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Predatory Pricing Down Under

ACCC v Boral - Protecting Weak Competitors Not Competition?

Section 46 of the Australian *Trade Practices Act 1974 (Cth)* deals with "*misuse of market power"*. While it is similar to section 2 of the Sherman Act and Article 82 of the *Treaty of Amsterdam* (previously Art. 86, *Treaty of Rome*), there are considerable differences as a recent decision of the Full Federal Court in *Australian Competition and Consumer Commission v Boral Ltd* (2001 FCA 30) indicates. Section 46 prohibits a corporation with a *"substantial degree of power in a market"* from *"taking advantage of that power"* for an anti-competitive purpose *("eliminating or substantially damaging a competitor*"; *"preventing entry*"; or *"deterring or preventing a person from engaging in competitive conduct"*).

The Facts

Boral is a manufacturer and supplier of concrete masonry products (CMP). The Australian Competition and Consumer Commission (ACCC) commenced proceedings in the Federal Court against Boral and a subsidiary (for convenience both are referred to as Boral) claiming that Boral had breached s 46. It was alleged Boral had substantial power in the Melbourne CMP market and misused its market power by pricing below avoidable cost. At the relevant time the building industry was in recession and there was considerable excess capacity.

The trial judge found that Boral did not have substantial market power and even if it did, it did not take advantage of it. He held that:

> *"... there must be a causal connection between the market power and the impugned conduct; that is, the conduct must be made possible only by the absence of competitive conditions; and if the conduct has a business rationale, this is a factor pointing against taking advantage of market power. Selling below avoidable cost, even for a prolonged period, can be a rational business decision."*

The Trial Judge decided, following United States jurisprudence, that predatory pricing in breach of s 46 required both selling below costs and a reasonable likelihood of recouping the consequent losses by charging supra-competitive prices. He also found the "*proscribed purpose"* had been established.

On Appeal

The ACCC appealed and the Full Federal Court reversed the decision, finding that the relevant market was the supply of CMP, in which Boral had a *'substantial'* degree of market power. The Court also found that Boral *'used'* its substantial market power for anti-competitive purposes.

The ACCC argued that Boral's conduct could still amount to *'taking advantage"* of substantial market power even if there was a business rationale. They argued that the Trial Judge should not have held that predatory pricing in breach of s 46 required both pricing below cost as well as a reasonable chance and ability to recoup its predatory pricing losses by higher prices in the future. The ACCC argued that because s 46 does not incorporate an effects test there is no need to determine whether there is a realistic likelihood of recoupment.

The Full Federal Court held that conduct that breaches s 46 is not excused if *"rational"* or "*commercial"'* in nature. As a result, there is no *"basis for implying a recoupment theory into the working of s 46"* (Beaumont J.). Originally, s 46 had only applied to dominant firms. In 1986 the s 46 threshold was lowered to apply to a corporation that has a *"substantial degree of power in a market"*. As a result, more than one firm can have a substantial degree of power in a market. Merkel J. pointed out that if the test for predatory pricing was both selling below cost *plus* recoupment by supra-competitive pricing then:

> *"... in a practical sense the criteria would necessarily limit predatory pricing under s 46 to a firm that is a monopolist or dominant in a market ... the test would render nugatory the lowering of the s 46 threshold."*

He also went on to point out that the result:

> *"... may not sit comfortably with the principles that have provided the underpinning for the European and United States case law on predatory pricing. However, the departure from those principles in the Australian context does not arise as a result of their rejection by the Court. Rather, it results from the 1986 amendments which, as stated in the Second*

> *Reading Speech, lowered the s 46 threshold to 'ensure that small businesses are given a measure of protection from the predatory actions of powerful competitors …".*

Finkelstein J also agreed that if the Court applied a recoupment test following United States case-law then:

> *"… it will be almost impossible to maintain a successful predatory pricing prosecution against a firm other than a monopolist…. It is also necessary to bear in mind the reason why the United States courts have sought to give a precise meaning to the notion of predatory pricing. It was an attempt to provide a standard that could be applied rationally to all circumstances, a 'bright line test' that would not depend upon the alleged predator's intent, which was regarded as an unsatisfactory criterion upon which to found liability… It must also be remembered that in the United States antitrust legislation is concerned with constraining the behaviour of a monopolist. That is not the focus of s 46. Our section is aimed at regulating a firm with a substantial degree of market power…"*

Finkelstein J went on to say that it did not matter for predatory pricing whether price was above total or average variable cost or not. Pricing above cost may be predatory. Pricing below cost may not be predatory – a firm may incur *"losses as a means of putting excess capacity into operation."* Whether pricing is predatory or not depends on the particular circumstances of each case.

Implications

This case has considerable implications for the way large firms operate in Australia. Competition law down under now says that if corporations use their substantial market power when pricing to prevent entry, to drive competitors out or inhibit competitive processes then they may breach s 46. Having a legitimate business reason may not be enough. Rather, a corporation will have to demonstrate that it would have priced similarly in a more competitive market – one in which they did not have substantial market power. This should lead to some interesting mind games in marketing departments.

The case may also have implications for the use of economics in future competition law cases. Australia's *Trade Practices Act 1974* contains more detailed prohibitions than in the United States or Europe. This means that outcomes are more likely to be dictated by the words of the statute than the underlying economics. While the use of economics in the courtroom in Australia has become more important in the last 10 years, the Boral case indicates that judges are prepared to limit the use of economics when the statute says otherwise. There may be a case for revising the competition statute to better reflect notions of efficiency and to put more decision-making power in the hands of a specialist tribunal with economic expertise.

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