FOREIGN AND INTERNATIONAL COMPETITION LAW AND POLICY DEVELOPMENTS

EVALUATING PRODUCT INTEGRATION: LESSONS FROM *U.S.* v. *MICROSOFT*

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U.S. v. *Microsoft*[2] raised issues that may increasingly apply to other companies in innovative industries, especially software. In particular, *Microsoft* involved issues of product combination and product integration.[3] Evaluating such activities when there are tying claims can pose special challenges to those who are not experts in the technology involved. In software, in particular, it can be difficult to determine whether blocks of code should be considered as one product or multiple products.

The prevalence of product combination and product integration in the software industry, combined with the potential complexity of evaluating these activities from an antitrust standpoint, suggest that a simple and uniform approach should be established to deal with this issue. In June 1998, as part of a case that preceded *U.S.* v. *Microsoft*,[4] the United States Court of Appeals for the District of Columbia Circuit laid out guidelines for identifying genuine product integration within the context of a consent decree negotiated between Microsoft, the Department of Justice, and European competition authorities.[5] The decree prohibited Microsoft from conditioning the licensing of certain operating system products, including Windows 95, on the licensing of other software products, but expressly allowed Microsoft to develop integrated products. The interpretation of the decree became an issue when the Department of Justice learned that Microsoft planned to require PC manufacturers who wanted to preinstall Windows 95 to preinstall Internet Explorer ("IE") 4.0 as well. Thus, one focus of the D.C. Circuit's inquiry was on whether Windows 95 and IE 4 should be considered to be separate products or a single, integrated product.[6]

The D.C. Circuit ruled that within the context of the consent decree, "integration may be considered genuine if it is beneficial when compared to a purchaser combination" but went on to state that "this analysis does not require a court to find that an integrated product is superior to its stand-alone rivals....The question is not whether the integration is a net plus but merely whether there is a plausible claim that it brings some advantage."[7] The D.C. Circuit retreated to this position because it felt that any deeper analysis would require the court to become "'enmeshed "in a technical inquiry into the justifiability of product innovations"'", and it did not want to "'put [ ] judges and juries in the unwelcome position of designing computers. '"[8]

The D.C. Circuit itself said that its criteria for genuine integration were crafted with the consent decree in mind and were not necessarily meant to differentiate tied products from an integrated product in the context of antitrust law generally.[9] In fact, despite Microsoft's assertions to the contrary,[10] the D.C. Circuit's standard cannot be the correct one for antitrust law generally because it would invite antitrust abuses among players

in the software and other innovative industries, sheltering actions with anticompetitive effects, no matter how large, as long as they were accompanied by "innovations" that bring any consumer benefits, no matter how small.[11]

A more sensible standard would analyze product design in the same way as other possibly anticompetitive conduct by asking:

> Would the defendant firm have engaged in the conduct in question regardless of the monopoly rents to be gained or protected by the conduct's effect on competition?[12]

If a firm finds it profitable to combine multiple functionalities and market them as if they were a single product when that action has a negative effect on competition, but does not find it profitable otherwise, then the combination should be considered anticompetitive rather than genuine integration and should not be permitted. Note that, because it considers costs as well as benefits, this approach can be used to help identify anticompetitive conduct even in cases where the conduct confers some benefits to end users. While some technical expertise is unavoidably required by this approach, the relevant information can be provided by a technical expert as well as documents in the record. *U.S.* v. *Microsoft* provides a prime example of the usefulness of this method of analysis.[13]

To appreciate how this approach was used in *U.S.* v. *Microsoft*, a brief overview of the issues in that case is required. Microsoft had achieved monopoly power in the market for operating systems for Intel-compatible desktop PCs because of a combination of "natural" phenomena. First, software programs written for one operating system will generally not run on others without very costly modifications. Second, software application writing exhibits strong economies of scale: the costs are practically all up front in the writing and debugging of the application. Hence, software writers have a very strong incentive to write (or write first) for the operating system with the most users. Finally, users want to have operating systems with a great many applications written for them and which are likely to be one of the first to support any future useful applications. Hence, the more popular a given operating system is with users, the more developers will choose to write applications for that operating system, and the more applications that are written for the operating system, the more popular it will be with users. In this circumstance, it was inevitable that one operating system would emerge as dominant. That operating system was Windows. Once this had occurred, the feedback phenomenon just described served as a barrier to effective competition with Windows—the "applications barrier to entry," as it was called in the case.

Had this been all, there would have been no antitrust case. However, Microsoft was not content with being the beneficiary of the phenomenon described. There arose threats to the applications barrier to entry, and Microsoft set out to crush them.

One such threat came from Sun Microsystems' invention of Java, an innovation which, if successful, would permit developers to write applications that could run on many different operating systems (which supported Java in a particular way) with minimal modifications. Microsoft acted to destroy this threat by "grow[ing] the polluted Java market"[14]—supporting Java in ways such that programs written for Microsoft's version would run well on Windows but would often not run properly on anything else.

But the actions that received the most attention and that involved product integration issues were related to the browser, commercially pioneered by Netscape.[15]

Netscape's Navigator was written to run on many different types of operating systems. Users who wanted to browse the Internet found Navigator to be an extremely attractive application. But Navigator itself was a platform to which applications developers could write. Were Navigator to become a popular platform for applications, the applications barrier to entry could have been seriously weakened or destroyed, and Windows would, in Microsoft's language, have been "commoditized."[16] To counter this threat, Microsoft was determined to exclude competition in browsers. If Microsoft could succeed in doing so, it would not be compelled by competition to offer a browser that could work on platforms other than Windows or to support competitors' browsers if they worked on platforms other than Windows. By only supporting technologies that were tied to Windows, Microsoft could effectively negate any threat to the applications barrier to entry.

One of several actions Microsoft took to hinder competition in the browser market was to enter into restrictive agreements with PC manufacturers.[17] PC manufacturers who wanted to license Windows 95 or Windows 98 were provided with a version that included IE on the desktop, and they were prohibited by the licensing agreement from deleting IE from the desktop. Moreover, the terms of the Windows licensing agreement limited PC manufacturers' ability to promote competing browsers.[18] PC manufacturers generally were not restricted from loading competing browsers on the desktop, but some PC manufacturers preferred to ship machines with only one browser loaded to avoid consumer confusion and to minimize testing costs. As a result, Microsoft's restrictive agreements with PC manufacturers were effective in limiting the distribution of competing browsers through PCs, one of the most important channels for browser distribution.

In light of this conduct, one issue important to the case was whether Microsoft would have conditioned the licensing of Windows on the licensing of IE regardless of the effect on competition. In other words, was Microsoft's bundling of IE and Windows procompetitive? The government's investigation uncovered ample evidence that Microsoft's purpose in tying IE to Windows 95 and Windows 98 was to leverage its monopoly in operating systems in order to prevent Netscape's Navigator from becoming established as the browser of choice, which in turn would help protect Microsoft's monopoly power in operating systems. For example, in December 1996, top Microsoft executive Jim Allchin wrote to his colleague Paul Maritz about how to increase Microsoft's share of the browser market, which at that time was dominated by Navigator:

> I don't understand how IE is going to win. The current path is simply to copy everything that Netscape does packaging and product wise. Let's [suppose] IE is as good as Navigator/ Communicator. Who wins? The one with 80% market share. Maybe being free helps us, but once people are used to a product it is hard to change them....My conclusion is that we must leverage Windows more. Treating IE as just an add-on to Windows which is cross-platform [means] losing our biggest advantage — Windows marketshare. We should dedicate a cross group team to come up with ways to leverage Windows technically more....We should think first about an integrated solution — that is our strength.[19]

Many similar e-mail messages bespeak similar intentions.[20]

The intentions revealed in these e-mails are consistent with other, related facts in the case. For example,

Microsoft's IE browser was a "no revenue product"—it was licensed for free, and Microsoft promised that IE for Windows and Macintosh would be "free forever."[21] Despite this, Microsoft not only gave away the expensively created IE but effectively paid Internet service providers to take and promote it – an act that made no sense except in so far as it protected the applications barrier to entry. Microsoft sought to gain control of browser technical standards, not to maximize profits by competing on the merits. In this connection, it is significant that Microsoft did not consider browsers like Encompass, that were based on IE technology, to be a competitive threat and relaxed its restrictions on PC manufacturers as to other browsers when these, rather than Navigator, were involved.[22]

Indeed, there is little evidence to suggest that Microsoft had a procompetitive rationale for tying IE to Windows 95 and Windows 98. For example, Microsoft argued that tying IE to Windows made Windows a more attractive product, but this cannot explain Microsoft's behavior. First, there is very little evidence in the record that Microsoft's purpose in tying IE to Windows was to increase demand for Windows. Second, if Microsoft's goal was to make Windows more desirable by including browsing functionality, it should have welcomed opportunities to have Navigator used with Windows; instead, several of Microsoft's agreements with third parties were designed to limit the use of Navigator on Windows. Third, the idea that Microsoft tied IE to Windows in order to make Windows more desirable does not explain why Microsoft entered into an agreement with Apple that required Apple to make IE the default browser on all Macintosh operating systems and limited Apple's ability to promote other browsers. Last, and perhaps most importantly, if the combination of IE and Windows did make Windows a more attractive product, there would have been no need to make the combination a requirement. Instead, PC manufacturers would have chosen the combination without being forced to take it. Thus, there is little to suggest that Microsoft's primary intent in tying IE to Windows was to make Windows a more attractive product.

Another rationale Microsoft proposed to explain its tying practices is that, without the tie, the integrity of the operating system would suffer and consumer benefits would be lost. This was the product integration argument made directly. The testimony of technical experts called these claims into question, however. Princeton University Assistant Professor of Computer Science Edward Felten, testifying for the government, found that IE Web browsing could be removed from Windows 95 and Windows 98, and in such a way that the non-Web-browsing functionalities of those operating systems were not degraded. Moreover, Felten then loaded Netscape's Navigator onto the version of Windows 98 from which IE Web browsing had been removed. He found that the non-Web-browsing functionalities of Windows 98 were not impaired, and that Navigator was fully functional. In fact, he found that "[t]his experience substantially duplicates what the user experiences with the combination of Windows 98 and IE."[23] In other words, Felten found that not only was IE not essential to the integrity of Windows, but that much of the benefit derived from the Windows 98/IE combination could be provided by a Windows 98/Navigator combination.

Perhaps even more significant was the testimony of one of Microsoft's own technical executives, James Allchin. Allchin's testimony indicated that most of the Web-related consumer benefits provided by the Windows98/IE tie could be attained if IE were used in conjunction with, but not tied to, Windows. Allchin testified that if a consumer purchased a retail version of Windows 95 onto which no browser had been loaded, and loaded onto it a separate, stand-alone

version of IE 4, that consumer would enjoy nearly all the same Web-related benefits as he or she would using the Windows 98/IE tied combination.[24] In other words, most of the Web-related benefits provided by the Windows 98/IE tie were not attributable to the tie itself, so that those benefits cannot rationalize the tie as pro-competitive.

This and other evidence suggest that Microsoft's purpose in tying IE to Windows was to leverage its monopoly in operating systems in order to eliminate the possibility that Navigator would become the overwhelming browser of choice, which in turn would protect Microsoft's monopoly power in operating systems; there is little to suggest a procompetitive rationale. Microsoft established the tie between IE and Windows because of its effect on competition; as such, its actions were clearly anticompetitive. Note, however, that under the D.C. Circuit's consent decree standard, all such evidence would be outweighed by any plausible benefit derived from the IE/Windows tie, no matter how small.[25]

The facts of *U.S.* v. *Microsoft* illustrate how little scrutiny the D.C. Circuit's standard would bring to bear on even the most egregious antitrust violations. In contrast, the approach proposed here (not really a new one), which was used in Fisher's testimony, considers whether the acts in question were the result of procompetitive profit maximization or were undertaken solely because of the monopoly rents to be gained or protected due to the effects on competition. Technical expertise on the part of judge or jury is not a requirement for utilizing this method of analysis. More importantly, this approach provides a framework for serious antitrust analysis, even where that analysis is made difficult by the innovative nature of the firms involved.

We close by quoting Judge Jackson's Conclusions of Law on this point:

> Viewing Microsoft's conduct as a whole also reinforces the conviction that it was predacious. Microsoft paid vast sums of money, and renounced many millions more in lost revenue every year, in order to induce firms to take actions that would help enhance Internet Explorer's share of browser usage at Navigator's expense. These outlays cannot be explained as subventions to maximize return from Internet Explorer. Microsoft has no intention of ever charging for licenses to use or distribute its browser. Moreover, neither the desire to bolster demand for Windows nor the prospect of ancillary revenues from Internet Explorer can explain the lengths to which Microsoft has gone. In fact, Microsoft has expended wealth and foresworn opportunities to realize more in a manner and to an extent that can only represent a rational investment if its purpose was to perpetuate the applications barrier to entry. Because Microsoft's business practices "would not be considered profit maximizing except for the expectation that ... the entry of potential rivals" into the market for Intel-compatible PC operating systems will be "blocked or delayed," Neumann v. Reinforced Earth Co., 786 F.2d 424, 427 (D.C. Cir. 1986), Microsoft's campaign must be termed predatory. Since the Court has already found that Microsoft possesses monopoly power, ... the predatory nature of the firm's conduct compels the Court to hold Microsoft liable under § 2 of the Sherman Act.[26] (some citations omitted)

Notes

[1] Fisher was a principal economics witness for the U.S. Department of Justice in the Microsoft case. Savio was his chief private staff assistant. We are grateful to Jeffrey Blattner, Timothy Bresnahan, Wayne Dunham, Joseph Farrell, Phillip Malone, and Diane Owen for comments. The opinions expressed here do not necessarily reflect those of the Department of Justice. All mistakes are our own.
[2] *United States of America* v. *Microsoft Corporation*, Civil Action No. 98-1232 TPJ (D.C.).
[3] Here, we use "product combination" to refer to separate products that are marketed together, and "product integration" to refer to a single product with the functionalities of two or more formerly separate products.
[4] The litigation surrounding the consent decree began earlier than and was separate from the more recent case involving violation of antitrust law (*U.S.* v. *Microsoft*, Civil Action No. 98-1232 TPJ (D.C.)). In this paper, we refer to the latter as *U.S.* v. *Microsoft*.
[5] *United States of America* v. *Microsoft Corporation*, 147 F. 3d 935 (D.C. Cir 1998).
[6] The D.C. Circuit heard this case on appeal from the United States District Court of the District of Columbia.
[7] *Supra*, note 5.
[8] *Ibid.*
[9] *Ibid.*
[10] Defendant Microsoft Corporation's Proposed Conclusions of Law.
[11] Microsoft advocated applying the D.C. Circuit's standard to *U.S.* v. *Microsoft* to resolve a tying claim brought under Section 1 of the *Sherman Antitrust Act*. But Section 2 of the *Sherman Act* was also involved, and, presumably if the D.C. Circuit's standard were to apply to one Section, it would also apply to the other. (See Microsoft's Proposed Conclusions of Law.)
[12] We are here considering Section 2 (*Sherman Act*) single firm monopoly cases.
[13] Again, we are referring here to Civil Action No. 98-1232 TPJ (D.C.), the recent case involving violation of antitrust law.
[14] Government Exhibit 259.
[15] Microsoft perceived platform threats from other technologies as well. See para. 78 of Court's Findings of Fact for other examples.
[16] Government Exhibit 20. Netscape's Navigator also served as a primary distribution channel for Java technology, which posed an additional threat to Microsoft, as discussed above.
[17] Tying and product integration were not the only types of conduct at issue in this case. For example, Microsoft also entered into restrictive agreements with Internet service providers ("ISPs"). As part of these agreements, Microsoft agreed to provide ISPs with access to users via the desktop, and ISPs agreed not only to promote IE but also to limit their promotion of other browsers.
[18] For example, PC manufacturers were prohibited from modifying the Windows start-up sequence (during which competing browsers might otherwise be offered to users) and were limited in their ability to highlight the existence of a competing browser with a large desktop icon.
[19] Government Exhibit 47.
[20] See Court's Findings of Fact, paras. 166-169, as well as Direct Testimony of Franklin M. Fisher, paras. 82-96, for examples and more details.
[21] Government Exhibit 39; Government Exhibit 336.
[22] Trial Testimony of Paul Maritz, January 25, 1999, afternoon session, p. 30; Trial Testimony of Joachim Kempin, February 25, 1999, morning session, at 5-10.
[23] Direct Testimony of Edward W. Felten, paras. 4-5, 63.
[24] Trial Testimony of James Allchin, February 1, 1999, afternoon session, at 28-54 and February 2, 1999, afternoon session, at 66-68.
[25] *Supra*, note 11.
[26] Conclusions of Law.

AUSTRALIAN NEWSLETTER

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Misuse of Market Power - Some Recent Australian Developments

The misuse of market power provisions in the *Australian Trade Practices Act 1974* have had a mixed history. Both the regulator, the Australian Competition and Consumer Commission ("ACCC"), and private litigants have taken actions under that provision, albeit with mixed success. The provision has been in place since 1974, although it has changed over time from referring to a business being in a position to control or dominate a market, to a business having a substantial degree of market power and engaging in specified proscribed conduct.

The current section reads:

> A corporation that has a substantial degree of market power shall not take advantage of that power for the purpose of:
>
> (a) eliminating or substantially

damaging a competitor,

(b) preventing the entry of a person into that market or any other market,

(c) deterring or preventing a person from engaging in competitive conduct in that or any other market.

'Purpose' can be inferred by conduct.

The landmark court decision in recent years was a private action involving a small steel fabricator/ distributor and Australia's largest and arguably dominant steel company, *Queensland Wire Industries Pty Ltd.* v. *Broken Hill Proprietary Co. Ltd.*[1] The case went through all possible court stages and ended up in the High Court where the small fabricator was successful. The case involved an unsuccessful intervention in the High Court by the regulator, although the regulator's arguments were clearly adopted by the High Court in its decision.

The High Court said the following about the object of the misuse of market power provision:

> The object of section 46 is to protect the interests of consumers, the operation of the section being predicated on the assumption that competition is a means to an end. Competition by its very nature is deliberate and ruthless. Competitors jockey for sales, the more effective competitors injuring the less effective by taking away sales. Competitors almost always try to 'injure' each other in this way.

These words are still law in Australia today, but there have been some important recent developments.

First, the regulator has taken a number of other actions, although with mixed outcomes. These actions are:

ACCC v. *Boral Ltd.*[2] The Court dismissed the case, finding no substantial degree of market power and Boral not to have used any such market power it may have had. The ACCC has appealed and the decision is pending.

ACCC v. *Safeways*. The judgment is pending.

ACCC v. *Simsmetal Ltd.* The action settled. The company pleaded to a breach of the cartel provisions, but the section 46 case was discontinued.

ACCC v. *Rural Press Ltd.* The decision is pending.

Second, there is an increasing amount of private actions, including one that is now in Australia's High Court. That case is *Hicks* v. *Melway Publishing Pty Ltd.*[3] and, again, it has gone the whole way up the court's hierarchy.

The *Melways* Case

The factual background to the *Melways* case is summarized below.

- Melway has for 30 years published the *'Melway'* street directory for the Melbourne metropolitan area.
- The *Melway* directory accounts for 80-90% of the retail market for Melbourne street directories.
- Except for a 16-month period in 1989-1990, Melway has always distributed the *Melway* directory through wholesalers who each dealt exclusively with a segment of the retail market.
- Robert Hicks (trading as Auto Fashions) was a distributor for the automotive parts retailer segment.
- In February 1995, Melway gave notice of termination of Auto Fashions' distributorship.

- In March 1995, Auto Fashions offered to acquire 30,000 – 50,000 *Melway* directories per annum on the basis that it would sell to any retailer, irrespective of segment.
- Melway declined to supply.

Trial Judge Decision

At first instance, the judge found that Melway had acted in breach of section 46 in refusing to supply its street directory to Auto Fashions. Melway subsequently appealed.

Appeal Court Decision

On appeal, the majority upheld the decision of the trial judge with one judge in dissent. It was accepted on appeal that Melway had a substantial degree of power in the wholesale and retail market for Melbourne street directories. The issues in contention on appeal were whether Melway, in refusing to supply, took advantage of its market power and whether it did so for a proscribed purpose.

Misuse of Market Power

The Majority agreed with the trial judge, who applied the test enunciated by the High Court in *QWI*, and analysed this issue in the following way:

> It is only by virtue of its dominant position in the Melbourne directory market and the absence of a competitive market that Melway can afford, in a commercial sense, to withhold from supplying 30,000 – 50,000 directories at its usual wholesale price and terms to Auto Fashions. If Melway lacked substantial market power – in other words if it were operating in a competitive market – it is highly unlikely that it would stand by, without any effort to compete, and allow Auto Fashions to secure its significant supply of directories from a competitor...one would not expect to observe a refusal to supply 30,000 – 50,000 directories in a competitive market. Accordingly, in refusing supply Melway has taken advantage of its market power.

The judge in dissent noted that Melway had adopted its segmented distribution system when it commenced publishing the *Melway* directory in 1968 and, except for a brief period in 1989 – 1990, had used the same system ever since. He went on to say:

> Thus the operation of its segmented market system was not dependent on the possession of market power. Put another way, the same activity, the maintenance of the segmented distribution system, cannot change its nature simply because a substantial degree of market power has been achieved.

He also stated that:

> The evidence did not support a hypothesis that in a more competitive market Melway would have necessarily supplied 30,000 to 50,000 directories to Auto Fashions because it (Melway) would have otherwise lost these sales. So in refusing to supply Auto Fashions, Melway was not denying itself sales which it would have been commercially compelled to make in a more competitive market...Melway would have made substantially the same sales.

The dissenting judge also noted that Melway had tendered a body of evidence as to the commercial reasons for adopting the distribution system. He accepted that:

> ...the existence of a legitimate business reason which would explain

> the impugned conduct irrespective of the degree of market power necessarily points against a conclusion that such conduct in fact involved taking advantage of that power.

And that:

> The spectacular success of the *Melway* directory was unlikely to have been achieved without some contribution by the particular system adopted.

He concluded that in making the decision to refuse to supply Auto Fashions, Melway did not take advantage of its substantial degree of market power.

Purpose

The Full Court unanimously agreed with the trial judge that preserving the existing distribution system and preventing competition by a would-be distributor against existing distributors were two sides of the same coin. Thus, Melway's purpose of refusing supply was a proscribed purpose.

Summary of Application for Special Leave to Appeal to the High Court

Summary of Applicant's Argument

In summary, the applicant made the following arguments on the law.

Taking Advantage of Market Power

The implementation of the distribution system was not predicated upon a use of market power. Thus, Melway's decision to refuse supply was not an act involving the use of market power. The applicant uses the same system in Melbourne, where it has a large market share, and in Sydney, where it does not. Market power was irrelevant to its decision.

There must be a causal connection between the conduct alleged and the market power pleaded such that it can be said that the conduct was a use of market power.

Factors that indicate Melway did not exploit its power in this case include:

- it used the same system in Sydney;
- it did not want to deal with the respondent for commercial reasons;
- it did not believe the respondent could sell the number of directories requested; and
- any directories the respondent might sell would have been cannibalised from existing distributors.

Proscribed purpose

(a) Melway was motivated by a desire to maintain its distribution system, which it believed was efficient and maximised sales.

(b) Melway gained nothing from restricting competition. It would receive benefits from extra sales, but would have increased costs if it had to deal with an increased number of distributors to make the same number of sales.

(c) The respondent's request for supply arose in the midst of legal negotiations concerning a claim of wrongful termination of the distribution arrangements. The request was not made as part of any considered market plan. Melway had already appointed a wholesaler in place of the respondent.

Queensland Wire Industries

This case should be distinguished from the *QWI* case because:

- there is no downstream monopoly being sought to be created. Melway does not compete with its distributors;
- Melway has offered a legitimate business reason for refusing supply; and
- it is open for the respondent to distribute a competing product manufactured by UBD.

Summary of Respondent's Argument

Proscribed Purpose

(a) All judges agreed that, if there was a taking advantage, it was for the purpose of preventing Auto Fashions from competing with existing distributors.

(b) The implementation of a distribution system in 1966 says nothing about Melway's purpose in refusing supply in 1995.

(c) No basis is advanced for the High Court to make findings of fact reversing those of the trial judge.

Taking Advantage of Market Power

All judges applied *QWI*. The judge in dissent reached a different conclusion on the facts of the matter.

Factual Issues

The trial judge and the Full Court were entitled to conclude that Auto Fashion's request for supply was genuine and that it intended to supply previously unserviced outlets as well as outlets supplied by existing distributors.

There was no evidence to suggest Melway would refuse to supply a potential distributor of a large number of directories at a time when Melway did not possess market power. Absent the brand loyalty that gives Melway its market power, it is inconceivable commercially that Melway would refuse an order for 30,000 – 50,000 directories.

There was evidence that the distribution system produced price distortion and ill-served customers.

Other Issues

Interestingly, the judge at first instance in the ACCC case involving Boral, (which the ACCC lost) was the judge in the minority in the *Melways* case. The *Boral* case is on appeal and the Full Federal Court decision is pending.

As can be seen, Australian law as it stands is somewhat problematic and it will be interesting to see what the High Court does. The regulator intervened in the *Melways* case to put forth some broad arguments in terms of the law and in particular the following:

- made submissions to support the learning of the High Court in *QWI* and refuting the suggestion of Melway and the dissenting judge that the conduct in this matter effectively could not amount to a breach of section 46. The ACCC submitted that the finding of the trial judge, supported by the majority on appeal, was open to the Court and that each case will necessarily turn on its own special facts; and
- provided detailed submissions on the meaning of the 'take advantage' and 'purpose' elements of section 46, along with the appropriate application of efficiency type arguments, "legitimate business reasons" and the relevance of US jurisprudence to section 46.

Unlike Canada, the misuse provision is seldom used in Australia with any great success. This is also in clear contrast to New Zealand. The irony is that in both Canada and New Zealand the threshold for such conduct is arguably higher than in Australia, but in Australia the courts have been far more rigorous in their assessment of misuse of market power and are reluctant to find misuse of market power when there is another strong competitor in the market or where

the conduct complained of is seen by some judges as normal commercial conduct. The *Melways* case will test this.

It is expected that the regulator will pursue further misuse of market power cases but will probably wish to see the outcome of the current cases and appeals. There is a saying in Australian regulatory folklore that unless you can get a 'smoking gun' or 'blood on the floor' you are unlikely to win these kinds of cases. There appears to be some truth in that.

Between 1988 and 1998 there were 50 section 46 cases, 8 by the regulator and 42 by private litigant. The bulk of these cases were lost by the applicant.

The exception was the *QWI* case, but even that had to go up to the High Court before the applicant won. The applicant had actually gone to the regulator to seek assistance but the regulator did not think it was a winnable case, with some justification, because the material obtained on discovery in the private action was what really won the case. That material would not have been available to the regulator at that time as then Australian law did not allow discovery by the regulator, only against the regulator.

There is considerable pressure in Australia to have laws to further control large companies, particularly in the highly concentrated retail sector, banking and petrol. The pressure is often to clearly proscribe the conduct that these companies cannot engage in and to further articulate what is meant by predatory pricing. An added pressure is to have narrowly defined markets to ensure that these companies are further constrained.

These pressures have so far been resisted despite a wide ranging Parliamentary Inquiry last year. Much will depend on whether or not firstly, the misuse of market power provisions are seen to be effective and secondly, whether the business to business unconscionability provisions that have been in the *Trade Practices Act* since 1997 are regarded as successful in assisting small business.

One outstanding issue is whether or not in relation to misuse of market power the Court should be given the power to order a divestiture. The Microsoft case has rekindled a dormant albeit real argument in the Australian Trade Practices and business communities.

Notes

[1] (1989) 167 CLR 177 [hereinafter *QWI*].
[2] [1999] FCA 1318 [hereinafter *Boral*].
[3] (1999) ATPR 41 668 [hereinafter *Melways*].