

# University of South Australia 12<sup>th</sup> Annual Competition and Consumer Law Workshop 2014

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## 1 Introduction

Today I wish to focus on the 'substantially lessening of competition' (SLC) test.

The Competition Policy Review Draft Report (**Draft Report**) advocates a move towards a competition framework which elevates the status of this concept as the underpinning arbiter of anti-competitive conduct. It already appears in several of our key competition provisions and this number will increase if the Harper recommendations are adopted.

The Harper Panel (the **Panel**) has also identified six attributes against which to test the 'fitness for purpose' of competition policy, including a focus on making markets work in the long term interests of consumers and encouraging efficient investment in infrastructure, innovation and new entry.<sup>1</sup> Importantly for the purposes of my comments today, one attribute of a fit for purpose competition policy identified by the Panel is that it should include laws that are 'clear, predictable and reliable'. In my view, for laws to be clear, predictable and reliable, they must be well-understood, by the courts, by the relevant regulatory bodies and by practitioners like myself.

Implicit in this increasing focus on prohibiting conduct or arrangements only where they substantially lessen competition is an assumption, albeit unstated, that it *is* a well understood concept. I wish to test that assumption. I will focus primarily on the test as it relates to the *effect or likely effect* of substantially lessening competition (rather than purpose) in my comments today.

## 2 Harper's Draft Recommendations

The test currently appears in sections 45, 47 and 50 of the Competition and Consumer Act (Cwlth) 2010 (**Act**), so as to prevent contracts, arrangements or understandings, exclusive dealing and mergers that substantially lessen competition.

The Draft Report released last month made a number of recommendations that, if adopted, would see the 'substantial lessening of competition' test embraced further.

For example, in addition to section 46:

- broader exceptions are proposed to the cartel provisions for joint ventures and similar forms of business collaboration on the basis that they would remain subject to the SLC test in section 45<sup>2</sup>;
- the per se exclusionary provisions in section 4D are recommended for removal, and they would instead fall for consideration under the cartel provisions or the section 45 SLC test<sup>3</sup>;

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<sup>1</sup> Competition Policy Review Draft Report September 2014 p 16.

<sup>2</sup> Competition Policy Review Draft Report September 2014, See draft recommendation 22 (p 41).

<sup>3</sup> Competition Policy Review Draft Report September 2014: See draft recommendation 23 (p 41).

- the authorisation and notification procedures are marked for simplification, including by allowing the ACCC the power to grant block exemptions (including for per se prohibitions) where conduct is unlikely to substantially lessen competition<sup>4</sup>;
- third line forcing is recommended to be subject to an SLC test, in the same way as the other provisions of section 47, and section 47 is to be simplified to render all forms of conditional vertical conduct subject to the test, rather than specified types<sup>5</sup>; and
- finally, the Panel has recommended the repeal of the price signalling provisions in Division 1A, and that section 45 be extended to cover ‘concerted practices’ where they have the purpose, effect or likely effect of SLC<sup>6</sup>.

### 3 Articulation of the SLC test

The Act itself does not define the term ‘substantial lessening of competition’, save for section 4G which provides that ‘references to the lessening of competition shall be read as references to preventing or hindering competition.’ That does not get us very far, and potentially just substitutes two new words for one: the first a very high test (stopping competition) and the second arguably less so (obstructing competition). In fact, the process I used to search for the meaning of these terms via the dictionary demonstrates its futility, as one word is defined using others that are themselves defined using more.

Section 4 also defines ‘competition’ but the definition is inclusive, rather than exhaustive, and adds little to the understanding of the SLC test.

At a general level, we know that the phrase is evaluative.<sup>7</sup> The Court in *South Sydney*<sup>8</sup> noted that the evaluation is both quantitative and qualitative. From that, one can infer that it is necessary to consider both the ‘amount’ or size of the lessening and its significance relative to another state.

We also know that other state is the counterfactual, and that the assessment is to be made by applying the ‘with or without’ test. This test was expressed in *Dowling v Dalgety* as would the conduct make the market ‘substantially less competitive than it otherwise would be’?<sup>9</sup>

Finally, we know that the test is concerned about the effect of conduct on *competition*, not on individual *competitors*. As Fitzgerald J articulated in *Dandy Power*:

It would, I think, be an unusual and exceptional case in which it could be shown that competition in a generally competitive market was or was likely to be substantially lessened by a refusal to supply one of a number of competitive retailers in the market with a product otherwise freely available and competitively marketed. Further, where there is a market which is generally competitive, it plainly does not follow that conduct which affects the balance of competition by advantaging or disadvantaging a particular dealer or dealers or a particular product or products necessarily lessens the competition in the market.<sup>10</sup>

### 4 The significance of ‘substantial’

Not all conduct that lessens competition is prohibited; the lessening must be ‘substantial’.

<sup>4</sup> Competition Policy Review Draft Report September 2014: See draft recommendations 34 and 35 (pp 51-53).

<sup>5</sup> Competition Policy Review Draft Report September 2014: See draft recommendations 27 and 28 (pp 45 and 46).

<sup>6</sup> Competition Policy Review Draft Report September 2014: See draft recommendation 24 (p 42).

<sup>7</sup> *ACCC v Australian Medical Assc Western Australia Branch Inc.* [2003] FCA 686 at [329].

<sup>8</sup> *South Sydney District Rugby League Football Club Ltd v News Ltd* [2001] FCA 862 [252].

<sup>9</sup> *Dowling v Dalgety Australia Ltd* (1992) 106 ALR 75, 103.

<sup>10</sup> *Outboard Marine Australia Pty Ltd v Hecar Investments (No 6) Pty Ltd* (1982) 66 FLR 120, 134

In *Rural Press*<sup>11</sup> at first instance, the Court acknowledged that there has been ‘much inconclusive debate’ about the proper construction of the term ‘substantial’ in the context of purpose, but did not find it necessary to resolve the debate in that case.<sup>12</sup> Justice Deane in *Tillmanns Butcheries* in the context of secondary boycotts described the word ‘substantial’ as ‘not only susceptible to ambiguity’ but as ‘a word calculated to conceal a lack of precision’.<sup>13</sup> Neither of these cases concerned the SLC test.

The Explanatory Memorandum accompanying the 1992 amendments to the merger provisions that reintroduced the SLC test into section 50 stated that ‘substantial’ means ‘real or of substance as opposed to large or weighty’. This is consistent with the meaning attributed to the term in the *Arnotts* case.<sup>14</sup>

Other interpretations have been given to the term ‘substantial’ over the years in different contexts, for example:

- considerable or large;<sup>15</sup>
- not insubstantial or nominal;<sup>16</sup>
- real or of substance (as distinct from ephemeral or nominal);<sup>17</sup> or
- substantial in a ‘relative sense’.<sup>18</sup>

The High Court in the *Rural Press* appeal (in the context of section 45) held that the relevant question was whether the effect of the impugned contract, arrangement or understanding was ‘substantial in the sense of being meaningful or relevant to the competitive process’.<sup>19</sup> This seems to be the widely accepted articulation of the phrase and was most recently reflected by Justice Greenwood in *Cement Australia*.<sup>20</sup> His Honour went on to observe that ‘the effect may be “relevant” to the competitive process in the sense of being “material” to rivalrous conduct’.<sup>21</sup>

This is perhaps to be contrasted with the ACCC’s expression of the test in the context of merger analysis. Its Merger Guidelines state that the ACCC generally takes the view that a lessening of competition will be substantial if it ‘confers an increase in market power on the merged firm that is significant and sustainable.’<sup>22</sup> It goes on to say that the level at which an increase in market power is likely to become significant and sustainable will vary from merger to merger.

Whether this approach can or should be taken in other SLC contexts is not clear: for example, will an effect only be meaning or relevant to a competitive process if it confers a significant increase in market power upon a market participant or participants?

The Merger Guidelines also expressly note that ‘the precise threshold between a lessening of competition and a substantial lessening of competition is a matter of judgement and will always depend on the particular facts’.<sup>23</sup> It is certainly true that the existence or otherwise of a

<sup>11</sup> *Rural Press Ltd v ACCC* [2002] FCAFC 213.

<sup>12</sup> *Rural Press Ltd v ACCC* [2002] FCAFC 213 [98].

<sup>13</sup> *Tillmanns Butcheries Pty Ltd v Australian Meat Industry Employees’ Union* (1979) 42 FLR 331, 348.

<sup>14</sup> John Duns & Arlen Duke, *Competition Law* (LexisNexis Butterworths, 3<sup>rd</sup> ed, 2011) 108.

<sup>15</sup> *Dowling v Dalgety Australia Ltd* (1992) 106 ALR 75.

<sup>16</sup> *Re Arnotts Limited; Arnotts Biscuits Limited; Fledspac Limited and the Dickens Corporation Pty Limited v Trade Practices Commission* [1990] FCA 473 at [104]

<sup>17</sup> *Tillmanns Butcheries Pty Ltd v Australian Meat Industry Employees’ Union* (1979) 42 FLR 331, 348.

<sup>18</sup> *ASX Operations Pty Ltd v Pont Data Australia Pty Ltd* (1990) 97 ALR 513, 530.

<sup>19</sup> *Rural Press Ltd v ACCC* [2003] HCA 75.

<sup>20</sup> *ACCC v Cement Australia Pty Ltd* [2013] FCA 909 at [3013].

<sup>21</sup> *ACCC v Cement Australia Pty Ltd* [2013] FCA 909 at [3014].

<sup>22</sup> *ACCC Merger Guidelines* at [3.5].

<sup>23</sup> *ACCC Merger Guidelines* at [3.5].

contravention of the Act will turn on the facts and conduct in question, but is it appropriate that the line between illegal and legitimate conduct be a 'matter of judgement'? And is it a concern that the state of Australian case law appears to make it so?

## 5 Cases

When you turn to the cases, there are relatively few that consider the test insofar as the effects element is concerned.

### *Section 45*

In the context of section 45, we have few cases that actually apply the test and form a conclusion on it:

- (a) *Dowling v Dalgety Australia Ltd*<sup>24</sup> - in some sense, a refusal to supply case (the supply in question being membership of a livestock sales association) allegedly because the existing members did not want anyone else conducting livestock auction sales on the association's saleyards, which were jointly owned by the existing members and subject to agreement between them not to let to outside agents. The effects case failed on the basis that the market (for the provision of livestock selling services including livestock auctioneering services) was highly competitive and was unlikely to be altered as a result of the conduct.<sup>25</sup> The factors considered included whether the applicant's admission to the association would have resulted in a substantial improvement in rivalry in relation to price, product or service or exert any downward pressure on price, and found that it would not.
- (b) *Stationers Supply Pty Ltd v Victorian Authorised Newsagents Association Ltd*<sup>26</sup> - involving arrangements between a subsidiary of VANA (the peak industry body), Vicsat and individual newsagents to establish a product line known as 'Newspower', with Vicsat as the preferred wholesaler to members of a Newspower Group. Members were obliged to pay a joining fee and other advertising fees and to purchase promotional stock from Vicsat. Stationers Supply was also in the business of supplying its own stationary products.

The alleged effect of the arrangements was that they prevented, hindered or restricted newsagents from purchasing stationary from alternative suppliers and thereby substantially lessened competition. The case did not succeed on the basis that there was no evidence that the arrangements compelled members to acquire stationary products from Vicsat, or that existing vigorous price competition would be diluted. Further, the evidence did not enable Justice Ryan to conclude that 'it is more probable than not that advertising members will ultimately purchase all their stationary from VNS as a result of their obligation to purchase promotional material from VNS' even assuming such an obligation was imposed.<sup>27</sup>

- (c) *ACCC v The Australian Medical Association Western Australia Branch Inc*<sup>28</sup> - which considered arguments that:
  - (i) absent the impugned pricing arrangements between AMA (on behalf of doctors) and developer of a hospital setting prices for the supply of certain medical services to public patients, fees would have been negotiated individually with

<sup>24</sup> (1992) 106 ALR 75.

<sup>25</sup> *Dowling v Dalgety Australia Ltd* (1992) 106 ALR 75, 103.

<sup>26</sup> (1993) 44 FCR 35.

<sup>27</sup> *Stationers Supply Pty Ltd v Victorian Authorised Newsagents Association Ltd* (1993) 44 FCR 35, 56-64.

<sup>28</sup> [2003] FCA 686.

practitioners and this would have been the first step in developing competition across the market<sup>29</sup>; and

- (ii) because there was little or no competition in the existing market, the loss of *any* actual or potential competition would be a substantial loss.

This second argument was rejected by the Court. Justice Carr stated emphatically that ‘any loss of competition will not, as a matter of law, equate necessarily to a substantial lessening of competition...it must be evaluated by the process of comparing that loss of competition to the level of competition which would otherwise exist’.<sup>30</sup>

- (d) *ASX Operations Pty Ltd v Pont Data Australia Pty Ltd (No 1)*<sup>31</sup> – a resale restriction case, in which the Court on appeal upheld the findings of the trial judge that the prohibition on wholesaling was likely to substantially lessen competition in the defined information market, but limited its reasons for this conclusion to a few paragraphs.<sup>32</sup>
- (e) *Monroe Topple & Associates Pty Ltd v Institute of Chartered Accountants in Australia*<sup>33</sup> - which concerned bundling of training programs and course materials by the Institute for certification that had previously been provided and charged separately, thereby affecting the business of Monroe Topple, which provided certification support materials. The SLC case was rejected on the basis that the Institute ceased to supply certification support materials in competition with Monroe Topple, and that the CA support services market had changed as a result – an analysis very clearly confined to its facts.<sup>34</sup>
- (f) *Seven Network Ltd v News Ltd* [2007] FCA 1062 – in which the market where the greatest competitive effect was alleged to occur was found not to exist.
- (g) *ACCC v Cement Australia Pty Ltd*<sup>35</sup> - the most recent SLC case, in which Cement Australia entered into agreements to acquire flyash from all the power stations in south-east Queensland with the effect of preventing a rival gaining access to unprocessed flyash and therefore from entering the south-east Queensland concrete grade flyash market. The ACCC alleged various breaches of section 45 regarding the purpose and effect of the arrangements, and was successful on both counts.

The ACCC also pleaded breaches of section 46, but was unsuccessful, and the case has been cited as one of the reasons for pursuing an effects test in section 46.

## Section 47

In the context of section 47, we have fewer cases again:

- (a) *Outboard Marine Australia Pty Ltd v Hecar Investments (No 6) Pty Ltd*<sup>36</sup> - a refusal by a manufacturer to supply on the basis that the retailer wished to also stock products of competing manufacturers. The case failed on the basis that the market was geographically wide and there was no evidence that barriers to entry had been raised or

<sup>29</sup> *ACCC v The Australian Medical Association Western Australia Branch Inc* [2003] FCA 686 [340].

<sup>30</sup> *ACCC v The Australian Medical Association Western Australia Branch Inc* [2003] FCA 686 [251] at [341].  
<sup>31</sup> (1990) 27 FCR 460.

<sup>32</sup> *ASX Operations Pty Ltd v Pont Data Australia Pty Ltd* (1990) 97 ALR 513, 538-539.

<sup>33</sup> [2002] FCAFC 197.

<sup>34</sup> *Monroe Topple & Associates Pty Ltd v Institute of Chartered Accountants in Australia* [2002] FCAFC 197 [107]–[113].

<sup>35</sup> [2013] FCA 909.

<sup>36</sup> (1982) 66 FLR 120.

that price completion had been reduced, and the effect on an individual retailer was considered insufficient to SLC.<sup>37</sup>

- (b) *Dandy Power Equipment Pty Ltd v Mercury Marine Pty Ltd*<sup>38</sup> - a similar fact scenario, with a similar conclusion.
- (c) *ACCC v Baxter Healthcare Pty Ltd*<sup>39</sup> - a true bundling case, but one in which the Court upheld a purpose claim, but not the effects arguments, on the basis that Baxter Healthcare's offer of significantly lower prices for a bundle of sterile fluids (in which it had an effective monopoly) and PD fluids (in which it did not) had not significantly raised barriers to entry and that, other than shutting out competitors for the period of the contract, there were no long-term impediments to competitors effectively competing for PD fluids in the future.<sup>40</sup>

## Section 50

When we come to section 50, the understanding of what constitutes an SLC is in a sense more advanced than in other contexts, notwithstanding the paucity of case law. Putting aside Tribunal decisions, only a handful of contested section 50 cases exist,<sup>41</sup> and even fewer actually apply the SLC test rather than the previous 'dominance' test.

Instead, much of our understanding of what may be enough to SLC is drawn from the ACCC's informal clearance decisions and its Merger Guidelines. We also have the benefits of the merger factors set out in section 50(3) of the Act.

The ACCC does not oppose the vast majority of the mergers that come before it, which supports that the bar set by the test it applies is a high one. Yet, it also has not succeeded when it has been challenged to meet the evidentiary burden required to prove its case, with the Court in *ACCC v Metcash* finding that the acquisition of Franklins by Metcash was not likely to have the effect of SLC, and AGL succeeding in obtaining a declaration to this effect in *AGL v ACCC*. This may indicate that it does not in fact set the bar high enough, it may point to deficiencies in evidence or argument, or it may simply highlight that the test is not as 'predictable' or 'reliable' as even our regulator may prefer.

## 6 Is the concept of SLC sufficiently clear to effectively distinguish competitive from anti-competitive conduct?

In querying the clarity of the SLC test, I am not intending to suggest that the Courts in any of the cases mentioned have got the test wrong, or have come to an incorrect conclusion. Each case must turn on its own facts, and all combination of facts are novel.

However, when you look at the cases, we have a better sense of what type of conduct or arrangement is **not** sufficient to constitute an SLC, rather than what is. Is understanding a positive concept primarily via the negative a satisfactory state of affairs?

What is perhaps particularly concerning is that we have very little consideration of when competition that is occurring 'on the merits' or in pursuit of legitimate pursuits such as greater efficiency could cross the line through its competitive effects.

<sup>37</sup> *Outboard Marine Australia Pty Ltd v Hecar Investments (No 6) Pty Ltd* (1982) 66 FLR 120, 125.

<sup>38</sup> (1982) 64 FLR 238.

<sup>39</sup> [2005] FCA 581.

<sup>40</sup> *ACCC v Baxter Healthcare Pty Ltd* [2005] FCA 581 [640]-[641].

<sup>41</sup> See, for example, *Australian Gas Light Company v ACCC (No 3)* [2003] FCA 1525; *ACCC v Metcash Trading Limited* [2011] FCA 967; [2011] FCAFC 151 (appeal); *Arnotts Limited v TPC* (1990) 24 FCR 313; *TPC v Australia Meat Holdings Pty Ltd* (1988) 83 ALR 299; and *QIW Retailers Ltd v Davids Holdings* (1993) ATPR 41-226.

The position of the ACCC to arguments related to the pursuit of efficiency in the context of the SLC test is not often tested. In the context of mergers, it acknowledges that ‘the potential for improved efficiency is a common motivation for firms to merge.’<sup>42</sup> But it draws a distinction between the effect of a merger on competition (including on the efficiency of markets) and the efficiency of individual firms. It also states that ‘if efficiencies are likely to result in lower (or not significantly higher) prices, increased output and/or higher quality goods or services, the merger *may not* substantially lessen competition.’<sup>43</sup> ‘*May not*’ – not ‘*will not*’.

In addition, many of the cases brought pursuant to sections containing the SLC test have failed by reason of market definition, focus on a single competitor, lack of the required conditionality or lack of compelling evidence. Often, a purpose and effect case are run together and the purpose element more often succeeds than the effects, which leaves the area of conduct with legitimate purposes, but problematic effects largely unexplored.

Examples have been given by the ACCC of unilateral conduct that could or should be caught by an amended section 46 with an effect element. These include ‘buying up all available land, restricting the supply of essential inputs, predatory pricing and anti-competitive bundling’.<sup>44</sup> However, we have no SLC cases on buying up all of the land (buying up all of the flyash in *Cement Australia* is the closest we have come), *Dowling v Dalgety*, *Outboard Marine* and *Dendy Power* as examples of refusal to supply (each of which failed), two discounted pricing cases (*Monroe Topple* and *Baxter*) with the later of the two also serving as our only quintessential bundling case.

Again, I am not suggesting that the move toward greater application of the SLC test within our competition framework is undesirable. It is a more sensible approach to the prescriptive per se provisions littered throughout the Act, that capture both benign and pro-competitive conduct through technical drafting and a desire to proscribe past ills long since curable – third line forcing being the prime example.

However, I am not convinced that we could say with confidence that the SLC test, in light of the existing case law on it, has the attributes of clarity, reliability or predictability put forward by the Panel as a measure of ‘fit for purpose’ competition laws, at least for the moment. I think it is capable of achieving that status over time, but only with significantly more litigation and testing of its boundaries by the Courts.

Whether corporations are prepared to accept the risk of potential investigation or litigation when making supply, investment, pricing, bidding or business collaboration decisions while this occurs, even where it could be viewed as efficiency enhancing or, on the other side, judged as likely to lessen competition a little, remains to be seen.

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<sup>42</sup> ACCC Merger Guidelines at [7.63].

<sup>43</sup> ACCC Merger Guidelines at [7.65].

<sup>44</sup> Rod Sims’ speech to Competition and Consumer Committee Law Council of Australia Workshop 2014.