The Problem of Collusion: How Best to Resolve it?

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I. INTRODUCTION

New Zealand's primary piece of legislation concerning competition law is the Commerce Act 1986. The main purpose of the Commerce Act is to promote competition in New Zealand which, if achieved, will in most cases increase the level of efficiency and innovation in the market place. The subject of this article – horizontal collusion – stands as one of the major impediments to the promotion of competition in New Zealand. For this reason horizontal collusion remains one of the most serious problems facing the New Zealand economy, and the means by which it is regulated one of the legislature's biggest concerns.

Horizontal collusion ("collusion") can be either explicit or tacit. The most basic distinction between the two is that explicit – or actual – collusion involves direct communication between competitors, whilst tacit collusion involves, at best, indirect communication. There are many different forms of horizontal collusion. For example, competitors may agree to allocate markets or sectors of markets amongst themselves either by customers or by territory, or may establish joint production and output restrictions on certain products. Arguably, the most prominent form of collusion is parallel pricing or price-fixing. Unlike other forms of collusion, price-fixing can easily be carried out in a tacit, subtle fashion, making it very difficult to detect and therefore penalise. For this reason it is the most prevalent form of collusion, and the one which poses the most serious problem for legislators.

Irrespective of what form the horizontal collusion takes, and whether or not it is carried out through direct communication, it nearly always produces undesirable results. The reduction in competition stemming from the collusion also leads to lower levels of innovation, along with losses in efficiency as firms

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charge higher prices and produce less output than they would do in perfectly competitive markets. The end result is the collective loss in welfare for the largest and most important group in the commercial equation, the consumers.

II. HOW SUCCESSFULLY DOES THE COMMERCE ACT CONTROL COLLUSION?

Having identified collusion as undesirable, does the Commerce Act adequately regulate it? As this article will illustrate, there is considerable uncertainty as to the extent of the Act's power to penalise collusion. My view is that the Act in its current form can only penalise actual and not tacit collusion, a serious shortcoming given the adverse effects of tacit collusion.

1. Controlling Actual Collusion

The Act does appear to have the scope to prevent most instances of actual collusion, but some will invariably escape punishment. The two sections of the Act designed to capture such collusion are sections 27 and 30. Section 30 of the Act has been specifically drafted to regulate price-fixing agreements. However, section 27 is a much broader provision which can encompass not only price-fixing, but also the other forms of horizontal collusion mentioned, in addition to anti-competitive vertical arrangements.

Whatever the form of alleged collusion, two elements must be established under section 27 for collusion to be found:

1. the competing parties entered into a contract, arrangement or understanding; and
2. this contract, arrangement or understanding had the purpose of, or has or is likely to have the effect of, lessening competition in a market.

The second element is less complex, easier to establish and can be dealt with quickly. Although very few colluding competitors would explicitly state or admit that the agreement they reached had the purpose of lessening competition, in several recent decisions it has been held – and all but conclusively established – that an infringing purpose can be measured objectively as well as subjectively,[1] and hence can be inferred from action and circumstances rather than having to be established through evidence of direct intention.

1 See *Port Nelson v Commerce Commission* [1996] 3 NZLR 554, 564. In this case, the Court of Appeal agreed with McGechan J in the High Court that purpose could conceivably be established or negatived on "either a subjective or objective analysis". However, this is only a general principle and may be constrained by statutory wording.

(a) Price-fixing

Before discussing the first element, which both sections 27 and 30 have in common, it is appropriate to discuss the unique elements of section 30, a clear demonstration of the legislature's intolerance of any collusion between competitors involving the pricing of goods or services. Not only is application of the provision restricted to those who "would be, or would be likely to be, in competition with each other",[2] but it is clear that once an agreement for the "fixing, controlling or maintaining"[3] of the price of goods has been established then, unlike section 27, there will be no requirement for the plaintiff to prove that the agreement has the purpose or the effect of substantially lessening competition. Instead, the lessening of competition will be presumed and it will be irrelevant that the actual effect of the agreement may be to improve competition. This was confirmed by Fisher J in *Commerce Commission v Taylor Preston Ltd*:[4]

> The result is that once a price-fixing provision has been established, it is to be conclusively assumed that it is inherently anti-competitive. It will not be open to a defendant to submit, or to call expert evidence to suggest, the contrary.

In *Commerce Commission v Caltex New Zealand Ltd*,[5] Salmon J supported Fisher J's interpretation in confirming the validity and applicability of the presumption.

The significant impact *Commerce Commission v Caltex* has had on section 30 warrants detailed examination. The case involved a simultaneous withdrawal of a promotion – a free car-wash with every $20 petrol purchase – by three oil companies. That the withdrawals were simultaneous, combined with evidence of communication between the three oil companies concerning the end of their promotions, prompted the Commerce Commission to allege that the defendants had directly communicated with one another to simultaneously discontinue the offer. This, it was alleged, amounted to a price-fixing arrangement and a breach of sections 27 and 30.

The difference between the alleged horizontal arrangement in *Commerce Commission v Caltex* and a normal price-fixing arrangement, upon which the defendants sought to rely, was that they agreed to remove an aspect of their service, namely the free car-wash, rather than directly agreeing to uniformly alter the price of the service. This, they argued, was not strictly an agreement to fix prices.

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2 Commerce Act 1986, s 30(2).

3 Commerce Act 1986, s 30(1).

4 (1998) 6 NZBLC 102, 470, 479. However the Australian courts have taken the opposite view. The full Federal Court of Australia in *Radio 2UE Sydney Pty Ltd v Stereo FM Pty Ltd* (1982) 62 FLR 437, 448, upholding the decision at first instance of Lockhart J, held that, because the price-fixing agreement in question improved competition in the relevant market, it did not constitute price-fixing for the purposes of the Trade Practices Act 1974 (Cth).

5 (2000) 9 TCLR 305 (HC).

However, Salmon J, in rejecting the defendant's argument, seemingly favoured a "substance over form" approach. His Honour appeared to acknowledge that, whilst the removal of a free car-wash could not amount directly to an agreement to fix prices, it effectively constituted a uniform price rise because it removed a common element of the defendants' cost structures. In making this finding his Honour relied upon the earlier judgment of Elias J, who concluded in her decision on the defendants' strike out application that "an agreement that in future petrol will be sold without a free car wash ... is as substantial and real as a simple agreement to increase price".[6]

Furthermore, Salmon J also considered that the agreement was in substance an agreement to increase prices because the promotion which the agreement removed operated as an "integral part of petrol or car wash pricing".[7] His Honour reasoned that, without the promotion, the car-wash would have cost $2. On this basis, the car-wash indirectly represented a 10 per cent reduction in the cost of petrol, hence its removal effectively increased the price of petrol.

The defendants then argued that, by failing to identify the prices that would be offered following the withdrawal of the free car-washes, they could not have sufficiently "fixed" or "controlled" prices relating to petrol or car-wash services.

The success of this argument was dependent on the Court adopting the same contrived interpretation of fixing and controlling as that of the defendants. In failing to adopt such an interpretation, Salmon J effectively closed off yet another potential escape route from section 30. In rejecting the defendants' argument, Salmon J once again relied upon the judgment of Elias J, in particular her statement that:[8]

> There is no authority for the proposition that in order to establish price-fixing or impact upon competition it is necessary to establish a fixed price or agreed discount for the future .... [I]f that were so it would be easy to drive a coach and four through the Act.

The impact of the case on section 30 has been significant. Not only has the case upheld the section 30 presumption, but it also appears to have broadened the scope of the section by giving a very liberal interpretation to the concept of price-fixing. In doing so it appears to have made the Commerce Act a much more effective weapon against explicit collusion when in the form of a price-fixing agreement.

(b) Establishing the Existence of a Contract, Arrangement or Understanding

For obvious reasons it is exceedingly rare that colluding parties will formalise their anti-competitive agreements. Thus in the vast majority of cases,

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6 Ibid 312.
7 Ibid 322.
8 Ibid 313.

explicit collusion will have to be established by showing the existence of an arrangement or understanding rather than a written contract. Such informal agreements are unlikely to be documented in any detail, which means they will usually need to be inferred and proven from circumstantial evidence – a very difficult task.

Essentially, an arrangement or an understanding will arise when two things are shown. There must first be some form of communication between the colluding parties, and secondly there must be a mutual intention to act for a common purpose. These requirements were stated succinctly in *Re British Basic Slag Agreements Ltd* where, for an arrangement to be unenforceable at law:[9]

> [T]he parties to it shall have communicated with one another in some way and that as a result of the communication each has intentionally aroused in the other an expectation that he will act in a certain way.

It is also clear that for an arrangement or understanding to be established, the communication and the resulting mutual intention must be strong enough so as to allow each party to rely upon the other's action – in essence the parties must create an expectation in the other parties, rather than a mere hope or prediction, that they will adopt a certain course of action. Justice Lockhart illustrated this point in *Trade Practices Commission v Email Ltd*, where he stated that:[10]

> [T]here is a fundamental distinction between a hope or prediction of future behaviour on the one hand and the expectation of certain behaviour on the other; that is behaviour which, as a result of communication between the parties, the party restricted is at least morally bound to adopt.

The courts have always been reluctant to establish actual collusion by inferring an arrangement or understanding from evidence, presumably aware of the consequences if they are wrong. However, this cautious approach, whilst understandable, has often prevented many instances of actual collusion from receiving the necessary condemnation.

The recent case of *Commerce Commission v Caltex New Zealand Ltd*[11] may have made section 27 a more effective weapon against explicit collusion, by allowing an understanding to be more easily established through inference. In this case, where an agreement between the parties to simultaneously withdraw the car-wash promotion could not be established by direct evidence, the test of whether an inference could be drawn was whether the defendants' actions involved "such a concurrence of time, character, direction and result as naturally to lead to the inference that there was an understanding between the parties".[12]

9 [1962] 3 All ER 247, 255.
10 (1980) 43 FLR 383, 397.
11 Supra note 5.
12 Ibid 323.

The court found that a number of factors led to such an inference. Among the most significant were:[13]

1. The fact that each of the oil companies had an incentive to cease a loss-making promotion;
2. The fact that the offer was no longer achieving any competitive advantage;
3. The disincentive the competitors had to move unilaterally;
4. The evidence of communication between the competitors about the removal of free car-wash promotions at PULP (Premium Unleaded Petrol) committee meetings; and
5. The communication by a Caltex employee to an employee of Shell as to Caltex's intention to cease the free car-wash.

By including the first three facts as ones which inferred an agreement to fix prices, the Court could be construed as adopting a more liberal approach towards establishing inferences. Indeed, neither the fact that the defendants had an incentive to cease a loss-making promotion, nor the fact that the offer was no longer giving them a competitive advantage, provide evidence of communication between the parties, yet they have still been used to draw inferences. In this way, the Court's approach could be interpreted as an intention to make section 27 a more effective weapon against actual collusion by setting a lower threshold for establishing an understanding.

Whilst this is one possible way of interpreting the Court's decision, it is probably not the correct one. Although Salmon J listed these facts as crucial to drawing the inference, in reality it was arguably the evidence of the actual communication between the parties that was decisive in allowing an understanding to be inferred on the facts. As such, it is suggested that the first three facts listed above merely strengthened and reinforced the inference; they did not actually create it. It is therefore unlikely that, in the absence of such strong evidence of communication, these three facts by themselves would be sufficient evidence from which to infer an understanding. Hence, while the case will gain significance and notoriety for its attack on an industry long suspected of price-fixing, it has not dramatically increased the effectiveness of section 27 to regulate against collusion.

2. Tacit Collusion

(a) Can Section 27 Cover Tacit Collusion?

Whether or not it is concluded that *Commerce Commission v Caltex* has increased the power of section 27 to control actual collusion, it has done nothing to solve the larger problem – that of tacit collusion. Although it is not entirely

13 Ibid 324.

clear whether the scope of sections 27 and 30 is wide enough to capture tacit collusion, it is submitted, for a variety of reasons, that tacit collusion is indeed not covered.

Although the fact that tacit collusion has no statutory basis in New Zealand provides some evidence that the legislature did not intend its regulation, this is not in itself decisive of the issue. It seems the key question in determining whether the Act covers tacit collusion is whether the need to establish the existence of an understanding will negate the ability of sections 27 or 30 to capture tacit collusion. A good starting point for answering this question is to examine the definition of tacit collusion. Tacit collusion is often loosely referred to as an "unspoken" understanding arrived at through indirect communication. Whilst this definition is useful for a basic understanding of tacit collusion, a more comprehensive definition is necessary for a more detailed analysis of the concept. Such a definition is provided by Pass and Sparkes, who define tacit collusion as an occurrence "arrived at through the firms' repeated experiences with each other's behaviour over time, proceeding to the point that all firms tacitly understand that they will act together uniformly, in a well-defined and regular manner".[14]

Under this definition of tacit collusion, firms must clearly have a mutual intention and an understanding to act together based on their repeated experiences with one another. However, on the basis of the ruling in *Basic Slag* discussed above,[15] New Zealand law clearly requires that, for an understanding to be established, the parties must not only have a mutual intention to act in a certain way but must also communicate with one another in some form to achieve the common desired outcome. Therefore, how "communication" is construed becomes of great importance. If communication is liberally construed, then uniform conduct on the basis of firms' "repeated experiences" with each other's behaviour may constitute communication and hence an understanding. As such, section 27 will have the scope to capture tacit collusion.

However, it is submitted that uniform conduct on the basis of "repeated experiences with each other" will not constitute communication. Firms that act on repeated experiences with fellow competitors but without any contact with them cannot expect to know enough to create in their minds "an expectation of certain behaviour",[16] a necessary result of communication identified in *Trade Practices Commission v Email Ltd.* Arguably the best outcome firms can hope to derive from this process is to be able to make a mere prediction of the other's behaviour. Therefore, it is tentatively submitted that tacit collusion does not involve sufficient communication between the parties to amount to an understanding under either section 27 or section 30 of the Commerce Act.

This submission appears to have been complemented by the refusal of the Court in *Trade Practices Commission v Email Ltd* to draw an inference of tacit collusion from parallel conduct. Justice Lockhart accepted that the parallel

14 Pass and Sparkes, "Control of Tacit Collusion in Britain" (1981) 15 JWTL 521, 522.
15 Supra note 9 and accompanying text.
16 Supra note 10.

conduct of the parties could be explained by "commercial considerations"[17] arising from the market structure rather than by collusion. Consequently, his Honour held that "the result [parallel conduct] does not justify an inference as to the process".[18]

(b) Does Section 36 Cover Tacit Collusion?

If section 27 cannot capture tacit collusion, then what about the other main regulatory provision of the Commerce Act, section 36? Broadly speaking, section 36 prevents a party from using a dominant position within the market for a number of anti-competitive purposes. Therefore, to penalise anti-competitive, concerted conduct in concentrated markets under section 36, it must first be established that the competitors hold a dominant position in the market.

Initial adoption by the Commerce Commission and the courts of an economic interpretation of dominance gave some scope for the conclusion that, in highly concentrated markets, firms could be jointly dominant if they were not adequately disciplined by their competitors' existence.[19] This conclusion did lend some, albeit very weak, support for tacit collusion to be captured under section 36.

More recently the dictionary meaning of dominance has been preferred to the economic interpretation. In *Telecom Corp of New Zealand v Commerce Commission*,[20] the Court considered that to be in a dominant position, a firm needed to have a "prevailing", "commanding" or "leading" influence in a market.[21] Critically, the Court also established that "only one person can be dominant in a particular aspect of a market at any one time".[22] The Court's finding removed the possibility of participants in a concentrated market being collectively dominant, thereby preventing the use of section 36 as a means of regulating tacit collusion.

III. HOW SHOULD TACIT COLLUSION BE CONTROLLED?

Assuming, therefore, that neither section 27 nor section 36 capture tacit collusion, how is it to be controlled? Should the Commerce Act be amended to expressly prohibit tacit collusion or even parallel conduct, or are there other methods which are more appropriate?

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17 Ibid 389.
18 Ibid 391.
19 *Re Magnum Corp and Dominion Breweries* (1986) 2 TCLR 177, 196.
20 [1992] 3 NZLR 429 (CA).
21 Ibid 434 per Cooke P.
22 Ibid 442 per Richardson J. The Court of Appeal's view on dominance was reaffirmed in *Port Nelson v Commerce Commission*, supra note 1.

1. Is There a Distinction between Tacit Collusion and Parallel Behaviour?

Before we can decide on the most appropriate means of regulating tacit collusion, it is first necessary to consider whether a distinction can be drawn between tacit collusion and parallel behaviour. It is argued by some that all parallel behaviour amounts to tacit collusion. Others believe that the two are not synonymous, identifying conscious parallelism as a legitimate, non-culpable form of parallel conduct.

(a) Conscious Parallelism – A Product of Oligopolistic Market Structure?

Richard Posner has made it clear that he sees no distinction between tacit collusion and parallel conduct, and consequently does not recognise conscious parallelism. He has commented that:[23]

> [I]n some circumstances competing sellers might be able to coordinate their pricing without conspiring in the usual sense of the term – that is, without any overt or detectable acts of communication. This is the phenomenon that lawyers call 'conscious parallelism' and some economists term 'oligopolistic interdependence', but which I prefer to call 'tacit collusion'.

However, those who recognise a distinction between parallel conduct and tacit collusion argue that conscious parallelism, unlike tacit collusion, is a legitimate form of action because it results, not from unspoken understandings between firms, but from firms acting rationally on the strength of the mutual interdependence which exists among them in certain markets.[24]

(b) Price Leadership – Is it Tacit Collusion?

Price leadership is a more complex issue. Price leadership has been defined as a situation whereby one firm attempts to adjust the prices offered by other firms by issuing a new announced price.[25] Some instances of price leadership are clearly tacit collusion, but others appear to be perfectly innocent forms of conscious parallelism. There have been a number of different types of price leadership identified, but only two forms will be discussed in this article.

Collusive price leadership is where the leader adjusts its price as a means of communicating with other firms. It sets its price to a level commensurate with that which would prevail if all the firms actually agreed on a set price level. Barometric price leadership is where the price change from the leader firm

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23 Posner, *Antitrust Law: An Economic Perspective* (1976) 40.

24 See, for example, Turner, "The Definition of Agreement Under the Sherman Act: Conscious Parallelism and Refusals to Deal" (1962) 75 Harv L Rev 655, 658-659 and 662-663. See also Blair and Kaserman, *Antitrust Economics* (1985) 202-204; Aldor, "Oligopolistic Conscious Parallelism under the Competition Law of the USA" (1986) 16 Fed L Review 74, 74-75 and 85.

25 Miller et al, *Price Setting and the Commerce Act*, Research Monograph No 37 (1987) 5-6.

merely represents its view that market conditions have changed. It adjusts its price to compensate for changes in demand or production costs, not as a means of communicating to its competitors.

There is no doubt that collusive price leadership is a form of collusion which deserves condemnation. However, whether barometric price leadership deserves similar treatment is heavily debated. Posner, taking the same stance as for conscious parallelism, concludes that no distinction can be made between price leadership and tacit collusion and hence barometric price leadership ought to be penalised. He argues that a price leader sets a price with the expectation that its competitors will follow and match the price set. If they do indeed follow, they not only show awareness that the leader expected that behaviour, but more importantly signal their agreement and understanding of the scheme and the outcome it seeks to achieve.[26]

It is submitted that there is one clear weakness in Posner's assertion. Arguably, the mere fact that rival firms choose to follow a leader's price does not necessarily mean that they understand and agree to a scheme of fixing prices. This is because there may be some completely innocent independent factor which has influenced their movement. For instance, the cost of producing the goods or services supplied by the firms may have genuinely increased. Consider a hypothetical situation in the airline industry, where each airline company contracts with a different engineering firm to service its aircraft. A law change is then made, which results in an increase in the cost of servicing aircraft for each engineering firm. It happens that the engineering firm which services the price leader is the first firm to re-evaluate its cost structure and pass its newly incurred costs onto its client. Therefore the price leader is the first company to raise the price of air travel. Once the other engineering firms examine their new cost structures, costs will be passed on and air travel prices will inevitably be raised by the remaining airline companies, not because they are "following the leader", but because the engineering firms they contracted with are slower to transfer their cost increases. This example is simplistic, yet it illustrates the idea that adoption of the leader's price by its rivals does not always signify that those rivals are aware of and approve of a particular price-fixing scheme.

Therefore, in accordance with the above arguments, it is submitted that a distinction can be made between tacit collusion and parallel behaviour, and hence that conscious parallelism and barometric price leadership do exist in their own right as legitimate forms of action.

2. Should the Distinction be Provided for?

The existence of this distinction raises the question as to what is the most appropriate means of regulating tacit collusion, if it is decided to do so. Should the distinction be statutorily recognised and provided for by the express prohibition of only tacit collusion, or is it preferable to ignore the distinction and

26 Posner, "Oligopoly and the Antitrust Laws: A Suggested Approach" (1969) 21 Stan L Rev 1562, 1568.

focus instead on "outcomes" and the prohibition of all forms of parallel conduct? In order to determine which option is better, it is necessary to assess how easily and accurately the distinction between conscious parallelism and tacit collusion can be drawn in real life situations. Such an assessment will necessarily involve a thorough examination of the guidelines which exist for distinguishing the two, to determine whether they are effective enough.

Perhaps the most comprehensive set of guidelines for distinguishing between conscious parallelism and tacit collusion comes from Pass and Sparkes in their research paper entitled "Control of Tacit Collusion in Britain".[27] They have suggested that in cases where competing firms are simply engaged in innocent conscious parallelism, "one would expect to see the transition from one price level to another to show a period of price instability before a new price level was established".[28] Alternatively, they suggest that there would be strong grounds for inferring tacit collusion where the price movement by the firms was "single, uniform, and nearly simultaneous".[29] Similar guidelines to those established by Pass and Sparkes were suggested by an earlier American report.[30] According to the report, deciding whether an instance of uniform conduct was legitimate behaviour or tacit collusion involved asking several questions:[31]

1. How identical is the uniformity?
2. What is the time lag, if any, between a change by one competitor and that of others? That is, has the uniformity between competitors occurred simultaneously?
3. How long has the uniformity continued?
4. How pervasive is the uniformity?
5. Does the uniformity only extend to price or to all other terms and conditions of sale?
6. Is the product or service involved homogenous or differentiated?

Although both sets of guidelines are of some relevance, it is submitted that they are too simplistic to allow one to make a confident, conclusive judgment on whether an incidence of parallel conduct by a group of competitors is legitimate conscious parallelism or illegitimate tacit collusion. To illustrate the point, it is worthwhile to consider the industry within New Zealand which has been subjected to the strongest accusations of tacit collusion – the petroleum industry. Despite the deregulation of the New Zealand retail petrol market in 1988, the "big four" firms within it have consistently engaged in price movements which have been identical, virtually simultaneous and very frequent in their occurrence.

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27 Pass and Sparkes, supra note 14.
28 Ibid 523.
29 Ibid.
30 *Report of the Attorney-General's National Committee to Study the Antitrust Laws* (1955).
31 If the product or service is differentiated then there will be much more scope for price variation between competitors on the basis of product quality and/or product features. As such, the incidence of identical prices for differentiated products will more likely be the result of tacit collusion.

The presence of these three features means that the parallel pricing exhibited by the four oil companies has largely satisfied the conditions identified in both sets of guidelines as necessary to draw an inference of price-fixing.

However, despite the petroleum industry meeting these "guidelines", it would arguably be premature for any regulatory body to conclude that the participants had engaged in the illegal practice of tacit collusion. Despite the speed and close uniformity of their actions, there are still plausible explanations for such behaviour. Since there are so few firms in the retail petrol market, and since all firms have the resources to obtain almost perfect information on each other's movements, it is highly conceivable that they could all uniformly match their competitors' prices very quickly without the benefit of any communication or understanding between them. This argument and others presented by the oil companies themselves[32] certainly do not disprove the numerous allegations of collusion in New Zealand's retail petrol market. Indeed, the probability that collusion is practised is at least as likely as the alternative.[33] The argument is merely that, in the retail petrol market, the satisfaction of either set of guidelines does not allow for a conclusive inference of tacit collusion from the parallel conduct exhibited.

On the basis of the above arguments it is submitted that is not appropriate to statutorily provide for the distinction by expressly prohibiting tacit collusion only. This option requires a clear ruling on the legitimacy of the conduct in each situation. Clearly certain instances of parallel conduct will arise where it cannot be asserted with sufficient confidence that illegitimate tacit collusion is being practised. Therefore, if tacit collusion is expressly prohibited there is strong potential for cases to result in the condemnation of innocent parties: a scenario which is in no way desirable.[34]

The other possible option, the prohibition of all parallel conduct, ignores the distinction between conscious parallelism and tacit collusion. The main advantage of this more extreme option is that, if firms know that parallel behaviour is illegal, they will naturally refrain from such conduct. This will mean that the financial cost to both businesses and government associated with resolving contentious "parallel conduct cases" will be removed along with the potential for unjust outcomes in those cases.[35] Unfortunately, whilst this option will prevent collusive behaviour, it will also almost certainly prevent firms from

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32 Perhaps the argument most frequently raised by the "big four" oil companies is that they purchase their oil from the same international supplier and process it in the same refinery at Marsden Point. Hence any increases or decreases in the price of oil by suppliers or the price of processing by the refinery will result in equal changes in the firms' cost structures and the prices they charge.

33 Of significant importance is a report issued by the New Zealand Institute of Economic Research, *Petrol Prices: An Investigation into Petrol Prices in New Zealand* (1996) 14, which concluded that the market for petrol was not a fully competitive one.

34 Of course, if the court takes a cautious approach in such uncertain cases, the converse scenario could apply whereby guilty parties would escape punishment – a similarly undesirable scenario.

35 The outcome would be unjust if either innocent parties were punished or guilty parties escaped punishment.

engaging in behaviour which is not only legitimate but also perfectly rational in their respective markets.[36] In situations where the uniformity results from competitive, rational behaviour, the prohibition of parallel conduct would represent an unwelcome and unjust restriction on the freedom of firms to conduct business in the manner they see fit. Furthermore, the imposition of such a restriction would inevitably have some adverse effect on economic growth and hence the prospects of the economy in general.

3. The "*Port Nelson*" Approach – A New Method of Controlling Tacit Collusion?

In the recent judgment of *Port Nelson Ltd v Commerce Commission*,[37] the Court of Appeal held that, to establish a contract, arrangement or understanding for the purposes of section 27, it was only necessary to show that one party to the agreement had the required purpose of substantially lessening competition.

This ruling arguably promotes one more approach to controlling tacit collusion. Instead of attempting the near impossible task of establishing collusion without direct evidence, it could be shown that firms breach section 27 when they contract with innocent customers because the firm has the requisite anti-competitive purpose.

While this is an interesting approach, it is arguable whether it would be successful in controlling collusive behaviour between firms in concentrated markets. A requirement of section 27 is that the agreement must have the "purpose or likely effect of substantially lessening competition". It is very doubtful that the vast majority of contracts with customers would be sizeable enough in monetary terms to "substantially lessen competition", given that "substantial" requires the effect on competition to be "real or of substance"[38] and "not insubstantial or nominal".[39] Even if some contracts were large enough to be construed as substantially lessening competition, I suggest that it would nevertheless be unwise to use these agreements as a means of regulating firms' behaviour. Pursuant to section 27(4), no provision which contravenes the section is enforceable. Therefore, the use of customer contracts to regulate anti-competitive conduct would frustrate the objectives of innocent customers by seemingly preventing them from purchasing the goods and services they require.

4. What is the Solution?

On the basis of the above arguments, it is submitted that any attempt to prohibit tacit collusion directly, either by prohibiting the practice itself or by prohibiting all forms of parallel conduct, will create more harm than good.

36 For instance, where parallel conduct resulted from fierce competition between a few sellers.

37 Supra note 1, 563-564, in which Gault J held that "not all parties [to the contract] need to be shown to share the purpose .... The promotion of competition should not be inhibited by the artificiality of search for unanimous purposes."

38 Commerce Act 1986, s 2(1A).

39 *Re Fisher & Paykel Ltd* [1990] 2 NZLR 731, 758-759 per Barker J and R G Blunt.

Similarly, the attempt to control collusion through the regulation of customer contracts is also undesirable. However, it is all too apparent that the current legislation, which gives no power to control tacit collusion, is equally unsatisfactory, as it will allow firms that can collude without directly communicating with each other to escape without penalty. So what is the solution? How can the legislature prevent firms from taking full advantage of the obvious gap that exists in the legislation to the detriment of competition and ultimately consumer welfare?

I consider that the best way to prevent tacit collusion from occurring is not to prohibit the conduct itself, but to restructure our legislation to prevent the development of industry structures which are conducive to tacit collusion. Essentially, this would be done by altering the merger threshold to allow for greater scrutiny of mergers in concentrated markets. This is by no means an original approach; indeed, it is one recently proffered as a solution by the Ministry of Commerce,[40] and perhaps more significantly an approach adopted by the European Union. The next part of this article will closely analyse the statutory and judicial development of the European Union's response to tacit collusion in an attempt to determine whether the Ministry's proposed changes to New Zealand competition law should be introduced, and if so, how they should operate.

IV. THE APPROACH OF THE EUROPEAN UNION

The two principal regulations associated with the control of horizontal collusion in the European Union are Articles 81 and 82 (formerly Articles 85 and 86) of the Treaty Establishing the European Community. The strongest focus will be on Article 82 – due to its recognition of joint dominance – and, more importantly, on the way the courts have applied this concept to the European merger regulations.

1. Article 81

Article 81 is substantially similar to section 27. The stated aim of Article 81(1) is to prohibit "all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market".

Article 81 focuses on three forms of arrangement between parties – agreements, decisions and concerted practices. As is the case in New Zealand with section 27, it is the widest of the three terms, concerted practice, which is predominantly relied upon by the European Commission. This is because, like

40 Ministry of Commerce, *Review of the Competition Thresholds in the Commerce Act 1986 and Related Issues* (1998) 4.

an "understanding", a "concerted practice" can be established by drawing inferences from factual evidence such as faxes, emails or other commercial documents.

Despite considerable pressure, neither the Commission nor the European Union Courts have held that parallel conduct producing the same anti-competitive effect as price-fixing in itself infringes Article 81. However, perhaps reflective of this pressure, both bodies have made strong advances in this direction, most notably with their respective decisions in *ICI Ltd v EC Commission* ("the *Dyestuffs* case")[41], and *The European Sugar Cartel v EC Commission* ("the *Sugar Cartel* case").[42] In the *Dyestuffs* case, the Court made it clear that Article 81 did not under any circumstances allow a producer to:[43]

> [C]o-operate with his competitors, in whatever manner, in order to determine a co-ordinated course of action relating to an increase in prices, and to ensure its success by the prior elimination of all uncertainty as to mutual behaviour relating to the essential elements of that action, such as rates, subject matter, date and place of the increases.

In the *Sugar Cartel* case, the Commission stated its intention that the announcement of price rises in advance to competitors, either directly or indirectly, would amount to a concerted practice and contravene Article 81. The Court then appeared to give some support to the Commission's view, by establishing that Article 81 would "strictly preclude any direct or indirect contact between such operators [competitors]".[44]

These two cases, especially *Dyestuffs*, caused a high degree of concern for producers. Indeed, to effectively communicate a future price rise to its customers, it was necessary for a firm to identify the subject-matter – that is, what goods would be subject to increases – as well as the amount of those increases, and the date when such increases would come into effect. Therefore, under the Court's rulings, a price increase specified to customers in such a manner could potentially be construed as indirect contact between rival firms which eliminated uncertainty and hence constituted a concerted practice in breach of Article 81.

It seems that the Courts, if their subsequent decisions are any indication, have acknowledged producers' concerns over this decision. In *Ahlstrom OY v Commission* ("the *Woodpulp* case")[45], the Court rejected the Commission's finding that a practice of individually announcing in advance to customers prices for the next three months, resulting in virtually identical prices being quoted by competing firms, amounted in itself to a concerted practice. Noting that "[i]n this case, the communications arise from the price announcements made to *users*",[46]

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41 [1972] CMLR 557.
42 [1976] 1 CMLR 295.
43 Supra note 41, 627.
44 Supra note 42, 425.
45 [1993] 4 CMLR 407.
46 Ibid 573 (emphasis added).

the Court was of the view that such communications "constitute in themselves market behaviour which does not lessen each undertaking's uncertainty as to the future attitude of its competitors".[47] It seems that, by emphasising that this communication to customers was acceptable, the Court was unwilling to allow a concerted practice to be inferred from indirect communication, therefore significantly limiting the scope of concerted practices.

(a) Is Article 81 More Effective than Section 27?

Since Article 81 does not appear to extend to the capture of tacit collusion, it could be argued that it is no more effective than New Zealand's section 27 in controlling collusion between competing firms. However, it is arguable that the Court in *Woodpulp* retained to some extent the ability of Article 81 to control tacit collusion, by allowing a concerted practice to be inferred from parallel conduct when "concentration constitutes the only plausible explanation for such conduct".[48] This approach, it is submitted, makes Article 81 slightly more effective than section 27 when regulating horizontal arrangements. Although it is acknowledged that on most occasions, firms that intend to collude will be able, if necessary, to give a satisfactory explanation for their conduct, it is conceivable that some situations will arise where an explanation either does not exist or fails to reach the plausibility standard. Therefore, under European law, firms with dishonourable intentions in such situations will generally be deterred by the *Woodpulp* ruling from engaging in collusive conduct. By contrast, under New Zealand's jurisdiction, rival firms in a similar situation will be more willing to collude, knowing that however suspect their conduct may be, there will need to be at least some evidence of communication between them in order for an "understanding" to be inferred. It is therefore suggested that the New Zealand courts should apply the *Woodpulp* test when dealing with tacit collusion cases, as it may have deterrence value for firms contemplating collusion.

2. Article 82 and the European Merger Regulation

Undoubtedly the most significant difference between New Zealand and EC competition laws is their differing interpretations of "dominance", which have resulted in each adopting different approaches towards regulating mergers and anti-competitive behaviour. In the European Union, Article 82 of the Treaty controls dominant behaviour by providing that:

> Any abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market insofar as it may affect trade between Member States.

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47 Ibid.
48 Ibid 574.

The key phrase in Article 82 is "one or more undertakings". Whilst section 36 only allows a single firm to be dominant, Article 82 embraces the concept of collective dominance by allowing one or more firms to be in a dominant position in a given market, thereby increasing the number of firms whose activities can be subject to scrutiny.

Unquestionably, the provision and development of the concept of collective dominance signifies a bold attempt by the European Union to control forms of anti-competitive conduct, including tacit collusion, in markets which have already become concentrated. However, it is arguably the Court's decision in the recent case of *Kali and Salz*[49] that will have the most positive effect on the control of tacit collusion in concentrated markets, by effectively formalising the relationship between collective dominance and the Merger Regulation.[50] Article 2(3) of the Merger Regulation requires the Commission to prohibit concentrations that "create or strengthen a dominant position as a result of which effective competition would be significantly impeded in the common market or in a substantial part [thereof]".

Whilst it clearly prohibits mergers which create or strengthen a dominant position, the regulation does not expressly refer to the possibility that more than one firm can be dominant. As a result, before *Kali and Salz*, considerable doubt remained as to whether the principle of collective dominance applied to the Merger Regulation. The Commission, in accordance with the view of many economists, had always enthusiastically asserted that it did apply,[51] but the Courts, although subtly indicating support for the Commission's position,[52] had not made a conclusive ruling on the issue. However, in *Kali and Salz* the Court ruled that collective dominance under Article 82 did apply to the Merger Regulation. Specifically, it stated that:[53]

> Article 2 [of the Merger Regulation] in referring to a 'concentration which creates or strengthens a dominant position', does not in itself exclude the possibility of applying

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49 *Societe Commerciale des Potasses et de l'Azote (SPCA) and Entreprise Miniere et Chimique (EMC) v EC Commission* [1998] 4 CMLR 829 ("*Kali and Salz*").

50 Council Regulation (EEC) No 4064/89 of 21 December on the control of concentrations between undertakings.

51 See, amongst others, Case No IV/M.0017 – *Aerospatiale/MBB,* 25 Feb 1991, Official Journal C 059/91; Case No IV/M.0068 – *Tetra Pak/Alfa-Laval*, 19 July 1991, Official Journal L 190/91; Case IV/M.0202 – *Thorn EMI/ Virgin Music*, 24 April 1992, Official Journal C 120/92.

52 See, for example Case No. IV/M.0190 – *Nestle/Perrier*, 22 July 1992, Official Journal L 356/92. Almost 95 per cent of sales in the bottled water market subject to the proposed merger were captured by three firms: Nestle, BSN (Nestle's main rival) and Perrier. It was argued the merger between Nestle and Perrier would strengthen the jointly-dominant position of Nestle and BSN. Apparently suspicious of collusion as a result of the recent, nearly-parallel price increases in the market in the previous five years, the Court hinted at the need to regulate mergers in oligopolistic markets. It emphasised that the maintenance or development of whatever competition there remains in the market therefore requires particular protection. Any structural operation, such as a merger, restricting even more the scope for competition in such a situation has to be judged severely.

53 Supra note 49, 935.

the Regulation to cases where concentrations lead to the creation or strengthening of a collective dominant position.

By applying the Merger Regulation to collective dominance, the Community Court has arguably made the Regulation a much more effective weapon against anti-competitive conduct, by helping to restrict the formation through mergers of certain concentrated market structures, which by their nature give participants the opportunity to tacitly collude.

Having confirmed that the Merger Regulation does apply to collective – or oligopolistic – dominance, the Court then held that the critical question to be determined when dealing with proposed mergers was whether or not the risk of oligopolistic dominance, effectively tacit collusion,[54] was great enough to justify disallowing the merger. Whilst acknowledging the broad scope of the assessment needed to be undertaken for this "risk test", the Court clearly indicated that an economic, prospective analysis of the market accommodating the merger was the most important element.[55] The economic analysis of the European Commission is especially extensive and thus will be the focus of the following section of this article.

3. The European Community Commission's Approach to Assessing Mergers

The Commission appears to have segregated its economic assessment of whether a merger will result in oligopolistic dominance into two stages of analysis.

For the first stage of analysis, there are four broad features of the relevant market which require scrutiny. There is the current market concentration, which is measured by the combined market share of the leading firms. In general, the Commission has been concerned about a proposed merger leading to oligopolistic dominance when it would result in the leading two firms holding greater than 60 per cent of the relevant market. Secondly, when assessing product characteristics, the Commission has consistently viewed the presence of strong product homogeneity and low product innovation in a market as factors likely to increase the risk of a merger resulting in oligopolistic dominance. If a product is similar or identical or unable to benefit from further innovation then this effectively removes variables upon which firms can compete with one another, and therefore reduces the extent to which each firm need monitor its rivals. This in turn enhances their ability to tacitly collude on the only other significant competitive variable – price.

Thirdly, for demand characteristics the Commission has consistently acknowledged the economists' view that greater demand inelasticity in a market

54 The principal concern about oligopolistic dominance is that it will involve tacit collusion. Hence, the terms "collective dominance", "oligopolistic dominance" and "tacit collusion" should, in this article, be construed as essentially synonymous with one another.

55 Supra note 49, 947.

will increase the risk of oligopolistic dominance, as the increase in profits resulting from a parallel price increase will more than offset any reductions in volume.[56] The other demand characteristic influencing the level of oligopolistic dominance is the level of growth in the market. Here, the Commission in the *Pilkington/SIV*[57] merger has also taken the popular economic view that the greater the level of growth, the lesser the potential for collusion, because a growing market has sufficient capacity for all firms to increase their sales without depressing those of their competitors. By contrast, in a mature market, any attempts by firms to engage in rigorous competition to increase their sales will be at the expense of one another. Therefore, firms will have a greater incentive to collude to avoid mutual harm.

A final critical factor is the degree of transparency in the market – essentially the extent to which the behaviour of firms can be monitored by their rivals. A high degree of transparency will discourage deviating behaviour and thus increase tacit collusion, because firms will have more difficulty concealing attempts to break any collusive agreements and so will not risk pursuing an individualistic approach.

Only if these four characteristics of the market itself are found to be conducive to the practice of tacit collusion will the second stage of analysis be relevant. This second stage essentially involves assessing whether the relevant market contains customers or competitors who, although not members of the oligopoly, would have the ability to constrain the anti-competitive conduct of those who are. If no such competitors exist or are not in sufficient abundance, then it is likely that the Commission will either conclude that the risk of oligopolistic dominance occurring is too substantial to allow the merger, or will only approve the merger subject to various conditions.

Finally, it must be noted that, although it is generally receptive to the Commission's economic analysis when assessing the risk of oligopolistic dominance, the Community Court has made it clear that a theoretical application of economic principles will not in itself be sufficient. In *Kali and Salz*, for example, the Court approved the merger for reasons largely independent of economic theory, namely that the asymmetries of production capacity between the two firms would lead to conflicts of interest and reduce the risk of collusion.

V. SUGGESTED SOLUTIONS FOR THE CONTROL OF TACIT COLLUSION

In my view, New Zealand ought to adopt an approach to tacit collusion similar to that taken by the European Union, whereby the concept of collective dominance is incorporated either directly or indirectly into our merger provisions

56 See, for example, the *Nestle/Perrier* case, supra note 52; see also Case IV/M.0206 – *Rhone-Poulenc/Snia,* 10 August 1992, Official Journal C 212/92.

57 Case IV/M.0358, 21 December 1993, Official Journal L 158/94; [1994] 4 CMLR 413.

– section 47 of the Commerce Act – to broaden the merger threshold. This will enable tacit collusion to be controlled indirectly by restricting mergers which create duopolistic and oligopolistic market structures that facilitate the practice of tacit collusion.

1. Method One: Redefine the Definition of Dominance

Directly incorporating the concept of collective dominance would involve amending section 3(8) of the Commerce Act to allow more than one person to hold a dominant position. New Zealand's "merger regulation", section 47, can then be aligned to the new definition of dominance so that it regulates mergers which create or strengthen a collectively dominant position.

2. Method Two: Adopt the Australian Threshold for Mergers

The other method is not to redefine the market dominance threshold currently in place for mergers, but instead to remove it entirely and replace it with the Australian threshold for regulating mergers. This threshold, found in section 36 of the Trade Practices Act 1974, provides that "[n]o person shall acquire assets of a business or shares if the acquisition would have the effect or be likely to have the effect of substantially lessening competition in a market for goods and services".

Although the threshold does not expressly provide for the regulation of mergers which create a collectively dominant position, it is wide enough to indirectly encompass and regulate such mergers. This is because a merger which results in the formation of a concentrated market with two to four firms could be prohibited on the ground that it would be likely to have the effect of substantially lessening competition by better enabling participants to tacitly collude.

3. Which Method Should be Adopted?

Both methods are preferable to New Zealand's current position, as both would prevent the mergers which create markets in which collusion can easily occur. However, it is submitted that, for a variety of reasons, the Australian approach is the more appropriate.[58]

The greatest benefit of using the "substantial lessening of competition" threshold is that it would create consistency between the treatment of restricted trade practices and mergers. Presently, competing firms have two main ways by which they can restrict competition to achieve an anti-competitive outcome. They can take the illegal option of expressly or tacitly entering into an agreement to collude, or they can adopt the legitimate option of merging with another firm. Since the Court of Appeal in *Telecom Corp of New Zealand Ltd v Commerce*

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58 It should be noted that at the time of publication, the present government had officially proposed the adoption of this Australian threshold for mergers: <http://www.med.govt.nz/buslt/bus_pol/comref/index.html> (last accessed 27 August 2000).

Commission[59] set such a high threshold for a merger to result in dominance, a legally acceptable merger and the associated anti-competitive outcome is simply too easy to achieve. Furthermore, these easily-attained mergers will result in the permanent loss of competition between the firms concerned, whereas collusion agreements only reduce competition for the time that they are in operation. On the strength of this argument, the New Zealand legislature could quite justifiably impose a stricter test for mergers than for anti-competitive agreements. At the very least, it seems that the tests for anti-competitive agreements and mergers should be aligned, a scenario possible if the Australian threshold is adopted.

The other obvious benefit of adopting Australia's merger threshold into our competition law is that it will make our Commerce Act more compatible with Australian legislation, and with the legislation of the many other countries in the OECD which adopt this threshold.[60] This will have obvious benefits for trade, as the costs and difficulties for overseas firms in complying with our legislation and vice versa will be considerably reduced. Furthermore, New Zealand's adoption of the Australian merger threshold will further harmonise the two countries' respective competition laws in fulfillment of the goals of the Australia-New Zealand Closer Economic Relations and Trade Agreement, which came into force in 1983.

It must be emphasised that, although not explicitly recognising collective dominance, the Australian merger threshold clearly has both the purpose and the ability to regulate against such dominance. Therefore, the European Commission's guidelines for analysing the risk of collective dominance will still be highly relevant when assessing the appropriateness of a merger.

4. The Costs and Concerns of Strict Merger Regulation

Although attractive, the above proposals must be considered in light of the arguments raised against them, most of which express concerns about the effect of lowering the present threshold.

Naturally, a lower, broader threshold will almost certainly increase the number of mergers which are scrutinised. The results of an Australian study,[61] conducted five years after Australia changed its merger threshold from dominance to "substantial lessening of competition", showed a significant increase in the numbers of mergers scrutinised each year by the Australian Commission. From 1992 to 1993, just prior to the change, 86 mergers were examined. From this point, the number examined each year increased steadily, culminating in 149 mergers being examined from 1996 to 1997. There is no reason why the same pattern will not occur in New Zealand, leading to an

59 Supra note 20, 434 per Cooke P. Applying the Court of Appeal's ruling in this judgment, a merger must result in a single firm having a "prevailing, commanding ... or leading influence" in the market.

60 Canada and the United States of America are two of many adopting this threshold. Both have strong trade relationships with New Zealand.

61 Australian Competition and Consumer Commission, *The ACCC's Approach to Mergers: A Statistical Summary* (1998) 4.

inevitable increase in both compliance costs for businesses and administrative costs for the government. In addition to the application fees involved in obtaining clearances and authorisations, firms will incur heavy expenditure on legal advice, first to determine whether an application need be made, and if so, as to preparing that application.

A potentially greater concern is that the New Zealand economy is not suited to the strict regulation of mergers which result in high market concentration. Since the New Zealand economy is so small in comparison to other OECD countries, New Zealand firms must achieve strong economies of scale to improve the country's international competitiveness, which is of ever-growing importance in an increasingly open world economy. Many argue that the most effective way for a country of New Zealand's size to realise these strong economies of scale and their resulting efficiencies is to encourage mergers and high market concentration rather than discouraging them.[62] Therefore, the current merger threshold, which promotes market concentration by only applying when a very high level of market power has been established, is preferable to a lower threshold.

In response to this argument, it is first acknowledged on the basis of microeconomic theory that well-planned mergers generally – but not always – result in a more efficient use of resources. The duplication of essential facilities like accounting, manufacturing and marketing is avoided, resulting in lower production costs. However, if the merger creates an oligopolistic market structure, any efficiency gains which may be achieved can potentially be completely eroded if firms tacitly collude by uniformly raising their prices above the perfectly efficient level. Therefore, whilst disallowing a merger will at worst only prevent the realisation of efficiencies, allowing a merger may, due to the incidence of tacit collusion or the incompetence of the merging firms, not only reduce overall efficiency but also reduce competition and one of its most important benefits – innovation. It is therefore submitted that it is potentially much more harmful to consumer welfare to allow mergers which result in concentrated market structures than to prohibit them.

It must also be recognised from analysing the Commerce Act that, although the promotion of efficiency is recognised, the stated purpose of the Act is to "promote competition in markets within New Zealand".[63] The current merger threshold is clearly not enhancing the promotion of competition by permitting concentrated market structures which encourage tacit collusion. Therefore, until the main aim of the Act is changed to that of promoting efficiency, the Australian merger threshold, with its potential to reduce the opportunity for collusion, better achieves the Act's purpose.

The final concern is that a change in the merger threshold would create much uncertainty for both the courts and the business community, with firms especially having no guidelines to help them predict the likely status of their planned

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62 See, for example, Brock, *The Antitrust Debate in New Zealand: Commentary* (1989) 2. This commentary paper was prepared for the New Zealand Business Roundtable.

63 See the Long Title to the Act.

mergers. Arguably, the uncertainty for both groups could be reduced by two initiatives. First, the legislature could adopt section 50(3) of the Trade Practices Act which identifies a list of factors to be considered when determining whether a merger substantially lessens competition.[64] The second means of reducing uncertainty would be to consider the economic analysis of both the European Community Commission and the Community Courts. The Commission's analysis in particular has been so comprehensive, and covers such a wide variety of mergers, that analysis of it would be useful both for a general understanding of the new threshold, and for a detailed examination of how a particular type of merger might be treated. Even with the assistance of both the above "guidelines", it is acknowledged that, at least initially, a degree of uncertainty as to the consequences of the new threshold will remain. However, the mere existence of uncertainty is rarely a good reason to oppose change, especially in this case.

VI. CONCLUSION

It is clear that there are virtually no legal or economic merits associated with horizontal collusion between firms. Rather, there are only significant detriments, such as the loss of efficiency and, more significantly, the lessening of competition which stifles innovation and ultimately the quality of goods and services produced. Yet, although collusion has such obviously harmful consequences, it seems that the Commerce Act is only strong enough to prevent actual collusion where an agreement or understanding can usually be captured under section 27 or section 30. These sections do not appear to capture tacit collusion – a serious concern, given the apparent ease with which tacit collusion can be practised by firms in certain industries.

However, harmful as it is, neither a statutory prohibition of tacit collusion nor a prohibition on all parallel conduct is an appropriate solution. Such prohibitions may penalise and prevent behaviour which is perfectly innocent and indeed rational in a concentrated market structure. The risk of this happening, and the resulting adverse consequences for business activity, are simply too substantial to make either form of prohibition an effective means of controlling tacit collusion.

The solution is therefore not to prohibit tacit collusion, but to adopt a lower merger threshold which prohibits mergers having the potential to create markets that facilitate tacit collusion. This approach will better prevent the occurrence of tacit collusion without the difficulties, costs and potential dangers in trying to identify whether conduct by firms in concentrated markets is innocent behaviour or illegitimate tacit collusion.

64 These factors include the level of actual and potential import competition in the market, the height of the barriers to entry to the market, the extent to which substitutes are available and the amount of growth, innovation and product differentiation in the market.