
Market Definition and Substitutability – Australian Courts Continue to Struggle with Part IV of the *Trade Practices Act 1974 (Cth)*

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Abstract

Australian courts have gradually developed a more economics based approach to the interpretation of Part IV of the Trade Practices Act 1974 (Cth). Despite this the courts still appear to encounter difficulties in defining the relevant market in Part IV cases. In particular, courts appear perplexed by market definition and the theory of substitutability.

Four recent cases concerned with Part IV of the Act, culminating in the decision in *News Limited v. Australian Rugby Football League Limited & Ors* (the 'Super League case'), are analysed to demonstrate the manner in which courts still struggle to apply economic theory to the Act.

1. Introduction

It has been observed that 'the judgements of the Australian courts do not exactly bristle with economic evidence'.¹ Fortunately, trade practices law has evolved since

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1 Maureen Brunt 'The Use of Economic Evidence in Antitrust Litigation: Australia' (1986) 14 *Australian Business Law Review* 261 at 266.

the times when a dictionary² was used to define the economic terms of Part IV of the *Trade Practices Act 1974* (Cth) ('the Act'). In recent years the approach of courts to concepts such as 'market' has increasingly gained an economic focus. Following the insertion of s.4E into the Act in 1977,³ courts have become aware of the need to apply an economic theory of supply and demand substitutability when defining the terms of Part IV. Despite this advancement, the concept of substitutability is one area in which the courts still appear to encounter difficulties in applying economic theory to the Act.

This paper analyses the failure by courts in Australia to adequately apply the fundamental economic theory of substitutability of demand and supply in defining the relevant market for the purposes of Part IV of the Act. Four recent cases, culminating in the recent decision of Burchett J in *News Limited v. Australian Rugby Football League Limited & Ors*,⁴ are analysed to illustrate the manner in which despite applying economic principles to the definition of market, courts still arrive at erroneous market definitions. A central weakness in the courts' methodology in these situations appears to be an inappropriately simplistic assessment of substitutability, which results from combining economic theory with the court's view of 'commercial reality'.

2. Economic Concepts and the Act

Over recent years economic theory has become an important element in the interpretation of Part IV of the Act. Since the days when it was possible for a court to find that a market for Datsun cars existed on the Gold Coast of Australia,⁵ or to treat economic evidence with suspicion,⁶ the approach to interpretation of Part IV of the Act has gradually matured. Since the 1977 amendments to the Act 'the courts, the Tribunal and the TPC have given economic theory steadily growing recognition in construing Part IV'⁷ of the Act. The High Court in *Queensland Wire Industries v. The Broken Hill Proprietary Company Limited & Anor*⁸ demonstrated that the object of the Act and the concepts therein are economic.⁹ This decision provided 'clear

2 *Top Performance Motors Pty Limited v. Ira Berk (Queensland) Pty Limited* (1975) ATPR 40-004.

3 Section 4E of the Act states "For the purposes of this Act, unless the contrary intention appears 'market' means a market in Australia and, when used in relation to any good or services, includes a market for those goods or services that are substitutable for, or otherwise competitive with, the first-mentioned goods or services".

4 *News Limited v. Australian Rugby Football League Limited & Ors* (1996) ATPR 41-466.

5 *Top Performance Motors Pty Limited v. Ira Berk (Queensland) Pty Limited* (1975) ATPR 40-004.

6 *Hecar Investments (No. 6) Pty Ltd v. Outboard Marine Australia Pty Ltd* (1982) ATPR 40-327.

7 Stephen Corones *Competition Law and Policy in Australia* Law Book Co. Ltd 1990 at 43.

8 (1989) ATPR 40-925.

9 *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor* (1989) ATPR 40-925, per Mason CJ, Wilson J at 50,009; Deane J at 50,011. See also Karen Yeung 'The Court-Room Economist in Australian Antitrust Litigation: An Underutilised Resource?' (1992) 20 *Australian Business Law Review* 461 at 463.

affirmation of the relevance of economic concepts'¹⁰ in the interpretation of the Act.

Despite the recognition that courts should adopt an economic approach to the construction of Part IV of the Act, there are problems in the 'blending of economic and legal concepts in the application of the statute'.¹¹ The rules of evidence in court trials are not predisposed towards the admission of the testimony of economic experts due to courts drawing a distinction between the admissibility of 'inferences and the facts on which they are based'.¹² Economic theories are often based on hypothetical situations or assumptions which cannot be wholly substantiated by evidence.¹³ This may result in the exclusion of the testimony of economists,¹⁴ or the rejection of their opinions¹⁵. A further problem is that even when expert economic evidence is received it is often contradictory,¹⁶ or not wholly understood by the court.¹⁷ Various solutions have been suggested in order to provide for the receipt of economic analysis and information in Part IV cases.¹⁸

The result of applying economic concepts to a legal framework impeded by such limitations has been that in Part IV cases 'a hybrid approach to statutory interpretation has evolved, which derives assistance both from the discipline of economics and ordinary commercial usage'.¹⁹ This is illustrated in many cases by the court referring to the analysis of a 'market' in economic terms, whilst emphasising that 'commercial realities' must also be considered.²⁰ Although it is clearly relevant to consider market realities in defining the market, the problem with such a 'half-way house' approach is that 'judges are more inclined to discard economic principles where those principles are counter-intuitive or lead to counter intuitive results'.²¹

10 Maureen Brunt 'Market Definition Issues in Australian and New Zealand Trade Practices Litigation', (1990) 18 *Australian Business Law Review* 86 at 89.

11 Maureen Brunt 'Lawyers and Competition Policy', *Australian Lawyers and Social Change*, p.266 at p.290, also quoted in Karen Yeung, *supra* n.9 at 461.

12 Maureen Brunt, *supra* n.1 at 304.

13 *News Limited v. Australian Rugby Football League Limited & Ors*, (1996) ATPR 41-466 at 41,669.

14 *Arnotts Limited & Ors v. Trade Practices Commission* (1990) ATPR 41-061.

15 *QIW Retailers Limited v. Davids Holdings Pty Limited & Ors; Attorney-General of the Commonwealth v. Davids Holdings Pty Limited* (1993) ATPR 41-226.

16 *Ibid*, where seven economists offered three different market definitions.

17 See for example *Re Queensland Independent Wholesalers Limited* (1995) ATPR 41-438 per Lockhart J at 40,950 — 'it has not been altogether easy to resolve the considerations [of four different economic experts] into a workable framework for analysis'. See also Pincus J in *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor* (1987) ATPR 40-810 at 40,812.

18 Stephen Corones 'Is the Adversary Process Appropriate in Restrictive Trade Practices Cases?' (1996) 24 *Australian Business Law Review* 71; Maureen Brunt, *supra* n.1; Karen Yeung, *supra* n.9 at 461.

19 Karen Yeung, *supra* n.9 at 471.

20 *Singapore Airlines Limited v. Taprobane Tours WA Pty Ltd* (1992) ATPR 41-159 per French J at 40,170; *Australia Meat Holdings Pty Ltd v. Trade Practices Commission* (1989) ATPR 40-932 per Davies J at 50,091; *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor* (1987) ATPR 40-810 at 48,812 per Pincus J.

21 Karen Yeung, *supra* n.9 at 473.

It also indicates that despite the acceptance of economic testimony, courts may hold lingering doubts as to the ability of economics to explain the real workings of a market.

The outcome of this situation is that in an attempt to blend economic theory with perceived market place reality the courts are liable to ignore economic theory and concentrate solely on a misguided notion of market place reality.²² Alternatively courts may rely on overly simplified economic theory ('economic theory with a dash of commercial reality' perhaps) with the result that actual market place structure is ignored.²³

The economic theory/practical reality approach can be seen to be a contributing factor in severable debatable market definitions in recent Part IV cases. As a result of this approach, courts have incorrectly assessed supply and demand side substitutability. The result has been market definitions which do not accord with market-place realities.

3. Market Definition and Substitutability

Definition of the relevant market in trade practices cases is usually the first step adopted by the courts, the Australian Competition Tribunal²⁴ and the Australian Competition and Consumer Commission²⁵ ('the Commission') in assessing whether a breach of Part IV of the Act has occurred.²⁶ Maureen Brunt has noted with amusement the statement of the Trade Practices Tribunal in *Re Queensland Co-Op. Milling Association Ltd; Defiance Holdings Ltd*²⁷ that 'the concept of a market [is] basically a very simple idea'.²⁸ Despite what would superficially appear to be a straight forward process, the definition of the relevant market has proved to be an issue with which the courts have struggled.

Since the clearly erroneous decision in *Top Performance Motors Pty Limited v. Ira Berk (Queensland) Pty Limited*²⁹ which adopted a dictionary definition of the term 'market', the courts and the Tribunal have gradually developed a more economically sound approach to the definition of the relevant market in trade practices cases. There is now clear precedent for the interpretation of the term 'market' for the purposes of the Act.

22 See for example the examination below of *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor* (1988) ATPR 40-841.

23 For example the examination below of *QIW Retailers Limited v. Davids Holdings Pty Limited & Ors; Attorney-General of the Commonwealth v. Davids Holdings Pty Limited* (1993) ATPR 41-226, and *Davids Holdings Pty Limited v. Attorney-General of the Commonwealth* (1994) ATPR 41-304.

24 Formerly the Trade Practices Tribunal.

25 Formerly the Trade Practices Commission.

26 Stephen Corones *supra* n.7 at 43.

27 *Re Queensland Co-operative Milling Association Ltd, Defiance Holdings Ltd* (1976) ATPR 40-012.

28 Maureen Brunt, *supra* n.10 at 86, quoting the decision of the Trade Practices Tribunal (of whom she was a member) in *Re Queensland Co-operative Milling Association Ltd, Defiance Holdings Ltd* (1976) ATPR 40-012 at 17,247.

29 *Top Performance Motors Pty Limited v. Ira Berk (Queensland) Pty Limited* (1975) ATPR 40-004.

The starting point is the explanation of 'market' given by the Trade Practices Tribunal in *Re Queensland Co-operative Milling Association Ltd; Defiance Holdings Ltd*³⁰ in what has become the basic definition adopted in Australia. Briefly, the Tribunal held that 'a market is the field of actual and potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given a sufficient price incentive'.³¹ Subsequent cases have further expanded the interpretation of what constitutes a market for the purposes of the Act.³²

The Commission analyses four dimensions of a market in the process of market definition. These dimensions are:

1. product;
2. geographic;
3. functional; and
4. time.³³

Product market analysis consists of identifying the product supplied by the firm in question, as well as those firms 'which supply, or would supply, a closely substitutable product in the event of a significant price rise, or equivalent exercise of market power' by the firm.³⁴ Factors relevant to this assessment include:

1. the end use of the product and any potential substitutes;
2. any physical or technical characteristics of the product;
3. the past behaviour of buyers as to the likelihood of switching to a substitute product;
4. the views of suppliers in relation to the impact of price and marketing decisions of suppliers of potential substitute products on sales of their own product.³⁵

The geographic market is delineated by identifying the area over which the firm in question, and any potential suppliers, distribute the product and in which consumers are able to source the product on a practical basis. The functional market refers to the functional level in the system of supply of the good (for example the wholesale or retail level) at which the firm operates, and whether there exist any close substitution possibilities at another functional level would constrain the firm from monopolistic behaviour.³⁶

30 *Re Queensland Co-operative Milling Association Ltd, Defiance Holdings Ltd* (1976) ATPR 40-012.

31 *Ibid* at 17,247.

32 See for example *In re Tooth & Co Ltd; In re Tooheys Ltd* (1979) ATPR 40-113; *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor* (1989) ATPR 40-925; *Singapore Airlines Limited v. Taprobane Tours W.A. Pty Ltd* (1992) ATPR 41-159.

33 Australian Competition and Consumer Commission *Merger Guidelines* Revised July 1996 at 31.

34 *Ibid* at 36.

35 *Ibid*.

36 *Ibid* at 37.

The time dimension of a market is the period over which any substitution possibilities are considered. The decision of the Trade Practices Tribunal in *Re Tooth & Co Ltd; In re Tooheys Ltd*³⁷ stated that 'we should be basically concerned with substitution possibilities in the longer run'.³⁸

From the above court decisions and the approach of the Commission it is clear that in defining the relevant market for the purposes of the Act that 'the focus quite clearly is on substitutability, with cross price elasticities of demand and supply providing a quantitative assessment of substitutability'.³⁹ In the High Court decision of *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor*⁴⁰ Dawson J stated:

The basic test involves the ascertainment of the cross-elasticities of both supply and demand, that is to say, the extent to which the supply of or demand for a product responds to a change in the price to another product.⁴¹

Toohey J made a similar observation.⁴²

The economic theory of substitutability involves an assessment of both the demand and supply sides of a market. Substitutability on the demand side involves identifying the range of products which in the event of a price rise for one good a consumer would consider to be close (although not necessarily perfect) substitutes.⁴³ The extent to which consumers will substitute one good for another in the event of such a price rise is measured by the cross-elasticity of demand. The cross-elasticity of demand measures the extent to which an increase in the price of one product would lead to an increase in the consumption of a substitute product. The Commission has adopted a five percent to ten percent level as the relevant price rise to consider for assessing substitutability of products.⁴⁴

Substitutability on the supply side involves ascertaining all alternative sources of supply available in the event of a rise in the price of a product.⁴⁵ It includes 'firms which are currently supplying close substitutes [to the product] or which can easily switch production to supply the relevant product within an accessible geographic area for the firm's customers'.⁴⁶ The cross-elasticity of supply measures the extent

37 *In re Tooth & Co Ltd; In re Tooheys Ltd* (1979) ATPR 40-113.

38 *Ibid* at 18,196.

39 Rhonda Smith 'The Practical Problems of Market Definition Revisited' 23 (1995) *Australian Business Law Review* 52 at 52. See also Stephen Corones *supra* n.7 at 83.

40 *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor* (1989) ATPR 40-925.

41 *Ibid* at 50,014.

42 *Ibid* at 50,021.

43 Australian Competition & Consumer Commission *supra* n.33 at 34.

44 Australian Competition & Consumer Commission *Draft Merger Guidelines Background Paper* 1992 at 16.

45 Australian Competition & Consumer Commission *Draft Merger Guidelines* 1992 at 23.

46 *Ibid* at p.24.

to which an increase in the price of a product by one supplier would lead to an increase in the supply of another product by another firm.⁴⁷

The economic theory of substitutability, although crucial to the definition of a market, has proved problematic in actual practice. Whilst the cross-price elasticity of demand or supply is a useful indicator of the boundaries of a market, there is rarely sufficient pricing information available to enable an actual figure to be calculated.⁴⁸ In addition, whilst courts repeatedly pay lip service to the concept of supply side substitutability, in reality this side of market definition appears to have been ignored by the courts in their assessment of the market. As Toohey J noted in *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor*⁴⁹ 'in delineating the scope of the product market demand substitutability has often been emphasised at the expense of supply substitutability'.⁵⁰

The courts in the United States are not required to consider the supply side in their assessment of the relevant market.⁵¹ Supply side substitutability is used only to assess actual and potential market participants in order to calculate market shares and market power. Demand substitutability alone is used to assess market definition. It has been observed that some Australian commentators regard this as a 'serious deficiency'⁵² in US anti trust law.

The importance of considering both demand and supply side substitutability is illustrated by several recent Australian cases involving the definition of a market for the purposes of the Act. In these cases it is arguable that courts have misapplied the concept of substitutability with the result that market definition has been seriously flawed. This problem appears to stem from the fact, outlined above, that courts either misapply economic theory when addressing the issue of substitutability, or alternatively ignore what economic analysis of substitution possibilities reveals and opt for a market definition based more on perceived current commercial realities. Illustrations of this dichotomy are evidenced in the cases analysed below.

47 Cross-price elasticity can be measured by the expression $\% \Delta Q1 / \% \Delta P2$. Where Q1 is the quantity of good 1 substituted for an increase in P2, the price of good 2. If goods are within the same market the cross-price elasticity of demand or supply is said to be 'high', that is, the goods are substitutable for each other — Jill Walker *Market Definition* Australian Competition & Consumer discussion paper 1995 at 4.

48 Rhonda Smith, *supra* n.33 at 52.

49 *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor* (1989) ATPR 40-925.

50 *Ibid* at 50,021.

51 George Hay 'Market Power in Australian Antitrust: An American Perspective', (1994) 1 *Competition & Consumer Law Journal* 215 at 219; Australian Competition & Consumer Commission *supra* n.44 at 18.

52 George Hay *supra* n.45 at 219.

4. *QIW Retailers Limited v. Davids Holdings Pty Limited & Ors; Attorney-General of the Commonwealth v. Davids Holdings Pty Limited*

The case of *QIW Retailers Limited v. Davids Holdings Pty Limited & Ors; Attorney-General of the Commonwealth v. Davids Holdings Pty Limited*⁵³ illustrates an example of a court misconstruing demand side substitutability, with the result that a submarket was identified as the relevant market. The case arose due to attempts by Davids Holdings Pty Ltd to take over Queensland Independent Wholesalers Limited.

At first instance Spender J held that the relevant market was the market for the supply of groceries by independent wholesalers to independent retailers in Queensland and Northern New South Wales. The downstream market, namely the retail sales of groceries by independent retailers and the major vertically integrated chain stores, was considered to be a separate market. This narrow definition of the market was upheld by the Full Federal Court.⁵⁴

Both at first instance and on appeal the Court found that the merger of the only two independent grocery wholesalers operating in Queensland would mean that independent retailers had no other sources of supply. The cross elasticity of supply in such a case would be close to zero because none of the vertically integrated chain stores would supply independent retailers, and the prospect of a new independent wholesaler entering the market was considered remote. Both Courts rejected the contention that there was no distinction between the wholesale and retail functional levels in the supply of groceries to consumers.

The decision was criticised by various commentators⁵⁵ who suggested that the definition of market was incorrect. The subsequent decision of the Trade Practices Tribunal in *Re Queensland Independent Wholesalers Limited*⁵⁶ throws the validity of the decision of the Full Federal Court in *Davids Holdings Pty Limited v. Attorney-General of the Commonwealth*⁵⁷ into doubt. In 1995 Davids Holdings Pty Limited (Davids) applied for, and was granted, authorisation from the Trade Practices Commission for the acquisition of the independent grocery wholesaler Composite Buyers Limited (CBL). Queensland Independent Wholesalers Limited (QIW) applied to the Trade Practices Tribunal for a review of this decision, arguing a narrow market definition similar to that adopted in *Davids Holdings Pty Limited v. Attorney-General of the Commonwealth*⁵⁸, namely a market limited to the supply of groceries from independent wholesalers to independent retailers.

The Tribunal rejected this definition, and instead held that there was 'an

53 *QIW Retailers Limited v. Davids Holdings Pty Limited & Ors; Attorney-General of the Commonwealth v. Davids Holdings Pty Limited* (1993) ATPR 41-226.

54 *Davids Holdings Pty Limited v. Attorney-General of the Commonwealth* (1994) ATPR 41-404.

55 George Hay, 'Market Definition and Market Dominance: Issues From the Davids-QIW Merger Case' (1995) 3 *Competition & Consumer Law Journal* 1; Maureen Brunt 'Issues From the Davids/QIW Merger Case — a Comment' (1995) 3 *Competition & Consumer Law Journal* 16.

56 *Re Queensland Independent Wholesalers Limited* (1995) ATPR 41-438.

57 *Davids Holdings Pty Limited v. Attorney-General of the Commonwealth* (1994) ATPR 41-404.

58 *Ibid.*

Australia-wide or national market for the distribution of grocery products to the consuming public via integrated retail chains and independent wholesalers supplying independent retailers'.⁵⁹ The Tribunal distinguished two important sub-markets within this overall market, namely markets for the supply of groceries by independent wholesalers to independent retailers in the New South Wales and Victorian regions respectively. Aside from a different geographic location, such a sub-market is what the courts in *QIW Retailers Limited v. Davids Holdings Pty Limited & Ors; Attorney-General of the Commonwealth v. Davids Holdings Pty Limited*⁶⁰ and *Davids Holdings Pty Limited v. Attorney-General of the Commonwealth*⁶¹ held to be the overall market.

Spender J in *QIW Retailers Limited v. Davids Holdings Pty Limited & Ors; Attorney-General of the Commonwealth v. Davids Holdings Pty Limited*⁶² concluded that on the demand side of the market for the supply by independent wholesalers to independent retailers that there would be almost no substitutability if Davids merged with QIW.⁶³ Independent retailers could not obtain wholesaling services from any of the large chain stores, since these were fully vertically integrated and unlikely to supply competitors.⁶⁴ There was also held to be little prospect of a new entrant entering the wholesale grocery distribution business in Queensland due to barriers to entry and the economies of scale required to make such a business profitable.⁶⁵ The Full Federal Court accepted these findings.

The decisions of Spender J and the Full Federal Court illustrate a simplistic approach to the determination of demand side substitutability, and the manner in which an incorrect assessment of this fundamental market characteristic can lead to the wrong market being identified. The Courts held that there was a margin of some two percent in which prices could be raised by the merged entity without affecting the level of demand at the retail level for the services of independent retailers. For this reason the Courts identified a separate market for the wholesale supply of groceries to independent retailers in Queensland. Had the cross elasticity of demand for wholesaling services been considered at a more economically relevant level,⁶⁶ it would have been apparent that a rise in the price of wholesaling

59 *Re Queensland Independent Wholesalers Limited* (1995) ATPR 41-438 at 40,952.

60 *QIW Retailers Limited v. Davids Holdings Pty Limited & Ors; Attorney-General of the Commonwealth v. Davids Holdings Pty Limited* (1993) ATPR 41-226.

61 *Davids Holdings Pty Limited v. Attorney-General of the Commonwealth* (1994) ATPR 41-404.

62 *QIW Retailers Limited v. Davids Holdings Pty Limited & Ors; Attorney-General of the Commonwealth v. Davids Holdings Pty Limited* (1993) ATPR 41-226 at 41,138.

63 *Ibid.*

64 In 1996 Woolworths took control of the grocery wholesaling company Australian Independent Wholesalers. In early 1997 this Woolworths subsidiary commenced supplying other independent supermarkets, thus creating direct competition between Davids and Woolworths in the provision of grocery wholesaling services. This development renders obsolete the market definition proposed by Spender J and the Full Federal Court.

65 *Supra* n. 62 at 41,139.

66 As noted above the Australian Competition and Consumer Commission has adopted a 5%-10% level as the level to which a hypothetical profit maximising monopolist would raise prices with the

services provided by a combined Davids/QIW would have had a ripple effect reaching wider than the wholesale market.

If a combined Davids/QIW raised prices the effect would be higher prices charged by independent retailers, a resulting shift in demand from independent retailers to chain stores, and ultimately a rise in the level of wholesale services carried out by the wholesaling divisions of those chain stores to meet the increased sales at chain retail stores.⁶⁷ The fact that a rise in the price of wholesaling services by Davids/QIW would have led to a rise in demand for wholesaling services of other companies is strong evidence of a high cross-elasticity of demand between the services. Accordingly this is an indication that the market as defined by the Court was too narrow.

The misapplication of the concept of substitutability resulted in both Courts identifying as the relevant market what is perhaps more appropriately viewed as a wholesale sub-market. The overall market is more accurately characterised as the distribution of grocery products to the consuming public via integrated retail chains and independent wholesalers supplying independent retailers.⁶⁸ By incorrectly applying the concept of substitutability the court not only ignored economic theory which would have indicated a broader market via the cross-elasticity of demand, but ignored the actual 'commercial reality' that the level of competition in the retail market impacts directly on the ability of a wholesaler to raise prices.

5. Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor

The High Court decision in *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor*⁶⁹ confirmed the importance in examining both demand and supply side substitutability when defining the relevant market in trade practices cases.⁷⁰ The case had been appealed from the Full Federal Court where it was held that there was no market for BHP's Y-bar because the product had never been sold.⁷¹ At first instance Pincus J did not define the relevant market conclusively, because he rejected the concept of supply side substitutability.⁷² The decisions of Pincus J and the Full Federal Court reflect the problem in trade practices cases of courts rejecting economic evidence regarding substitutability and instead

result of a substantial lessening of competition — Australian Competition & Consumer Commission *Draft Merger Guidelines Background Paper* 1992 at 11.

67 George Hay *supra* n.49 at 5.

68 *Re Queensland Independent Wholesalers Limited* (1995) ATPR 41-438 at 40,952.

69 *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor* (1989) ATPR 40-925.

70 Stephen Corones *supra* n.7 at 48.

71 *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor* (1988) ATPR 40-841.

72 *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor* (1987) ATPR 40-810 at 48,812.

opting for what they perceive to be a more commercially realistic definition of the market.

The Full Court did not even consider substitutability in its reasoning, since it was simply held that a market in which no sales occurred could not constitute a market. The Court instead adopted a 'common sense' but clearly economically flawed view that no sales equated with no market. Whilst Pincus J considered supply side substitutability, as mentioned above he rejected its application as leading to 'odd consequences'.⁷³ Economic evidence was presented to Pincus J regarding both supply side substitutability and the fact that in economic terms a market could exist even if no sales occurred therein. Both Pincus J and the Full Federal Court ignored this evidence.⁷⁴

Whilst recognising the importance of supply side substitutability, it is interesting to note that in their joint judgement Mason CJ and Wilson J 'concentrated on demand substitution rather than supply substitution'.⁷⁵ It appears that even in a High Court judgement which confirms the importance of supply side substitutability there is a reluctance by judges to explore the issue in depth.

6. *Taprobane Tours WA Pty Ltd v. Singapore Airlines Limited*

The case of *Taprobane Tours W.A. Pty Ltd v. Singapore Airlines Limited*⁷⁶ provides a further example of an erroneous market definition that can arise from an incorrect assessment of substitutability, particularly when a monopoly supplier exists at some level of the functional market. At first instance the judge held the market to comprise the supply of airline services to persons engaged in providing wholesale tours to the Maldives.⁷⁷ There was only one such supplier in Australia, namely Singapore Airlines Limited (Singapore Airlines). On appeal this decision was overturned and a market for the sale of wholesale tours for island holidays was identified.⁷⁸

The trial judge appears to have fallen into the same error as the Court in *QIW Retailers Limited v. Davids Holdings Pty Limited & Ors; Attorney-General of the Commonwealth v. Davids Holdings Pty Limited*.⁷⁹ The trial judge did not examine the extent to which Singapore Airlines' ability to raise the wholesale prices for tours to the Maldives would be constrained by demand side substitutability. Both wholesalers and customers were able to substitute other island holiday destinations for a Maldives tour. The case illustrates the manner in which a judge's perception of 'commercial reality' may be seriously at odds with what economic theories of supply and demand side substitutability would otherwise indicate.

73 *Ibid.*

74 Karen Yeung *supra* n.9 at 468.

75 Stephen Corones *supra* n.7 at 49.

76 *Taprobane Tours WA Pty Ltd v. Singapore Airlines Limited* (1990) ATPR 41-054.

77 *Ibid* at 51,705 per Lee J.

78 *Singapore Airlines Limited v. Taprobane Tours WA Pty Ltd* (1992) ATPR 41-159 at 40,178.

79 *QIW Retailers Limited v. Davids Holdings Pty Limited & Ors; Attorney-General of the Commonwealth v. Davids Holdings Pty Limited* (1993) ATPR 41-226.

7. *News Limited v. Australian Rugby Football League Limited & Ors*

The case of *News Limited v. Australian Rugby Football League Limited & Ors*⁸⁰ is the latest decision of the courts involving a market definition which did not involve a supply side analysis.

The much publicised case involved an attempt by News Limited to set up a rival Australian rugby league competition, Super League, to the competition run by the New South Wales Rugby Football League Limited and the Australian Rugby Football League Limited ('the League'). In November 1994, in an effort to prevent Super League being established, the League sent out a Commitment Agreement to all clubs in the premier division competition providing for the continued participation of each club until the end of the 1999 playing season. Further agreements ('Loyalty Agreements') were entered into by the clubs in February 1995. News Limited commenced proceedings against the League arguing that the Commitment Agreement and/or the Loyalty Agreement were void pursuant to s.45 and s.46 of the Trade Practices Act.

News Limited in its Further Amended Statement of Claim pleaded a variety of markets. These included:

1. A 'Rugby League Competitions Market', being a market for the supply of the service of conducting national premier rugby league competitions to various customers. Such a service included supplying viewing of games to members of the public; television rights to broadcast television proprietors; transmission rights to pay television proprietors; broadcast rights to broadcast radio proprietors; intellectual property rights to persons associated with merchandising; and sponsorship rights to commercial and other sponsors.
2. A 'Teams Market', being a market for the supply of teams of premier players suitable for participation in the Rugby League Competitions Market.
3. A 'League Market', being a market for the supply of a rugby league competition, participants of which include teams of suitable premier players supplied by corporate clubs, and a competition organiser who provides the service of conducting a competition, as well as the other associated services outlined in the Rugby League Competitions Market.
4. Various other markets included within the Rugby League Competitions Market.

Burchett J held that the relevant market for the purposes of the Act was wider than any of the markets relating to rugby league proposed by News Limited.⁸¹ Other forms of sport and entertainment were held to be relevant in defining the market. Burchett J did not conclusively define the limits of the market in the case, leaving an open ended sports/entertainment market. In this market rugby league clubs competed against other forms of entertainment which at the least included 'rugby

80 *News Limited v. Australian Rugby Football League Limited & Ors* (1996) ATPR 41-466.

81 *Ibid* at 41,685.

union, soccer, Australian rules football and basketball'.⁸² Burchett J reached this conclusion largely on the basis that rugby league clubs competed with these other sports for corporate sponsorship, for spectators, for media coverage, for television audiences and also for merchandise sales.⁸³ In the long term rugby league was seen to be substitutable in all these areas with the other main professional team sports played in Australia.

It is interesting to note that Burchett J criticised one of the markets proposed by News Limited because it 'completely misconceives the principle of substitutability'.⁸⁴ However, Burchett J appears to have himself overlooked a major principle of substitutability in defining the relevant market, which is that both supply and demand side substitutability must be assessed. Burchett J's judgement concentrates wholly on demand side substitutability for rugby league and the effect that a rise in prices would have upon the level of demand for the sport. The judgement does not address the issue of supply side substitutability in any detailed manner. This failure can be seen to be a major omission in the analysis of the market involved.

The market for the supply of rugby league to the consumer can be described as one in which professional football players are employees under a contract of service to their respective clubs.⁸⁵ Such contracts are outside the jurisdiction of the Trade Practices Act pursuant to s.4D(1). Those clubs then supply a team to the League to compete in the national competition, in accordance with the provisions of the League's memorandum and articles of association, and various League rules and regulations.⁸⁶ It was not pleaded that the League and the clubs were in competition with each other, and Burchett J held that the clubs themselves did not compete against each other.⁸⁷ The League itself provides a competition to the various demand side consumers outlined above, namely spectators, sponsors, and the media. By concentrating on demand side substitutability, and holding that rugby league clubs competed against other forms of entertainment, Burchett J appears to have overlooked the situation on the supply side.

Burchett J ironically refers to the US case of *Philadelphia World Hockey Club Inc v. Philadelphia Hockey Club Inc*⁸⁸ in which it was found that the National Hockey League had contravened US antitrust laws by precluding players from joining teams in a rival league. Burchett J observed that:

Obviously, the players of hockey are not competing, for places in professional hockey teams, against other persons who are players of basketball or football; they are only

82 *Ibid.*

83 *Ibid* at 41,680.

84 *Ibid* at 41,685.

85 *Ibid* at 41,653.

86 *Ibid* at 41,650.

87 *Ibid* at 41,698. On appeal the Full Federal Court rejected this finding, stating that "the clubs were or were likely to be in competition for the services of the League and ARL as competition organisers" – *News Limited & Ors v Australian Rugby Football League & Ors* (1996) ATPR 41-521 at 42,650.

88 *Philadelphia World Hockey Club Inc v. Philadelphia Hockey Club Inc* (1972) 351 F Supp 462.

competing against other hockey players. Similarly, hockey clubs do not compete *for players* against basketball clubs or football clubs. Accordingly a market confined to hockey is easy to comprehend in the context of this case.⁸⁹

Burchett J considered the restriction in that case to be of 'a special kind',⁹⁰ apparently because it related to the players rather than the clubs. With respect it is difficult to see how the situation in *Philadelphia World Hockey Club Inc v. Philadelphia Hockey Club Inc*⁹¹ differed greatly from the supply side situation confronting both players and clubs who were attempting to enter a rival competition to that provided by the League.

As outlined above, an assessment of supply side substitutability involves identifying those firms which are currently supplying a close substitute to the product, or those firms which have the ability to switch production to supply the relevant product within an accessible geographic area. An assessment of supply side substitutability in the circumstances of the case would require analysis of the ability of alternative suppliers to provide a rugby league competition. Although it has been noted that 'cases where there are no alternative outlets for supply or where alternative outlets are unlikely to develop are probably rare',⁹² the position of the League in relation to the supply of a rugby league competition may be one such situation.⁹³

It is extremely unlikely that organisations such as the Australian Football League or the Australian Soccer Federation would provide a rival rugby league competition in the event of monopolistic behaviour by the Australian Rugby Football League Limited. In addition, Australian rules clubs or basketball clubs cannot supply the League with their services, nor is it likely that any other sport besides rugby union would be capable of supplying players or forming clubs that would offer a valid supply side substitute to the existing rugby league clubs.

In his analysis of demand side substitutability Burchett J appears to have conducted an assessment of the cross elasticity of demand, as evidenced by his statement that other competing sports 'would attract a significant proportion of rugby league's crowds if the League chose to attempt to assert market power by significantly raising prices or giving less'.⁹⁴ Even assuming Burchett J was correct in identifying rugby union, soccer, basketball and Australian rules football as close substitutes for rugby league, a thorough assessment of the cross elasticity of supply between rugby league and those sports should have been conducted to assess the

89 *News Limited v. Australian Rugby Football League Limited & Ors* (1996) ATPR 41-466 at 41,675. Emphasis as per original.

90 *Ibid* at 41,675.

91 *Philadelphia World Hockey Club Inc v. Philadelphia Hockey Club Inc* (1972) 351 F Supp 462.

92 Australian Competition & Consumer Commission *Draft Mergers Guideline Background Paper* 1992 at 10.

93 The Australian Competition and Consumer Commission has noted that market power on the supply side of markets may arise in respect of the market power of large retailers over the distribution of the products of small producers — Australian Competition & Consumer Commission *supra* n.44 at 10. This situation is analogous to the supply of rugby league teams by clubs to the League, such clubs having no other outlet in which to market their product.

94 *News Limited v. Australian Rugby Football League Limited & Ors* (1996) ATPR 41-466 at 41,685.

supply side implications of a rise in the price of a league ticket.

It is interesting to examine what the cross elasticity of supply in the case indicates about the substitutability of rugby league for the other sports outlined. As mentioned above, cross elasticity of supply measures the extent to which an increase in the price of a product by one supplier would lead to an increase in the supply of another product by another firm. A small but significant rise in the price of a rugby league ticket⁹⁵ appears unlikely to lead to a significant increase in the supply of soccer, basketball or Australian rules football games. On the demand side, an increase in the level of spectator support for those alternatives sports may occur to some degree following a rise in the price of a rugby league ticket. However, in measuring the supply side response of other sports, it is questionable whether even a ten percent rise in the price of a rugby league ticket would for example cause the Australian Football League or the Australian Soccer Federation to increase the level of supply of their sport.

Burchett J acknowledged that the very nature of national sporting leagues involves a restriction in the number of clubs involved, and strict tests for the admission of new members, in order for the financial viability of the league to be maintained.⁹⁶ Even with restricted membership, the financial situation of various professional Australian sporting clubs, most notably several Australian rules clubs, is precarious. In such a situation it is questionable whether, aside from the natural growth rate of the competition due to an increasing population, any new clubs would be formed specifically due to monopolistic behaviour by the League. For example in the traditional rugby league states of New South Wales and Queensland it is unlikely that a new Brisbane or Sydney Australian rules football team would be established because the price of attending a rugby league match increased.

The test for supply side substitutability is also based on the short term ability of an alternative supplier to switch their production facilities to supply a substitute product without significant investment.⁹⁷ News Limited invested of hundreds of millions of dollars in an attempt to create an alternative rugby league competition in which clubs could participate, and a multimillion dollar cost would be incurred to establish a new football team (even assuming that existing clubs agreed to such an addition). These factors strongly suggest that any short term ability of potential suppliers to constrain an exercise of monopoly power by the League is limited.

The above analysis suggests that there is a low cross elasticity of supply between rugby league and sports such as soccer, Australian rules football and basketball. The success of the Australian Rugby Union Ltd's Super Ten series in 1996⁹⁸ on the other hand may be seen as evidence a medium level of cross elasticity of supply between

95 As noted, a 5% to 10% price increase level has been adopted by the Australian Competition and Consumer Commission. A 10% price rise in the cost of a \$25 rugby league ticket would see the ticket priced at \$27.50.

96 *News Limited v. Australian Rugby Football League Limited & Ors* (1996) ATPR 41-466 at 41,964-41,695.

97 Australian Competition and Consumer Commission, *supra* n.33 at 34.

98 Now expanded to the 1997 Super Twelve Series.

rugby union and rugby league. During the period of turmoil brought about by the entire Super League debate, the Super Ten series provided an increase in the supply of rugby union games to the viewing public, the media and sponsors. This increase provides a basic indication that rugby union may offer a valid supply side substitute to rugby league. This substitutability is apparent in two areas. In terms of supply side substitutability itself, the Australian Rugby Union Ltd has some ability to supply potential teams to compete in a rugby league competition. It may also be possible, although less likely, that due to the similarities between rugby league and rugby union the Australian Rugby Union Ltd could start up a rival rugby league competition. Furthermore, by way of the cross elasticity of supply, the Australian Rugby Union Ltd appears to have the ability to increase supply of rugby union games in the event of an increase in the price of attending rugby league games.

Burchett J appears to have followed Pincus J's approach in *Qld Wire* and overlooked the issue of supply side substitutability due to the difficult economic questions such an assessment would raise. Having defined the demand side of the market as one in which there were numerous substitute forms of entertainment and sport to rugby league, Burchett J appears to have baulked at the task of reconciling this assessment with a difficult supply side analysis.

A simplistic assessment of supply side substitutability would indicate that it is highly unlikely that the various sporting leagues in control of Australian rules football, soccer or basketball would enter the market to provide an alternative rugby league competition. Burchett J's failure to address the supply side element of the market may have been because he regarded this fact as self evident. However, as the above analysis indicates, a thorough supply side assessment threatens the open ended market definition adopted by Burchett J by revealing the differing supply side substitution possibilities for each sport identified by Burchett J as a substitute. Such an analysis presents a much more complex framework in which to analyse the relevant market for Part IV of the Act.

Burchett J may well be correct in stating that switching on the demand side allows for the market to be defined widely. Whilst it is beyond the scope of this paper to suggest an alternative market definition, it is important to realise that consideration of the supply side situation is vital in the process of market definition. Such a consideration did not occur in the case.

Unfortunately the Full Federal Court on appeal declined to address the issue of market definition, stating that "whatever view we might have taken on market issues would not have altered the result".⁹⁹ The Court held that the ARL had contravened s. 45(2) of the Act since the Commitment and Loyalty Agreements were exclusionary provisions within the meaning of s. 4D of the Act. There is no requirement for market definition in such a situation since it is a per se offence. The Full Court did note that the issue of market definition in particular "raised many difficult questions".¹⁰⁰

99 *News Limited & Ors v Australian Rugby Football League & Ors* (1996) ATPR 41-521 at 42,540.

100 *Ibid.*

8. Conclusion

The four recent cases outlined above illustrate the manner in which courts have failed to adequately approach market definition for the purposes of Part IV of the Act. The approach of courts to the statutory interpretation of Part IV by reference to economic theories combined with an attempt to provide a 'commercially realistic' framework has led to the over simplification or ignorance of the key economic concept of substitutability. Substitutability on the supply and demand side is a vital factor in the definition of markets, and the cases listed illustrate the flawed market definitions that can occur as a result of the misapplication of this theory.

The cases of *News Limited v. Australian Rugby Football League Limited & Ors*¹⁰¹ and of *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor*¹⁰² indicate the problems with market definition that can arise when supply side substitutability is ignored by the courts. *QIW Retailers Limited v. Davids Holdings Pty Limited & Ors; Attorney-General of the Commonwealth v. Davids Holdings Pty Limited*¹⁰³ and *Taprobane Tours WA Pty Ltd v. Singapore Airlines Limited*¹⁰⁴ on the other hand highlight the manner in which sub-markets can be erroneously identified as actual markets when demand side substitutability is misapplied or ignored.

Unfortunately until a process is developed to assist courts interpret and apply economic evidence¹⁰⁵ relating to substitutability it is likely that market definition will continue to be misapplied by judges attempting to apply the simplified economic theory/market reality approach to the definition of markets.

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101 *Ibid* at 41,675.

102 *Queensland Wire Industries Pty Ltd v. The Broken Hill Proprietary Company Limited & Anor* (1987) ATPR 40-810.

103 *QIW Retailers Limited v. Davids Holdings Pty Limited & Ors; Attorney-General of the Commonwealth v. Davids Holdings Pty Limited* (1993) ATPR 41-226.

104 *Taprobane Tours W.A. Pty Ltd v. Singapore Airlines Limited* (1990) ATPR 41-054.

105 For a more detailed discussion of the need for a rationalisation of the methods by which courts receive economic evidence, see Stephen Coronos *supra* n.18; Maureen Brunt *supra* n.1; Karen Yeung *supra* n.9.

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