



Australian
Competition &
Consumer
Commission

Interim Guidelines on misuse of market power

October 2017

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Purpose of these Guidelines

Section 46 of the *Competition and Consumer Act 2010 (CCA)* has been significantly altered. It now prohibits a firm with a substantial degree of market power from engaging in conduct that has the purpose, effect or likely effect of substantially lessening competition in a market.

The ACCC has responsibility for investigating and instituting proceedings for breaches of the competition provisions of the CCA, including s. 46. It can take proceedings in the Federal Court to determine whether there has been a breach of the CCA and whether penalties and other remedies should be imposed. Private parties can also take action against businesses for contraventions of s. 46.

These Guidelines sets out how the ACCC currently proposes to interpret s. 46 and describes the general approach the ACCC will take in investigating alleged contraventions of s. 46.

Australian courts are ultimately responsible for:

- interpreting the CCA
- determining if s. 46 has been contravened
- determining what, if any, penalty or other order should be imposed.

Decisions of the courts may be inconsistent with the ACCC's approach referred to in these Guidelines. If so, those decisions will be incorporated in revisions of these Guidelines as appropriate.

These Guidelines sets out the ACCC's understanding of the law and is prepared for the general guidance of legal practitioners and business advisors. It is not a substitute for legal advice.

1. Why the ACCC takes action under section 46

- 1.1. Markets function well where firms strive to develop and offer products that are more attractive to customers than the products offered by their rivals. A firm with substantial market power may be able to damage this competitive process by preventing or deterring rivals, or potential rivals, from competing on their merits. That is, a firm with substantial market power may maintain or advance its position by restricting or undermining its rivals' ability to compete, rather than by offering a more attractive product. Sometimes this is referred to as 'exclusionary conduct'. Such conduct undermines the effective operation of markets and the economy.
- 1.2. Preventing firms with a substantial degree of market power from engaging in conduct that has the purpose or effect of substantially lessening competition is now a central limb of Australia's competition laws. Where it considers s. 46 has been contravened, the ACCC will take action to protect the competitive process and address consumer harm.
- 1.3. Section 46 does not prohibit a firm from obtaining a substantial degree of market power. Nor does it prohibit a firm with a substantial degree of market power from 'out-competing' its rivals by using superior skills and efficiency to win customers at the expense of firms that are less skillful or less efficient. This conduct is part of the competitive process, which drives firms to develop and offer products that are more attractive to customers, and should not be deterred.

2. Section 46 – key concepts

- 2.1. Subsection 46(1) of the CCA provides that 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

- (a) that market; or
- (b) any other market in which that corporation, or a body corporate that is related to that corporation:
 - (i) supplies goods or services, or is likely to supply goods or services; or
 - (ii) supplies goods or services, or is likely to supply goods or services, indirectly through one or more other persons; or
- (c) any other market in which that corporation, or a body corporate that is related to that corporation:
 - (i) acquires goods or services, or is likely to acquire goods or services; or
 - (ii) acquires goods or services, or is likely to acquire goods or services, indirectly through one or more other persons.

2.2. The key concepts in s. 46 are:

- a) 'market'
- b) 'substantial degree of power in a market'
- c) purpose, effect or likely effect
- d) 'substantially lessening competition'.

Market

2.3. A market is the product and geographic dimensions in which the competitive process takes place. It is defined in s. 4E of the CCA to mean 'a market in Australia', and includes goods or services that are substitutable for, or otherwise competitive with, the goods or services under analysis.

2.4. The ACCC's starting point for assessing market definition is to identify:

- a) the good or service supplied by the relevant firm and its close substitutes (product market); and
- b) the geographic region in which the good or service is supplied (geographic market).

2.5. The ACCC may also consider the functional dimension of the market (the different levels in the distribution chain such as the wholesale or retail functional level) and the timeframe over which substitution possibilities should be assessed.

Product market

2.6. To determine the product market, the ACCC considers the good or service under analysis and then identifies substitute products - typically those products to which consumers would switch if the price of the good or service under analysis increased.

2.7. In addition to this substitution by customers (demand-side substitution), a firm can also be constrained by the potential behaviour of firms supplying other products (supply-side substitution). If the price of a good or service increased, the ability of suppliers to switch quickly and without significant investment to supply the product to a substitutable product will be relevant.

Example 1. Product market

Firm A is a supplier of a popular brand of ice cream. Firm A decides to increase the price of its product by 10% above the competitive level, resulting in a significant number of Firm A's customers switching to a brand of frozen yoghurt produced by Firm B. In this scenario, both Firm A's ice cream and Firm B's frozen yoghurt would be included in the relevant product market.

Geographic market

- 2.8. To determine the geographic market, it is first necessary to identify the area in which the good or service under analysis is supplied. The ACCC then considers the geographic areas where consumers would be able or willing to find substitutes for the goods or services in question.
- 2.9. A number of factors will determine the extent of the relevant geographic market, including the portability of the relevant good, costs to customers of obtaining supply from alternative regions, and any regulatory or other practical constraints on suppliers selling to alternative regions.
- 2.10. Although s. 4E refers to a 'market in Australia', the geographic market may contain goods or services from overseas. Section 4 of the CCA makes it clear that competition includes competition from imported goods or from services rendered by persons not resident or not carrying on business in Australia.

Example 2. Geographic market

Firm A operates the only pet supply store in the regional town of Kiama. It decides to increase the price of pet food by 5%, resulting in a substantial number of customers switching to a pet supply store in a neighbouring town. In this scenario, the relevant geographic market in which Firm A competes would include at least Kiama and its neighbouring town.

- 2.11. Market definition is purposive. In *ACCC v Flight Centre* [2016], the High Court observed that:

Identifying a market and defining its dimensions is "a focusing process", requiring selection of "what emerges as the clearest picture of the relevant competitive process in the light of commercial reality and the purposes of the law".¹

- 2.12. This means that a market is not defined in isolation. The definition of a relevant market will be considered in the context of the particular conduct under investigation. It is well recognised that market definition is not an exact science and that it is not possible or necessary to identify precise boundaries.²

Substantial market power

- 2.13. Whether or not a firm has substantial market power is an important threshold which needs to be met before considering whether a firm has misused its market power.

¹ [2016] HCA 49 at [69].

² For example see: Gordon J in *Air New Zealand Ltd v ACCC*; *PT Garuda Indonesia Ltd v ACCC* [2017] HCA 21 at [57]–[66]; Deane J in *Queensland Wire* at [196]; Allsop J in *ACCC v Liquorland* (2006) [2006] FCA 826 at [428]–[430]; Dowsett J in *ACCC v ANZ* (2015) 324 ALR 392 at [135].

- 2.14. Market power comes from a lack of effective competitive constraint. A firm with market power is able to act with a degree of freedom from competitors, potential competitors, suppliers and customers. The most observable manifestation of market power is the ability of a firm to profitably sustain prices above competitive levels. Substantial market power may also enable a firm to reduce the quality of goods or services, raise barriers to entry or slow innovation.³
- 2.15. There are a range of factors that can influence the degree of competitive constraint faced by a firm which are likely to be relevant to the ACCC's assessment. These factors were outlined by the Trade Practices Tribunal in *Re Queensland Co-Op Milling Association Limited and Defiance Holdings Limited*:
- (1) the number and size distribution of independent sellers, especially the degree of market concentration
 - (2) the height of barriers to entry, that is the ease with which new firms may enter and secure a viable market
 - (3) the extent to which the products of the industry are characterised by extreme product differentiation and sales promotion
 - (4) the character of 'vertical relationships' with customers and with suppliers and the extent of vertical integration
 - (5) the nature of any formal, stable and fundamental arrangements between firms which restrict their ability to function as independent entities.⁴
- 2.16. The ACCC does not impose a market share threshold in determining whether a firm has a substantial degree of market power. While market share can be an important factor, more than one corporation may have a substantial degree of power in a market.⁵ Further, a firm may have market power even though it does not substantially control the market or have absolute freedom from the constraint of competitors.⁶ The ACCC will assess each case on its merits according to the specific nature of the good or service, the industry and the particular competitive impact likely to result in each case.

Purpose, effect or likely effect

- 2.17. Even with a substantial degree of market power, a firm will only contravene s. 46 if its conduct has the purpose, effect or likely effect of substantially lessening competition in a relevant market.
- 2.18. '**Purpose**' refers to a firm's intention to achieve a particular result. It can be established by direct evidence or by inference. The purpose specified in s. 46 need not be a firm's only purpose, but it needs to be a substantial purpose.

³ See discussion on market power in Kaysen and Turner, *Antitrust Policy* (1959), p. 75 in QWI at [200].

⁴ (1976) 8 ALR 481 at 515–516.

⁵ Section 46(7) of the CCA.

⁶ Section 46(5) of the CCA.

- 2.19. **'Effect'** refers to the direct consequence of a firm's conduct. This is determined objectively by examining the actual impact on the competitive process within the relevant market. Although not determinative, evidence of consumer or competitive detriment will be relevant to the ACCC's consideration of whether to pursue a matter.
- 2.20. **'Likely effect'** refers to the likely consequences of a firm's conduct, including its potential impact on the competitive process. 'Likely' means that there is a real chance or a possibility that is not remote.
- 2.21. When assessing a firm's conduct, the ACCC considers the nature and extent of that conduct, including the firm's commercial rationale. When assessing effect or likely effect on competition, the ACCC may undertake a 'with or without test'. This compares the likely state of competition 'with' the conduct, to the likely state of competition 'without' the conduct, to determine whether the conduct lessened competition as a result of the firm's conduct.

Substantially lessening competition

- 2.22. There is no legislative definition of 'substantially lessen competition' however the term is well understood within Australia's competition laws. In essence, conduct substantially lessens competition when it interferes with the competitive process in a meaningful way by deterring, hindering or preventing competition. This can be done by raising barriers to competition or to entry into a market.
- 2.23. **'Substantially'** means meaningful or relevant to the competitive process. It is a relative concept and does not require an impact on the whole market.
- 2.24. In *Rural Press v ACCC* (2003), the majority of the High Court relevantly assessed 'substantially' by asking:
- ...whether the effect of the arrangement was substantial in the sense of being meaningful or relevant to the competitive process, and whether the purpose of the arrangement was to achieve an effect of that kind.⁷
- 2.25. In *Universal Music v ACCC* (2003), the Full Court observed:
- ... The lessening of competition must be adjudged to be of such seriousness as to adversely affect competition in the market place, particularly with consumers in mind. It must be 'meaningful or relevant to the competitive process': *Stirling Harbour Services Pty Ltd v Bunbury Port Authority* [2000] FCA 38 at para 114.⁸
- 2.26. **'Lessening competition'** means that the field of rivalry is diminished or lessened, or the competitive process is compromised or impacted. 'Lessening competition' extends to 'preventing or hindering competition' (s. 4G of the CCA).

⁷ (2003) 216 CLR 53 at [41].

⁸ (2003) 131 FCR 529 at [242].

2.27. When assessing whether the conduct has the purpose, effect or likely effect of substantially lessening competition, the ACCC will consider the commercial rationale for the conduct. For instance, if a firm is engaging in conduct to make its products more attractive to customers, the conduct is unlikely to substantially lessen competition.

3. Types of conduct that may involve a misuse of market power

- 3.1. It is not possible to identify with precision particular types of conduct that necessarily involve a misuse of market power. Whether or not conduct is a misuse of market power will always depend on the circumstances.
- 3.2. Despite this, competition agencies and courts have regarded some types of conduct as having greater potential to involve a misuse of market power, either in isolation or combined. These include:
- a) refusal to deal
 - b) restricting access to an essential input
 - c) predatory pricing
 - d) loyalty rebates
 - e) margin/price squeezing
 - f) tying and bundling.

Refusal to deal

- 3.3. Businesses are generally entitled to choose whether or not they will supply or deal with another firm, including a competitor. Even if a firm has a substantial degree of market power, there is usually no obligation for it to deal with other firms.
- 3.4. However, in limited circumstances, a refusal to deal by a firm with a substantial degree of market power may amount to a misuse of market power. For instance, where a firm that has a substantial degree of market power in the supply of a key input:
- a) refuses to supply that input to its competitors in a downstream market and the purpose, effect or likely effect of the conduct is to substantially lessen competition in the downstream market, or
 - b) states a willingness to supply a key input to its competitors in a downstream market, but only on terms at which no competitor would be willing to buy the input, (e.g. by charging an excessively high price), and if the purpose, effect or likely effect of the conduct is to substantially lessen competition in the downstream market.

Example 3. Refusal to deal

A firm owns the only cement works supplying a regional town. The next closest cement works is a considerable distance away. The cost of transporting cement to the town from the next closest cement works is significant. The firm owns all the ready-mix concrete plants servicing the regional town. Cement is an essential input into ready-mix concrete.

A new entrant plans to set up two ready-mix concrete plants in the regional town. The new entrant has a strong track record of operating successful ready-mix concrete operations in other towns. The new entrant approaches the firm to acquire supplies of cement. The firm refuses to supply the new entrant with cement. One of its reasons for doing so is to protect the employment of its workers in its ready-mix concrete plants. The new entrant does not proceed with its plans to set up two ready-mix concrete plants.

Assessment

It is likely that the firm has a substantial degree of market power in the supply of cement in the regional town. It is the only supplier and the nearest potential competitor would incur very high transport costs in transporting cement to the regional town.

While one of the firm's motivations is to protect the employment of its workers, the end result it is seeking to achieve is that the rival firm is not able to enter the market and compete away business which could ultimately cause the incumbent firm to lay off workers. Further, a purpose of substantially lessening competition only needs to be a substantial purpose for the conduct and does not need to be the only purpose.

The effect of the firm's refusal to supply is to prevent the new entrant entering the market for the supply of ready-mix concrete and competing with the firm on its merits.

The conduct has the purpose and effect of substantially lessening competition.

The ACCC is of the view that the conduct is likely to breach s. 46.

Restricting access to an essential input

- 3.5. In some circumstances, a firm with a substantial degree of market power may prevent or restrict a competitor's access to an essential input. Where this conduct has the purpose, effect or likely effect of substantially lessening competition, it may breach the misuse of market power provision.
- 3.6. 'Essential inputs' are non-substitutable resources which are indispensable for the provision of goods and services. Restricting access to an essential input has the potential to prevent competitors from competing with a firm on their merits.

Example 4. Land banking

A firm operates 6 out of 8 retail fuel sites in a major town. The local planning authority has designated 2 other sites in the town as suitable for the establishment of new retail fuel sites. The town is some distance removed from the nearest alternative retail fuel stations and a potential new entrant is considering purchasing the designated sites. The firm buys the first option to purchase the 2 sites before the new entrant can do so. The firm has no plans to use the sites.

Assessment

It is likely that the firm has a substantial degree of market power. It has 75% of retail fuel sites in the town and access to suitable sites creates a considerable barrier to establishing a new fuel retailing business.

The firm plans to leave the sites idle for the foreseeable future. By excluding the new fuel retailing business, the conduct has the effect of substantially lessening competition.

The conduct has the effect of preventing the entry of a new fuel retailing business in the town. Given the high degree of concentration in fuel retailing in the town, new entry would likely substantially increase competition. The conduct has the effect of excluding the new fuel retailing business and therefore has the effect of substantially lessening competition.

The ACCC is of the view that the conduct is likely to breach s. 46.

Predatory pricing

- 3.7. Businesses compete by providing more compelling offers to consumers than their competitors. This often involves businesses undercutting prices offered by rivals. In almost all circumstances low pricing is beneficial for consumers and is part of the competitive process.
- 3.8. However, in rare circumstances, very low pricing by a firm with a substantial degree of market power may be predatory. Predatory pricing occurs when a firm substantially reduces its prices below its own cost of supply for a sustained period with the aim of:
 - a) causing competitors to exit the market
 - b) disciplining or damaging competitors for competing aggressively, or
 - c) discouraging potential competitors from entering the market.
- 3.9. Predatory pricing might result in a firm losing money in the short to medium term. However, if the practice causes competitors to exit the market or prevents new entrants from entering the market, the firm may be in a position to charge higher prices and maintain or increase its market share in the longer term.
- 3.10. Predatory pricing by a firm with a substantial degree of market power can harm an individual competitor; however, the test is whether the conduct has the purpose, effect or likely effect of substantially lessening competition in a market.

Example 5. Predatory Pricing

A firm publishes the only newspaper in a major regional town. The firm provides the newspaper for free and has built up a substantial readership through its focus on local news and events. The firm attracts substantial revenues from local businesses who advertise in the newspaper and earns substantial profits. Most local businesses consider it essential to advertise in the newspaper.

A new entrant commences publishing a competing regional newspaper and offers advertising rates comparable to those offered by the firm. The new entrant starts to win some advertising sales from the firm.

The firm reduces its advertising rates for all of its customers to less than 50% of the rates offered by the new entrant. At the new advertising rates, the firm does not cover its costs of printing and distributing its newspaper. The firm's board documents indicate it is willing to incur these losses to reinstate its position as the sole regional newspaper and the profits that position generates.

The new entrant is unable to attract sufficient advertisers and closes its newspaper. After the closure, the firm raises its advertising rates to their original level.

Assessment

It is likely that the firm has a substantial degree of market power. Being the only regional newspaper has enabled the firm to build a substantial readership. Advertising in the newspaper is the most effective way for local businesses to reach local residents, and there are no close substitutes available.

The firm's reduction in advertising rates was substantial. The reduced rates were substantially below those offered by the new entrant and were not sufficient to cover the costs of printing and distributing the newspaper. The reduced advertising rates were not temporary, lasting until the rival newspaper closed. The financial losses made by the firm during this period were substantial.

The firm had the purpose of forcing the rival newspaper to close and prevent it from competing on its merits. In reducing its prices, the firm had the purpose of substantially lessening competition.

The ACCC is of the view that the conduct is likely to breach s. 46.

Loyalty rebates

- 3.11. Businesses are generally free to set their own sales promotions, including rebates. Rebates usually do not harm competition. In many cases, they promote competition by reducing the overall price customers pay for goods and services.
- 3.12. However, in limited circumstances, a firm with a substantial degree of market power offering loyalty rebates can substantially lessen competition. This is most likely to occur where a rebate is conditional on a distributor meeting certain sales targets.

For instance, where a firm offers its customers long-term supply terms with volume rebates which are conditional on the customer purchasing a very large quantity of its requirements from the firm.

- 3.13. Unconditional rebates, which simply reduce the price of an item with no additional conditions placed on the distributor, will likely only raise concerns if the reduced price amounts to predatory pricing.

Example 6. Loyalty rebates

Firm A is a large supplier of transmissions used in heavy-duty vehicles. It has significant market share of 80% for these products in Australia. Heavy duty vehicle manufacturers prefer to use Firm A's patented transmission systems in most heavy-duty vehicles. However, there are some heavy-duty vehicles where Firm A's transmissions are not an optimal fit, and manufacturers generally fit transmissions from Firm A's competitors. Consequently, demand for Firm A's transmissions has generally been stable relative to demand for its competitors' transmissions.

To address this, Firm A offers its customers a new supply agreement. The agreement contains an offer to pay its customers a conditional 10% rebate on the price of every truck transmission they purchase. The customer will only qualify for the 10% rebate if the customer purchases at least 10% more truck transmissions from Firm A than they did the previous financial year. That is, Firm A's customers will receive \$0 rebate if they do not meet the 10% target, and a 10% rebate on every truck transmission purchased that year if they do.

Assessment

It is likely that Firm A has a substantial degree of market power in the market for heavy-duty truck transmissions. It has significant market share in Australia and there are no close substitutes available.

The likely effect of the rebate is to deter or prevent competing truck transmission suppliers from being able to compete effectively on their merits. The structure of the conditional rebate creates a very strong incentive for heavy-duty vehicle manufacturers to increase their purchases from Firm A by 10%, as the rebate will then be applied to every transmission sold. Firm A's rivals could not effectively respond by offering a 10% (or higher discount) on their transmissions, as this rebate would not provide manufacturers with any saving on the majority of transmissions that they already buy from Firm A. The conduct is likely to have the effect of substantially lessening competition in the supply of heavy-duty truck transmissions.

The ACCC is of the view that the conduct is likely to breach s. 46.

Margin/price squeeze

- 3.14. Businesses are generally entitled to charge different prices to different buyers for the supply of goods or services along the supply chain.

- 3.15. However, a firm with a substantial degree of market power in the supply of an essential input can disadvantage its competitors in downstream markets by reducing the margin available to these competitors. It could do this, for example, by charging its competitors an input price that makes it uncommercial for them to offer a competitive price in the downstream market.⁹
- 3.16. As competitors in the downstream market require the input and have limited alternative sources of supply, a margin or price squeeze has the potential to prevent equally efficient competitors from competing with the firm on their merits.

Example 7. Margin/price squeeze

Firm X holds 90% of the world's known deposits of a rare earth mineral (REM) which becomes essential in the development of touchscreens. While exploration is underway in a number of potential new REM sites and touchscreen technologies, it is not known how many years it will be before either becomes available.

Firms A, B and C are the major producers of touchscreens for use on smartphones, tablets and other devices. They account for 70% of the world's demand for REM. Firm X establishes a subsidiary to begin competing with Firms A, B and C in the manufacture and supply of touchscreens.

Shortly after, Firm X substantially increases the price at which it sells REM. Even with access to the remaining sources of REM (which also increase their prices in response to X's price increase), Firms A, B and C all require access to REM from Firm X to make their touchscreens.

Firm X offers a number of two-year contracts to provide touchscreens to major mobile phone and tablet producers where the price offered per screen is only just above what it will now cost Firms A, B and C to buy the REM required to produce each touchscreen.

Assessment

It is likely that Firm X has a substantial degree of market power in the supply of REM. It has 90% of the world's supply and new entry is unlikely.

Firm X offers touchscreens at a price above what it would cost its competitors to buy the REM required to produce each touchscreen. If Firm X had to pay the same price for REM as it charged Firms A, B and C, it would make a loss on each touch screen sold to these smaller buyers when taking into account its other production and distribution costs.

The conduct is likely to have the effect of substantially lessening competition in the supply of touchscreens. The ACCC is of the view that the conduct is likely to breach s. 46.

⁹ For example a price that is similar to the price the corporation charges in the downstream market.

Tying and bundling

- 3.17. Businesses are generally entitled to supply goods or services as part of a tied or bundled arrangement. Tying and bundling are common commercial arrangements which usually do not harm competition and in many scenarios promote competition by offering consumers more compelling offers.
- 3.18. **'Tying'** occurs when a supplier sells one good or service on the condition that the purchaser buys another good or service from the supplier. For example, a printer supplier may sell a printer on condition that the customer also acquires ongoing servicing from the supplier.
- 3.19. **'Bundling'** occurs when a supplier offers a lower price if two products are purchased as a package. For example, mobile phone operators offer bundles of handsets and mobile phone services plans where the price of the handset and plan is cheaper if consumers buy them together than if they buy each one separately.
- 3.20. However, in limited circumstances, tying or bundling by a firm with a substantial degree of market power may amount to a misuse of market power. This can occur when a firm with substantial market power in one market uses a tie or bundle to extend or 'leverage' this market power into another market.

Example 8. Tying and Bundling

A firm has the patent over the active ingredient in the only drug that can treat a common heart condition (Drug A). The patent for Drug A lasts for another five years. The firm has the patent for another drug that treats a different heart condition (Drug B). The patent for Drug B is about to end. Manufacturers of generic drugs are making plans to manufacture a generic version of Drug B.

The firm decides to alter its selling practices to only sell Drug A and Drug B as a bundle. The firm writes to all pharmacies stating that it will only sell Drug A to a pharmacy if the pharmacy agrees to purchase all of its requirements of Drug B from the firm. Pharmacies acquire drugs from a range of manufacturers. There are no benefits to pharmacies in acquiring Drug A and Drug B from the same manufacturer.

Assessment

It is likely that the firm has a substantial degree of market power in the supply of Drug A. It is the monopoly supplier of Drug A (for the duration of the patent) and there are no comparable drugs.

Pharmacies must dispense Drug A to service their customers effectively. If a pharmacy cannot dispense Drug A, it is likely to lose a significant number of customers. As a result, it is likely that almost all pharmacies will purchase Drug A and Drug B as a bundle from the firm. This will prevent or hinder manufacturers of generic drugs from competing to supply Drug B to the vast majority of pharmacies.

The conduct is likely to have the effect of substantially lessening competition. The ACCC is of the view that the conduct is likely to breach s. 46.

4. Types of conduct that may not involve a misuse of market power

- 4.1. The ACCC investigates misuse of market power allegations with the aim of distinguishing between vigorous competitive activity which is desirable, and economically inefficient monopolistic practices that may exclude rivals and harm the competitive process.
- 4.2. Whether conduct breaches s. 46 will depend on all the circumstances. Conduct that enhances efficiency, innovation, and product quality or price competitiveness is unlikely to substantially lessen competition.
- 4.3. The ACCC considers that the following conduct would not generally raise concerns:
 - a) innovation, regardless of how 'big' the firm is
 - b) efficient conduct designed to drive down costs
 - c) responding to price competition with matching or more competitive (above cost) price offers
 - d) responding efficiently to other forms of competition in the market such as product offerings and terms of supply.
- 4.4. The aim of s. 46 is to preserve the integrity of markets so that businesses have the incentive to enter or operate more efficiently, price competitively and offer better products to their customers. Businesses that compete by undertaking a successful promotional campaign, undertaking research and development which results in better products or more efficient processes, or passing savings through to consumers will be enhancing competition, not lessening it.

Example 9. Research and development

A firm with 80% of the market has developed a substantially improved version of an existing technological product. This new product supersedes the first generation products currently on the market. The vast majority of consumers prefer the new product causing many suppliers of the first generation product to close.

Assessment

Investment by the firm to innovate and improve its product to make it more attractive to consumers is part of the competitive process. The exit of other suppliers is the result of the firm engaging in competitive activity, not the result of the firm engaging in conduct which deters its rivals from competing on their merits. The ACCC is of the view that the firm's conduct **would not** have the purpose or the effect of substantially lessening competition.

Example 10. Price War

Three firms each with 25% of a market compete with a significant fringe of smaller suppliers. Periodically, one of the firms significantly discounts the prices of its product to win more customers. These price reductions are quickly matched by the other firms causing a price war. While the three firms remain profitable during the price war, some smaller suppliers do not and decide to close.

Assessment

It is unlikely that any of the firms have a substantial degree of market power. Each firm faces significant competitive constraint from the other firms and smaller suppliers. The firm leading the price discounting has the purpose of winning customers from its rivals. The price matching by the other firms is a competitive response. This is competition on the merits and the conduct **would not** breach s. 46.

Example 11. Investing in new production technology to increase efficiency

A firm manufactures an iconic brand of lawn mowers. The popularity of the brand means that it currently supplies 70% of lawn mowers sold in Australia. It is rumoured that a large established international manufacturer of lawn mowers is planning to commence selling its lawn mowers in Australia. The firm invests in new production technology to lower its costs and improve the reliability of its lawn mowers. As a result of its lower production costs, the firm reduces the prices of its lawn mowers. The firm advertises the price reductions and improved reliability of its lawn mowers extensively. The international manufacturer of lawn mowers decides not to sell its lawn mowers in Australia.

Assessment

Investing in new production technology to improve the reliability of its lawn mowers and to enable it to reduce its prices is a competitive response by the firm to the threat of new entry. The firm's conduct is not exclusionary. That is, it did not prevent or deter the potential new entrant from competing with the firm on its merits. The decision by the international manufacturer not to enter the market is because the firm improved its offer to consumers. The conduct **would not** have the purpose, effect or likely effect of substantially lessening competition.

Example 12. Rewarding behaviour

Firm A identifies a new way of treating timber to prevent termite infestation and markets its new product extensively under the brand Tproof Timber. Tproof Timber becomes very popular for residential construction in regional, bushland and rural

areas. While the research and development costs were high, the new treatment is very inexpensive to apply. However, Firm A charges a very substantial premium on the product, keeping the price near but below steel beams and almost double the price of other treated timbers.

Assessment

Even though Firm A is making a considerable profit on each Tproof Timber product sold, the ACCC is of the view that the conduct **would not** breach s. 46.

Even if Firm A did have substantial market power, which would depend on the Tproof Timber's substitutability with other building products among other factors, its ability to charge higher prices is Firm A's reward for its innovation. Rather than deterring competition on its merits, Firm A's higher profits should incentivize other timber producers to seek to develop better termite resistant products that compete directly with Firm A's offering.

Example 13. Standardised or national pricing by large retail chains

A firm which operates a large national retail chain opens up a retail store in a regional town. The retail chain has not had a presence in that town previously. The firm offers a standard product range and sets the same retail prices at all of its retail stores, including at the new store. As a result of operating a national retail chain, the firm is able to achieve substantial efficiencies (including securing low prices for purchasing goods from suppliers). This enables the store to offer low prices to customers, while operating profitably. Some existing small retailers in the town are unable to match the retail prices offered by the firm and become unprofitable and close.

Assessment

If the retail chain has had an established practice of offering customers at all of its stores a standardised range with standardised prices, the application of that same practice to a new store **would not** have the purpose or effect of substantially lessening competition.

In this example, the retail chain's model is to attract customers with a standardised offer, which relies on the greater efficiencies and lower purchasing costs it enjoys due to its greater scale and scope. If the store, and each of its major product segments (such as bakery products), are operating profitably, it is competing on its merits. This is likely to drive competition by causing competitors to seek to lower their costs and to focus on other aspects of competition, such as service, convenience and differentiated products. The relevant issue is whether there has been an interference with the process of competition, not whether competition has resulted in some competitors with a higher cost base being forced to close.

The ACCC is of the view that the conduct **would not** breach s. 46.

5. Authorisation

- 5.1. Authorisation provides protection against legal action for future conduct that might breach the competition provisions of the CCA, including s. 46. Parties can apply to the ACCC for authorisation where they believe that there is some risk that the conduct they propose to engage in would or may breach s. 46 and they require the certainty provided by an authorisation to undertake the activity.
- 5.2. In general, the ACCC may grant authorisation if it is satisfied that the proposed conduct is either unlikely to substantially lessen competition or likely to result in a net public benefit.
- 5.3. Authorisation is a formal and public process. The application and supporting submission will be available on the ACCC's public register and provided to interested parties for their comment or response. All public responses are made available on the public register. The ACCC's draft and final determination including the reasons for the decision are also publicly available.
- 5.4. The ACCC cannot retrospectively grant authorisation for conduct that has already occurred. Parties are encouraged to contact the ACCC if they have any concerns about future or ongoing conduct.
- 5.5. Further detailed information on the authorisation process is available in the ACCC's authorisation guidelines at <https://consultation.accc.gov.au/compliance-enforcement/interim-guidelines-mergers-and-authorisations/>

6. The ACCC's approach to investigating allegations of misuse of market power

- 6.1. In assessing allegations of misuse of market power under s. 46, the ACCC will consider:
 - a) the nature and extent of competitive constraints on the firm engaging in the conduct
 - b) the nature and extent of the conduct
 - c) competitors or areas of competition to understand the impact of the conduct
 - d) likely market outcomes, including what would likely happen if the conduct did not occur, and
 - e) whether and the extent to which the competitive process is being restricted, deterred or prevented in any relevant market
- 6.2. In deciding whether to take enforcement action, the ACCC focuses on the extent to which matters will, or have the potential to, harm the competitive process or result in widespread consumer detriment. The ACCC cannot pursue all the complaints it receives and will direct its resources to matters that provide the greatest overall benefit for competition and consumers.

- 6.3. To assist with this determination, the ACCC gives compliance and enforcement priority to matters that demonstrate one or more of the following factors:
- a) conduct resulting in a substantial consumer (including small business) detriment
 - b) conduct demonstrating a blatant disregard for the law
 - c) conduct involving issues of national or international significance
 - d) conduct involving essential goods or services
 - e) conduct detrimentally affecting disadvantaged or vulnerable consumer groups
 - f) conduct in concentrated markets which impacts on small businesses or suppliers
 - g) conduct that is industry-wide or is likely to become widespread if the ACCC does not intervene
 - h) where ACCC action is likely to have a worthwhile educative or deterrent effect, or
 - i) where the person, business or industry has a history of previous contraventions of competition, consumer protection or fair trading laws.

7. Sanctions

- 7.1. If a court determines that a person has contravened, attempted to contravene or has been involved in a contravention of s. 46 (as set out in s. 76 of the CCA), the court may impose orders including but not limited to:
- a) requiring that person to pay a civil pecuniary penalty
 - b) requiring that person to pay damages
 - c) preventing that person from engaging in certain conduct
 - d) declaring that person has contravened the CCA
 - e) in the case of individuals, disqualifying a person from managing a corporation.
- 7.2. The maximum penalty payable by a body corporate for each act or omission (as set out in ss. 76(1A)(b) of the CCA) is the greatest of:
- (i) \$10,000,000;
 - (ii) if the Court can determine the value of the benefit that the body corporate, and any body corporate related to the body corporate, have obtained directly or indirectly and that is reasonably attributable to the act or omission—3 times the value of that benefit;
 - (iii) if the Court cannot determine the value of that benefit—10% of the annual turnover of the body corporate during the period (the turnover period) of 12 months ending at the end of the month in which the act or omission occurred.
- 7.3. The maximum penalty for any other person, including an individual, is \$500,000 for each act or omission (ss. 76(1B)(b) of the CCA).