Misuse of market power

› Harper Review – Allens' view on the Final Recommendation

Introduction

The Harper Review's Final Report recommends that s46 be amended in two respects. First, by removing the 'taking advantage' requirement. Second, by replacing the existing 'purpose' element with a requirement that the conduct have the 'purpose or effect or likely effect of substantially lessening competition'.[1]

In our view, s46 should not be amended by removing the 'taking advantage' requirement and subjecting all conduct engaged in by a firm with substantial market power to a 'substantial lessening of competition' test. It is important, as a matter of policy, to achieve an appropriate balance between ensuring that firms with substantial market power are able to engage in legitimate competitive conduct, while protecting the competitive process and ensuring that markets remain competitive. The 'taking advantage' element performs that role.

While there may be some debate as to whether the 'taking advantage' element is currently achieving that function, a 'substantial lessening of competition' test, divorced from any link between a firm's market power and the impugned conduct, is not an adequate replacement. The distinction between vigorous competitive conduct and anti-competitive conduct becomes unclear, and the 'substantial lessening of competition' test does not perform an adequate filtering role. Adopting the Panel's recommendations is likely to deter firms from engaging in legitimate, vigorous competitive conduct.

The 'taking advantage' requirement

An important policy consideration recognised by both Australian and overseas courts is that it is desirable for firms with market power to compete vigorously, even if this harms competitors. It is equally clear, however, that it is important to achieve a balance between allowing firms with market power to compete vigorously and protecting the competitive process from anti-competitive conduct.[2] The 'taking advantage' element seeks to play an important filtering role to achieve this balance. It does this by ensuring that s46 does not capture all conduct engaged in by a firm with substantial market power, but only conduct that is causally connected to the firm's market power. In this respect, it directs the court to address a series of questions, including:

- whether a profit-maximising firm operating in a workably competitive market could in a commercial sense profitably engage in the conduct in question[3], or whether it is likely the firm would have engaged in the conduct if it did not have substantial market power[4]; and
- whether the conduct was materially facilitated by the firm's substantial market power.[5]

The Harper Panel expressed concerns as to whether the 'taking advantage' element is sufficiently clear so that business is reasonably able to determine, in advance, whether its conduct is likely to contravene the *Competition and Consumer Act 2010* (Cth). We do not agree with this view. We consider that there is now greater understanding as to the application of the test, having regard to the number of decided cases over the past 10 years relating to s46. Further, we do not agree that the amendment proposed by the Harper Review – namely, to capture all conduct engaged in by firms with substantial market power, subject only to a 'substantial lessening of competition' test – is the solution. Such an amendment is likely to result in 'over-capture' and deter firms with market power from engaging in legitimate competitive conduct.

The 'substantial lessening of competition' test alone does not achieve an appropriate balance

We do not think the 'substantial lessening of competition' test is appropriate as the sole filter. The courts have stated on many occasions that the Act is not about protecting competitors but about protecting competition or the competitive process. The courts have also indicated that the Act does not seek to deter vigorous competition but anti-competitive conduct. However, there is no clear line as to where the distinction should be drawn.

While ss45 and 47 require a company that is entering into a contract to give consideration as to whether the purpose or likely effect of that agreement is to substantially lessen competition, the cases (and ACCC authorisations) in relation to those provisions illustrate that the number of business agreements that give rise to a real potential of raising concerns is, in practice, relatively limited. An analysis of compliance with those provisions can be structured by businesses into the normal legal process of contract review and internal sign-off.

By contrast, applying a 'substantial lessening of competition' test to any activity at all by a corporation with market power, including where there is no correlation at all between the activity and that underlying position of market strength, presents a markedly different compliance exercise for a company. It is unclear, for example, whether, in the light of the decisions to date, the

following conduct will be prohibited if it results in a firm with substantial market power gaining market share at the expense of its competitor or competitors, or if it results in a competitor or competitors exiting the market:

- aggressive discounting, such that a firm's prices are above its costs but at a level which competitors cannot meet (eg because there are economies of scale not available to competitors);
- vertically integrating upstream into the production of an input in order to reduce costs and secure greater control over the quality of the final product, resulting in existing suppliers of the input exiting the market, but lower final prices to consumers;
- launching a better quality product with which competitors cannot compete (eg because of patent protection);
- in a market characterised by tenders – successfully competing for tenders, based on price and quality to the extent that it is no longer economically viable for a competitor to remain in the market;
- vertically integrating downstream into the retail supply of a product and changing distribution arrangements (eg reducing number of retail distributors);
- in a concentrated market:
  - refusing to supply a new competitor that consists of a number of ex-employees who have split from the company and launched their own venture, but who require supply of some input products/services; or
  - refusing to supply a competitor where there are genuine commercial concerns (even if ultimately wrong) about that competitor, such as its credit worthiness or business ethics.

We have real concerns about how companies could implement internal compliance processes that would not create a significant potential to deter legitimate pro-competitive activity, as well as the increase in compliance costs.

The Harper Review proposes that, to reduce the risk of firms being deterred from engaging in competitive conduct, the Act direct the court to consider a range of matters.[6] The Harper Review also recommends that the ACCC issue guidelines concerning the operation of s46. It is far from clear that introducing a provision that requires a court to have regard to a number of evidentiary matters will address the fundamental issues identified above concerning the operation of a 'substantial lessening of competition' test. Further, the ACCC guidelines will have no weight in court proceedings and could not safely be relied on by businesses in their decision-making processes.

Meet the team

Please feel free to contact a member of the team to discuss the Harper Review in more detail.

Jacqueline Downes
Practice Leader
T +61 2 9230 4850
M +61 411 498 505
Jacqueline.Downes@allens.com.au

Fiona Crosbie
Chairman
T +61 2 9230 4383
M +61 404 042 879
Fiona.Crosbie@allens.com.au

Ted Hill
Partner
T +61 3 9613 8588
M +61 411 646 761
Ted.Hill@allens.com.au

Carolyn Oddie
Partner
T +61 2 9230 4203
M +61 404 074 203
Carolyn.Oddie@allens.com.au

Kon Stellios
Partner
T +61 2 9230 4897
M +61 404 802 694
Kon.Stellios@allens.com.au

John Hedge
Partner
T +61 7 3334 3171
M +61 421 545 794
John.Hedge@allens.com.au

Rosannah Healy
Partner
T +61 3 9613 8421
M +61 411 776 662
Rosannah.Healy@allens.com.au

Robert Walker
Partner
T +61 3 9613 8879
M +61 478 527 188
Robert.Walker@allens.com.au

Felicity McMahon
Managing Associate
T +61 2 9230 5242
M +61 450 123 681
Felicity.McMahon@allens.com.au

Allens is ranked:

TOP TIER Competition/Antitrust – Australia
Chambers Asia-Pacific 2017

TOP TIER 'Elite' ranking – Australia
Global Competition Review 2017

TOP TIER Competition and Trade – Australia
The Legal 500 2017

1. *Boral Besser Masonry Ltd v Australian Competition and Consumer Commission* (2003) 215 CLR 374; *Commerce Commission v Carter Holt Harvey Building Products Group Ltd* [2004] All ER (D) 235 (Jul); *Brooke Group Ltd v Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993).
2. *Commerce Commission v Carter Holt Harvey Building Products Group Ltd* [2004] All ER (D) 235 (Jul).
3. *Australian Competition and Consumer Commission v Cement Australia* [2013] FCA 909.
4. Section 46(6A)(c).
5. Section 46(6A)(a).
6. Harper Report 344-345.