there should be greater flexibility in the nomination of participants and counterparties;**
- **greater flexibility should be provided to the ACCC regarding the length of the protection provided by the notified arrangements; and**
- **the current \$3 million maximum value threshold for a party to notify a collective boycott arrangement should be reviewed (and, if necessary, raised) to ensure that it is not restricting participation by small businesses.**

What are collective bargaining and collective boycotts?

To deal with imbalances in bargaining power, small businesses (including primary producers) may wish to enter into collective bargaining arrangements in their dealings with larger businesses. Collective bargaining¹⁸⁸ by small businesses, including primary producers, can generate public benefits by improving the efficiency of the bargaining process and negotiated arrangements. These benefits are achieved by reducing the time and costs associated with establishing supply arrangements (transaction costs), overcoming information asymmetries and strengthening bargaining power.

Collective bargaining proposals may also involve collective boycott conduct.¹⁸⁹ In certain circumstances, an ability to threaten and/or engage in a collective boycott can be an efficient negotiating tool, and may be necessary to enable the efficiency benefits of collective bargaining to be realised. The ACCC considers that where such arrangements are in the public interest they should be granted exemption under the CCA. There are, however, also circumstances where a collective boycott will be detrimental to efficiency.

Case study – collective bargaining and collective boycott by chicken growers

In 2005, the ACCC authorised chicken growers in Victoria to form collective bargaining groups and negotiate with the chicken meat processor to whom they supplied growing services. In this decision, the ACCC also authorised the bargaining groups to engage in collective boycotts where they had met certain requirements. The collective boycott aspect of the ACCC's authorisation was reviewed by the Tribunal following an appeal by the chicken meat processors.

In its decision, the Tribunal reversed the ACCC's decision to grant authorisation to the collective boycott arrangements. While it recognised the significant bargaining advantage that the large chicken meat processors have over the farmers who provide chicken growing services, the Tribunal concluded that the outcome of a collective boycott, given its potential to inflict harm, was just too uncertain.

The Tribunal decision made it clear that parties seeking immunity for collective boycott bear a heavy onus.

Small businesses can apply to the ACCC for an exemption to engage in collective bargaining and collective boycotts through the authorisation or notification provisions of the CCA (discussed in section 4.3.3 of this submission). Since 2007, when the collective bargaining notification process was first introduced, the ACCC has considered 34 collective bargaining proposals pursuant to the notification regime compared with 78 collective bargaining proposals under the authorisation provisions.

Reforming notification of collective boycott

The ACCC has received very few notifications of proposed collective boycott activity by bargaining groups.

The ACCC is concerned that deficiencies in the current collective boycott notification provisions may be deterring bargaining groups from seeking an exemption for efficiency-enhancing conduct.

The ACCC considers that the collective boycott notification process should be amended to better facilitate its use by small businesses. In particular, the ACCC recommends the following amendments to the existing provisions:

¹⁸⁸ In the context of the CCA, collective bargaining occurs when two or more competitors agree to negotiate terms and conditions (which may include price) collectively with a supplier or buyer (referred to as the target or counterparty).

¹⁸⁹ Under the CCA, a collective boycott involves two or more competitors agreeing not to acquire goods or services from, or not to supply goods or services to, a business with whom the group is negotiating, unless the business accepts the terms and conditions offered by the group.

- **ACCC should be able to impose conditions:** Under the current provisions, the ACCC can only allow, or object to, a notification. If concerns are identified that could otherwise be addressed by amendments to the proposed conduct, the ACCC is not able to allow the notification to stand subject to conditions, and so currently must object to the notification in these circumstances.

This is particularly relevant in assessing collective boycott notifications where the risk of harm arising as a result of inadequately constrained boycott activity is likely to give rise to significant anti-competitive detriment. The potential for such public detriment could, however, be addressed by enabling the ACCC to impose appropriate conditions (as it can do in relation to authorisation applications) on the use of the boycott power by the bargaining group.

- **Increased ACCC assessment period:** A longer time period before a collective boycott notification would come into force (60 days) would allow the ACCC adequate time to consult with the counterparty and assess the proposed conduct.
- **The ACCC should have a limited ‘stop power’:** A ‘stop power’ would enable the ACCC to intervene in exceptional circumstances and require collective boycott conduct to cease by removing the protection provided by the notification (e.g. a short period of time after the ACCC has made such a decision). The stop power should only be available where there are reasonable grounds to be satisfied that the boycott has led, to or is likely to lead to, imminent serious detriment to the public. The ACCC’s decision to use the stop power should be reviewable by the Tribunal.

Improving the flexibility of the process for notifying collective bargaining and collective boycott arrangements

The notification process was introduced to increase participation by small business in efficiency-enhancing collective bargaining by providing a more straight forward process for obtaining statutory protection than that required for authorisation. However, small businesses do not use the notification process to seek protection from legal action under the CCA for collective bargaining arrangements as frequently as they use the authorisation process. The ACCC considers that this is because of the lack of flexibility of the notification process which decreases its attractiveness as an alternative method of seeking protection to engage in collective bargaining conduct. The ACCC recommends the following amendments to the existing provisions:

- **Greater flexibility for nomination of participants:** Under the current provisions all members of the bargaining group are required to be identified and give their consent to the notification. This makes the notification process less suited to loosely described groups (such as members of an association) or for groups whose membership may change regularly. The notification provisions should be amended to allow for greater flexibility in the nomination of participating parties.
- **Greater flexibility in the nomination of counterparties:** Under the current provisions bargaining groups are required to lodge a separate notification for each counterparty. The ACCC has considered collective bargaining proposals from 34 bargaining groups under the notification regime (between them these groups have lodged 282 collective bargaining notifications). The requirement that a separate notification is lodged for each counterparty significantly increases the volume of paperwork that must be dealt with by a bargaining group. The notification application form should be amended to allow for the nomination of multiple counterparties.

More generally, the application form should be reviewed to ensure that the information needs of the ACCC and third parties affected by the proposed conduct are balanced appropriately against the compliance burden which may be experienced by small businesses lodging a notification.

- **Greater flexibility in the timeframes for expiration of notifications:** The CCA currently provides that notifications automatically expire three years after their lodgement date. The ACCC notes that most authorised collective bargaining arrangements are ultimately granted for longer timeframes. The ACCC should be given the power to set a timeframe for the expiration of collective bargaining/collective boycott notifications to suit the circumstances, with the three year period remaining as a default.

In addition, the maximum threshold value for a party to notify a collective bargaining arrangement should be set at an appropriate level to ensure that it is not unduly restricting the accessibility of the notification regime. The threshold, which is generally equal to or less than \$3 million per annum, should be subject to regular review to ensure that it is not restricting participation by small business.

4.5.6 Industry code provisions require reform to improve their enforceability

The Australian Government is currently consulting on important amendments to the Franchising Code of Conduct. The ACCC considers that these important amendments should apply to all codes prescribed under the CCA.

The ACCC recommends that prescribed codes provide for civil pecuniary penalties, infringement notices and enhanced audit powers.

In addition, where a prescribed code provides for the ACCC to perform functions or exercise powers then the CCA should make clear that the ACCC may perform those functions or exercise those powers in accordance with the provisions of the industry code.

The Horticulture Code should be amended to address ongoing concerns about its effectiveness, including its lack of coverage of the sector.

Industry codes and the CCA

Industry codes set out specific standards of conduct for an industry, including how to deal with its members and customers. They are intended to address market failures on a confined sectorial or industry basis. For example, the Franchising Code of Conduct seeks to address information asymmetry by requiring franchisors to provide a disclosure document to prospective franchisees; the Horticulture Code seeks to improve the clarity and transparency of transactions between growers and wholesalers of fresh fruit and vegetables.

There are many different types of industry codes. In practice, Australian businesses are confronted by a wide diversity of codes, and they can be voluntary or mandatory, state or federal.

Voluntary codes are generally developed by industry in response to specific concerns. Voluntary industry codes have two forms: (i) an industry self-regulation model, or (ii) where a voluntary code has been prescribed under regulations, it will be enforced by the ACCC applying the same CCA enforcement provisions as apply to mandatory codes.

Codes providing for industry self-regulation can in some circumstances raise concerns under the competition provisions of the CCA, and such codes can be authorised by the ACCC where the public benefit exceeds the anti-competitive detriment. Voluntary codes can be an effective tool for industry self-regulation where they provide an effective and enforceable governance regime.

There are four mandatory codes under the CCA – the Franchising Code of Conduct, the Horticulture Code of Conduct, the Oilcode and the Unit Pricing Code. The Australian Government is currently consulting on a bulk wheat code, which if prescribed, will regulate

the conduct of port terminal service providers to ensure that exporters of bulk wheat have fair and transparent access to port terminal services.¹⁹⁰

The Franchising Code of Conduct was reviewed in 2013 and the Australian Government is currently undertaking public consultation¹⁹¹ on proposed changes to the code which will implement a number of important recommendations.

Sanctions for breaches of prescribed codes should be amended to provide for civil pecuniary penalties

The ACCC considers that it is important to have effective deterrents in place to incentivise compliance with the CCA. As has been discussed elsewhere in this submission, effective deterrence requires:

- a range of regulatory responses to suit the diverse nature of the conduct and contraveners;
- the consequences of a breach of the law outweigh any potential benefits; and
- credible threat of swift detection and enforcement action.

The range of remedies must be sufficiently flexible to enable the ACCC, or courts, to shape a proportionate response to each unique set of circumstances.

In the ACCC's view, civil pecuniary penalties for contraventions of a prescribed code are of key importance when considering appropriate regulatory tools to efficiently and effectively promote compliance with the CCA.

the absence of civil pecuniary penalties for breaches of prescribed codes represents a significant gap in ensuring that such conduct is met with an appropriate regulatory response.

Infringement powers should be introduced to broaden the range of regulatory response available for contraventions of section 51AD

An infringement notice¹⁹² is a notice under which a financial penalty is paid by a trader for conduct which is alleged to contravene certain provisions of the Australian Consumer Law. The ACCC may issue an infringement notice in circumstances where it has reasonable grounds to believe that a contravention of certain provisions of the Australian Consumer Law has.

Once an infringement notice is paid, the ACCC cannot take the recipient of the notice to court in relation to the contravention specified in the notice. The ACCC will only consider issuing an infringement notice where it is likely to seek a court-based resolution should the recipient of the notice choose not to pay.

The CCA does not currently provide for the issuing of infringement notices in relation to possible contraventions of section 51AD. The ACCC recommends that infringement notices be available for code breaches, allowing the ACCC to quickly and efficiently address code contraventions.

The ACCC notes that the Australian Government's proposed franchising reforms create a platform for the introduction of penalties and infringements notices for all prescribed codes. At this stage, the government has only expressed an intention to introduce these sanctions in relation to certain provisions of the Franchising Code.

¹⁹⁰ Department of Agriculture, *Mandatory Port Access Code of Conduct for Grain Export Terminals* (June 2014) (available at: <http://www.daff.gov.au/agriculture-food/crops/wheat/port-access>).

¹⁹¹ The Treasury, *Exposure Draft of Amendments to the Franchising Code of Conduct and Relevant Provisions in the Competition and Consumer Act 2010* (2 April 2014) (available at: <http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2014/Franchising-Code>).

¹⁹² CCA Division 5 – Infringement notices, sections 134-134G.

Audit powers should be strengthened to improve their effectiveness

The ACCC has a range of powers relevant to its role in industry codes, including the power to audit traders for compliance with mandatory codes. Relevantly, the ACCC can require a corporation to provide any information or documents it is required to keep, generate or publish under a prescribed code.

Case study – audits of code compliance

The ACCC has audited more than 70 traders under both the Franchising and Horticulture Codes. This examination of documents found that the majority of audited traders complied with their respective industry code, while a small number required further investigation for matters of non-compliance.

The ACCC has found that compliance audits can be a useful tool for identifying areas of concern – this was particularly the case for the franchising sector where audits revealed some concerns with disclosure documents and marketing fund financial statements.

In its submission to the 2013 Franchising Code Review, the ACCC noted the very limited nature of the audit power and argued that its scope should be extended to allow the ACCC to more accurately assess compliance with all aspects of the Franchising Code of Conduct. The ACCC's recommendations have been accepted by the Australian Government¹⁹³ as they more narrowly apply to the Franchising Code of Conduct.

The ACCC considers that the audit provisions for prescribed industry codes should be addressed to improve their effectiveness and functionality. The audit power is an important investigative tool for ensuring that a business subject to a prescribed code complies with all aspects of that code.

In addition, the CCA does not impose any sanction for non-compliance with an audit notice. The ACCC notes that this lack of sanction is inconsistent with other CCA information provisions. Furthermore, it fails to offer any effective deterrent for non-compliance with an audit notice. The ACCC considers that this deficiency should be addressed.

Section 51AE should be amended to clarify the scope of the ACCC's powers and functions under a prescribed industry code

In some circumstances a prescribed code may enable the ACCC to exercise a discretionary power. In the ACCC's experience, the exercise of a discretionary power can give rise to confusion about the scope of the ACCC's functions and powers. Such concerns have been specifically addressed under the CCA in the context of access undertakings.¹⁹⁴

The ACCC considers that section 51AE should be clarified through the adoption of an amendment providing that where a prescribed code provides for the ACCC to perform functions or exercise powers, then it may perform those functions or exercise those powers in accordance with the provisions of the industry code.

The ACCC considers that this amendment is largely mechanical in nature.

Improving the effectiveness of the Horticulture Code

The Horticulture Code is an important mechanism to improve the clarity and transparency of transactions between growers and wholesalers of fresh fruit and vegetables. The Horticulture Code also provides a process for dispute resolution.

¹⁹³ The Treasury, *Exposure Draft of Amendments to the Franchising Code of Conduct and Relevant Provisions in the Competition and Consumer Act 2010* (2 April 2014) (available at: <http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2014/Franchising-Code>).

¹⁹⁴ CCA s. 44ZZA and s. 152CBA.

In its 2008 Grocery Inquiry,¹⁹⁵ the ACCC made a number of recommendations aimed at improving the effectiveness of the Horticulture Code. The ACCC considers that a number of the key recommendations made in the 2008 Grocery Inquiry still require attention. These are set out below.

Introduce civil penalties and infringement notices for breaching a prescribed code

As discussed above, the ACCC considers that for a code of conduct to be effective, the consequences of breaching that code must be sufficiently serious to deter non-compliance. The lack of penalties and infringement notices in the Horticulture Code means there is little to deter rogue traders from continuing to engage in conduct that breaches the code.

Increased coverage – provisions should be introduced to ensure that pre-existing agreements are included within the scope of the Horticulture Code

In its submission to the Inquiry into the Competition and Consumer Amendment (Horticulture Code of Conduct) Bill, the Mareeba District Fruit and Vegetable Growers Association estimated that more than 90 per cent of growers and wholesalers are not covered by the Horticulture Code.

The limited coverage of the Horticulture Code risks creating distortions within the industry and has limited its effectiveness in addressing market failures. In addition, the exemption of pre-existing contracts (contracts entered prior to 15 December 2006) from the Code continues to raise compliance and enforcement challenges for the ACCC because it is difficult to identify industry participants that fall within the scope of the Code.

Increased coverage – the Horticulture Code should be extended to apply to sales between a grower and a retailer or processor

The major retail supermarkets source a significant percentage of their fresh fruit and vegetables directly from growers. These growers have limited protection under the existing voluntary *Retail Grocery Industry Code of Conduct*, to which a number of major retailers are signatories. In particular, retailers are not required to enter into written agreements with growers under this code.

The ACCC is also aware of issues between producers and processors (e.g. in the wine grape industry) that may be addressed if the Horticulture Code is extended to cover processors.

4.5.7 Enhanced educative and research role for the ACCC

The ACCC recommends that the scope of section 28 of the CCA should be broadened to explicitly recognise the ACCC's role in providing information to, and conducting research in relation to, the business sector.

Section 28 broadly provides for the ACCC to disseminate information about the rights and obligations arising under the CCA for both business and consumer audiences. It also provides for the ACCC to undertake research and to report on consumer protection laws. The ACCC considers that section 28 should be amended to more accurately reflect the expectations of Parliament and the community in regard to the educative and research functions of the ACCC arising under the CCA. It is the ACCC's view that it is required to have both a business and consumer focus in its educative and research work and that this obligation should be accurately reflected in the CCA.

¹⁹⁵ ACCC, *Report of the ACCC Inquiry into the Competitiveness of Retail Prices for Standard Groceries* (July 2008) (available at: <http://www.accc.gov.au/about-us/public-consultations/grocery-inquiry-2008>).

4.6 Further information to assist the Review Panel

Further information to assist the Review Panel

- In response to specific queries raised by the Issues Paper, the ACCC considers that:
 - (i) resale price maintenance should continue to be prohibited outright; and
 - (ii) the potentially negative effects on competition and consumers should be considered in relation to any proposed legislative response to international price discrimination.
- The ACCC has provided information regarding merger processes in Australia, the ACCC's approach to merger review and an overview of merger processes in the EU and the US to further inform the Review Panel's consideration of these issues.
- The ACCC has provided further explanatory information regarding the role of market definition in competition matters and other related factors that arise in relation to merger analysis.

4.6.1 Resale Price Maintenance

Resale price maintenance (RPM) conduct is a vertical restraint whereby a supplier:

- induces or attempts to induce a person not to sell the supplier's products at a price less than a price specified by the supplier;
- makes known to a person that they will be refused supply unless the person agrees not to sell the supplier's products at a price less than the price specified by the supplier;
- withholds supply from a person because the person has sold or is likely to sell the supplier's products at a price less than a price specified by the supplier;
- uses a statement of price that is likely to be understood by a person to whom the products are or may be supplied as the price below which the products are not to be sold; or
- enters into an agreement for the supply of goods or services containing a provision that the purchaser will not sell below the supplier's specified price.

Under the CCA, RPM is prohibited *per se*. The CCA does not prevent a supplier from making price recommendations to a reseller (RRP) provided that the supplier does not seek to force the reseller to adhere to that price.

Recent International developments

Prior to 2007, RPM was a *per se* contravention in the United States, however following the Leegin decision,¹⁹⁶ RPM was brought into line with the treatment of other vertical restraints (exclusive territories and exclusive dealing) by courts in the United States. Since 2007, RPM will only be unlawful under United States federal antitrust law if, having weighed all the circumstances, the conclusion is that the restrictive practice should be prohibited as imposing an unreasonable restraint on competition.

In Canada, RPM was decriminalised in 2009 and replaced by a civil provision requiring an applicant to demonstrate that the RPM conduct has had, is having or is likely to have an adverse effect on competition in a market. In contrast RPM remains a 'hard core restriction' in the European Union and is presumed to have negative effects (such as facilitating collusion between suppliers or buyers and reducing intra-brand competition leading to higher prices to consumers).

¹⁹⁶ Leegin Creative Leather Products, Inc. v PSKS, Inc 127 S. Ct. 2705 (2007).

In the European Commission, RPM is regarded as an 'object' restriction. This means that there is no requirement to demonstrate harm caused by a particular RPM agreement in order to find it unlawful. An RPM agreement can be exempted if it is broadly shown to be indispensable to achieving evidenced efficiency gains that benefit consumers and does not eliminate competition.¹⁹⁷

Should RPM remain a per se prohibition in Australia?

The ACCC is concerned that RPM can cause significant harm to the competitive process. It can do this by:

- facilitating collusion between suppliers: RPM conduct may be used by suppliers to reduce or eliminate price competition between its customers, including to help enforce a price-fixing arrangement;
- facilitating collusion between retailers: a bottom up RPM occurs when one or more retailers compel a supplier to adopt RPM conduct to reduce or eliminate price competition at the retail level, including to help enforce a price-fixing arrangement;
- supplier exclusion: an incumbent supplier may use RPM conduct to guarantee margins for retailers to make them unwilling to carry the products of a rival or new entrant;
- retailer exclusion: RPM conduct can be used as a means to eliminate retail competition from discount or more efficient retailers.

Case study – Mitsubishi Electric Australia Pty Ltd¹⁹⁸

In 2013, the Federal Court ordered Mitsubishi Electric Australia Pty Ltd (Mitsubishi Electric) by consent to pay \$2.2 million in penalties for engaging in RPM.

The Court found that on three occasions between 2009 and 2011, Mitsubishi Electric through the conduct of its senior managers:

- induced and attempted to induce one of its dealers, Mannix Electrical Pty Ltd (Mannix) not to sell Mitsubishi Electric branded air conditioning products at prices below a minimum specified price; and
- reduced the discounts Mannix had received from Mitsubishi Electric by terminating its 'dealer' status, for reasons including Mannix's failure to increase its prices of Mitsubishi Electric branded air conditioning products to the minimum specified price.

Justice Mansfield accepted that deterrence was of paramount importance in this case, stating further that 'there is a need for a significant level of penalty in respect of resale price maintenance to deter large corporate groups from engaging in such conduct in the future'.

In relation to the termination of Mannix's 'dealer' status, His Honour said that 'this type of conduct is considered to be at the serious end of the scale of resale price maintenance conduct because it involved [Mitsubishi Electric] taking action, partly driven by complaints from Mannix's competitors, to prevent Mannix from acting as an effective competitor in the market'.

Balanced against this harm, the ACCC recognises that RPM can, in certain circumstances, promote efficiency and be pro-competitive. The CCA therefore provides that efficiency promoting RPM conduct can be authorised by the ACCC where it is satisfied that benefit to the public outweighs the detriment to the public.¹⁹⁹ More generally the ACCC's Compliance and Enforcement Policy identifies a number of factors that the ACCC will have regard to in setting its enforcement priorities. These include:

¹⁹⁷ Revised competition rules for vertical agreements were adopted by the EC in April 2010.

¹⁹⁸ *ACCC v Mitsubishi Electric Australia Pty Ltd* [2013] FCA 1413.

¹⁹⁹ CCA ss. 88(8A) and 90(8).

- conduct of significant public interest or concern;
- conduct resulting in a substantial consumer (including small business) detriment; and
- conduct that is industry-wide or is likely to become widespread if the ACCC does not intervene.

The ACCC will have regard to such factors in determining the appropriate enforcement response to allegations of RPM conduct.

The *per se* nature of RPM was considered by the Hilmer Review, which concluded that although there may be some instances where RPM may be efficiency enhancing, there was not convincing evidence that efficiency enhancing RPM occurred with such frequency that it should be assessed under a competition test. The Hilmer Review recommended that efficiency enhancing RPM be considered under the authorisation provisions.²⁰⁰ The ACCC broadly shares this view.

4.6.2 International price discrimination

What is price discrimination?

Price discrimination refers to a situation where a firm with some pricing power is able to charge consumers different prices for the same product according to differences in their willingness to pay for the product, rather than differences in the cost of supply. For example, students or seniors may be charged a different price to adults for admission to a cinema, or a frequent flyer card holder may pay a lower price for an airline ticket than an infrequent flyer in the same class.

A price discrimination strategy enables a firm to earn higher profits than it would if all consumers were charged the same price (or price differences reflected cost differences). This is because consumers who highly value a product pay more than they would if prices were uniform. However, price discrimination is only possible if a firm has some price setting ability, is able to identify differences in consumers' willingness to pay, and is able to prevent resale (or arbitrage) from customers who pay lower prices to those who pay higher prices.

In recent times, there has been considerable focus and concern in relation to higher prices for the same product charged to Australian consumers compared with prices in different countries.²⁰¹ While such practices are not new, the rise of the digital economy has increased consumers access to global marketplaces and awareness of different (higher) prices that may be charged in their home country.

There are numerous reasons why prices may vary across countries. In some instances, price differences may be explained by differences in the costs of supplying the goods, or exchange rate fluctuations, rather than a price discrimination strategy.

However, in other instances, international price differences may be the result of a supplier engaging in international price discrimination. International price discrimination is a form of 'third degree' or imperfect price discrimination, whereby a supplier is able to charge different prices to consumers in different countries based on differences in their aggregate willingness to pay. A supplier that practices international price discrimination maximises its total profit by maximising its profits from sales in each country separately. Prices will be higher for consumers in countries that have a relatively high willingness to pay.²⁰²

²⁰⁰ Section 88 of the CCA was amended in 1995, implementing this recommendation.

²⁰¹ For example, on 29 July 2013, the Standing Committee on Infrastructure and Communications tabled its report on the inquiry into IT pricing, *At What Cost? IT Pricing and the Australia Tax*. A focus of the inquiry was the reasons for the differentials in prices for IT hardware and software sold in Australia compared with overseas.

²⁰² Profits are maximised overall when the supplier equates marginal revenue (MR) to marginal cost (MC) in each country. If MC is the same across countries, the profit maximising suppliers equates MR across countries. The percentage mark-up of each country's price over marginal cost will then be inversely

International price discrimination is only possible if a supplier is able to prevent arbitrage from low price countries to high price countries. In some instances, restrictions on parallel importation in intellectual property laws have prevented arbitrage and supported international price discrimination to the detriment of Australian consumers who pay higher prices as a result. Parallel importation may circumvent such international price discrimination by allowing consumers to access goods sold (at lower prices) in non-Australian markets. The ACCC therefore considers that there is no reason to justify a blanket legislative restriction on parallel imports (see section 3.3.8).

Technological developments such as 'geo-blocking' also provide a relatively easy mechanism for suppliers to both identify the consumers' geographic location and prevent arbitrage from low price to high price locations. Thus geo-blocking supports international price discrimination.

The efficiency and welfare effects of price discrimination are, however, ambiguous.²⁰³ In some instances price discrimination can be pro-competitive and have substantial efficiency benefits. However, in some instances price discrimination can be anti-competitive and, in even absent anti-competitive effects, can have negative effects on welfare. In relation to international price discrimination, Australian consumers are worse off if they pay higher prices as a result.²⁰⁴

Issues relating to prohibition of price discrimination

The ACCC considers that the potentially negative effects on competition and consumers should be considered in relation to any proposed legislative response to international price discrimination.

An explicit prohibition on price discrimination was repealed from the then Trade Practices Act in 1995 (s. 49). A number of reviews (1976, 1979 and 1993) recommended its repeal, finding that the prohibition: reduced price flexibility; had inflationary effects; and that conduct of concern could be addressed under other sections of the Trade Practices Act (now CCA).

Measures to implement and support discriminatory pricing will be unlawful under the CCA if they involve a misuse of market power (section 46) or have the purpose, effect or likely effect of substantially lessening competition, either through an exclusive dealing arrangements (section 47) or a contract, arrangement or understanding (section 45).

Additional considerations may be raised by international price differences that are not based on differences in underlying costs. Economic and legal views on international price discrimination are developing, both in Australia and internationally, with a range of approaches being considered and adopted.

As price discrimination may be pro-competitive in some cases, it may be difficult to impose a simple legislative solution that would not also have other potentially negative effects on competition and consumers. For example, attempting to legislate a form of international price parity could lead to significant complexity and concern during sizeable and/or rapid exchange rate fluctuations.

Market forces may also to some extent undermine the ability of firms to practice international price discrimination to the detriment of Australian consumers. For example, consumers may switch to lower priced existing substitute products and/or relatively high prices may provide a signal for the entry of new substitute products. However, substitution may take time and

proportional to its elasticity of demand. Countries with high elasticity of demand will pay lower prices than countries with low elasticity of demand.

²⁰³ Price discrimination unambiguously reduces welfare only when it does not raise total output. The effect on welfare is ambiguous in other situations.

²⁰⁴ Overall welfare rises if international price discrimination is defeated and the firm still has an incentive to supply all countries. See M. Motta, M, *Competition Policy, Theory and Practice* (Cambridge University Press, 2004) p. 496.

substitutes may not be valued as highly as the product whose price is high as a result of international price discrimination.

Similarly, consumers may to some extent be able to circumvent measures which support price discrimination, such as geo-blocking. However, these circumvention measures are not available to all consumers and are themselves likely to create inefficiencies, e.g. setting up virtual post boxes in the United States to take delivery of products that are not shipped direct to Australia. In the meantime, international price discrimination that results in Australian consumers paying higher prices than they would if access to lower priced markets was readily available, impose welfare losses on those consumers.

4.6.3 Merger processes in Australia

Unlike in jurisdictions with mandatory merger notification processes, the CCA does not require merger parties to notify the ACCC of their intent to enter into a transaction. Merger parties are encouraged however, to notify the ACCC as early as possible when an acquisition potentially raises competition issues. Merger parties can elect to have their proposal:

- considered under the ACCC informal clearance process (substantial lessening of competition test);
- formally 'cleared' by the ACCC pursuant to the statutory process set out in Subdivision B, Division 3 of Part VII of the CCA (substantial lessening of competition test); or
- formally authorised by the Tribunal pursuant to Subdivision C, Division 3 of Part VII of the CCA (net public benefits test).²⁰⁵

Merger parties may also elect to go ahead with the proposed arrangement without seeking clearance. By doing so, the parties risk an ACCC investigation, including public inquiries, and potential legal action if the transaction raises competition concerns.

Merger parties can also apply to the court seeking a declaration that a proposed acquisition does not contravene section 50 of the CCA.

Informal clearance

Merger parties may request that the ACCC assess their proposed merger on an informal basis. The informal clearance process is the most commonly used of the merger clearance options; the ACCC considered almost 300 transactions on this basis in 2012-13.²⁰⁶

²⁰⁵ As merger authorisations are discussed in section 4.2.3, they are not discussed further below.

²⁰⁶ Of these informal reviews, more than 70% were pre-assessed by the ACCC as not raising concerns. While most pre-assessments are completed within two weeks, some will require the ACCC to undertake targeted market inquiries prior to forming a view on the acquisition.

Key aspects of the informal merger clearance process

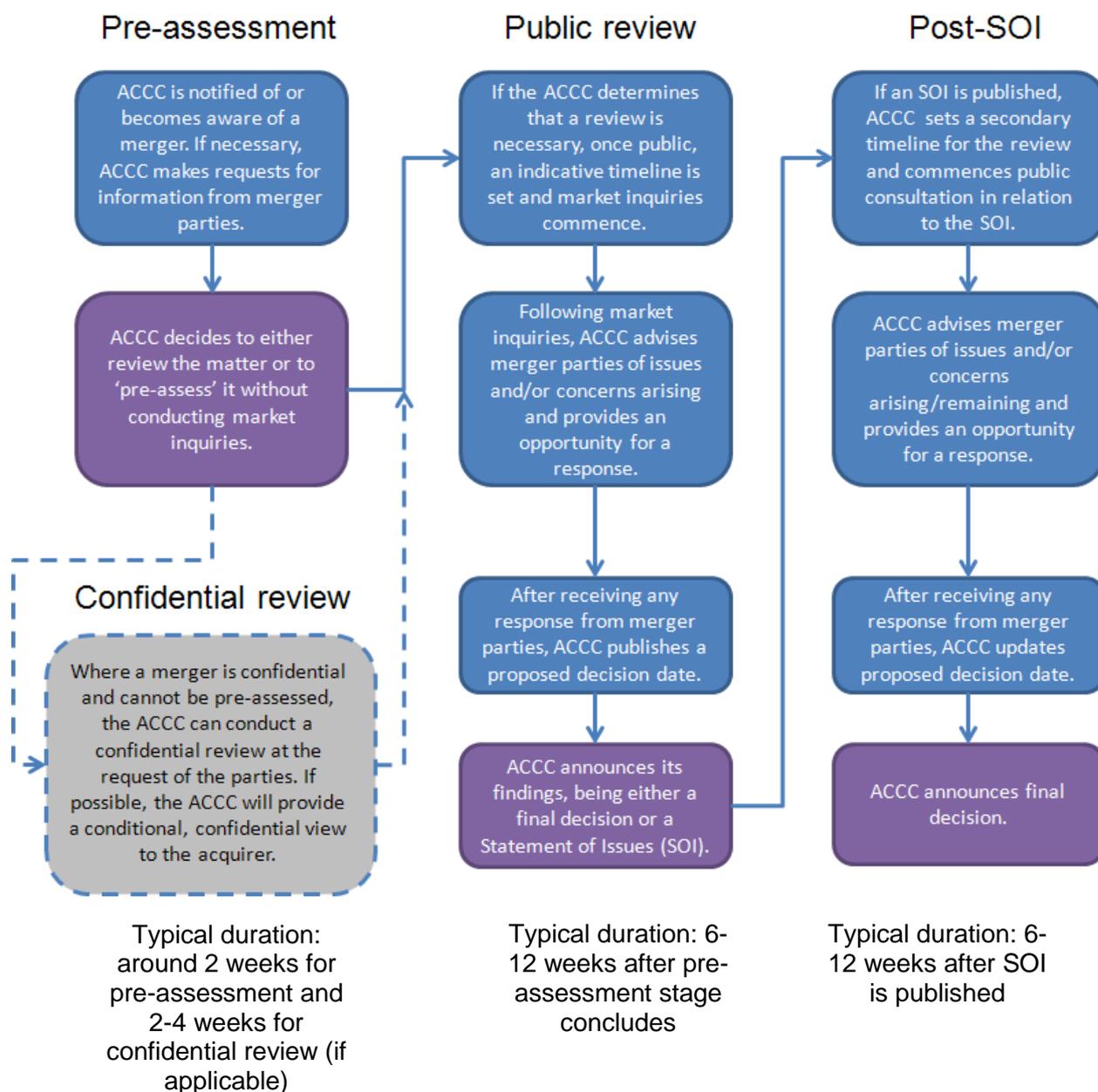
- Clearance by the ACCC does not provide statutory protection from legal action under section 50. It provides the ACCC's view on whether an acquisition is likely to breach section 50.
- It is not suspensory, that is, merger parties are not prevented from completing an acquisition while the ACCC completes its review. Where an acquisition raises competition concerns, the ACCC may ask merger parties to provide undertakings not to complete the acquisition pending completion of the ACCC review.
- Notification is not compulsory.
- There are no prescribed up-front information requirements imposed on merger parties. In practice, merger parties are expected to provide a base level of information initially and requests for additional information will then depend on the complexity of the matter and the potential competition concerns raised.
- There is no statutory timeframe for reviews.
- There is no filing fee.

The informal clearance process is highly flexible including in relation to confidentiality, information required to support the application, processes of public engagement and timeliness. It is scalable and can be adjusted to suit the issues raised by the particular clearance request. The informal clearance process has developed over time to provide an avenue for merger parties to seek the ACCC's view prior to completion of a merger – and it has been reviewed during this time to ensure that it continues to provide an efficient and effective mechanism for businesses.

There are three categories of assessment that a transaction may undergo under informal clearance. These categories are neither mutually exclusive nor sequential.

- Pre-assessment: a view is formed, based on the available information, that the risk of a substantial lessening of competition in a market is low without the need for a confidential or public review.
- Conditional confidential: a preliminary conditional view is provided to merger parties on a confidential merger proposal upon request by the merger parties.
- Public: a final decision is made following a public review and in some cases will be preceded by the publication of a Statement of Issues (a document published by the ACCC in merger reviews where the ACCC has come to a preliminary view that a proposed merger raises competition concerns that require further investigation).

The categories of assessment and the likely duration of these are illustrated below.



Notes: Undertakings may be offered at any time during or prior to the commencement of a review. This will generally impact on the sequence and duration of stages.

The ACCC aims to review mergers efficiently, transparently and effectively, having particular regard to the commercial imperatives of the parties involved. The ACCC's experience is that there can be significant variation in the duration of informal clearance reviews and this depends on a number of factors, including:

- the complexity of the matter and the issues involved;
- the sufficiency of information available to the ACCC;
- the responsiveness of merger parties and other information providers in supplying information to the ACCC;

- whether the merger parties request that the ACCC suspend its review to allow the merger parties additional time to provide further submissions;
- whether a Statement of Issues is published;
- whether and at what stage undertakings are proposed by the merger parties; and
- whether overseas competition regulators are also reviewing the merger.

The ACCC aims to provide balanced transparency in undertaking informal clearance reviews – to this end the ACCC maintains an internet based public register for all public reviews. This register provides merger parties and other interested stakeholders with a range of information about a matter, including indicative timeframes for the ACCC to complete its review. Indicative timelines are published by the ACCC to allow the merger parties and the public to monitor the progress of the review and the likely timing of the ACCC's decision. However, these timelines are subject to review and amendment where circumstances require, such as when a Statement of Issues is published or if an undertaking under section 87B of the CCA is offered to the ACCC. The timeline will record any changes and the reasons for the change.

The ACCC takes a scaled approach to information requirements which does not require merger parties to provide a complete information package at the outset and instead advises merger parties of the information that will be required throughout the review depending on the issues raised. The trade off in this approach is that merger parties are required to respond to these information requests promptly. Failure to provide the ACCC with a base level of information at the outset may delay the ACCC's review and final decision. A list of the initial level of information that the ACCC will generally require in order to undertake an informal review is available at Annexure A of the ACCC's Informal Merger Review Process Guidelines.²⁰⁷

The ACCC also seeks to provide, in a timely manner, merger parties with details of any relevant issues or concerns arising during market inquiries. The ACCC provides feedback to support a 'no-surprises' approach, to afford merger parties an opportunity to respond to the issues raised and to allow them to provide any additional information prior to the release of a Statement of Issues and before the ACCC makes a final decision. This process of providing feedback to merger parties has been in place for some time but more recently the practice of providing written market feedback has been formalised into the review process in response to feedback from the Trade Practices Committee of the Law Council.

The flexibility of the informal clearance regime is demonstrated in many of the transactions that are pre-assessed by the ACCC, often within a very short period with minimal information required from the merger parties.

Case study – confidential pre-assessment

For example, in a recent confidential transaction the parties approached the ACCC seeking a confidential view within one week due to pressing commercial timing issues. The ACCC was familiar with the industry and on this basis the transaction was considered and a decision made by the ACCC on a confidential basis within seven days to accommodate the commercial timing.

²⁰⁷ See ACCC, *Informal Merger Process Guidelines* (2013) (available at: <http://www.accc.gov.au/publications/informal-merger-review-process-guidelines-2013>).

Case study – Thermo Fisher Scientific Inc proposed acquisition of Life Technologies Corporation

This review involved Thermo Fisher and Life Technologies which are both global companies that operate in the life sciences sector. Given the global nature of the transaction, the review involved considerable engagement with regulators in other jurisdictions on the substantive competition issues and then subsequently cooperation on the remedy proposed by the merger parties to ensure that the remedy would be effective across jurisdictions.

The ACCC decided to clear the transaction subject to a section 87B undertaking requiring Thermo Fisher to divest its Australian cell culture business and comply with its commitments to the European Commission to sell its global HyClone cell culture and Dharmacon gene silencing businesses. The ACCC's approach in this matter avoided a duplication of remedies.

The ACCC's review, which involved complex markets and close cooperation with a significant number of competition authorities worldwide, was completed in 39 total review days (i.e. business days less time taken for the merger parties to respond to information requests).

Australia is unique in offering an informal clearance process. In many jurisdictions outside Australia it is mandatory for merger parties to notify regulators of proposed arrangements subject to certain filing thresholds being met and merger parties seeking clearance must make a formal application. Typically in these jurisdictions, transactions must be cleared prior to completion (that is, a suspensory clearance regime operates).

Formal clearance

Merger parties may also apply to the ACCC for formal clearance of a merger under section 95AD of the CCA. A formal clearance provides merger parties with statutory protection from legal action under section 50 of the CCA.

It is suspensory while the ACCC or the Tribunal complete their review. However, even if clearance is not granted, the merger parties are not prevented from completing the acquisition.

Key aspects of the formal merger clearance process

- Notification is not compulsory.
- Review timeframes are proscribed in legislation.
- Form O requires the merger parties to provide substantial information up-front at the time of the application.
- The ACCC is required to maintain a public register of submissions and other documents in relation to the application unless excluded for confidentiality or other reasons.
- The applicant can appeal the ACCC's decision to the Tribunal.
- Filing fee: \$25,000.

Formal clearance is a public process and clearance may only be granted if the ACCC is satisfied that a merger would not have the effect, or be likely to have the effect, of substantially lessening competition in a market. If the ACCC denies clearance, the merger parties (but not other interested parties) may apply to the Tribunal for review of the ACCC's decision.

The formal clearance process was introduced in 2007 following recommendations made in the Dawson Report. These amendments brought merger regulation in Australian into line with many overseas jurisdictions. Consistent with the United States and European merger processes the Australian formal clearance process has a number of 'upfront' information

requirements (set out by the application Form O) as well as statutory timeframes for decision making.

Merger clearance by the European Commission²⁰⁸

- Notification mandatory where the proposed arrangements have a 'community dimension' and turnover thresholds are met.
- Suspensory regime (that is, notified transactions cannot complete until clearance is obtained).
- No filing fee

Timeframes

The EC must reach a Phase I decision within 25 business days from the effective date of notification and this can be extended to 35 days in certain circumstances. In the event that the EC initiates a Phase II investigation (that is, where the transaction raises doubts as to its compatibility with the common markets), the EC must reach a decision within 90 business days from the beginning of Phase II. During this time, the EC will also issue a Statement of Objections. This 90 day period may be extended to 105 days in certain circumstances and there is also scope for a further 20 day extension (in total) if the merger parties request a one-off extension or the EC extends Phase II with the consent of the merger parties.

Pre-notification discussions with the EC are a standard part of all merger reviews (including simplified cases) and usually take a minimum of two weeks but can be extended in complex cases.

The review time periods may be suspended (that is, the clock stopped) if the EC has to request information (pursuant to Article 11) or order an inspection.

There is no formal means of accelerating a merger review but it is understood that the EC has shown some flexibility in certain circumstances by issuing accelerated clearance decisions.

Information requirements

Merger parties must complete Form CO at the time of notification which requires them to provide detailed information regarding the transaction, the merger parties (corporate details and structure), definition of the relevant markets and the impact of the merger on the affected markets (including information on competitors and customers and economic evidence in more complex cases). For less complex matters, parties may file a Short Form CO which has less onerous information requirements.

European Commission's Directorate General for Competition (EU DG Comp) may require additional information from the merger parties, which if in the form of an Article 11 request, may impact on the review time frame. If a transaction goes into Phase II, a Statement of Objections is issued and parties have limited access to the EC file (non-confidential versions or summaries) and upon request a formal oral hearing.

²⁰⁸ The European Union merger control regime is enforced by the Directorate General for Competition of the EC. Global Competition Review, *Getting the Deal Through* (2014) p. 131.

Merger clearance in the United States²⁰⁹

- Notification mandatory where jurisdictional, size of the transaction and size of the parties thresholds are met. Note the Federal Trade Commission (FTC) or Department of Justice (DOJ) may review a transaction that raises competition concerns even if the mandatory notification thresholds are not met.
- Suspensory regime (that is, notified transactions cannot complete prior to termination of the waiting period). However, if the relevant agency decides that the acquisition is likely to result in a substantial lessening of competition in a market, a Court order must be sought to prohibit the acquisition.
- Filing fee: \$45,000 – \$280,000 (depending on size of transaction, which is adjusted annually).

Timeframes

Following receipt of the notification, a 30 day (in some cases 15 day) waiting period commences during which the agency (either the Federal Trade Commission or Department of Justice) will consider whether the transaction raises significant competition issues. For those transactions that do, the agency will issue a broad 'request for additional information and documentary material' often referred to as a 'second request'.

Issuing a second request extends the waiting period to the 30th day after the date of substantial compliance with the second request unless otherwise agreed between the parties and the relevant agency.

Information requirements

The Hart-Scott-Rodino (HSR) Notification and Report Form requires the merger parties to provide basic information about their United States revenues, corporate organisation and structure of the transaction as well as a variety of business documents. In complex transactions, merger parties often provide more detailed information up front on a voluntary basis.

A second request is a detailed set of interrogatories, data, and document requests designed to provide the agency responsible for reviewing the transaction with information on issues such as market structure, entry conditions, competition, marketing strategies and the rationale for the transaction. It is understood that compliance with the second request in complex transactions may take some months to complete.

Similar to the ACCC's informal clearance process, third party information provided to the reviewing agency is not made available to the merger parties. However it is understood that agency staff meet with the merger parties during the review to discuss concerns arising in the review, including concerns raised by market participants.

The Australian formal clearance process strikes a balance between the information needs of the public and the ACCC (as interested parties and decision maker respectively) and the commercial timeframes of merger parties. As with the international examples provided above, the rigid statutory timeframes within which the ACCC must reach a decision necessitate applicants providing all relevant information at the outset of the process. Recognising that a formal exemption is being sought from the CCA the formal clearance process is also transparent. As part of this, the ACCC is required to maintain a public register (accessible from its website).

As at June 2014, no applications for formal clearance had been made to the ACCC.

²⁰⁹ Global Competition Review, *Getting the Deal Through* (2014) pp. 440-443.

4.6.4 Market definition and merger analysis

In determining whether Part IV of the CCA has been contravened, the Courts and the ACCC adopt a purposive approach to market definition. At a general level, the purposive approach involves defining markets in a manner to capture the substitution possibilities that constrain the firm in relation to the disputed conduct.

The purposive approach to market definition does not, as a rule, result in broader or narrower market boundaries. Rather, it aims to define the market in a way to best determine the field of inquiry relevant to the conduct of interest. It also does not mean there will not be differences in opinion about what the market boundaries should be. The ACCC uses a number of analytical tools, for example the hypothetical monopolist test, in developing market definition. The ACCC recognises that such analytical tools are not determinative of market boundaries; they are an aid or framework to consider degrees of substitution. Analytical tools do not replace market evidence or common sense.

The ACCC's approach to market definition is consistent with the approach taken by its international counterpart agencies. For example in the United States, market definition is but one of many economic tools that are flexibly employed to assess potential harm to consumers and competition.²¹⁰ In the European Union, market definition is considered to be a central tool and starting point to identify situations where there might be competition concerns. It is an important qualitative first step in a structured effects based investigation as it enables the investigators to scope the competitive landscape and identify the relevant (potential) competitors.²¹¹

The CCA also provides that when assessing the likely effect of a proposed merger, the 'market' must be a market in Australia or in a state, territory or region of Australia. The ACCC's view is that this does not preclude it from analysing a merger proposal in the context of a geographically broader market provided that at least some part of the market is located in Australia. The ACCC considers that this requirement reflects the objective of the CCA to enhance the welfare of Australians through the promotion of competition.

The CCA also recognises that Australia operates in a global economy and provides a framework for such matters to be taken into account. For example when assessing the likely competitive effect of a proposed merger, the potential for competitive constraint to be provided by suppliers located outside Australia is taken into account by considering import competition. Where the ACCC can be satisfied that import competition or the potential for import competition provides an effective constraint on domestic suppliers, it is unlikely that a merger would result in a substantial lessening of competition.

Similarly, where a merger could create market power in terms of the acquisition of a product, the ACCC will have regard to the ability of domestic producers to redirect their supply into export markets. This is because the export price drives a 'floor' under the price that a domestic buyer can impose on those sellers.

The potential for a merger to result in increased exports, increased substitution of domestic products for imported goods or other matters relating to international competitiveness of any Australian industry are factors to be explicitly considered in weighing up the potential public benefits of an authorised merger.²¹²

²¹⁰ For a more detailed discussion on the use of market definition in the United States see OECD, *OECD Policy Roundtables Market Definition* (2012) <http://www.oecd.org/daf/competition/Marketdefinition2012.pdf> commencing at page 321.

²¹¹ *Ibid*, commencing at page 333.

²¹² CCA s. 95AZH.

5 Institutions and implementation

The principles for microeconomic reform and the competition rules discussed in chapters 3 and 4 of this submission are critical elements of a competition policy. However, successful competition reform also depends upon institutional design. This chapter covers:

- the lessons that have been learnt since the 1990s on how to ensure competition reforms are implemented and that competition remains at the forefront of policy making in Australia; and
- institutional arrangements including the role and functions of the ACCC.

5.1 Competition reform in Australia: Learning from what worked before

Key points

The 1995 NCP could provide a model for future competition reform in Australia. This includes:

- the use of independent expert bodies to progress reform within the framework agreed to by governments
- a shared vision and commitment to a clear set of principles across all Australian governments and across political parties
- the Productivity Commission to quantify expected net benefits from the proposed reforms, and impact on government budgets
- where reform to be undertaken by the states/territories is expected to result in an increase in Commonwealth tax revenue, some distribution by the Commonwealth to the States/Territories of that increase in revenue, subject to states/territories implementing the reform
- a statutory body to undertake monitoring and transparent reporting on outcomes, including where commitments are not being delivered
- tying the intergovernmental commitments to legislation
- targeting social assistance and adjustment packages to facilitate adjustment to, instead of preventing, structural change.

From 1995 to 2005, the NCP process maintained momentum despite four Commonwealth elections (and one change of government) and 26 state/territory elections (involving 11 changes of government). The architecture for the 1995 reforms included four key instruments:

- Competition Principles Agreement 1995²¹³
- Conduct Code Agreement 1995²¹⁴
- Agreement to Implement the National Competition Policy and Related Reforms 1995²¹⁵

²¹³ The CP Agreement covers: oversight of GBEs; competitive neutrality; structural reform of public monopolies; legislation review; access to services provided by means of significant infrastructure facilities; application of the principles to local government; and the operation of the NCC.

²¹⁴ Each state/territory agreed to enact legislation to extend the application of Part IV beyond corporations to all persons. The Agreement also covers exceptions from the competition law, and the operation of the ACCC.

- *Competition Policy Reform Act 1995 (Cth)*.²¹⁶

The experience from 1995 suggests that there are a number of components which contributed to the success of microeconomic reform in Australia:

1. The use of independent expert bodies to progress reform within the framework agreed to by governments.

Case study

Electricity is an example of where governments created an expert body to explore the potential for, and then to develop the detail of, the agreed reform.²¹⁷

- The national electricity market arose out of the 1991 Industry Commission report *Energy Generation and Distribution* which recommended a major restructure of the electricity industry.
- In 1991, Australian Heads of Government established the National Grid Management Council to perform studies into the potential for a national electricity market and models for that market.
- In 1996, participating jurisdictions agreed to adopt the National Electricity Law to give effect to the National Electricity Code. Changes to the NEC were to be managed by the National Electricity Code Administrator Limited (NECA). The COAG Ministerial Council on Energy (MCE) and NEM Forum of Ministers were later established in 2001 to improve ministerial oversight and leadership.
- In 2005, the National Electricity Code was replaced by the National Electricity Rules, with the MCE to provide national governance, and the AEMC to manage changes to the NER. The MCE was subsequently replaced by the Standing Council on Energy and Resources in 2011 and the COAG Energy Council in 2014.

The approach used for electricity sector reform provides a model to progress potential reforms identified in the current Competition Policy Review. These reforms may be sector specific (such as road transport) or broader (such as review of legislation that impedes competition).

2. A shared vision and commitment to a clear set of principles across all Australian governments (Commonwealth, state/territory and local) and across political parties. NCP succeeded because, as the OECD reported, it resulted in a “deep-seated ‘competition culture’”.²¹⁸
3. The Productivity Commission to quantify expected net benefits from the proposed reforms, and impact on government budgets.

²¹⁵ Provided for payments by the Commonwealth to the states/territories for implementation of the agreed reforms.

²¹⁶ Amended the *Trade Practices Act 1974* to: create the ACCC and NCC; ensure that Part IV applies to state/territory (in addition to Commonwealth) government bodies that carry on a business; tighten the process by which states/territories can exempt conduct from Part IV; and allow access to services provided by infrastructure facilities in order to compete in another market (Part IIIA).

²¹⁷ An overview of the energy market reforms is set out in AER, *State of the Energy Market (2007) Part 1 Essay A*.

²¹⁸ OECD, *Economic Survey of Australia 2004: Economic Performance and Key Challenges* (February 2005).

Case study

The April 1995 NCP intergovernmental agreements followed a March 1995 Industry Commission report which estimated the Hilmer Review recommendations would increase Australia's level of real GDP by 5.5 per cent.²¹⁹ COAG had also requested that the report determine the increase in Commonwealth revenue that might be expected from the reforms and the appropriate percentage share which would accrue to states/territories and local government.²²⁰

4. Where reform to be undertaken by the states/territories is expected to result in an increase in Commonwealth tax revenue (the fiscal dividend), some distribution by the Commonwealth to the states/territories of that increase in revenue, subject to states/territories implementing the reform.
5. A statutory body to undertake monitoring and transparent reporting on outcomes including where commitments are not being delivered (as the NCC did in respect of the 1995 intergovernmental agreements). Such a body also needs to be an advocate of the reform agenda.²²¹ The process by which members are appointed to the statutory body (which could be a new or existing statutory authority) should involve the states/territories, as well as the Commonwealth.
6. Tying the intergovernmental commitments to legislation. Incorporating agreed principles into legislative regimes can increase the impact of those principles. Making the operation of legislative provisions contingent upon the performance of commitments in intergovernmental agreements can provide momentum for reform.

Case study

The 1995 amendments to the Trade Practices Act provided that:

- For a state to be involved in the appointment of members to the NCC and ACCC, the state must be a party to the CP Agreement (NCC) and Conduct Code Agreement (ACCC).
- For conduct to be exempt under state legislation from Part IV of the CCA (under section 51(1), the state must be a party to the Conduct Code Agreement and CP Agreement.
- The NCC and Commonwealth Minister, in assessing whether a state access regime is an effective access regime under Part IIIA of the CCA, must apply the CP Agreement principles.
- A state access regime ceases to be an effective access regime if the state ceases to be a party to the CP Agreement.
- The decision on whether to declare a service provided by a state body is made by the state minister (instead of the Commonwealth minister) only if the state is a party to the CP Agreement.
- Goods or services provided by a state body cannot be subject to prices surveillance under Part VIIA of the CCA unless certain conditions are met. This may include an assessment by the NCC, against the CP Agreement principles, of whether there is already effective supervision of prices.

²¹⁹ Industry Commission, *The Growth and Revenue Implications of Hilmer and Related Reforms: A Report by the Industry Commission to the Council of Australian Governments* (1995).

²²⁰ Council of Australian Governments' Communiqué, 19 August 1994, Darwin.

²²¹ The OECD, in its review of Australia, noted the need for a body to continue the policy narrative on the benefits of regulatory reform: 'This policy narrative should help to promote greater engagement by the business sector and more ownership of the regulatory policy goals within government. Building a broader constituency within government to support regulatory reform will strengthen the resilience of the regulatory policy agenda'. See OECD, *OECD Reviews of Regulatory Reform: Australia: 2010: Towards a Seamless National Economy* (2010).

7. Targeting social assistance and adjustment packages to facilitate adjustment to, instead of preventing, structural change.²²² As the OECD notes, following the 1995 reforms, concerns were raised over the social consequences of NCP particularly in relation to rural and regional areas. Subsequent inquiries affirmed the beneficial effects of NCP but also recognised the need to ensure that the reform agenda was properly communicated and explained to the wider community. Importantly, as the OECD put it, the policy response should not be to maintain special interest protections.²²³

The framework outlined above for implementing competition reform was described by the OECD, in 2009, as 'exemplary':²²⁴

Australia's reform program is a model for embodying policy choices and methods in institutional structures. Co-ordinating among governments at all levels to create the National Competition Policy in the 1990s, and the National Reform Agenda since 2006, shows constitutional creativity within a federal structure and cements wide political backing for market-based approaches.

This framework has been used to guide competition reform in other countries,²²⁵ and could similarly provide the model for future competition reform in Australia.

5.2 Institutional arrangements

Key points

The structure of the ACCC (combining competition enforcement, consumer protection and economic regulation into a single, economy-wide body with the single objective of making markets work to enhance the welfare of Australians) has been one of the core strengths of Australia's NCP, and is consistent with international trends.

The ACCC considers that a broader market study function is needed for the ACCC to assess whether, in particular sectors, competition problems exist or not, and to support better targeted action by the ACCC or others in response.

Along with the NCC, the two other institutions arising from the 1995 reforms were the ACCC²²⁶ and Australian Competition Tribunal.²²⁷

5.2.1 Australian Competition & Consumer Commission

'Joined-up' competition policy²²⁸

The ACCC was created as a single economy-wide body with a single objective – making markets work to 'enhance the welfare of Australians'.²²⁹ The ACCC's functions of competition, consumer protection and economic regulation reinforce one another:

- Competition law focuses on supply side efficiency. Competition law thus prevents certain types of conduct that interfere with competition such as restrictive agreements including cartels, harmful conduct by a firm with substantial market power and anti-competitive mergers and acquisitions. Through competition law, consumers have the widest possible range of choice of goods and services at the lowest possible prices.

²²² See the principles set out in Productivity Commission, *Impact of Competition Policy Reforms on Rural and Regional Australia* (Inquiry Report No. 8, 8 September 1999) chapter 13.

²²³ OECD, *Country Study: Australia – The Role of Competition Policy in Regulatory Reform* (2009).

²²⁴ OECD, *Country Study: Australia – The Role of Competition Policy in Regulatory Reform* (2009).

²²⁵ E.g. OECD, *Australia's National Competition Policy: Possible Implications for Mexico* (2009).

²²⁶ By amalgamating the Trade Practices Commission and Prices Surveillance Authority.

²²⁷ In place of the Trade Practices Tribunal.

²²⁸ See Jeremy Tustin and Rhonda Smith, 'Joined-up Consumer Protection and Competition Policy: Some Comments' (2005) 12(3) *Competition and Consumer Law Journal* 305.

²²⁹ CCA s. 2.

- Consumer law focuses on demand side efficiency. Consumer law thus addresses information asymmetry between sellers and buyers, false and misleading advertising, and contract terms that are unconscionable or unfair. Through consumer law, consumers are able to exercise the choice that competition provides, and in turn provide clear signals to businesses to drive competitive, efficient responses.²³⁰
- Economic regulation focuses on replicating, as far as possible, the outcomes of a competitive market where competition is not feasible. Economic regulation thus creates a system of incentives to drive economically efficient conduct. Through economic regulation, competition in related markets is promoted and the long term interests of users are protected where the supplier has market power.

A single body, performing the functions of competition, consumer protection and economic regulation:

- Fosters a 'pro-market' culture across the three functions. An example is the winding back of economic regulation where a market becomes effectively competitive and can deliver efficient outcomes to the benefit of consumers.
- Facilitates coordination and depth of analysis across common issues. This ensures market failures are analysed holistically – through consideration of supply side (competition), demand side (consumer) and economic regulation – and provides the skills and expertise to tailor responses accordingly.
- Ensures small business issues do not fall 'between the cracks'. Small firms often rely equally on the consumer protection provisions (such as the prohibitions on misleading and deceptive conduct and unconscionable conduct) and the competition provisions (such as the prohibition on misuse of market power), along with mandatory industry codes in some sectors, to protect them from unfair conduct by larger firms. The complementary combination of consumer, competition and small business expertise enables these issues to be efficiently dealt with in a single agency and ensures small business does not get caught between regulatory regimes.
- Provides one source of consistent information, guidance and education to both consumers and businesses about their rights and obligations.
- Provides administrative savings and skill enhancement through the pooling of information, skills and expertise. In particular, as competition cases arise less frequently but are generally of longer duration than consumer protection cases, this allows the ACCC to align resources and pool investigative skills. For this reason, the ACCC has a single Enforcement Division responsible for both competition and consumer law enforcement. It would be very damaging to the 'fabric' of the ACCC to pull this apart.
- In relation to a multi-sector economic regulator:
 - reduces investor uncertainty and the need for regulatory intervention through learning economies as a decision creates a precedent for other industries;
 - reduces distortions across industries; and
 - reduces the risk of regulatory capture.

In particular, a Productivity Commission paper on how to finance public infrastructure in Australia notes that regulatory policy is an important factor for private sector

²³⁰ The effect of demand conditions on competition and productivity is discussed in Michael Porter, *The Competitive Advantage of Nations* (1990).

investment. Varying institutional arrangements and regulatory regimes can distort investment decisions across sectors.²³¹

- Through consumer protection work and outreach, develops the expertise in consumer issues that is necessary to support economic regulation. As discussed in section 3.2 of this submission, successful microeconomic reform may require measures to promote consumer engagement in new markets, and to ensure all interests are represented in economic regulatory processes. The ACCC's broader consumer protection experience has been essential in supporting the ACCC/AER's functions in sectors such as energy, communications and water trading.
- Promotes greater accountability as the performance of one regulator is easier to monitor.

The following four case studies illustrate, in practice, the synergies achieved from amalgamating functions.

Case studies – broadband, wheat export supply chains, premium claims and drip pricing

Broadband

Most internet traffic within Australia is currently carried on the network of copper wires owned and operated by Telstra. A smaller number of broadband services are provided using other networks such as Telstra's and Optus' cable networks, mobile networks and fibre networks. But, until it is replaced by the NBN, Telstra's copper network remains the main network for carrying internet traffic.

Broadband services are provided on Telstra's copper network using a technology called Asymmetric Digital Subscriber Line (ADSL). ADSL services are supplied by a large number of competing internet service providers including Telstra and its competitors such as Optus, iiNet, TPG and Dodo. Telstra's competitors can supply broadband services to their customers using Telstra's copper network by either buying a wholesale ADSL service from Telstra or renting Telstra's copper wires and installing their own equipment.

The ACCC's competition enforcement function under Part XIB of the CCA has been used to promote competition in the supply of internet products. The first competition notice issued by the ACCC concerned Telstra charging internet access providers (IAPs e.g. Optus) for connecting to the Big Pond Internet backbone but refusing to pay its competitors for connecting to their backbones (internet peering). The investigation drew upon the ACCC's broader competition law enforcement skills.

The knowledge gained by the ACCC through a competition investigation can also be used to identify a systemic issue requiring economic regulation. A 2005 competition investigation into Telstra increasing the wholesale price for line rental without increasing its retail price (margin squeeze) was resolved by a regulatory remedy. The ACCC declared these wholesale services under the access regime in Part XIC of the CCA.

Together, Parts XIB and XIC of the CCA have promoted competition in the supply of internet products which in turn benefits consumers through lower prices and greater choice. However, in a rapidly evolving market, there is significant potential to mislead customers, particularly those who do not have a high level of technological literacy. The ACCC has used the knowledge gained through its regulatory role to take consumer protection action. For example, the ACCC has issued a series of information papers to provide guidance to industry on how the ACCC approaches claims as to broadband internet speeds.

²³¹ C. Chan, D. Forwood, H. Roper and C. Sayers, *Public Infrastructure Financing — An International Perspective* (Productivity Commission Staff Working Paper, March 2009).

In 2012, the ACCC received a court enforceable undertaking from CNT Corp Pty Ltd and issued three infringement notices under the Australian Consumer Law after CNT Corp offered and charged for wholesale 'fibre to the premises' broadband internet services at data transfer rates that its network could not support. The ACCC used the Australian Consumer Law to protect consumers who were paying for a service that they were not receiving, and to promote a level playing field between internet service providers.

It can be seen from the above examples that the ACCC's competition, consumer protection and economic regulation functions have been complementary tools to deliver the overarching objective of making telecommunications markets work for the benefit of Australians.

Western Australian wheat export supply chain

The ACCC has promoted competition in wheat export and transport markets by bringing to bear both economic regulatory and competition enforcement mechanisms in respect of the Western Australian wheat export supply chain.

In 2009 and 2011, the ACCC accepted a Part IIIA access undertaking covering bulk wheat port terminals owned and operated by Co-operative Bulk Holdings (CBH) in Western Australia. CBH, in addition to owning and operating four wheat port terminals in WA, is also vertically integrated into wheat exporting.

These access arrangements promote competition in the export of bulk wheat by ensuring that third party wheat exporters (such as Louis Dreyfus, Cargill and Bunge) are able to negotiate access at a fair price to the port terminal operated by the vertically integrated CBH. This improves productivity by ensuring the efficient use of monopoly infrastructure.

Separately, in 2008, CBH had lodged an exclusive dealing notification with the ACCC concerning an arrangement whereby grain growers wishing to use CBH's up-country storage facilities to store grain prior to it being moved to port for export were required to use transport services provided by CBH to move the grain to port. The bundled storage and transport service was known as 'Grain Express'.

CBH argued that allowing it to centrally control all grain movements would generate efficiencies and the arrangement originally had the support of industry. However, over time concerns arose about the transport services being supplied by CBH in circumstances where growers were given no option but to utilise Grain Express to move their grain to port.

In June 2011, the ACCC revoked the notification because it was concerned that, by preventing growers and marketers from making their own transport arrangements, the conduct had foreclosed competition for the supply of grain transport services. CBH sought a review of the ACCC's decision by the Australian Competition Tribunal. The Tribunal upheld the ACCC's decision.

The Tribunal's decision did not affect CBH's ability to continue to offer Western Australian growers the bundled Grain Express service. It simply meant that growers and marketers storing grain with CBH were no longer forced to use CBH's Grain Express system to move it. Revocation of the notice came into effect on 20 May 2013.

The dual roles allowed the ACCC to build up a broad knowledge base on wheat export supply chains which were applied to both its economic regulation and competition enforcement roles with the overriding objective of increasing choices for grain producers and lowering costs to export wheat.

Premium (credence) claims

Credence claims, particularly in the food industry, potentially have a significant impact on markets. Consumers are increasingly placing weight on premium claims such as where or how something was made, grown or produced. When the claims are genuine, they offer consumers more choice, and provide an opportunity for businesses to compete by innovating their products. False claims, however, harm both consumers and the competitive process. The complaints received by the ACCC primarily come from businesses who have been placed at a competitive disadvantage by false claims.

In June 2013, the ACCC instituted Federal Court proceedings against Coles Supermarkets Australia Pty Ltd (Coles). The ACCC alleged Coles engaged in false, misleading and deceptive conduct in relation to its supply of 'par baked' bread products that were partially baked and frozen offsite (in some cases, overseas), transported to Coles stores and 'finished' in-store.

The bread products were promoted at Coles' supermarkets with in-store bakeries as 'Baked Today, Sold Today' and in some cases 'Freshly Baked In-Store'. In addition, some of these products were offered for sale close to prominent signs that stated 'Freshly Baked' or 'Baked Fresh'.

The ACCC brought proceedings because it was concerned that Coles' claims were likely to mislead consumers and also placed nearby competing bakeries (often smaller, independently-owned and franchised businesses) that bake from scratch each day, at a competitive disadvantage.

On 18 June 2014, the Federal Court found that Coles' claims amounted to a misleading representation that the par baked bread products had been baked on the day of sale, or baked in a fresh process using fresh, not frozen, product. In the Court's view, it was misleading to claim that a par baked frozen product was 'baked today' if it had been substantially baked previously.

Consumer protection laws that prevent misleading information provision are essential to making markets work. Misleading credence claims harm consumers and have a detrimental impact on the businesses of competitors by undermining the level playing field.

Drip (component) pricing

An emerging issue in the online marketplace is drip pricing where consumers see a 'headline' price advertised at the beginning of the booking process but, as they progress to the payment phase, they find that additional fees and charges have been added.

Drip or component pricing can, in some cases, be beneficial for consumers as they can tailor their decision to choose only the services that they need. However, the way in which drip pricing practices can be employed may in some cases mislead consumers as to the total price of goods/services. Even if consumers become aware of the additional fees and charges that are added to the headline price, they will have committed time to the ordering process, and may be reluctant to switch. If consumers are misled about the headline price at the beginning of the booking process, and are less inclined to switch during the process, then this may impact on competition by disadvantaging competitors who include all fees and charges in the headline. This in turn creates an environment where other businesses in the market, who were previously disclosing all fees and charges, may adopt the misleading practices in order to be competitive.²³²

On 19 June 2014, the ACCC instituted proceedings against Jetstar Airways Pty Ltd and Virgin Australia Airlines Pty Ltd for alleged contraventions of the Australian Consumer Law. The ACCC is using the Australian Consumer Law to both protect consumers from misleading conduct and protect the competitive process.

²³² See UK Office of Fair Trading, *Advertising of Prices* (Market study, December 2010).

A closely related institution to the ACCC, the AER, was created in 2005 by merging enforcement and economic regulatory functions previously exercised by NECA, the ACCC and state/territory regulators. The AER, which has an independent board, shares resources, staffing and facilities with the ACCC. In practice, this has meant that the organisation as a whole has been able to draw upon:²³³

- the ACCC's consumer protection function to facilitate consumer engagement in newly created energy retail markets;
- the AER's industry specific knowledge to support the ACCC's consumer protection function and assessment of mergers and agreements that may substantially lessen competition; and
- the AER's energy network functions and the ACCC's functions in telecommunications, transport and the Murray-Darling Basin to facilitate best practice economic regulation across sectors.

The co-located functions of the ACCC/AER encourage much greater consistency leading to increased efficiency and effectiveness of the agency and a much greater likelihood of market outcomes that promote and balance consumer and business interests for the benefit of society as a whole.

The amalgamation of functions is also consistent with international trends. Jordana and Levi-Faur observed that, since the second half of the 1990s, the trend in agency design is towards multi-sector economic regulators particularly in smaller economies and in Europe.²³⁴ The OECD, in 2008, noted the growing recognition of the interface between competition and consumer protection policies, and the implications for institutional design.²³⁵ For example, the Chief Executive of the new UK Competition and Markets Authority (CMA) referred to reinforcing 'supply-side efficiency and innovation' with 'demand-side choice and value', so that the agency can make a 'strong contribution to economic performance, including growth and recovery'.²³⁶ Along with the FTC and Canadian Competition Bureau, other more recent examples of this trend include:²³⁷

- Italy in 2007 through the conferral of consumer functions on the Italian Competition Authority
- Denmark in 2010 through the creation of the Danish Competition and Consumer Authority²³⁸
- Finland in 2013 through the creation of the Finnish Competition and Consumer Authority²³⁹
- Ireland in March 2014 through the publication of a Bill to create the Competition and Consumer Protection Commission.²⁴⁰

²³³ As an example, the energy sections in this submission were drafted by the ACCC in conjunction with the AER.

²³⁴ J. Jordana and D. Levi-Faur, 'Exploring Trends and Variations in Agency Scope' (2010) 11(4) *Competition and Regulation in Network Industries* 342.

²³⁵ Competition Committee, Directorate for Financial and Enterprise Affairs, OECD, *The Interface Between Competition and Consumer Policies* (DAF/COMP/GF(2008)10, 5 June 2008).

²³⁶ Alex Chisholm, *The UK Competition and Markets Authority: A New Institution to Tackle a New Set of Challenges* (ESRC Centre for Competition Policy Annual Conference, 7 June 2013).

²³⁷ Other examples, collated by the FTC, include: Azerbaijan, Barbados, Bulgaria, Burkina Faso, China, Colombia, Ecuador, France, Guyana, Jamaica, Kyrgyz Republic, Liechtenstein, Luxembourg, Malawi, Malta, Mongolia, Panama, Papua New Guinea, Peru, Philippines, Poland, Senegal, Seychelles, Sri Lanka, Tanzania, Uzbekistan, Vietnam and Zambia.

²³⁸ The Danish Competition and Consumer Authority merged the Danish Competition Authority and the Danish Consumer Agency.

²³⁹ The Finnish Competition and Consumer Authority merged the Finnish Competition Authority and the Finnish Consumer Agency.

Other recent institutional reforms include:

- Spain: In 2013, merged competition and economic regulation by creating the National Authority for Competition and Markets;²⁴¹ and
- Netherlands: In 2013, merged competition, consumer protection and economic regulation (as in Australia and New Zealand) by creating the Authority for Consumers and Markets²⁴² to 'increase efficiency and effectiveness of competition oversight and market regulation'.²⁴³

The Australian institutional structure arising from the 1995 reforms has been one of the core strengths of Australia's NCP. In 2009, the OECD concluded that 'it is a model for combining complementary functions of sector regulation, consumer protection, market oversight and competition enforcement'.²⁴⁴

To separate the ACCC into three institutions covering these three functions, and to duplicate expertise across the separate regulators would be a costly step, inconsistent with the international trend and would significantly damage the effectiveness of the ACCC for the reasons given above.

For the financial year 2012/13, the ACCC/AER reported a staffing level of 798 people, well under half that of ASIC (1,844), smaller than the Reserve Bank of Australia (1,115), and only a little larger than the Australian Prudential Regulation Authority (599) and the Australian Communications and Media Authority (598), which are industry specific regulators. Creating separate competition, consumer protection and economic regulators would require a substantial increase in resources to achieve the objective of making markets work to enhance the welfare of Australians. There would also be significant potential for an overlap in functions, and an increase in the overall regulatory burden on business.

The ACCC has consistently ranked well internationally. In a benchmarking exercise conducted for the UK Department of Trade over the period 2001 to 2007 (which covered factors such as: the quality and technical competence of economic analysis; political independence; technical competence of legal analysis; quality of head(s) of authorities; and clarity of procedures) the only agencies ranked ahead of the ACCC were the United States, German and the UK agencies, and the EU DG Comp.²⁴⁵ The Global Competition Review similarly gives Australia a four star ranking, putting Australia behind only EU DG Comp, France, Germany, United States, Japan and the UK.²⁴⁶ The OECD, in its 2009 and 2010 reviews of Australia, concluded that the ACCC is 'generally highly regarded as an independent and effective enforcement agency'.²⁴⁷

The ACCC has a commitment to improve the way in which it performs its functions. Under the red tape reduction program, the ACCC is identifying how to improve the way it administers regulation.²⁴⁸ The ACCC is also a member of the International Competition

²⁴⁰ The Competition and Consumer Protection Commission will merge the Competition Authority and National Consumer Agency.

²⁴¹ The National Authority for Competition and Markets merged the competition authority (the CNC) with several sector regulators responsible for Telecom, Energy, Railway, Postal, Audiovisual and Airport Tariffs. Consumer protection is the function of the Spanish Agency for Consumer Affairs, Food Safety and Nutrition created in 2014.

²⁴² The Authority for Consumers and Markets merged the Netherlands Consumer Authority, Netherlands Competition Authority and the Netherlands Independent Post and Telecommunications Authority.

²⁴³ Dutch Ministry of Economic Affairs, Agriculture and Innovation cited in 'Reforms for Regulatory, Competition and Consumer Agencies' (12 July 2012) Issue 40 *Regulatory Observer* 1.

²⁴⁴ OECD, *Country Study: Australia – The Role of Competition Policy in Regulatory Reform* (2009).

²⁴⁵ PriceWaterhouseCoopers, *Peer Review of the UK Competition Policy Regime* (18 April 2001); KPMG, *Peer Review of the UK Competition Policy Regime* (6 June 2007).

²⁴⁶ The most recent assessment was published on 4 June 2014.

²⁴⁷ OECD, *Country Study: Australia – The Role of Competition Policy in Regulatory Reform* (2009) & OECD, *OECD Reviews of Regulatory Reform: Australia: 2010: Towards a Seamless National Economy* (2010).

²⁴⁸ The ACCC/AER also obtains feedback from consultative committees (Consumer Consultative Committee; Franchising Consultative Committee; Fuel Consultative Committee; Infrastructure Consultative Committee;

Network (ICN), which is currently identifying key elements of a well-functioning competition agency and developing best practices including strategy, planning, implementation, operations, and investigative tools and procedures.²⁴⁹

The current Competition Policy Review provides a welcome opportunity for the ACCC to obtain suggestions for improvement, to ensure that Australia's competition regime remains amongst the best in the world.

Market studies

One issue consistently raised in OECD assessments of Australia's competition policy framework is that the ACCC does not use market studies to supplement its enforcement function.²⁵⁰

The ICN provides the following definition of market studies:²⁵¹

Market studies are research projects conducted to gain an in-depth understanding of how sectors, markets, or market practices are working.

They are conducted primarily in relation to concerns about the function of markets arising from one or more of the following: (i) firm behaviour; (ii) market structure; (iii) information failure; (iv) consumer conduct; (v) public sector intervention in markets (whether by way of policy or regulation, or direct participation in the supply or demand side of markets); and (vi) other factors which may give rise to consumer detriment.

The output of a market study is a report containing findings based on the research. This may find that the market is working satisfactorily or set out the problems found. Where problems are found the market study report can include: (i) recommendations for action by others, such as legislatures, government departments or agencies, regulators, and business or consumer bodies; and/or (ii) commitments by the competition (or competition and consumer) authority itself to take advocacy and/or enforcement action.

In 2003, the OECD found that, along with investigating infringements of competition law, close to all of the respondent competition authorities conducted general sector investigations or economic studies, with on average 10% of resources allocated to this function.²⁵² The ICN, in 2012, reported that 40 ICN member authorities were using market studies, and that the number continues to grow.²⁵³

Small Business Consultative Committee; Wholesale Telecommunications Consultative Forum; and AER Customer Consultative Group).

²⁴⁹ ICN Agency Effectiveness Working Group.

²⁵⁰ Caron Beaton-Wells, *The ACCC: Roots and Branches: Proposals to Enhance ACCC Effectiveness* (Competition Law Conference, Sydney, 24 May 2014); OECD, *Country Study: Australia – The Role of Competition Policy in Regulatory Reform* (2009); OECD, *OECD Reviews of Regulatory Reform: Australia: 2010: Towards a Seamless National Economy* (2010); Enrico Alemani, Caroline Klein, Isabell Koske, Cristiana Vitale and Isabelle Wanner, Economics Department, OECD, *New Indicators of Competition Law and Policy in 2013: For OECD and Non-OECD Countries* (OECD Economics Department Working Papers No. 1104, ECO/WKP(2013)96, 12 December 2013).

²⁵¹ Market studies are sometimes discussed under the heading 'competition advocacy'. Advocacy Working Group, International Competition Network, *Market Studies Good Practice Handbook* (2012).

²⁵² Secretariat, Centre for Co-operation with Non Members, Directorate for Financial, Fiscal and Enterprise Affairs, OECD, *Global Forum on Competition: Optimal design of a Competition Agency* (CCNM/GF/COMP(2003)2, 3 February 2003). See also The World Bank & OECD, *A Framework for the Design and Implementation of Competition Law & Policy* (1998).

²⁵³ Examples include Canada, Denmark, EU DG Comp, Germany, Ireland, Italy, Japan, Republic of Korea, Netherlands, United States, and the UK. Advocacy Working Group, International Competition Network, *Advocacy and Competition Policy Report* (2002); Advocacy Working Group, International Competition Network, *Market Studies Good Practice Handbook* (2012). See also John Clark, 'Competition Advocacy: Challenges for Developing Countries' (2005) 6(4) *OECD Journal of Competition Law and Policy* 69; Maurice E. Stucke, 'Better Competition Advocacy' (2008) 82 *St John's Law Review* 951.

As the UK CMA puts it, market studies and investigations are regarded as sitting alongside competition rules by allowing the competition authority to focus on the functioning of the market as a whole rather than on the conduct of particular firms within it.²⁵⁴ A market study could be used by the ACCC:

- as a lead-in to competition or consumer protection enforcement action when anti-competitive behaviour is suspected in a sector but the exact nature and source of the problem is unknown;
- to identify a systemic market failure (instead of ad hoc compliance action against individual firms) and to better target a response (whether, for example, through enforcement action or compliance education);
- to identify market problems where affected parties are disadvantaged and either have difficulty making a complaint to the ACCC or accessing the legal system to take private action;
- to address public interest or concern about markets not functioning in a competitive way; the market study could either confirm such concerns, and propose some solutions, or reveal them to be unfounded; or
- to fact-find to enhance the ACCC's knowledge of a specific market or sector, particularly where a market is rapidly changing, and raises issues across the ACCC's functions.

Examples of market studies conducted by the UK Office of Fair Trading include:

- payment systems (2003)
- care homes for older people (2005)
- liability insurance market (2005)
- medicines distribution (2007)
- airports (2007)
- personal current accounts (2008)
- aggregates (2012)
- private motor insurance (2012)

The World Bank, OECD and ICN identify key features for effective market studies including: the process by which the competition authority may initiate a market study; investigative tools; and securing good outcomes.²⁵⁵

- Initiating market studies: The ICN notes that one of the major advantages of authorities having the ability to initiate market studies themselves is that it allows them greater freedom to identify potential concerns in markets or sectors and ensure that market studies focus on the most critical issues. Nevertheless, other parties, like government agencies, parliament or consumer groups may have a broader perspective, and may also help authorities draw issues for market study from a wider base.²⁵⁶

²⁵⁴ Competition and Markets Authority, *Towards the CMA: CMA Guidance* (15 July 2013) & *Market Investigations: Supplemental Guidance on the CMA's Approach* (January 2014); Competition Commission, *Guidelines for Market Investigations: Their Role, Procedures, Assessment and Remedies* (April 2013).

²⁵⁵ See also Caron Beaton-Wells, *The ACCC: Roots and Branches: Proposals to Enhance ACCC Effectiveness* (Competition Law Conference, Sydney, 24 May 2014).

²⁵⁶ Advocacy Working Group, International Competition Network, *Market Studies Good Practice Handbook* (2012).

- Investigative tools: In a joint 2013 report, Nordic competition authorities refer to the need, in a sector inquiry or market study, for access to relevant market data which companies are often reluctant to disclose e.g. market shares, strategies, prices, margins and costs.²⁵⁷
- Securing outcomes: The ICN notes the importance of being clear, at the outset of a market study, about the reasons for the particular study, and the possible types of outcome at the end of the study (for example, recommendations to business, recommendations to government, information campaign, launching an enforcement case).²⁵⁸

The ACCC currently has some scope to conduct market studies. Under section 28 of the CCA, the ACCC has functions in relation to dissemination of information, law reform and research although the information gathering powers set out in the CCA do not apply to this section.²⁵⁹ Under Part VIIA of the CCA, the Minister may require the ACCC or another body to hold a price inquiry. The ACCC may also hold such inquiries with the Minister's approval – although this power has been exercised only once in 2007 when the ACCC, as part of its petrol monitoring role, sought approval from the Treasurer for an inquiry under Part VIIA into the petrol industry.

The ACCC considers that a broader market study function is needed to support better targeted action, although the ACCC is not proposing the UK model where the CMA, if it identifies a competition problem in a market investigation, can impose legally enforceable remedies.²⁶⁰

5.2.2 Australian Competition Tribunal

The ACCC supports the OECD assessment that: 'The Australian Competition Tribunal plays an important role as a merits review body, and the economic content in its determinations has made a significant contribution to both the legislative and judicial development of the law'.²⁶¹

In the ACCC's view, however, the capabilities of the Tribunal are best suited to reviewing decisions rather than resource-intensive investigative process required to make decisions in the first instance. Accordingly, chapter 4 of this submission recommends that the CCA be amended to remove the provision for merger authorisation applications to be made directly to the Tribunal.

²⁵⁷ Report from the Nordic Competition Authorities, *A Vision for Competition: Competition Policy Towards 2020* (No.1/2013).

²⁵⁸ Advocacy Working Group, International Competition Network, *Market Studies Good Practice Handbook* (2012).

²⁵⁹ CCA s. 28.

²⁶⁰ A 2013 review by the OECD reports that there is an obligation on government to respond to market study recommendations only in Denmark, the United Kingdom, Ireland, Norway, and Russia: Enrico Alemani, Caroline Klein, Isabell Koske, Cristiana Vitale and Isabelle Wanner, Economics Department, OECD, *New Indicators of Competition Law and Policy in 2013: For OECD and Non-OECD Countries* (OECD Economics Department Working Papers No. 1104, ECO/WKP(2013)96, 12 December 2013); Competition and Markets Authority, *Towards the CMA: CMA Guidance* (15 July 2013) & *Market Investigations: Supplemental Guidance on the CMA's Approach* (January 2014); Competition Commission, *Guidelines for Market Investigations: Their Role, Procedures, Assessment and Remedies* (April 2013).

²⁶¹ OECD, *Country Study: Australia – The Role of Competition Policy in Regulatory Reform* (2009) & OECD, *OECD Reviews of Regulatory Reform: Australia: 2010: Towards a Seamless National Economy* (2010).

5.3 Conclusion

As the Second Reading Speech for the 1995 Competition Policy Reform Bill stated, the payoff from competition policy for ordinary Australians is very real; 'it paves the way for cheaper prices, more growth and more jobs'.²⁶² The Trade Practices Commission, in its 1993 submission, noted that implementation of the Trade Practices Act in 1974 was a major step but that the Hilmer Review had the 'potential to make a significant contribution to enhancing the competitiveness of the Australian economy'.²⁶³

The ACCC likewise expects the same outcomes from the current Competition Policy Review.

²⁶² Second Reading Speech to the Competition Policy Reform Bill 1995: Commonwealth, *Hansard*, Senate, 29 March 1995, 2433.

²⁶³ Trade Practices Commission, *Submission to the National Competition Policy Review* (April 1993).

Glossary

ACCAN	Australian Communications Consumer Action Network
ACCC	Australian Competition and Consumer Commission
ADSL	Asymmetric Digital Subscriber Line
AEM Agreement	Australian Energy Market Agreement 2006
AEMC	Australian Energy Market Commission
AER	Australian Energy Regulator
AGCNCO	Australian Government Competitive Neutrality Complaints Office
ALRC	Australian Law Reform Commission
APRA	Australasian Performing Right Association
ARTC	Australian Rail Track Corporation
ASIC	Australian Securities and Investments Commission
CCA	<i>Competition and Consumer Act 2010</i> (Cth)
CMA	UK Competition and Markets Authority
CMI Act	<i>Chicken Meat Industry Act</i> (WA) 1977
COAG	Council of Australian Governments
Competition Policy Review	Competition Policy Review (2014)
Copyright Act	<i>Copyright Act 1968</i> (Cth)
Copyright Review	ALRC review into Copyright and the Digital Economy (Final Report dated 30 November 2013).
Copyright Tribunal	Copyright Tribunal of Australia (established under the Copyright Act)
Corporations Act	<i>Corporations Act 2001</i> (Cth)
CP Agreement	Competition Principles Agreement 1995
CRRP	COAG Road Reform Plan
CSO	community service obligation
Dawson Report	Report of the Committee, <i>Review of the Competition Provisions of the Trade Practices Act</i> (January 2003)
Dawson Review	Review of the Competition Provisions of the Trade Practices Act (2002 – 2003)
DOJ	Department of Justice (United States)
DTCS	Domestic Transmission Capacity Service
EC	European Commission
ERA	Economic Regulation Authority (Western Australia)
ESC	Essential Services Commission (Victoria)
EU DG Comp	European Commission's Directorate General for Competition
FTC	Federal Trade Commission (United States)

Food and Grocery Code	<i>Food and Grocery Prescribed Industry Code of Conduct</i>
GBE	government business enterprise
Hilmer Review	Independent Committee of Inquiry, National Competition Policy (25 August 1993)
HFC	Hybrid fibre coaxial
HVAU	Hunter Valley Access Undertaking
HVCN	Hunter Valley Coal Network
ICN	International Competition Network
IIOs	irrigation infrastructure operators
IP	intellectual property
IPART	Independent Pricing and Regulatory Tribunal of NSW
Issues Paper	Competition Policy Review: Issues Paper (14 April 2014)
IT	information technology
MCE	COAG Ministerial Council on Energy
NBN	National Broadband Network
NCC	National Competition Council
NCP	National Competition Policy
NEC	National Electricity Code
NECA	National Electricity Code Administrator
NECF	National Energy Customer Framework
NEL	National Electricity Law
NEM	national electricity market
NEMMCO	National Electricity Market Management Company
NER	National Electricity Rules
NSWRAU	NSW Rail Access Undertaking
NTC	National Transport Commission
OECD	Organisation for Economic Co-operation and Development
PSA	Prices Surveillance Authority
Prices Surveillance Act	<i>Prices Surveillance Act 1983 (Cth)</i>
Review Panel	Panel completing the Competition Policy Review
RPM	resale price maintenance
SSU	Telstra's Structural Separation Undertaking (accepted by the ACCC February 2012)
Trade Practices Act	<i>Trade Practices Act 1974 (Cth)</i>
Trade Marks Act	<i>Trade Marks Act 1995 (Cth)</i>
Tribunal	Australian Competition Tribunal

Attachment A - Further potential reforms to investigative tools

Issue	Proposed reform	Purpose of reform
Broader reforms		
Section 155 and unfair contract terms	<p>The ACCC considers that section 155 does not extend to apply to the unfair contract terms provisions of the Australian Consumer Law (as inclusion of an unfair contract term is not considered to be a contravention) and therefore it is not an available option for investigations. Further, the only remedy available is the ability to seek a declaration that an unfair contract term is considered void.</p>	<p>To allow the ACCC to properly investigate allegations of unfair contract term conduct through use of section 155.</p> <p>To suggest consideration be given to further remedies be made available to address unfair contract terms.</p>
Technical oversights in the CCA		
CCA regulations	<p>Regulation 12 of the <i>Competition and Consumer Regulations 2010</i> sets out the requirements for service of notices under the CCA. The ACCC may seek to serve a variety of statutory notices pursuant to this provision including, but not limited to, section 155 notices. Service can be effected upon a person or a corporation either in person or by registered post in certain circumstances.</p> <p>The ACCC considers that the regulations have not maintained sufficient currency when considered in the context of the evolution of new technology. Electronic service is a useful way to expedite the service process and avoid any unnecessary delay to the recipient in receiving a statutory notice. It is particularly important given the timeframes imposed for compliance with such notices.</p> <p>The ACCC considers that the regulations require amendment and should provide for 'service' to include electronic service on both domestic and foreign corporations and persons engaged in trade or commerce in Australia or with Australians.</p> <p>The ACCC also considers the regulations also require amendment for consistency with the Federal Court Rules on service particularly, given that such rules allow for service to be effected upon a lawyer or</p>	<p>To ensure that the regulations on service of notices under the CCA maintain sufficient currency and allow for efficient service of CCA notices.</p>

Issue	Proposed reform	Purpose of reform
	representative where they have been notified as an authorised representative of the relevant person or corporation for service.	
Part VIIA – prices surveillance	<p>Reform of the price notification provisions in order to reflect how the provisions are applied in practice is considered necessary. The current application of the price notification provisions is very different to when the price notification provisions were introduced in the <i>Prices Surveillance Act 1983 (Cth)</i> (Prices Surveillance Act) as part of prices and incomes policy and were intended to apply to a short sharp process of price determination rather than a detailed price assessment process. In contrast, the provisions are now being used for a form of regulation of monopoly service providers.</p> <p>While amendments were made to the objectives of Part VIIA in 2004 when the Prices Surveillance Act was incorporated into the now CCA, the substantive provisions were not changed.</p>	To make the provisions of Part VIIA fit for purpose.
Part VIIA – secrecy provision	<p>Section 95ZP prevents information obtained under Part VIIA from being disclosed to other regulators and it can only be produced in Court in very limited circumstances. ACCC staff are subject to a maximum criminal sanction of two year jail for breaches of the provision. The provision was carried over into the CCA with the repeal of the Prices Surveillance Act but with an increased penalty (a fine based on penalty units was replaced with sanction of imprisonment). The provision applies to all unpublished information obtained under the legislation since 1983.</p> <p>It is considered that the regime in section 155AAA should be sufficient protection for commercially sensitive information that is not made available to the public under Part VIIA rather than section 95ZP. Alternatively, the criminal sanction in section 95ZP should be limited.</p>	To rectify the disproportionate risk to ACCC staff as a result of the attributable criminal sanction and to rectify the level of sanction so that it is comparable to other provisions in CCA.

Issue	Proposed reform	Purpose of reform
Part VIIA – section 25 delegation	Section 25 exempts Part VIIA from the range of functions that the ACCC can delegate. This reduces the efficiency with which price inquiries could otherwise be run under Part VIIA.	To remove an unnecessary impediment to efficiency of price inquiries under Part VIIA.
Search warrants and the <i>Crimes Act 1914</i> (Cth)	<p>The search warrant provisions of the <i>Crimes Act 1914</i> (Cth) relating to electronic data served as a template for the introduction of various Part XIX search warrant provisions of the CCA. The Crimes Act search warrant provisions were significantly amended in 2010. The ACCC believes the rationale for such changes related to problems faced by the Australian Federal Police when dealing with electronic material under a Crimes Act search warrant. A number of important inconsistencies now exist between the CCA search warrant regime and the relevant provisions in the Crimes Act upon which the CCA regime was modelled. Some of the areas of inconsistency relate to the removal and use of seized items and when a warrant can be obtained in respect of accessorial liability. For example, the test for when electronic equipment can be copied is higher under section 154H of the CCA which imposes a more onerous burden upon executing officers of a warrant.</p> <p>It is suggested that the CCA search warrant provisions, modelled upon now repealed or amended provisions of the Crimes Act, should be amended to avoid the shortcomings of the former provisions.</p>	To rectify shortcomings in the search warrant provisions of the CCA.
Ministerial consent to rely on extraterritorial conduct in private legal proceedings	<p>In respect of proceedings for damages arising from a contravention of the CCA, section 5(3) prohibits reliance on evidence of conduct outside of Australia unless ministerial consent is obtained. The relevant minister is obliged to give such consent unless the relevant foreign country authorised such conduct or its release would not be in the national interest.</p> <p>However, the Courts are in a position to determine their approach to overseas evidence, including whether conduct was required by overseas law.</p>	Repeal of the requirement will remove an unnecessary impediment to private parties seeking to enforce their rights under the CCA.