The Metaphysics of Market Power

The Zero-Sum Competition and Market Manipulation Approach

George Raitt

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FOREWORD

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This thoughtful and forward-looking book is about competition law and policy in relation to misuse of market power. It begins with the proposition that the law in Australia is informed by a Structure-Conduct-Performance approach which has been overtaken by economic theory. The author, Dr George Raitt, argues that current legal criteria of liability for misuse of market power do not meet legal determinacy requirements and rule of law concerns. The judicial application of the central provision relating to misuse of market power, s 46 of the *Competition and Consumer Act 2010* (Cth) is said to have relied upon 'commercial intuition' with insufficient legal and economic reasoning to provide certainty and predictability for business. The recent amendment to the section has not delivered predictability and certainty in the law.

The Final Report of the Competition Policy Review, released on 31 March 2015 (the Harper Review) included a recommendation that s 46 include mandatory factors to be considered by a court in determining whether conduct covered by the section had the prohibited purpose, effect or likely effect. One of those factors was:

> The extent to which the conduct has the purpose, or would have or be likely to have the effect, of increasing competition in the market including by enhancing efficiency, innovation, product quality or price competitiveness in the market;

In the event, s 46 as amended in 2017 did not include that requirement. The Senate Economics Legislation Committee which reported on the *Competition and Consumer Amendment (Misuse of Market Power) Bill* in February 2017 received a submission from the Australian Competition and Consumer Commission that the subsection 'creates scope for judicial interpretation about the interaction between efficiencies and competition and innovation and competition.' The Committee recommended that it be removed from the Bill. By way of contrast, the introduction of an authorisation process for conduct falling within s 46 and the application of a public benefit test in that connection allowed the ACCC to have regard to efficiencies.

Dr Raitt contends that the legal concept of market power as it now stands is insufficiently determined and that efficiency would be an appropriate matter for consideration in the exercise of the judicial function. He draws, by way of analogy, on the concept of efficient markets in securities industry laws. He argues that the legal concept of market power and standards to determine its use or misuse should

be based on a model of competition which is more reflective of the real world than that presently embodied in the legislation. On that model, market power is conceived as the power of the market which cannot be possessed but can be manipulated. Profit maximising conduct is justified not because it is rational or logical but because it may be efficient. Different kinds of efficiency need to be identified and forensic tests developed. A legal theory of market power based on this approach requires the adaptation of economic principles. The market manipulation approach is concerned with determining whether market forces are operating without being distorted by manipulative use of market power.

The book directs attention to the argument that consideration of economic efficiency is not a matter upon which courts are competent to embark, having regard to the skills and experience of judges and the constitutional function of courts as determining disputed matters of fact and law. It is arguable that the weighing of anti-competitive effects against a range of public benefits in the context of authorisation, now available under the law through the ACCC, falls outside the notion of judicial power. It may be noted that 'public benefit' as a criterion is not unknown to the common law. In any event, it does not seem likely that the concept of judicial power would exclude the consideration of issues of efficiency to the extent that they are relevant to the characterisation of the purpose or effect or likely effect of conduct.

The scheme of the book in Part I includes discussion of four concepts of market power deficiency. The concept of market manipulation in securities is drawn upon in support of what the author calls 'an alternative legal model'. Changing approaches in Australia, the United States and the European Union in relation to reliance upon market structure and changes in market structure to infer competitive effects are considered. The book reviews and critiques market structure and direct approaches to assessing the impact of conduct on the process of competition. These approaches are contrasted with the market manipulation approach to affects.

In Part II the author analyses the application of the most recent version of s 46 to Australian appellate decisions relating to refusal to deal, margin squeezes, predatory pricing, meeting competition, raising rivals' costs, and bundling. He also looks to institutional limitations on the power of the courts to consider efficiencies.

The final Part of the book argues the author's conclusion that s 46 as it now stands may be applicable to large firms simply because they are large firms. It is contended that there is a risk that they will be exposed to liability for conduct which is efficient in the sense that it does not distort the operation of markets. The principal proposition for which the author contends is that a market manipulation approach is to be preferred and that efficiency can be adapted to become a centrepiece of a positive and normative legal theory of market power.

No doubt the author's arguments are contestable and will be contested. They do, however, provide the kind of high level reflection that is necessary for the informed development of competition law and policy in Australia.

PREFACE

Australian competition legislation was amended in late 2017 following a controversial three-year law reform process. This monograph has been in preparation before, during and since that process was completed.

Review of the Australian and overseas literature indicates enduring controversy about market power in Australia and overseas. The author suggests this arises because our legal concept of market power is insufficiently legally determined. The law and policy has been internationally criticised for lacking clear positive and normative standards that would enable us to distinguish between normal competitive conduct and conduct that should be condemned. The monograph covers mainly Australian and EU law, but also compares key points of US and Canadian law on market power. The issue of market power addressed in this monograph is of universal significance for competition laws around the world.

The traditional legal concept of market power as the ability to give less and charge more (or the ability to behave differently than a hypothetical competitive market would enforce) is based on a paradigm of the hypothetical competitive market in which no firm has market power. The author suggests that such a benchmark does not provide a useful standard of conduct in real-world markets. This monograph proposes a new approach to both our conception of market power and the paradigm of competition in which we assess the misuse of market power.

The author proposes that market power can alternatively be related to the response of market demand to firms' price/output decisions, and thus can be legally conceived as the power of the market, which cannot be possessed, but can be *manipulated*. All firms have this power to some degree. The author derives this concept of market power from the correlation between market power and elasticity of demand revealed by well-known analysis of the Lerner Index, which is used to measure market power. This approach is also supported by analogy with laws prohibiting the manipulation of securities markets, which is theorised without the overlay of conflicting welfare objectives and economic efficiency standards that has troubled competition law over a long period.

The author critically examines the assumptions underlying the paradigm of the hypothetical competitive market and suggests that we can alternatively identify a paradigm of competition, more closely resembling real-world competition, in which to assess misuse of market power. This is derived from the conventional description of real-world competition as rivalry for the same object. The author calls this paradigm 'zero-sum', or survival, competition in which one firm's gain is another firm's loss, where firms cannot freely exit the market and so must compete for survival.

When we consider market power as power to manipulate the market, we can distinguish firms' price/output decisions and other decisions which respond to market demand from conduct which manipulates the market, distorting the market's efficient operation. It is proposed that by reconceptualising market power in the context of zero-sum competition and by developing the legal concept of an efficient market from the law prohibiting manipulation of securities markets, we can develop positive and normative standards to frame our legal theory of liability for misuse of market power.

The recent *Harper Review* in Australia challenged conventional thinking that economic efficiency is not a matter that the courts are competent to assess. The *Review* recommended that the statutory provision be amended to require courts to consider the efficiency effects of conduct when applying the test to assess whether alleged misuse of market power causes harm. The current legislative reform in Australia is based on the traditional legal conception of market power and, despite the *Review*'s recommendation, rejects explicit consideration of economic efficiency, so is unlikely to quell the controversy. The author suggests that conventional concepts of economic efficiency cannot be forensically applied and so must be adapted and redefined if we are to apply them in our legal theory of liability. He also suggests that the concept of market manipulation, which distorts the efficient operation of the market, enables us to do this.

The market manipulation theory is tested on the facts of leading Australian cases under past law, using mainly EU, but also US and Canadian law, as a context in order to show what difference the new and proposed laws would make. The monograph compares the application of the market manipulation theory with the *Harper Review*'s recommended approach, which would consider economic efficiency, and the new law as enacted by Parliament, which prohibits conduct of a dominant firm that has the purpose or likely effect of substantially lessening competition.

2

The Mischief and Australia's Institutional Response

I. Introduction

Economic teaching of the 1960s and the following decades in Australia was dominated by the neoclassical model and policy strictures against high industry concentration (ie, few sellers).[1] As we have seen, high industry concentration still seems to be of concern to regulators, and some argue that the purpose of regulating market power is to prevent the maintenance of high concentration.[2] We have also seen that such concerns are associated with the SCP approach, which held that the presence of dominant firms weakens the competitive process, but that economic theory now accepts that competition can function well even with large firms.[3]

In this chapter we examine how SCP thinking still affects the way in which Australian competition law views market power and its misuse, and the division of functions between the courts and the administrative agencies, the ACCC and the ACT.

II. The Continuing Influence of the SCP Approach in Australia

As we will see in Chapter 3, the courts in the US moved away from the position in the 1960s that atomistic competition is to be promoted even at the expense

[1] See, eg, PH Karmel and M Brunt, *The Structure of the Australian Economy* (Melbourne, FW Cheshire, 1966); R Caves, *American Industry: Structure Conduct and Performance* (Englewood Cliffs, Prentice Hall, 1967).

[2] See R Sims, 'Is Australia's Economy Getting More Concentrated and Does This Matter?', speech delivered at the RBB Economics Conference, Sydney, 27 October 2016, www.accc.gov.au/speech/keynote-address-rbb-economics-conference-0; and A Gavil, 'Imagining a Counterfactual Section 36: Rebalancing New Zealand's Competition Law Framework' (2015) 46 *Victoria University of Wellington Law Review* 1043.

[3] See G Niels, H Jenkins and J Kavanagh, *Economics for Competition Lawyers* (Oxford, Oxford University Press, 2011) 180; MS Gal, *Competition Policy for Small Market Economies* (Cambridge, MA, Harvard University Press, 2003) 55.

of efficiency.[4] At the time of writing, the position in Australia seems to be that, while there is no authoritative appellate decision on the point, observations of influential appellate judges suggest they consider that the CCA endorses a more atomistic view of competition.[5]

We have seen that the SCP approach fell out of favour in the US and elsewhere about the time it was being applied in Australian competition law in the 1970s.[6] According to Corones, our courts and the ACCC/ACT still apply a modified SCP approach.[7] For the purposes of this study, structuralist thinking is relevant in four respects. First, under the SCP approach, 'market structure is the primary source of market power'.[8] I suggest that this concept of market power derives from the paradigm of the hypothetical competitive market and can be reconceptualised in the context of zero-sum competition.

Second, the SCP approach provides a chain of causation (under which market structure determines market conduct which determines market performance, ie, efficiency outcomes), which it is said enables inferences to be made about market performance from observations of market structure and conduct.[9] Thus, the ACT in 1976 explained that the 'process of competition' is very much a matter of market structure.[10] However, the ACT has more recently said that this approach has been overtaken by developments in economic theory: market structure does not determine conduct and performance; regard must be had to strategic behaviour.[11] Nevertheless, we still have a situation where the 'process of competition' is a proxy, or surrogate test, for efficiency and market structure is considered to be a key determinant of the process of competition.

Third, we see that the mischief that SCP addresses with respect to market power is that market power is said to maintain high industry concentration and by that means to produce inefficient outcomes. I suggest that we ought to focus on efficiency, as harm to efficiency is the principal mischief which the SCP approach seeks to address. Carl Kaysen and Donald Turner, while advocating the SCP approach, are clear that 'in so far as reduction of market power is incompatible with efficiency', efficiency should prevail.[12]

[4] See, eg, D Evans and K Hylton, 'The Lawful Acquisition and Exercise of Monopoly Power and its Implications for the Objectives of Antitrust' (2008) 4 *Competition Policy International* 203, ssrn.com/abstract=1275431, discussing the famous opinion of Learned Hand J in *US v Alcoa* 148 F 2d 416 (2d Cir 1945).

[5] See *Rural Press* (2003) 216 CLR 53 [49] (Gummow, Hayne and Heydon JJ); *ACCC v Flight Centre Travel Group Ltd* [2016] HCA 49 [141] (Nettle J); compare the observations of the majority in *Melway* (2001) 205 CLR 1 [52].

[6] H Hovenkamp, *Federal Antitrust Policy* (St Paul, West Publishing, 2005) 42–47. See also S Stroux, *US and EC Oligopoly Control* (The Hague, Kluwer Law International, 2004) 10–12; T Muris, 'Improving the Economic Foundations of Competition Policy' (2003) 12 *George Mason Law Review* 1, 3–6.

[7] S Corones, *Competition Law in Australia*, 6th edn (Sydney, Lawbook Co, 2014) 41.

[8] ibid 23.

[9] ibid 23–26.

[10] *QCMA* (1976) 8 ALR 481, 516.

[11] *Application by Chime Communications Pty Ltd (No 3)* (2009) ACompT 4 (hereinafter '*Chime*') [11].

[12] C Kaysen and D Turner, *Antitrust Policy: An Economic and Legal Analysis* (Cambridge, MA, Harvard University Press, 1959) 45.

Fourth, the SCP approach has implications for the forensic determination of competition and efficiency effects. Proponents of SCP consider that market structure and conduct (which the ACT and courts traditionally equate with the 'process of competition') provides the only test which is capable of being administered by the courts.[13] We know the resulting test as the SLC test. Indeed, Kaysen and Turner suggest that neither 'efficiency' nor 'competition' is sufficiently determinate and prefer market structure as the appropriate surrogate test.[14] As we will see in Chapter 3, many theorists believe there is a need for direct measures of competition effects that do not rely on structuralist reasoning.[15] Nevertheless, these doubts about the capability of the courts are shared by influential Australian judges.[16] Thus, the view that courts are not capable of determining economic effects such as efficiency appears to be entrenched in the CCA by virtue of the division of functions between the courts and the administrative agencies, the ACCC and the ACT. The CCA reserves to those agencies the power to authorise conduct which fails the SLC test, but which results in overriding public benefits such as efficiency.[17] The authorisation process has not previously applied to section 46; however, the legislative changes being introduced to implement the *Harper Review* recommendations will allow it.

We will consider efficiency, and how we may forensically determine it, in more detail in Chapter 3. For the present purposes, we may regard the debate about the objectives of competition law, or the original intention of the legislatures, in Australia and overseas as somewhat unproductive. For example, Howard Shelanski notes attempts in the US to resolve the debate about objectives by reference to the presumed legislative intention behind the Sherman Act in the 1890s, and that while efficiency is increasingly recognised in the US as a defence, debate continues over which kinds of efficiencies may be considered.[18] The concern of this monograph is with the *consequences* of the law, and law reform initiatives. It is recognised that conduct which lessens competition may nevertheless be justified because it has efficiency or other benefits. I suggest it is equally important to ask whether our real-world paradigm of competition, zero-sum competition, may produce inefficient outcomes. We may suspect that the key SCP thinkers mentioned in the present chapter would respond to the effect that, if this were the case, we need to re-adjust the way we apply the SLC test.

[13] Corones (n 7) 23, citing E Mason, 'The Current Status of the Monopoly Problem in the United States (1949) 62 *Harvard Law Review* 1280.

[14] Kaysen and Turner (n 12) 59.

[15] See, eg, Muris (n 6) 14.

[16] See, eg, French J in *Australian Gas Light Company v ACCC (No 3)* [2003] FCA 1525 [607].

[17] M Brunt, 'The Australian Antitrust Law after 20 Years: A Stocktake' (1994) 9 *Review of Industrial Organisation* 483, 499. Corones (n 7) 41 says the same in more qualified terms: 'the courts, for the most part, are required to assess the effect or likely effect of conduct or the competitive process without regard to efficiency, except where the efficiencies will have a bearing on the future state of competition in the market'. We will discuss in ch 3 differing views on the latter issue.

[18] Howard Shelanski, 'Efficiency Claims and Antitrust Enforcement', in R Blair and D Sokol (eds), *The Oxford Handbook of International Antitrust Economics* (Oxford, Oxford University Press, 2015) vol 2, 452 at 457.

The remainder of this chapter addresses the institutional division of functions. I suggest that 'efficiency' as we can adapt it for the proposed legal theory is capable of being determined by the courts or at least is no less determinate than the 'process of competition' that is addressed by the SLC test.

III. Australia's Institutional Division of Functions between Courts and Agencies

The precursor to the current CCA was the Trade Practices Act 1965 (Cth). Under that scheme, restrictive trade practices would be reviewed by the regulator and if held by a tribunal to be contrary to the public interest, the tribunal could make restraining orders that were enforceable through judicial process.[19] In a paper assessing the success of Australia's competition law after the first 20 years, Maureen Brunt explains the reasoning behind that approach: in the early days of competition law in Australia, it was unclear to legislators how and why restrictive trade practices might be justified.[20] Clearly, this presumes there may be some justification. Brunt notes that the public interest criterion was retained in the 1974 version of the CCA, deliberately casting a wider net than 'efficiency'.[21]

Brunt appears to favour excluding efficiency from the jurisdiction of the courts on the grounds that the standard of legal liability ought to be 'positive', whereas efficiency raises 'normative' issues.[22] Yet Brunt considers that efficiency may be relevant to section 46 in either or both of the 'taking advantage' and 'exclusionary purpose' requirements.[23] Now, of course, these aspects of section 46 have been removed by the *Harper Review* amendments. Brunt considers that 'legitimate business justification', if read as 'production efficiency … may well have a role in Australian antitrust, despite the presence of authorisation'.[24] As we will see in Chapter 3, Australian courts have subsequently given some credence to legitimate business rationale, without making the connection with efficiency that Brunt contemplates. It may well be that the *Harper* amendments, absent any reference to efficiency following that aspect being removed by Parliament, may raise further obstacles to courts interpreting section 46 in a way that would make efficiency relevant. However, I will suggest in Chapter 3 that there should still be some

[19] R French 'The Role of the Courts in the Development of Australian Trade Practices Law' in F Hanks and P Williams (eds), *Trade Practices Act: A Twenty-Five Year Stocktake* (Sydney, Federation Press, 2001) 103.

[20] Brunt (n 17) 506.

[21] ibid 507.

[22] ibid 510–11.

[23] ibid 512.

[24] ibid. This point is also made by E Mason, 'Market Power and Business Conduct: Some Comments' (1956) 46 *American Economic Review* 471, 479.

causal connection between market power and SLC under the *Harper* section 46, which may open the door to efficiency, though this is not free from doubt.

Brunt goes on to discuss the limits of court-centred competition law, quoting Edward Mason to suggest that courts can only apply competition law if 'valid inferences can be made from relatively simple statements of fact' and that 'an attempt to push enquiry into effects very far is clearly an invitation to non-enforcement'.[25] The reference to valid inferences may well suggest the kind of inferences facilitated by the SCP approach. He observes that how far any enquiry into 'economic consequences' needs to go depends on 'what confidence courts should have in the process of economic analysis'.[26] It is now over half a century since Mason expressed that concern, and Brunt expressed concerns in relation to the Trade Practices Act 1965 regarding the lack of experience with business practices that may be justified. I suggest that by now, we should have greater confidence in the ability of economics and the courts to address the economic consequences of business conduct. I will suggest in Chapter 3 that economic efficiency can be adapted to become the centrepiece of both a positive and normative legal theory of market power.

It seems reasonably clear from Mason's discussion of 'effects' that he uses the term to embrace both competition and efficiency effects which can be revealed by 'economic enquiry'.[27] However, he makes it clear that, in his view, 'we expect from the competitive system a set of effective limitations to the growth of private economic power'.[28] This objective is one that the words of Australia's section 46 (and apparently section 2 of the Sherman Act) manifestly do not contain. Mason acknowledges that 'the importance of efficiency as a desideratum inevitably condemns any purely "limitist" interpretation of antitrust policy'.[29] A few years after Mason published that paper, Carl Kaysen and Donald Turner, while advocating the SCP approach, stated that 'we would discard the general limiting of big business power as an independent goal of antitrust policy'.[30] I suggest it is time to let go of the remaining vestiges of the SCP approach embedded in the CCA that impede consideration of economic efficiency.

A. The Role of the Court

At this point, we need to revisit the views of Robert French (before he became Chief Justice of the High Court) about the objectives of competition law and the role of the courts. He refers to a dimension of competition law being 'the potential

[25] Brunt (n 17) 516–17; Mason (n 24) 478 and 475.
[26] Mason (n 24) 477.
[27] ibid 474–76.
[28] ibid.
[29] ibid 479.
[30] Kaysen and Turner (n 12) 49.

for social engineering of commercial behaviour' which appeals to 'aesthetic sensibilities with the vision of a better world'.[31] Clearly, economists of the SCP school have been greatly concerned by the growth in economic power of big business, though with the rise of globalisation, expressions of concern from the 1940s to the 1960s regarding, eg, the impact of big business on 'village life' may seem quaint today.[32]

French explains the normative role of judges in applying 'standards', eg, due care in torts law, as opposed to 'rules', and suggests that Part IV of the CCA sets out standards that require 'normative and evaluative judgments in their application'.[33] Further, the judicial function is constitutionally limited to finding facts and applying law to determine legal rights and obligations, to be distinguished from executive arms of government such as the ACCC and the ACT.[34] French argues that the kinds of decisions involved in authorisation matters, such as public benefit or efficiency issues, are beyond the constitutional or institutional competence of the courts.[35] In a subsequent judicial role on the Federal Court, French J describes authorisation proceedings as involving 'polycentric decision-making of a kind which the Court is not institutionally competent nor authorised by statute or the Constitution to undertake'.[36] Polycentric decision-making connotes discretionary decision-making, which may require trading off competing objectives. This is ordinarily associated with public interest functions of the executive branch of government as distinct from judicial functions of the courts under the rule of law.[37] French also considers that neither the courts nor the regulators are equipped to micro-manage business decisions of market participants, eg, terms of supply in refusal to supply cases under section 46.[38]

French's remarks relate specifically to authorisation proceedings, ie, concerning the administrative discretion of the ACCC/ACT to authorise conduct that would otherwise contravene Part IV of the CCA. These do appear to involve polycentric decision-making. However, we might ask why this is so. I suggest it may be because conventional components of economic efficiency such as productive and allocative efficiency are not congruent objectives under conditions of imperfect competition. Further, as we will see, authorisation proceedings permit consideration of broader public interest factors than economic efficiency.

[31] French (n 19) 98.

[32] See, eg, EAG Robinson, *Monopoly* (Cambridge, Cambridge University Press, 1941) 183–90; Karmel and Brunt (n 1) 55.

[33] French (n 19) 105.

[34] ibid 107.

[35] ibid 108.

[36] *Australian Gas Light Company v ACCC (No 3)* (2003) 137 FCR 317 [607].

[37] See, eg, C Finn, 'The Justifiability of Administrative Decisions: A Redundant Concept?' (2002) 2 *Federal Law Review* 239. An example would be a ministerial declaration under the access regime in pt IIIA of the CCA: see, eg, *The Pilbara Infrastructure Pty Ltd v ACT* (2012) 246 CLR 379, [2012] HCA 36.

[38] French (n 19) 108.

Clearly, in some legal contexts, courts are familiar with the type of evaluative process that involves weighing up factors that may point in different directions. To give one example, the statutory prohibition of unconscionable conduct spells out a number of factors that the court must consider when it determines whether conduct is unconscionable (formerly in Part IVA of the CCA, now found in s 22 of the Australian Consumer Law). Thus, while Brunt considers efficiency to have normative or evaluative implications, the courts are able to undertake such tasks in some legal contexts. However, there may well be a limit to which a theory of legal liability can embrace polycentricity. We might speculate whether the problems that have been encountered with the theory of liability for misuse of market power under past law arise from undisclosed issues of polycentricity, such as differing views about the economic and non-economic objectives of competition law or differing views about conflicting standards of welfare or efficiency. The same issues could well apply to the new section 46 as recently enacted. Suffice to say that the criticisms made by French J of polycentric decision-making as a judicial function would not appear to raise any impediment to a unicentric legal theory of liability, which is the focus of this monograph.

I will argue in Chapter 3 that the determination of issues of efficiency, as we can adapt and redefine it for the purposes of our legal theory, can be seen to be no more than traditional fact-finding and need not involve weighing up offsetting competition and efficiency effects, if we accord primacy to efficiency as a higher-order objective of competition law.

B. The Role of Administrative Agencies

We do not address here questions of constitutional law which concern the validity of laws conferring broad, even polycentric, decision-making powers on administrative agencies.[39] Nor do we address questions of constitutional and administrative law concerning the valid exercise of such powers. It seems that there is no constitutional barrier to Parliament conferring power on agencies to make polycentric decisions, even though (by definition) the outcome of such decisions cannot be predicted with certainty.[40] However, it is recognised that regulatory uncertainty creates risk for business and adds to the costs of regulation.[41] For the purposes of the present study, we will assume, without further consideration, that the authorisation process set out in the CCA is constitutional. Our enquiry considers whether a broad public interest test, which does not clarify the priority to be given to efficiency, may have undesirable *consequences* because it is unpredictable.

[39] See, eg, L Crawford, 'Can Parliament Confer Plenary Executive Power? The Limitations Imposed by Sections 51 and 52 of the Australian Constitution' (2016) 44 *Federal Law Review* 287.

[40] ibid 296–97.

[41] See, eg, Oxford Economic Research Associates, *Costs and Benefits of Market Regulators, Part 1: Conceptual Framework*, report for Dutch Ministry of Economic Affairs, October 2004, 16.

To pursue this enquiry, we can draw on the study by Vijaya Nagarajan of authorisation decisions by the ACCC/ACT under the CCA in the period from 1974 to 2010.[42] Nagarajan finds that authorisation decisions have been justified on wide-ranging public benefit grounds, and consequently principles have not yet emerged to elucidate the role of efficiency.[43] Clearly, there are issues about assessing efficiencies, which remain to be resolved, though we may conclude that mere transfers of surplus do not generate value for society.[44] It appears that protection of small business has been accepted as a public benefit, though this may not be consistent with efficiency.[45]

I suggest that the authorisation process recognises that efficiency is a higher-order objective than the pursuit of competition. Thus, conduct which would be anticompetitive and a contravention of the law can be excused by the administrative agencies (but not the courts) if efficiency benefits result. However, it is not clear whether the CCA gives priority to efficiency over other public interest factors, eg, equity. Presumably by not mentioning efficiency, the CCA fails to give it priority.[46] We saw in Chapter 1 that it may be doubted whether competition law is a suitable vehicle to address equity, since markets work by excluding producers and consumers based on cost-efficiency and ability to pay respectively.

We may thus question whether authorisation should be possible on non-economic grounds (or at least whether they should be allowed to prevail over efficiency) and whether the competition agencies are appropriately placed to undertake that assessment. Does the CCA authorise administrative agencies to, eg, sacrifice productive efficiency (national income) in order to redistribute surplus to consumers (or small business) in a particular market? That is, does the CCA contemplate authorising conduct that may be inefficient yet arguably justified on public interest grounds, such as redistributive equity? Those who argue that the objectives of competition law include distributive equity would presumably answer in the affirmative. However, I suggest that it is not obvious that the

[42] V Nagarajan, 'The Paradox of Australian Competition Policy: Contextualising the Coexistence of Economic Efficiency and Public Benefit' (2013) 36 *World Competition* 133.

[43] ibid 161–62. Curiously, Nagarajan (at 144) classifies 'promotion of competition in industry' as an efficiency justification for anticompetitive conduct.

[44] ibid 142.

[45] ibid 148. Gal (n 3) 49 rebuts the argument sometimes put forward that even inefficient competitors provide increased consumer choice; see also *TPC v Email Ltd* (1980) 31 ALR 53, from which we might infer that an inefficient competitor provides no effective competition or real choice. However, the European Commission, 'Guidance on the Commission's Enforcement priorities in Applying Article 82 EC Treaty to Abusive Exclusionary Conduct by Dominant Undertakings' [2009] OJ C45/7 [24] expresses the view (which is not elaborated) that 'in certain circumstances a less efficient competitor may … exert a constraint' on dominant firms. D Geradin, A Layne-Farrar and N Petit, *EU Competition Law and Economics* (Oxford, Oxford University Press, 2012) [4.149]–[4.150] describe this approach as 'regrettable', since it appears to protect less efficient competitors and thus creates uncertainty.

[46] Brunt (n 17) 507 notes that the Commonwealth of Australia, *National Competition Policy* (Australian Government Publishing Service, 1993) (hereinafter '*Hilmer Report*') 121 recommended that efficiency should be recognised as the primary consideration in authorisation matters, though the availability of other public benefits was not opposed. However, this has not been implemented.

CCA does or should confer that authority on the competition agencies. Greater certainty would be provided if the legislation expressly gave guidance on priorities.

We might also ask whether the CCA contemplates authorising conduct which is competitive (ie, there is no anticompetitive harm) but inefficient. We will see in Chapter 3 that this is not something that competition law generally contemplates;[47] nevertheless, we must confront inefficiency when we analyse the consequences of zero-sum competition.

On the basis of Nagarajan's study, I suggest that the administrative processes contemplated by the CCA have not tended to develop principles of economic efficiency by which we can predict with reasonable certainty whether conduct which is anticompetitive may be excused from the consequences of contravening the law. This issue has not previously been addressed in Australia with respect to market power, but the *Harper Review* amendments have made it a live issue.

IV. Institutional Arrangements in the EU and the US: Court-Centred or Agency-Centred?

We can note here some views from the EU and the US that are pertinent to our institutional framework. Dirk Schroeder argues that:

> Predictability is a key factor if competition law is not to restrain unduly legitimate economic activity. Predictability is created through effective judicial control and the development of transparent and generally applicable tests.[48]

We will discuss the trend in the EU towards a more economic evaluation of dominant firm conduct in Chapter 3. Schroeder argues that 'a shift from a form-based to an effects-based approach' means that we must 'openly admit that economic assessment is part of applying the legal rule'.[49] I agree, and suggest further that experience indicates that, over time, administrative functions must develop transparent and generally applicable principles in order to gain community respect. For example, the modern equitable jurisdiction of our courts began as an administrative exercise of discretionary practical justice, which over a period of 500 years morphed into a court with settled principles and precedents.[50] This experience also demonstrates that the divided jurisdiction of the common law courts and courts of chancery was a continual problem until the fusion of jurisdictions, which occurred in Victoria in 1883.[51]

[47] The possibility is briefly noted by Nagarajan (n 42) 159.

[48] Dirk Schroeder, 'Normative and Institutional Limitations to a More Economic Approach' in J Drexl, W Kerber and R Podszun (eds), *Competition Policy and the Economic Approach: Foundations and Limitations* (Cheltenham, Edward Elgar, 2011) 279, 280.

[49] ibid 283.

[50] See, eg, M Evans, *Equity and Trusts* (Chatswood, LexisNexis Butterworths, 2012) 4–10.

[51] ibid 11.

Hylton discusses the US 'court-centred' process, which he contrasts with the EU 'agency-centred process'.[52] He argues that prosecutorial and adjudicative functions should be separated, as is the case in the US system, because it is only in the court-centred process that 'evidence and arguments [adopted by agencies] are subjected to a rigorous and independent evaluation of merit'. We will see in Part II that this argument may well be applicable to the CCA's dual prosecutorial and administrative 'authorisation' roles.

Hylton also argues that the development of monopolisation law in the US by common law method is a strength of the US system and is to be preferred to the EU system of agency-led development.[53] This may be contrasted with the way in which section 46 has developed in Australia through a cycle of enforcement failure and subsequent legislative amendment (briefly summarised in the Appendix to this monograph addressing the legislative history of section 46). However, the Australian legislation is very detailed and prescriptive, unlike the US equivalent, which means that there is not the same scope for Australian courts to develop section 46 of the CCA by common law method as there may have been in the US. In any event, I suggest that the development of the law by judicial law-making using the common law method is a slow and erratic process, and that legislative amendment to clarify the role of efficiency would be preferred.

V. Conclusion

In the 40 years since competition law was enacted in Australia, there has been significant change in the fundamental ideas of economics and law around the world. Policy debates continue in Australia and overseas about the interpretation and application of section 46 and its corresponding provisions. However, the implications for our concepts of 'market power', 'competition effects' and 'efficiency effects' (which are still influenced by SCP thinking) remain to be addressed. Certainly, the *Harper Review* did not address the implications. This study addresses these issues and proposes that the courts should be capable of determining issues of efficiency as it can be adapted and redefined for the purposes of the market manipulation approach proposed by this study.

I suggest that our institutional framework is a legacy of the 1960s, when the legal approach in Australia regarded the essential issue as one of policy, based on weighing up public interest factors, ie, an executive or administrative function rather than a judicial function. Under our system, actions for penalties and civil damages are prosecuted in the courts (as they must be for constitutional reasons).

[52] K Hylton, 'Antitrust Enforcement Regimes' in R Blair and D Sokol (eds), *The Oxford Handbook of International Antitrust Economics* (Oxford, Oxford University Press, 2015) vol 1, 17 at 29.

[53] ibid 27–28, pointing out that the Sherman Act says relatively little, and the law has effectively been developed by the courts.

I suggest that it would be undesirable for the courts to continue to be excluded from determining efficiency issues that are recognised internationally to be relevant to misuse of market power and that could be raised in authorisation proceedings.

The recommendation of the *Harper Review* to include express reference to efficiency in the *Review*'s proposed section 46(2) is to be welcomed. However, had it been enacted, it would have raised difficult conceptual and forensic issues for the courts. These issues are addressed in the present study.

In the next chapter, drawing on experience in the EU, the US and Canada, we will develop our understanding of the relationship between 'competition effects' and 'efficiency effects' in connection with market power under the paradigm of zero-sum competition. We will contrast the current section 46 'purpose' test, the *Harper Review* section 46 modified SLC test and the market manipulation approach which looks to actual efficiency effects in the market. We will see how economic concepts of efficiency and legal concepts of an 'efficient market' derived form securities markets manipulation laws can be used or adapted for the purpose of the legal theories examined in this monograph.