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TUE FUTURE OF COMPETITION POLICY

Speech given by

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1. INTRODUCTION

I will begin with some comments on the Government's records deliberations.

2. AN ERA OF CHANGE FOR THE TRADE PRACTICES COMMISSION

On my appointment as Chairman of the Trade Practices Commission some people have asked what changes I intend to make at the Trade Practices Commission. Let me say from the outset that I did not arrive at the Commission with preconceived plans to make major changes. I think the TPC does a good job applying a basically good Act.

Nevertheless there will be major changes in the Trade Practices field in the next five years whilst I am Chairman because of changes in the economic environment and in general policy attitudes rather than because of the impact of any individuals. I will talk more about this as the speech develops.

The emphasis on the need for competition policy has been growing in recent times; the most recent being the Government's Industry Statement of March 12 entitled 'Building a Competitive Australia'.

A further indicator was the fact that the Business Council of Australia held a Summit Meeting in February 1991 on the theme of Australian competitiveness.

More generally there has been growing recognition around the world amongst business people, policy makers and researchers that competition is the key to economic growth, innovation and the dynamism need in today's world. In Australia, the promotion of competition is the key to most markets needing microeconomic reform.

3. WHAT IS COMPETITION POLICY?

But just what does competition policy mean? It is far wider than trade practices legislation. It encompasses a wide variety of policies such as trade, foreign investment and tax policies and the whole range of other policies affecting the general economic environment and ultimately affecting the general climate of competition in the country. These include such things as small business policy, intellectual property policy, the legal system, public and private ownership, contracting out, bidding for monopoly franchises and prices policy as a complement to competition policy.

Moreover, there is a range of areas of policy making where it is important to recognise that competition can contribute to the achievement of wider objectives of policy than just economic ones. A good example is our media policy where one objective is diversity. One of the keys to diversity is to have a competitive media sector. Whether or not this is sufficient is currently under consideration by the Lee Inquiry.

In Australia, the cornerstones of competition policy are our international trade policy and the Trade Practices Act 1974.

4. PRIORITIES OF COMPETITION POLICY

National competition policy priorities must be influenced by the fact that there is now a program of gradually reduced protection. In addition the exposure of Australian business to international competition grows every day. Accordingly the Commission believes that the priorities of competition policy should switch more than in the past to those parts of the economy not engaged in international trade. This does not mean of course that the TPC will fail to enforce the Trade Practices Act vigorously in every sector including the internationally traded goods and services sector, but the priorities may need to move more into the domestic sector. The domestic sector includes not only areas currently covered by the Act but also numerous exempt areas adverted to by the Prime Minister in his Industry Statement in March 1991 e.g. public enterprise, Statutory Marketing Boards, the professions, other areas currently exempt from the Trade Practices Act particularly as a result of the fact that they are unincorporated enterprises engaged in intrastate trade. I come back to this point later.

It is nevertheless the Commission's intention to continue its firm enforcement of the anti—competitive provisions of the Trade Practices Act in all of its established fields of operation. Any agreements between competitors to fix prices will be vigorously prosecuted and will soon be helped by higher fines. The Commission will continue its role in seeking compliance with the Act through other actions as well, such as information campaigns, industry-specific guidelines and codes of conduct.

5. THE TRADE PRACTICES ACT - CHARACTERISTICS AND PRINCIPLES

The objective of the Trade Practices Act is to ensure Australian consumers, both business and domestic consumers, have the widest range of goods and services to choose from and at the highest quality and lowest possible price. To this end the Act seeks to foster a competitive, efficient marketplace that is freed of anticompetitive and unfair trading practices by corporations and others.

Through the administration of the Trade Practices Act, the Commission has a responsibility to foster both competition and fair trading. Today I shall discuss the competition provisions of the Act, as I want to do a separate speech later on consumer protection. The Act prohibits:

- price agreements between competitors and other agreements which substantially lessen competition
- resale price maintenance, in which individual suppliers seek to force distributors to charge fixed prices for their products
- misuse of market power, where a firm uses its market power in order to damage a competitor or prevent a firm entering the market
- some exclusive dealing arrangements which substantially lessen competition
- price discrimination which is likely to substantially lessen competition

- mergers that result in market dominance or enhancement of market dominance.

The Trade Practices Act is largely governed by two simple principles.

- Any actions which substantially lessen competition in a substantial Australian market should be prohibited under the Act.
- Such actions should be able to be authorised by the Trade Practices Commission (and on appeal to the Trade Practices Tribunal) if they can be demonstrated to be in the public interest.

These two principles apply generally in most parts of the current Trade Practices Act but mergers are a notable exception as I discuss later. Apart from mergers, however there are numerous lessor deviations from these two principles.

The Commission believes that there could be a case for moving towards simplification of the Trade Practices Act. At present Part IV of the Act is quite long and complex. It contrasts with the simplicity of the Sherman Act in the USA and of Sections 85 and 86 of the EEC Treaty. The present Act with its complexities tends to distract attention from the key economic requirements of competition policy. It may not be particularly suitable for the process of microeconomic reform in coming years where the policy requirements could prove to be a little different from those involved in the application of the Act to other sectors. There are also possible difficulties in some parts of the Act for example Section 46 may open up some difficulties with the present wording. Some of the prescriptions in the Act such as those prohibiting resale price maintenance outright do not accord with modern economic thinking. The US courts have moved away from a strict ban on resale price maintenance and have regarded it as legitimate in certain circumstances and there could be some scope for this to happen in Australia.

The kind of simplification that the Commission has in mind is that Part IV would be replaced by two principles:

1. That any behaviour which has the purpose or affect of substantially lessening competition in a (substantial) market should be prohibited.
2. Such behaviour should be able to be authorised on the basis of the current authorisation tests.

We have done some preliminary inquiries in the legal arid business world and at this stage have not found strong opposition. Rather the attitude is that the idea is well worthy of consideration but people would like to think about it. The Commission itself is considering the idea as a possible long—term target. It might be possible to relate any future amendments to the Act to these two principles — and at a later stage achieve a general simplification.

6. EXEMPTIONS FROM THE ACT

Although the Prime Minister describes the Trade Practices Act as *"our principal legislative weapon to ensure that consumers get the best deal from competition"*,[1] it does not apply to some of the most important areas of the economy - areas in which there are potential for large gains from the greater efficiency resulting from competition.

There are a number of sources of immunity from the Act:

- The Shield of the Crown doctrine affords immunity in certain areas of Government activity, mainly at State level.
- Generally, the Act applies only to corporations, and to other enterprises engaged in interstate trade and commerce, and not to unincorporated enterprises operating intrastate.

[1] Prime Minister, 12 March 1991, Building a Competitive Australia

- Section 51 makes legislative exceptions primarily in respect of:
    - matters relating to remuneration etc. of employees;
    - standards approved by Standards Australia;
    - certain clauses concerning termination of partnerships, goodwill, as well as certain contracts of service;
    - certain export arrangements;
    - certain patent, trademark and copyright laws; and
    - very importantly matters specifically allowed for by Federal or State law.
- There is also provision for Commonwealth government exemptions by regulation under s.172. These have been mainly for the marketing of primary products.

In the Prime Minister's 12 March Statement he made particular reference to the "*many areas of the Australian economy today that are immune from [the] Act: some Commonwealth enterprises, State public sector businesses, and significant areas of the private sector, including the professions*". The Prime Minister said "*This patchwork coverage reflects historical and constitutional factors, not economic efficiencies: it is another important instance of the way we operate as six economies, rather than one*".

The benefits for the consumer of expanding the scope of the Trade Practices Act could be immense: potentially lower professional fees, cheaper road and rail fares, cheaper electricity.

Years ago in 1977 the Swanson Committee said:

> "We believe it to be extremely important that the Trade Practices Act should start from a position of universal application to all business activity, whether public sector or private sector, corporate or otherwise".

The Commission agrees and considers, in principle that the Act should have universal reach. In recent years it has drawn attention to its limited coverage and the consequent adverse effects on the economy, as well as the associated inequities and anomalies. At present the Act, although the cornerstone of competition policy does not apply to some of the most important areas of the economy — areas in which there is potential perhaps the greatest potential for large gains from the greater efficiency resulting from competition.

7. COMMERCIALISATION, CORPORATISATION, PRIVATISATION AND DEREGULATION

I recently visited East Europe and curiously found that there were some lessons and parallels for Australia despite the vast differences between the economies. It has been recognised in all these countries that there needs to be an appropriate competition law and some measure of price regulation in certain cases. If this does not happen then as privatisation occurs public monopolies will simply be replaced by private monopolies which are just as prone to operate inefficiently and to exploit consumers.

I discussed with policy makers whether traditional anti—trust and trade practices legislation would be appropriate in East Europe. The answer seemed to be that it was a necessary but not sufficient condition in their circumstances.

In East Europe the inherited structure of enterprises in an industry is highly monopolistic. For example it seems that in Czechoslovakia at present there is a monopoly or near monopoly in nearly every sector of the industry. Consequently a key requirement of competition policy in those countries is to try to break up enterprises, both horizontally and vertically, at the very outset of the privatisation process so that they will compete with one another. In countries like Australia the emphasis of these laws is on preventing anti—competitive conduct. The law does not try to change structures (e.g. by divestiture) only behaviour.

There is a debate occurring in these countries on the issue of "deconcentration". What is interesting, however, is the general recognition that the initial steps taken in establishing industry structure will have a crucial bearing on how well competition works. Deconcentration is not a feature of anti—trust laws in capitalist countries. The conventional competition laws of the West are not very useful in this regard.

While I do not advocate such deconcentration or restructuring for established areas of TPC operation, I think it is an issue we will have to think about here as we start to move into new areas of microeconomic reform especially those undergoing corporatisation, privatisation and the like.

It is worthwhile noting that the recent draft OECD "Synthesis Report on Competition Policy and Deregulation" suggested the first lesson to be learnt from the experience of regulatory reform within OECD Member countries is that wherever possible; restructuring should precede deregulation or privatisation. *"The purpose of deregulation and privatisation should be to pave the way for competition to emerge, and the most effective means of ensuring that it does so is to create market and industry structures that are competitive. …. Such restructuring can be desirable even where local or regional natural monopolies would remain by ensuring that the performance of the resulting firms in the industry can be compared".*[2]

I shall return to this subject in a moment when talking about micro economic reform developments in Australia.

8. CHANGES IN POLICY

Thus over the next five years there will be major changes.

The first area of change will concern microeconomic reform. There will be strong demand for the application of competition policy and in particular the Trade Practices

[2] OECD. Synthesis Report On Competition Policy and Deregulation, Section 7, Paris: May 1991.

Act to a neither of areas which have not hitherto felt the pressure of competitive policy or the Act to any great extent. Already the TPC is active in areas like the waterfront, coastal shipping, towage and aviation.

Secondly, the Special Premiers Conference is considering the possible removal of the Section 51 exemptions insofar as they limit the application of Trade Practices Act to the States. Most relevant is the area of State public enterprises: electricity, gas, water, etc. Some other important areas affecting the cost of living such as the professions, marketing boards and a range of other areas are largely shielded from the Trade Practices Act. Note that State legislation establishes monopoly power and entry barriers in these areas and that removal of exemptions from the Trade Practices Act may be necessary but not sufficient for there to be competition, efficiency and lower prices.

In a recent valuable report addressing energy generation and distribution sectors, namely, electricity arid gas, the Industry Commission made radical and far reaching recommendations (which go far beyond what could be achieved merely by removal of the exemptions from the Trade Practices Act). The proposals include the speedy corporatisation of all (and later privatisation) of most parts of these industries; drastic regulatory change; and promotion of greater competition.

The Industry Commission has also made radical recommendations of a similar flavour in its more recent draft report on rail transport.

In its report on statutory marketing arrangements for primary products, the Industry Commission's report called for a wholesale reassessment at State, and where appropriate, national levels of statutory marketing authorities with a view to their deregulation and privatisation, and subject to the Trade Practices Act. It has also called, here and elsewhere, for freeing up of interstate trade.

In a number of other countries, including the United Kingdom, New Zealand and the United States, professional regulation has been under review, and particular emphasis has been placed on exposing the professions to increased competition.

The Trade Practices Commission announced in 1988-89 that it would conduct a research study of the impact on competition of professional regulation in Australia. The Commission will continue its study into the various professions and I encourage informed debate on the many competition issues which are sure to arise.

Third, another issue, perhaps less far reaching, stems from the release of the background paper by the TPC examining the relationship between intellectual property rights and the Trade Practices Act. A number of sections of the Trade Practices Act potentially may impinge on the usage of intellectual property rights e.g. Sections 45 (arrangements restricting or affecting competition), 46 (misuse of market power), 47 (exclusive dealing) and 49 (price discrimination). There may be a need for a review of the proper scope of the intellectual property exemptions from the Trade Practices Act. I do not see a need for fundamental change here, but some modifications could occur. Copyright laws for example are an important means of preventing the unlawful use or abuse of intellectual property, and I support them, but what I find concerning is that the import restrictions attached to these laws are used to stifle legitimate competition, inflate prices and create a monopoly situation at least in the areas of books and records.

Thus the economic and political environment in which competition policy is being formed is in a state of active debate and many changes lie ahead. As a consequence, I envisage the priorities for the Commission will also have to change sooner or later with a greater focus on competition issues in newly privatised or corporatised enterprises.

9. MERGER PROVISIONS AND THE ACT IN GENERAL

Competition policy in Australian is an evolving one and it is heartening to see recent proposed amendments to increase penalties for Part IV of the Act of up to $10 million for corporations and up to $500,000 for individuals. The proposed prenotification of mergers to the TPC is another welcome move which will enable the Commission to give proper consideration to a merger transaction before it is carried through.

No doubt it will be apparent from n talk that changes in mergers laws are not the Commission's top priority. Nevertheless, the issue has arisen because of the Cooney Inquiry.

As we have pointed out there is an inconsistency between the merger provisions and the remainder of the Act. The Commission is puzzled as to why Governments having accepted the principle that any competitive behaviour that substantially lessens competition should be prohibited unless authorised the Act has not carried over this principle into the field of merger policy. It would seem to the Commission in principle that any merger which substantially lessens competition should also be prohibited unless authorised. By definition a merger between two competitors which substantially lessons competition means almost certainly that they can raise prices significantly. Such mergers should be examinable.

In coming years with the emphasis on the need for microeconomic reform and competition throughout the economy including in the non traded goods sector the Commission believes that the current merger test is inappropriate.

The test 'substantial lessening of competition' is compatible with mergers in the traded goods sector provided that the term 'competition' is properly interpreted by the courts to include international competition, eg from imports. Moreover, Australia's Trade Practices Act has unique authorisation provisions enabling mergers which substantially lessen competition to occur if it can be demonstrated that the public benefit exceeds any detriment to competition.

The present test is that a merger is only prohibited if it leads to or strengthens 'dominance'. 'Dominance normally refers to a situation in which one firm has a majority of the market including imports. Other mergers (say they reduce the number of firms from four to two) cannot normally be examined. Dominance' is interpreted more restrictively in Australia than in Europe.

The present test means that the ultimate restrictive trade practice - the merger of two rivals -- may not be scrutinised whereas an anti-competitive arrangement between them as two separate entities (eg an agreement to fix prices) would contravene the Act unless authorised.

An important lesson to be learnt from the experience of regulatory reform within OECD Member countries is according to the OECD that *"competition authorities should be particularly vigilant in their implementation of merger policy"*[3]. It has been the experience of OECD countries that merger activity becomes prominent in the period following deregulation. These mergers, *"like mergers in any sector, will need strict scrutiny by competition authorities to ensure that they are not anti competitive"*.

It is worth noting the view of the Harvard University economist, Michael Porter, in his recently published book "The Comparative Advantage of Nations"[4]

> *Deregulation and privatisation on their own, however, will not succeed without vigorous domestic rivalry. That requires, as a corollary, a strong and consistent anti-trust policy.*
>
> *A strong anti-trust policy - especially for horizontal mergers, alliances, and collusive behaviour - is fundamental to innovation.*

[3] ibid

[4] Porter, Michael, The Comprtitive Advantage of Nations as reprinted in *The Australian Financial Review*, July 17. 1990. ppl4.

> *While it is fashionable today to call for mergers and alliances in the name of globalisation and the creation of national champions, these often undermine the creation of competitive advantage.*
>
> *Real national competitiveness requires governments to disallow mergers, acquisitions and alliances that involve industry leaders.*

Professor Michael Porter of Harvard has also pioneered research which shows that the key to international competitiveness is competitiveness in the home market. This contrasts with the older view that to establish monopolies or restrict competition in the home market was the best way of promoting exports. If firms cannot compete at home, they will not be able to withstand more vigorous competition overseas.

The TPC expressed concern that a substantial number of important mergers in recent years had not been able to be properly examined by the Commission or the courts despite their substantial effects on competition. The TPC submission to the Cooney Inquiry cites a large number of examples including News Ltd/Herald & Weekly Times, Coles/Myer, Ansett/East West Airlines.

The need for mergers if Australian industry is to be internationally competitive has often been cited as a reason for Australia's relatively weak merger test.

In fact, the weak test has been used as a shield enabling anti competitive mergers in those large parts of the Australian economy not exposed to international competition. An uncompetitive domestic sector loads high costs on to sectors of the Australian economy involved in international trade and thereby actually hinders international competitiveness.

In coming years with the emphasis on the need for microeconomic reform and competition throughout the economy including in the non traded goods sector the current test is inappropriate.

There is limited scope under the Act to do anything about a merger once it has taken place. This is because there are no divestiture provisions under the Trade Practices Act (divestiture powers enable the breaking up of an established monopoly). Hence it is important that any mergers likely to substantially lessen competition should be carefully examined given their irreversible character.

A similar test to the one recommended by the Commission applied from 1974 to 1977. In those early years of the Trade Practices Act when policy makers were on a learning curve the test may have held up some mergers which would otherwise have occurred but 17 years later with far more experience these difficulties are not likely to reoccur. Also, in that period, the test applied to all markets. Today it only applies to "substantial markets".

An extended merger test would also enable more 'sensitive' mergers (eg regarding the media) to be examined by the TPC than at present. There seem to be a growing number of sensitive areas e.g. oil, civil aviation, telecommunications, broadcasting.

10. PROPOSED TPC/PSA MERGER?

You are probably aware that the government is considering the possibility of a merger between the TPC and PSA.

In my view the TPC and the PSA are twin arms of competition policy. From a purely practical perspective, there has been quite a heavy overlap of enquiries between the two organisations into such areas as the oil industry, the waterfront, coastal shipping, towage and aviation. This overlap is not due to some administrative oversight but due to the intrinsically overlapping nature of the work of the two bodies. On each

occasion the enquiries by both the organisations have been essentially concerned with similar issues of competition.

However, any merger decision is one for the government to make.

The possible benefits from closer coordination and integration are rather obvious. But an important longer term point concerns the possible role of competition and prices policy in regard to areas such as public utilities areas as they face commercialisation, corporatisation, privatisation, liberalisation, deregulation and all that! In coming years these areas will undergo a transition. Ideally they will undergo a transition from having a high degree of market power with ability to raise prices at consumer expense to a situation where they are mainly governed by competition. This transition may take many years in some cases.

In these circumstances someone will need to keep an eye both on competition and prices. Whether the latter takes the form of price regulation, price surveillance, price monitoring or some other form is rather unclear at this stage.

There are, however, a number of important institutional options. Should prices and competition questions in these cases be dealt with at a State level or federally? Or by some combination of Federal and State authorities on an interim basis with a long term view to dealing with those matters nationally?

Should these issues be dealt with by an industry specific body or should they be dealt with by a general body spanning a number of industries?

In the UK contrary to popular impressions the regulatory industry including the prices regulatory part thereof is flourishing. There is an OFTEL, OFGAS, OFELEC, OFWATER and possibly more to come. These bodies regulate prices and certain

aspects of competition in these industries (telecommunications, gas, electricity and water) as they become privatised.

In Australia if we do this we face the spectre of having industry specific bodies at state level, e.g. WAOFGAS, VICELEC and so on. There is quite a strong case for having a national approach particularly as the industries are becoming national and as there are considerable benefits as well as administrative economies of scale in the national approach.

Let us suppose that one agrees that there should be a national approach. Should there be a national regulator of all those industries? I am not keen on the idea of having a separate national regulator. I believe that it would be better to locate the regulator in a competition body. When regulatory bodies are left on their own they can develop a tendency to pursue their own goals at the expense of the important long term goals of the promotion of competition. From this point of view I see longer term merit in a possible merging of the Prices Surveillance Authority into the larger Trade Practices Commission so that the proper balance is struck between competition and prices policy.

I admit that this is a consideration relevant to the longer term and possibly not a decisive factor in the immediate issue of whether there should be a merger between the TPC and the PSA. But I believe that it is an issue we shall have to address before very long irrespective of the Government's final decision on a TPC/PSA merger. There are some important federal issues here and I merely point out at this stage that with the Prices Surveillance Act there is not power to look at state prices and no one is seeking this power but it could become relevant for states to consider in coming years as to whether they would refer such prices to a national body as part of a corporatisation/privatisation package.

11. RESOURCES

No doubt you will we wondering what my view is concerning the resources available to the Trade Practices Commission. At this early stage of my Chairmanship I do not wish to take a particularly strong public stand on the issue until I have a better feel for the situation. At this stage I know that there have been no important trade practice cases in the last few years that the Commission has been unable to pursue because of lack of resources. In other words whenever an important case has arisen the TPC has pursued it and where necessary has applied to the

Government and always received the resources it needed. There has been a significant increase in the real resources made available to the TPC in recent years. It seems that a few lawyers may have been unwilling to work for the Trade Practices Commission at the general government rate paid to barristers but I understand the standard of lawyers engaged by the TPC has been generally excellent and certainly quite a number of Australia's top QC's have worked for the Commission in important cases in recent years.

My own impression at this stage nevertheless is that the TPC is somewhat overstretched but there are quite a few government organisations in this position.

What is even more important and extremely clear is that if the Commission is to carry out new and more important roles in the government's microeconomic reform proposals it will need additional resources.

I might add that I see a TPC/PSA merger as enabling some improvements in regard to resource utilisation.

12. THE MEDIA POLICY

The Trade Practices Commission believes there should be a strengthening of Australia's merger laws to enable all major newspaper mergers to be examinable by it.

The media industry is characterised by a strong economic drive to increased concentration.

Economies of scale in producing newspapers and in operating groups of newspapers rather than individual newspapers, together with the difficulty of establishing new newspapers in markets where there are established newspapers, has led to a high rate of merger activity with undesirable side effects on the degree of competition within the industry and with consequent restrictions on the diversity of opinion that should be possible in a democratic society.

The current weak "dominance" merger test was a factor enabling the News Limited/Herald and Weekly Times takeover to occur.

Had the test been 'substantial lessening of competition' the whole merger would have been examinable.

There are at least two options possible. The first was to tighten the merger test across the board in its application to all industries. Under this test any merger which substantially lessened competition in a substantial market could be examined in public interest terms by the TPC.

An alternative would be that all major newspaper mergers should be referred to the TPC irrespective of the competition or dominance test and could be examined by the Commission.

Approach to Fairfax bids

I wish to outline the TPC approach to bids for the John Fairfax group.

It seems unlikely that the AIN and O'Reilly bids, as currently structured, would raise any trade practices issues at all.

In the case of the Tourang bid there are two key questions

first, whether Consolidated Press Holdings controls or significantly influences the Tourang consortium, and

second, whether a successful bid would give Consolidated Press Holdings dominance or enhanced dominance of any market.

A fundamental issue, as in all trade practices cases, is the definition of the relevant market.

This is not clear cut. At one extreme it could be regarded as the entire media market, including the electronic media, or as narrowly as the market for business publications. Other intermediate possibilities include the advertising market across all media or in particular sectors.

If the Commission considers the acquisition would lead to dominance of a market, it could challenge the acquisition in Court.

In this particular case the TPC would have to **prove** in Court both that there was both control by CPH and that this led to dominance of a market.

The TPC has held discussions with Tourang's Managing Director, Mr Trevor Kennedy, and Tourang had supplied information about the way its bid is structured.

However the TPC has not yet reached a firm conclusion on the control question.

The TPC is working as closely as possible with the Australian Broadcasting Tribunal which, under its different legislation, is also expected to face questions regarding control if the Tourang bid is successful.

If the Commission decided to challenge the Tourang bid it would be open to Tourang either to contest the challenge in Court or to seek authorisation.

In essence this would require Tourang to persuade the Commission that its bid would result in public benefits which outweighed any accompanying detriments.

The Commission would have 45 days in which to consider the application and publicly report its decision and reasons. It would invite, and consider, comment by interested parties on the proposal.

Some authorisation applications lead to negotiated modifications of bids to avoid a breach of the Act -- for example by divorcing some assets from the overall proposal.