RETHINKING THE CCA: DRAFT LEGISLATION LAYS GROUNDWORK FOR SIGNIFICANT CHANGE

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I. INTRODUCTION

Australia's competition laws have been under review for over two years. The Competition Policy Review chaired by Professor Ian Harper ("Harper Review") received its Terms of Reference on March 27, 2014 and proceeded briskly through its allotted 12 months to deliver its Final Report on March 31, 2015. It then took another 12 months for the Commonwealth Government to finalize its response to the Harper Review, having deferred its decision on the Section 46 (misuse of market power) recommendation to a further inquiry that ended on March 16, 2016.

The Australian Government has finally released exposure draft legislation, to amend the Competition and Consumer Act of 2010 ("CCA") in line with the majority of the recommendations of the Harper Review, including:

- The controversial proposed changes to Section 46 of the CCA (misuse of market power) will be implemented according to the "Full Harper" formulation.
- The price signaling prohibitions in the CCA will be removed, to be replaced with a new prohibition on anti-competitive concerted practices.
- The ACCC has released draft guidelines on their interpretation of these two provisions, seeking feedback. Treasury has also released a set of questions seeking specific

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feedback on a number of the changes.

- The cartel provisions will be simplified and their exceptions relating to joint ventures and vertical arrangements will be strengthened.
- The third-line forcing provisions of the CCA will become subject to a competition test. The ACCC will be given additional powers to:
  - authorize mergers, subject to review by the Australian Competition Tribunal (which will lose its power to authorize mergers in the first instance);
  - grant exemptions for conduct that would otherwise contravene the competition prohibitions of the CCA; and
  - grant class exemptions in relation to common business practices that do not generate competition concerns and could otherwise be authorized individually.
- In exercising many of its powers, the ACCC will not be limited to applying a competition test, but may also assess whether the public benefit of a proposed merger or proposed conduct will outweigh any detriment.
- The legislation does not pick up recommended changes that would have extended the application of the CCA to some government activities not currently caught, including some activities of local government.
- The amendments are also limited to changes to the CCA itself, and do not address any of the wider competition policy proposals raised by the Harper Review such as introducing greater competition in health and human services, intellectual property, transport and the state and territory areas of planning and zoning, retail trading hours and taxi licensing.
- The changes also do not seek to implement a number of the institutional changes recommended by Harper, such as the introduction of a new "access and pricing regulator."

II. MISUSE OF MARKET POWER

A. The New Section

Market power is by far the most controversial reform throughout the Harper Review, the reformulation has changed very little since the Draft Report and not at all since the Final Report. The proposed Section 46 now provides that:

> (1) A corporation that has a substantial degree of power in a market must 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.

The new test removes the "take advantage" element, introduces an "effects" alternative, and replaces the specific categories of exclusionary conduct with an overall "substantial lessening of competition" standard, which is to be assessed with regard to the following factors:

> (2) Without limiting the matters to which regard may be had in determining for the purposes of sub-Section (1) whether conduct has the purpose, or has or is likely to have the effect, of substantially lessening competition in a market, regard must be had to the extent to which:
>
> (a) the conduct has the purpose of, or has or would be likely to have the effect of, increasing competition in that market, including by enhancing efficiency, innovation, product quality or price competiveness in that market; and
>
> (b) the conduct has the purpose of, or has or would be likely to have the effect of, lessening competition in that market, including by preventing, restricting, or deterring the potential for competitive conduct or new entry into that market.

The new Section 46 applies the same test as the current Sections 45 and 47, though it is not clear how that test might operate in the context of unilateral conduct. Unlike most provisions of the CCA, the new Section 46 does not apply to any specific kind or category of conduct, such as an agreement, an acquisition or an exclusive dealing. Unlike the current Section 46 and similar laws in other jurisdictions, the proposed prohibition does not explicitly target exclusionary conduct.

The new Section 46 removes the specific provisions dealing with predatory pricing, including the infamous "Birdsville amendment." It also removes the guidance relating to the interpretation of "take advantage" but retains the guidance on establishing when a corporation has substantial market power.

B. ACCC Interpretation

The ACCC has issued a draft Framework for Misuse of Market Power Guidelines ("Draft Guidelines") which provides that:

> The objective of a misuse of market power provision is to prohibit unilateral conduct by a corporation with substantial market power that interferes with the competitive process by preventing or deterring rivals or potential rivals from competing on their merits. Sometimes this is broadly referred to as 'exclusionary conduct'.[2]

The Draft Guidelines identify refusal to deal, predatory pricing, tying and bundling and margin/price squeeze as potential misuses of market power, and list as examples:

- refusal to supply an essential input (e.g. refusing to supply cement to a rival ready-mix concrete plant);
- land banking (e.g. a fuel retailer with 7 out of 8 retail fuel sites in a major town buys the first option to purchase two new designated sites with no plans to use them);
- predatory pricing (e.g. for 12 months the publisher of a free regional newspaper reduces its advertising rates to less than 50 percent of the rates offered by a new entrant, which does not cover its printing and distribution costs); and

[2] At p 4.

- bundling a competitive product with a monopoly product (e.g. a firm will only sell its patented drug to pharmacies to agree to buy all their requirements of a drug that is about to lose its patent from the firm).

The Draft Guidelines also note conduct that would not raise concerns under the new Section 46:

- innovation, regardless of how "big" the firm is;
- efficient conduct designed to drive down costs;
- responding to price competition with matching or more competitive (above cost) price offers; and
- responding efficiently to other forms of competition in the market such as product offerings and terms of supply.

As examples of this conduct, the Draft Guidelines list:

- research and development (e.g. a firm developing a substantially improved version of an existing technological product that causes many suppliers of the first generation product to close);
- standardized or national pricing by large retail chains (e.g. a firm opens a store in a new town and its above-cost prices cause small retailers to become unprofitable and close);
- price war (e.g. four large firms without market power engage in a price war that causes smaller suppliers to close); and
- investing in new production technology to increase efficiency (e.g. an iconic lawnmower manufacturer invests in new production technology to lower the cost and improve the reliability of its lawnmowers in order to prevent an international manufacturer from entering).

The ACCC's statement of the objective of a misuse of market power section is a sensible one, but it is not clear how that objective is fulfilled by the new Section 46. The ACCC's examples are a useful guide to the ACCC's interpretation and its enforcement priorities, but they will not bind third parties or a court. Early court consideration of the scope of the section will be critical.

It also remains unclear whether the mandatory factors, requiring consideration of pro- and anti-competitive purposes and effects, will provide much clarity or predictability to the new law, since there is no legislative guidance on what weight should be given to each purpose or effect. The well-accepted challenge with this law is to avoid chilling the competitive conduct of larger firms (which would leave consumers worse off) while also preventing firms with market power from excluding competitors from the market.

III. PRICE SIGNALING AND CONCERTED PRACTICES

The Exposure Draft also amends Section 45 of the CCA to provide that a corporation must not: "engage with one or more persons in a concerted practice that has the purpose, or has or

is likely to have the effect, of substantially lessening competition."

The ACCC has in some past cases found it difficult to establish the element of commitment, rather than mere hope or expectation, which is required to establish an understanding under the current Section 45. The addition of a prohibition against concerted practices is designed to capture anti-competitive information exchanges where there is no commitment to act.

The Harper Review considered that the meaning of "concerted practice" did not require any legislative definition, but described it in the following terms:

> The word "concerted" means jointly arranged or carried out or coordinated. Hence a concerted practice between market participants is a practice that is jointly arranged or carried out or coordinated between the participants. The expression "concerted practice with one or more persons" conveys that the impugned practice is neither unilateral conduct nor mere parallel conduct by market participants (for example, suppliers selling products at the same price).

The Exposure Draft legislation follows the Harper recommendation and does not provide any definition of the term "concerted practice." The Explanatory Memorandum provides that:

> The concept of a concerted practice is well established in competition law internationally. The amendment to introduce the concept of a "concerted practice" is made to recognize that lesser forms of coordination than what has been judicially interpreted as required for a contract, arrangement or understanding, should be captured by Section 45, provided the practice has the purpose, effect or likely effect of substantially lessening competition…

The interpretation of a "concerted practice" should be informed by international approaches to the same concept, where appropriate. Broadly, international jurisprudence suggests that coordination between competitors, where cooperation between firms is substituted for the uncertainties and risks of independent competition, is potentially a concerted practice.

International approaches to the "concerted practices" concept are complicated by the fact that in Europe the concept needs to cover all forms of coordination below an agreement – there is no separate category of "understanding" as there is in Australia. In Europe there is also an exception for concerted practices that contribute to efficiencies, and it is not clear that the Australian "substantial lessening of competition" would protect such practices.

The Explanatory Memorandum appears to focus on private disclosures of information, noting that: "The public disclosure of pricing information can help consumers to make informed choices and is unlikely to be harmful to competition."

However, the new section is not limited to private information and the new prohibition may extend to the disclosure of public information.

The ACCC has provided a draft Framework for Concerted Practices Guidelines which provides a similar definition to that set out in the Explanatory Memorandum: "A concerted practice is a form of coordination between competing businesses by which, without them having entered a contract, arrangement or understanding, practical cooperation between

them is substituted for the risks of competition."[3]

The ACCC sets out a number of examples of conduct that would be likely or unlikely to constitute concerted practices, but does not identify clear principles beyond its initial definition. There remains a great deal for the courts and the ACCC to do before the definition of concerted practices is established in Australia with any certainty.

The ACCC has expressed concern about price signaling and information sharing conduct in relation to the boycott of beef cattle sales,[4] bank rate-setting,[5] airline capacity,[6] eggs[7] and of course petrol prices, in relation to which the ACCC settled court proceedings in late 2015.[8] As with the new misuse of market power prohibition, the ACCC can be expected to take action under the concerted practices prohibition as soon as it has an opportunity to do so.

Consistent with the overall simplification of the CCA, the current price signaling provisions – which currently only apply to the banking sector – will be repealed as they will be replaced with this broader prohibition. They have never been used and are unlikely to be missed.

IV. CARTEL PROVISIONS

One of the more significant amendments to the CCA is in relation to the cartel provisions, which are considered both overly complicated and confusing in their current form and provide only limited exceptions for joint ventures and vertical arrangements.

A. Simplification

The Exposure Draft does not simplify the cartel provisions – which we can expect in the next round of changes – but it does remove the overlap between the new cartel provisions and the old framework by removing all references to exclusionary provisions and modifying the cartel provisions to cover collective boycotts, that is, restrictions on acquisition as well as supply.

It also removes the definition of "likely" that was specific to the application of the cartel provisions to "actual or likely competitors." That definition provided that "likely" meant "a possibility that is not remote," which was found to be a low threshold in *Norcast v. Bradken*.[9] The definition of "likely" will now be aligned throughout the CCA as interpreted by the courts.

B. Extra-territoriality

The Exposure Draft confines the application of the provisions to cartel conduct that affects

[3] At p 3.
[4] Senate Rural and Regional Affairs and Transport References Committee, *Effect of market consolidation on the red meat processing sector*, Interim Report, May 2016 at p 26.
[5] ACCC's Rod Sims warns of "gaps" in cartel laws, *Australian Financial Review*, April 23, 2015.
[6] ACCC concerned by Qantas comments over price war, *Sydney Morning Herald*, September 3, 2013.
[7] ACCC demands tougher competition laws, *The Land,* April 7, 2016.
[8] Petrol price information sharing proceedings resolved, ACCC Press Release, December 23, 2015.
[9] *Norcast S.ár.L v. Bradken Limited (No 2)* [2013] FCA 235 (March 19, 2013).

competition in Australian markets, that is, conduct occurring in trade or commerce within Australia or between Australia and places outside Australia.

C. Joint Venture Exception

The Exposure Draft broadens the current exception for joint ventures to provide appropriate exemptions for joint venture activity, which will no longer be limited to contracts or to supply joint ventures. Instead, the exception will apply to any restriction in a contract, arrangement or understanding that is for the purposes of, or is reasonable necessary for undertaking, a joint venture for the production, supply or acquisition of goods or services. Notably, the current drafting would not exempt a pure R&D joint venture.

D. Vertical Arrangements Exception

The Harper Review recommended that vertical arrangements be exempted from the cartel provisions and addressed by Sections 45 or 47 to the extent that they have the purpose, effect or likely effect of substantially lessening competition. The Exposure Draft provides a broad exception for restrictions in vertical arrangements for the supply or acquisition of goods or services.

This exception is notable for its potential to exempt dual distribution models, where a supplier provides services both directly to the public and through intermediaries, from *per se* liability as was argued in the ACCC's recent price-fixing cases against ANZ and Flight Centre. These arrangements would instead be assessed under the substantial lessening of competition test, which would arguably have been a more appropriate basis for the ACCC to pursue those cases.

The new exception may also lead to different results in matters such as the ACCC's recently concluded investigation into Expedia and Booking.com, which was similar in some respects to the *Flight Centre* case in that the online booking agencies prevented hotels from directly offering rooms at cheaper prices through other channels including the hotels' own offline channels.[10]

If these issues are, in the future, to be assessed through a substantial lessening of competition test rather than a *per se* prohibition, some suppliers may be more willing to defend their arrangements rather than settling.

V. VERTICAL ARRANGEMENTS

A. Third-Line Forcing

Under the Exposure Draft, third-line forcing will no longer be prohibited *per se* but will be subject to a competition test. This will bring Australian law in line with comparable international jurisdictions and other provisions of the CCA. At present the ACCC receives hundreds of notifications of third-line forcing conduct each year and has only ever taken action against a handful, so this change will relieve a significant administrative burden on

[10] Expedia and Booking.com agree to reinvigorate price competition by amending contracts with Australian hotels, ACCC Press Release, September 2, 2016.

both business and the ACCC.

B. Resale Price Maintenance

By contrast, resale price maintenance will remain prohibited on a *per se* basis, that is, it will not be subject to a competition test. The Harper Review recognized that attitudes towards resale price maintenance had shifted internationally, notably in the US Supreme Court case of *Leegin Creative Leather v. PSKS*,[11] which in 2007 overturned almost 100 years of precedent and examined – and approved – resale price maintenance conduct under a "rule of reason" analysis. However, the history of third-line forcing regulation in Australia shows how long it can take for a *per se* rule to be relaxed.

However, resale price maintenance will now be able to be notified to the ACCC, immunizing notified conduct from prosecution unless the ACCC overturns the notification, and ensuring the ACCC's notification team will be busy even without third-line forcing notifications. Resale price maintenance will become immune 60 days after notification, significantly longer than the 14 days that currently applies to third-line forcing. The Exposure Draft also includes an exception for resale price maintenance conduct between related corporate bodies.

C. Section 47 Simplification

The Harper Report recommended that Section 47 be repealed and its role taken over by its revised Sections 45 and 46, which together would address conduct by a business with market power, contracts, arrangements, understandings and concerted practices that have the purpose, effect or likely effect of substantially lessening competition. If not repealed, Section 47 should be simplified to improve its legibility and expand its coverage.

The Exposure Draft retains 47 and does not yet simplify it. Although much of Section 47 conduct will be addressable under Sections 45 or 46, there is value in a separate section that specifies forms of conduct that may contravene the CCA and gives guidance to business.

VI. MERGER PROCESSES

There will be some significant changes to the formal merger process, following the Government's acceptance of the Harper Panel's recommendation to combine formal clearance with authorization. The current formal merger clearance process will be removed, and the merger authorization process will be reformed according to the following structure:

- the ACCC will be the decision maker at first instance and be able to authorize a merger if it:
  - does not substantially lessen competition; or
  - would result or be likely to result in a benefit to the public that would outweigh any detriment;

[11] *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, 551 U.S. 877 (2007).

- this process will not be subject to any prescriptive information requirements, but the ACCC will be empowered to require the production of business and market information;
- strict timelines will apply, which can only be extended with the consent of the merger parties;
- decisions of the ACCC are to be subject to review by the Australian Competition Tribunal under a process that is also governed by strict timelines; and
- the Tribunal will make its decision based upon the materials that were before the ACCC, but will have the discretion to allow further evidence or to call and question a witness.

The removal of the option of direct application to the Australian Competition Tribunal for merger authorization will be missed by a number of businesses and their advisers who have begun to see authorization as a useful alternative to the ACCC processes. Successful applications to the Tribunal in the *AGL/Macquarie Generation* and *Sea Swift/Toll* matters have demonstrated the different approaches of the ACCC and the Tribunal in assessing these mergers.

VII. AUTHORISATION, NOTIFICATION AND CLASS EXEMPTIONS

In line with Harper and the Government's overall approach to the simplification of the CCA, amendments will be made to the authorization and notification process to ensure that:

- only a single authorization application is required for a single business transaction or arrangement;
- the ACCC can grant exemptions from Sections 45, 46, 47 and 50 of the CCA; and
- the ACCC can grant a "class exemption" in respect of classes of conduct unlikely to raise competition concerns.

In determining whether to grant an authorization or exemption, the ACCC will be able to take into account both competition and public benefit considerations.

The class exemption power for "common business practices that do not generate competition concerns, or are likely to generate a net public benefit," is particularly interesting. It mirrors the block exemption power of the European Commission, which has been exercised to exempt certain categories of vertical restraint and concerted practices,[12] technology transfer agreements[13] and cargo liner shipping.[14] This last area is expected to be an early application of the ACCC's class exemption power if the international cargo liner shipping

[12] Commission Regulation (EU) No 330/2010 of April 20, 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices.
[13] Commission Regulation (EU) No 316/2014 of March 21, 2014 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of technology transfer agreements.
[14] Commission Regulation (EC) No 906/2009 of September 28, 2009 on the application of Article 81(3) of the Treaty to certain categories of agreements, decisions and concerted practices between liner shipping companies (consortia).

framework in Part X of the CCA is repealed.

VIII. PRIVATE ACTIONS

The CCA currently supports private actions by allowing a party to proceedings to rely on a finding of fact made by a court in civil penalty proceedings as prima facie evidence of that fact. The Exposure Draft implements the Harper Review's recommendation that parties to private proceedings will additionally be able to rely on admissions of fact made by the person against whom the proceedings are brought. This could, for example, enable parties to private proceedings to rely on evidence given by witnesses during cross-examination in civil penalty proceedings or, more significantly, in statements of agreed facts provided as part of a negotiated settlement.

IX. POWER TO OBTAIN INFORMATION

The Exposure Draft would increase the ACCC's power to obtain information, documents and evidence under Section 155 to include investigations of alleged contraventions of court enforceable undertakings, and also increases fines for non-compliance to 100 penalty units (up from 20) or two years imprisonment (up from six months).

However, it also introduces a "reasonable search" defense for a failure to produce documents on the basis that a person has undertaken a reasonable search for the documents. In determining whether they have made a reasonable search, a person may take into account:

- the nature and complexity of the matter to which the notice relates;
- the number of documents involved;
- the ease and cost of retrieving a document;
- the significance of any document likely to be found; and
- any other relevant matter.

X. ACCESS TO INFRASTRUCTURE

The Government simultaneously released its response to the 2013 Productivity Commission inquiry into the National Access Regime as part of its response to the Harper Review, and accepted the Productivity Commission's recommendations rather than those made by Harper. The Exposure Draft implements the Productivity Commission's proposed amendments to the declaration criteria, including the following:

- instead of assessing whether access would promote a material increase in competition in at least one market, a comparison will be made of competition with and without access on reasonable terms and conditions following declaration, which would reverse the Tribunal position in the *Glencore/Port of Newcastle* decision currently

under appeal (though the Explanatory Memorandum occasionally slips into the "with and without access" formulation);[15]

- the test for whether it would be "uneconomical" for anyone to develop another facility will be satisfied where total foreseeable market demand over the declaration period could be met at the least cost by the facility (taking into account the costs of coordinating multiple users);
- the decision-maker must consider whether access (or increased access) would promote the public interest (taking into account investment incentives and compliance and administration costs), and not whether it would be contrary to the public interest; and
- the criterion relating to existing access regimes be replaced with a threshold clause stating that the decision-maker does not need to consider an application or recommendation if the regime is subject to an effective access regime.

There are also some process changes, such as automatic declaration where the Minister does not make a decision within the time period (rather than the opposite), and automatic revocation of certification if a state regime changes.

Finally, the changes resolve an uncertainty about the scope of what the ACCC can order a facility owner to build by making it clear that the ACCC's order can include increasing the capacity of infrastructure and not just its geographic reach (a particularly relevant debate in the pipeline sector).

XI. COMPETITION

The Exposure Draft has changed the definition of "competition," but this is not as dramatic as it sounds. The new definition includes competition from goods and services that are capable of importation, not only those that are actually being imported. This recognizes that credible threats of imports can exert competitive pressure on the relevant market in Australia, and is sure to be referred to extensively in merger submissions.

XII. WHAT'S MISSING?

The Exposure Draft omits two of the Harper Review recommendations that were accepted in principle by the Commonwealth Government last year. These are:

- Recommendation 24, which would extend the competition law provisions of the CCA to the Crown insofar as it engages in any activity in trade or commerce, rather than applying only insofar as the Crown carries on a business as under the current position; and
- Recommendation 26, which would extend the extraterritorial reach of the CCA to apply to overseas conduct that has relates to trade or commerce within Australia or between

[15] Explanatory Memorandum at [13.20].

places in Australia and outside Australia, rather than requiring a connection with Australia based on residence, incorporation or business presence.

By its nature, the Exposure Draft deals only with changes to the CCA and does not progress the broader competition policy reforms recommended by the Harper Review in the areas of health and human services, intellectual property, transport and the state and territory areas of planning and zoning, retail trading hours and taxi licensing. These reforms are continuing under different Commonwealth, State and Territory and intergovernmental processes.

The changes also do not pick up on significant proposals made by Harper to reform a number of the institutional arrangements, such as a proposal for a new "access and pricing regulator," a new national competition policy body and the re-introduction of competition payments. These reforms will also require inter-governmental support.