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# Legal briefing

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## *Application of the Trade Practices Act to companies conducting business with government*

**In *Australian Competition and Consumer Commission v Baxter Healthcare* [2007] HCA 38 (29 August 2007) (*Baxter*), the High Court found that the *Trade Practices Act 1974* (Cth) (TPA) applies to companies conducting business with government entities, even when those government entities are not bound by the TPA because they are not themselves carrying on business.**

**The decision constrains the types of contracts that government agencies may enter into and has important implications for procurement by agencies, even when those agencies are not subject to the TPA.**

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### Introduction

*Baxter* concerned the negotiation of, and entry into, contracts for supply of pharmaceutical products to public hospitals. It involved negotiations and contracts between Baxter Healthcare, a trading corporation, and various state governments which were not carrying on a business and were therefore not themselves subject to the TPA.[1]

In the 1979 decision in *Bradken Consolidated Ltd v BHP* (1979) 145 CLR 107 (*Bradken*), the High Court held that the TPA did not bind the Crown in right of the states. Therefore, the TPA could not be enforced against corporations otherwise bound by the TPA when those corporations were dealing with the Crown if to do so would be, in effect, to enforce the TPA against the Crown.

The decision in *Bradken* was the basis for the respondents' arguments in *Baxter* that, even if Baxter Healthcare had otherwise contravened the TPA, it was immune from the TPA where its breaches related to dealings with state entities that were not carrying on business and thus not subject to the TPA. This is often referred to as the concept of derivative immunity.

At first instance before Allsop J in the Federal Court (*Australian Competition and Consumer Commission v Baxter Healthcare Pty Ltd* (2005) ATPR 42-066) and on appeal before Mansfield, Dowsett and Gyles JJ in the Full Federal Court (*Australian Competition and Consumer Commission v Baxter Healthcare Pty Ltd* (2006) 153 FCR 574), the case was decided on the basis that Baxter Healthcare had the benefit of a derivative Crown immunity.

The High Court has now reversed the previous decisions and remitted the remaining appeal points (relating to whether or not the conduct of Baxter Healthcare contravened the TPA) to the Full Federal Court for reconsideration. In so doing, it has also signalled that *Bradken* no longer accurately represents the law (*Baxter* at [58]).

## Factual background

In 2002, the Australian Competition and Consumer Commission (ACCC) instituted proceedings in the Federal Court seeking declarations that Baxter Healthcare had contravened ss 46 and 47 of the TPA. The ACCC also sought injunctions, pecuniary penalties and an order that Baxter Healthcare develop and implement a trade practices compliance program.

During the course of the proceedings, the states of Western Australia, South Australia and New South Wales applied to be joined as respondents. The ACCC then sought an additional order that would ensure continuity of supply to hospitals on terms at least as favourable as those in the impugned contracts.

Some of the following findings by the trial judge are under appeal and will now fall to be determined by the Full Federal Court, following the High Court's decision to remit the matter to the Full Federal Court. However, in substance, the conduct of concern to the ACCC was an offer strategy used by Baxter Healthcare in responding to calls for tender for the supply of sterile fluids and dialysis products to public hospitals.

Baxter Healthcare, which is part of a multinational pharmaceutical company, was the only Australian manufacturer of certain sterile fluids, such as intravenous solutions, which were needed in high volumes by hospitals but were of relatively low value. Baxter Healthcare therefore had a monopoly over these products.

Baxter Healthcare also manufactured other products, notably solutions used in peritoneal dialysis (PD), for which it did have competitors. These were needed in lower volumes but were of much higher value.

State purchasing authorities (SPAs) in Western Australia, South Australia, New South Wales, the Australian Capital Territory and Queensland administered contracts for supply of sterile fluids and PD products to public hospitals. Baxter Healthcare developed a practice of responding to calls for tender by offering long-term contracts that required exclusive, or almost exclusive, supply of PD products together with substantial discounts on sterile fluids. These bundled offers were typically made together with an alternative 'item-by-item' offer, under which SPAs could choose to acquire only sterile fluids from Baxter Healthcare but on much less attractive terms.

The ACCC alleged that, by negotiating and entering into long-term supply contracts with SPAs in New South Wales, the ACT, South Australia, Western Australia and Queensland between 1998 and 2001, Baxter Healthcare had breached s 46 of the TPA, which prohibits taking advantage of market power for certain anti-competitive purposes. It also alleged that, by requiring SPAs not to acquire PD products (or to acquire them only to a very limited extent) from competitors, Baxter Healthcare had breached s 47, which prohibits exclusive dealing.

*The ACCC alleged that Baxter Healthcare had breached s 46 of the TPA, which prohibits taking advantage of market power for certain anti-competitive purposes, and s 47, which prohibits exclusive dealing.*

## First instance decision

At first instance, Allsop J found that, but for the application of Crown immunity, he would have granted relief in respect of one contravention of s 46 and several contraventions of s 47 of the TPA.

His Honour's starting point was the principle of statutory construction that a statute does not bind the Crown unless expressly stated or by necessary implication (*Province of Bombay v Municipal Corporation of Bombay* [1947] AC 58). The High Court followed that principle in *Bradken* and concluded that

the TPA did not apply to the Crown in right of the states. This included entities, instrumentalities, emanations or agents of the Crown entitled to Crown immunity.[2] In *Bass v Permanent Trustee Company Ltd* (1999) 198 CLR 334 (*Bass*), the High Court said that *Bradken* stood for the proposition that 'a statute is not to be construed as divesting the Crown of its property, rights, interests or prerogatives in the absence of express words or necessary implication to that effect' (*Bass* at [42]).

The High Court further considered *Bradken* in *NT Power Generation Pty Ltd v Power and Water Authority* (2004) 210 ALR 312 (*NT Power*). In *ACCC v Baxter Healthcare Pty Ltd* (2005) ATPR 42-066, Allsop J distilled four principles from the reasons of the majority in *NT Power*. These were (at [680]):

(1) Properly understood the authority of Bradken remains unimpaired, though, of course, now within the framework of s 2B of the Act.

(2) The principle applies to proprietary, contractual and other legal rights and interests such that it can be said that there is an impairment of the existing legal situation of the Crown.

(3) The principle does not extend to circumstances in which the legal situation of the Crown remains unaffected, but its commercial interests are affected.

(4) If a State or Territory has a contract with a non-government party, the Act is to be construed as not applying to that contract such that the State or Territory and non-government party is not bound by the terms of the Act in relation to the entry into and performance of that contract.

Allsop J considered that the relief sought by the ACCC against Baxter Healthcare would deny the states 'the contractual and legal embodiment of [their] self-perceived economic or political interests', and in this way interfere with their legal rights (at [685]), which included their lawful capacity to call for, negotiate and enter into contracts with Baxter Healthcare (at [691]).

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## Full Federal Court decision

The ACCC appealed the findings as to derivative Crown immunity as well as aspects of the findings on ss 46 and 47. Baxter Healthcare also contested several findings through a Notice of Contention (although it did not formally cross-appeal).

Although these matters were fully argued in a four-day hearing, the Full Federal Court (Mansfield, Dowsett and Gyles JJ) confined themselves to deciding the case on grounds of Crown immunity. The court noted (*ACCC v Baxter Healthcare Pty Ltd* (2006) 153 FCR 574 at [100]):

> ... it is difficult to see why the circumstance that the executive government is not bound by a statute should lead to the conclusion that conduct in breach of the statute by others is not prohibited, so permitting unrestrained restrictive practices in connection with the acquisition of goods and services on behalf of the executive government or its instrumentalities by all concerned. The interests affected are essentially commercial in nature.

*The Full Federal Court confined themselves to deciding the case on grounds of Crown immunity.*

Nevertheless, although the Full Federal Court doubted the basis upon which *Bradken* had been decided, as an intermediate appellate court it felt bound by the decision (at [104]-[105]). The Full Federal Court therefore affirmed the first instance decision.

## The High Court's decision

The majority of the High Court allowed the appeal (Callinan J dissenting). As Kirby J reached his conclusions for different reasons from the remainder of the majority, this note focuses on the joint judgment by Gleeson CJ and Gummow, Hayne, Heydon and Crennan JJ.

The High Court noted that, since the *Bradken* decision, the TPA had been relevantly amended in 1995 (by the insertion of s 2B) to provide that state entities are bound by the Act to the extent that they are carrying on business and that the canons of statutory construction relied on in 1979 had been overtaken by subsequent High Court decisions — in particular, the 1990 decision in *Bropho v State of Western Australia* (1990) 171 CLR 1 (*Bropho*).

*Bropho* substantially modified the previous inflexible rule of statutory construction that an Act was to be taken as not intended to bind the Crown unless the Act either expressly states that or the Act must on its terms, by necessary implication, have been intended to bind the Crown. The court now requires a more flexible approach, taking into account the nature of the provisions, the legislative scheme generally, and the activities that would be affected if the Crown were bound (*Baxter* at [38]-[42]). It now may be that some provisions of an Act will bind the Crown or affect its interests while others do not.

Applying this to the TPA, the court said (at [62]):

> ... since the Act does not bind the Crown in right of a State or Territory when it is not carrying on a business, then, save to the extent to which a contrary intention appears, the Act will not be read so as to divest the Crown of proprietary, contractual or other *legal* rights or interests. [Emphasis in original.]

Importantly, the court emphasised that, in applying this rule of construction, there must be a focus on legal rather than governmental, commercial or political interests of the Crown. The joint judgment suggests that a *legal* right is not to be confused with a mere freedom to do or not do something. Specifically, freedom to contract is not necessarily the same as a right to contract, especially considering that any such freedom is already constrained by the application of many laws, some of which bind the Crown (at [60]).

Their Honours expressly held that protecting the legal rights of the Crown does not make it necessary to extend a general immunity to any non-government party negotiating or contracting with the Crown (at [70]), noting that such an immunity in favour of a non-government entity that was carrying on business would in fact exceed the immunity of the Crown itself when carrying on business (at [68] and [74]).

It was further noted that reading the TPA so as not to divest the Crown of its legal rights was a very different thing to reading the TPA to grant to the executive Crown, and all of its servants and agents, freedom from laws enacted for the promotion of competition and fair trading in the public interest (at [68]). This is particularly so in light of s 51(1), which their Honours noted provided state legislatures (as opposed to their executive) a means to exempt conduct that would otherwise contravene the TPA (at [64], [68] and [73]).

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## Implications of the Baxter decision

### *The TPA applies for all aspects of the tender process and contract*

The decision in *Baxter* means that the TPA applies to companies doing business with government entities.

— This applies even if those government entities are not themselves bound by the TPA.

— All conduct by companies, including pre-contractual conduct and conduct (such as negotiations in the course of government tender processes) that does not ultimately result in entry into a contract (*Baxter* at [71] and [72]), is covered.

— In the context of tendering processes, the TPA applies regardless of whether or not the contravening conduct was contemplated by the government entity calling for tenders (at [73]).

*The decision in Baxter means that the TPA applies to companies doing business with government entities, even if those government entities are not themselves bound by the TPA.*

### *Contracts in breach of the TPA may be unenforceable or void*

In *Baxter*, the court rejected arguments by the respondents that granting relief (including injunctions restraining Baxter Healthcare from giving effect to the offending provisions of the contracts) would deny the Crown in right of a state the right, power and capacity to enter into any contract it wished. In doing so, the court rejected the notion that the TPA gave the Crown any freedom to permit corporations dealing with it to 'propose and make any kind of contract, unfettered by any constraint under the Act' (at [68]) on the basis that any purported freedom of this kind was irreconcilable with the subject matter and purpose of the TPA.

The joint judgment emphasised that, except for where the legislative intent otherwise requires, the TPA will not be read in a manner that will divest the Crown, when not carrying on a business, of its legal rights. This suggests that the Crown may be divested of contractual and other legal rights where the TPA evinces an intention that this should occur. While the issue did not squarely arise (as the ACCC did not seek orders that would divest the states of any of their legal rights), it may now be that a contract between a government entity not carrying on business and a non-government entity can be set aside if, for example, its central provisions contravened the TPA and giving effect to it would defeat the very purpose of the Act.

If a non-government party has breached the TPA in the course of doing business with government, this will not necessarily render any resulting contract entirely unenforceable or void. This is reinforced by s 4L of the TPA, which requires the severance of any offending provisions where this is possible (at [17] and [70]).

*It may now be that a contract between a government entity not carrying on business and a non-government entity can be set aside if, for example, its central provisions contravened the TPA and giving effect to it would defeat the very purpose of the Act.*

## What can be done

Be alert for warning signs of anti-competitive behaviour, including price fixing, exclusive dealing, market sharing, bid rigging and misuse of market power. If you have any basis for being suspicious, consider seeking legal advice or referring the matter to the ACCC. Your legal adviser or the ACCC will be assisted if you retain and make available documents including:

— those recording any communications between your agency and tenderers

— copies of pre-tender documents, including calls for expressions of interest and requests for tender

— copies of all tenders received

— logs of when and who delivered the tender

— your records relating to any of the suspicious behaviour described below.

There are certain industries or circumstances where anti-competitive behaviour can more easily occur. They may have characteristics such as:

- 'homogenous' products – that is, competing products which have broadly the same features, benefits, functions and purposes and are not readily differentiated and are not subject to significant technological change (for example, concrete blocks, cement or diesel fuel)
- the industry is dominated by a small number of large companies with few new companies ever entering the market
- the product or service is uncomplicated and does not permit suppliers to meaningfully differentiate their offer other than on price
- the product has few or no close substitutes (for example, glass windows and aviation fuel)
- the industry has an active trade association which facilitates meetings of competitors and may assist in coordinating activities among firms.

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Indicia of possible collusion include the following:

- tendered prices exceed published price lists or pre-tender estimates given by the same firms
- the successful bidder subcontracts work to its competitors that submitted higher bids for the same contract
- tender documents from competing companies are similar in form or contain the same irregularities, such as spelling or calculation errors
- competitors submit tenders containing identical prices or other terms and conditions
- a tenderer expresses to you some knowledge of the detail of a competitor's tender before the tender has been awarded
- you are aware that only one bidder contacted wholesalers to obtain the prices logically required to prepare bids
- tenders received from local companies contain the same transport price as competing companies that must transport the product further
- bidders explain their prices by referring to industry suggested pricing or 'standard market prices'
- discounts commensurate with efficiencies from supplying in volume are not offered or are offered only by one supplier.

Signs of possible misuse of market power include the following:

- one tenderer has substantially lowered its prices below what you believe its costs are likely to be
- the tenderer insists on 'bundling' its offer – that is, requiring the agency, in order to get a good price on a product for which there is no competition, to source other products from the tenderer as well
- the tenderer requires that it be the exclusive supplier rather than simply requiring minimum quantities that fairly reflect available cost savings or necessary investment.

## Tips for clients

- Look for warning signs of anti-competitive behaviour in government procurement, including price fixing, exclusive dealing, market sharing, bid rigging and misuse of market power.
  - AGS *Commercial Note* 14 [3] provides more background about circumstances where anti-competitive behaviour may arise in government procurement.
  - The ACCC's website (www.accc.gov.au) also contains useful information about cartels in government procurement.
  - Consider training procurement staff in competition policy issues in government procurement. AGS is able to assist with training.
- Ensure that your request for tender, statement of requirement and proposed contracts do not contain provisions that would require tenderers to breach the TPA to comply with your requirements.
- If a tenderer makes an alternative offer, consider any anti-competitive elements that might attach to that offer.
- Include in your tender a requirement that tenderers not engage in anti-competitive behaviour in relation to the tender process.
- For larger or higher-risk procurements, it may be appropriate to require tenderers to demonstrate compliance with relevant regulatory regimes, including the TPA in appropriate cases.

AGS acted as solicitor for the ACCC in the Baxter matter.

Text of the decision is available at:
http://www.austlii.edu.au/au/cases/cth/HCA/2007/38.html

***Glenn Owbridge*** *practises exclusively in the trade practices area and has been the leader of our trade practices team in Brisbane since 1998. He is a member of the Law Council of Australia's Trade Practices Committee in its Business Law section and is the leader of our national trade practices network.*

***Dr Lici Inge*** *has advised extensively on administrative decision making, procedural fairness and statutory interpretation for a range of agencies. Most recently, she has worked on large-scale trade practices matters in the Federal Court and High Court. She assisted in preparation of the Baxter matter for hearing at first instance in the Federal Court, and subsequently worked on the Full Federal Court and High Court appeals.*

### *Notes*

1 In 1995, the TPA was amended by the insertion of s 2B, which provides that the TPA applies to states and territories only so far as they are carrying on business. In *Baxter*, it had been conceded that the states dealing with Baxter Healthcare were not carrying on business.

2 The same position applies to the Crown in right of the Northern Territory (*Burgundy Royale Investments Pty Ltd v Westpac* (1987) 18 FCR 212).

3 http://www.ags.gov.au/clients/agspubs/legalpubs/commercialnotes/ComNote14.htm

## AGS contacts

AGS has a large national team of lawyers specialising in government procurement, including trade practices law. For further information on this issue, or on other procurement or competition issues, please contact John Scala (procurement) or Glenn Owbridge (competition) or any of the lawyers listed below.

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