

**THE EVOLUTION OF THE DOCTRINE OF RESTRAINT OF TRADE IN AUSTRALIA:  
A LAW REFORM PERSPECTIVE**

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## **ABSTRACT**

This thesis examines the present state of the common law doctrine of restraint of trade from a law reform perspective. The doctrine was developed in England between the 1600s and mid-1800s and its evolution over the centuries has been a slow and ongoing process. The present state of the doctrine and its application in the Australian jurisdiction presents a challenging set of circumstances due to the difficulties faced by contracting parties when they wish to engage in restraint of trade.

This thesis will begin by reviewing the history of the doctrine from its earliest days in a bid to identify the moments in time when the doctrine was chopped and changed to accommodate the social and economic needs of society. It will critique English and Australian cases which had a fundamental role in the evolution of the doctrine, analyse the development of legislation that is unique to New South Wales and evaluate the use of cascading clauses when parties seek to contract with one another in restraint of trade.

It will also examine the influence of economic theories such as the perfectly competitive model and its impact on the development and interaction between the doctrine and competition legislation in Australia by way of the *Competition and Consumer Act 2000* (Cth).

The law reform proposition advanced in this thesis is that the doctrine should be abolished in its entirety. Through the body of this work, it will be demonstrated that the doctrine is no longer necessary or desirable for the proper function of society. In addition, this thesis will also present alternative recommendations for change in the event that abolition of the doctrine appears to be unpalatable to those in the legislature and judiciary.

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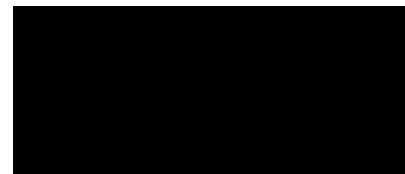
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JWC

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## INTRODUCTION

The Doctrine of Restraint of Trade ('Doctrine') is an ancient common law doctrine which was developed between the 1600s and mid-1800s.<sup>1</sup> Diplock LJ, in the matter of *Petrofina (Great Britain) Ltd v Martin*,<sup>2</sup> which was later approved by Lord Hodson in *Esso Petroleum Co Ltd v Harpers Garage (Stourport) Ltd*<sup>3</sup> defined a contract in restraint of trade as follows:

A contract in restraint of trade is one in which a party (the covenantor) agrees with any other party (the covenantee) to restrict his liberty in the future to carry on trade with other persons not party to the contract in such manner as he chooses.<sup>4</sup>

Naturally, the subject matter of the restraint can be extremely wide. Forms of restraints that are commonly affected by the operation of the Doctrine may include post-employment restraints, restraints imposed on a seller of business by a purchaser and restraints imposed by a licensor to a licensee etc. The evolution of the Doctrine is akin to a never ending tug of war as legislators and judges attempt to balance the competing interests of contracting parties between two opposing ideologies in the law of obligations: the freedom to contract vs. the freedom to trade. Over the centuries, the Doctrine has been shaped and re-shaped to suit the needs of society and commerce. Law makers have in turn, attempted to influence the operation of the Doctrine by passing legislation to expand the capabilities of the Doctrine in relation to contracts that are anti-competitive and to provide an alternative position in relation to the law of restraints in the State of New South Wales.<sup>5</sup>

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<sup>1</sup> John Heydon, *The Restraint of Trade Doctrine* (LexisNexis Butterworths Australia, 3<sup>rd</sup> ed, 2008) 3.

<sup>2</sup> [1966] 1 All ER 126 ('*Petrofina*').

<sup>3</sup> [1967] 1 All ER 699, 720 ('*Esso*').

<sup>4</sup> *Petrofina* [1966] 1 All ER 138.

<sup>5</sup> *Restraint of Trade Act 1976* (NSW) ('RTA').

## LITERATURE REVIEW

Much has been written about the Doctrine and especially notable among these writings is a publication by the recently retired Justice John Dyson Heydon of the High Court of Australia.<sup>6</sup> His Honour's 'The Restraint of Trade Doctrine'<sup>7</sup> is an insightful resource of leading cases and commentary on the operation of the Doctrine across various forms of restraints. Taken together with the writings of other recognised experts such as Professor Michael Trebilcock who published, 'The Common Law of Restraint of Trade – A Legal and Economic Analysis',<sup>8</sup> Dr David Meltz who published 'The Common Law Doctrine of Restraint of Trade'<sup>9</sup> and Professor Warren Pengilley who published numerous journal articles examining the interaction between the Doctrine and various theories of economics,<sup>10</sup> it is fair to say there exists in Australia an abundance of academic discourse addressing the author's subject matter.

Notwithstanding this plenitude, restraint of trade ('RT') cases continue to feature regularly throughout the Courts of Australia. Its notorious difficulty in application is well known. Accordingly, it is almost always the case that the literature on the Doctrine focuses entirely on the consequences of incorrect application whilst providing updates on judicial interpretation of what are enforceable restraints in a particular context. Analysis however, rarely extends beyond this and one will be challenged to find arguments that point to viable options for law reform. Aside from law reform milestones brought about by Part IV *Trade Practices Act 1974* (Cth) ('TPA'),

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<sup>6</sup> Heydon, above n 1.

<sup>7</sup> Ibid.

<sup>8</sup> Michael Trebilcock, *The Common Law of Restraint of Trade – A Legal and Economic Analysis* (Carswell, 1986).

<sup>9</sup> David Meltz, *The Common Law Doctrine of Restraint of Trade in Australia* (Blackstone Press, 2005).

<sup>10</sup> See, eg, Warren Pengilley, 'Thirty Years of the *Trade Practices Act*: Some Thematic Conclusions' (2004) 12 *Competition & Consumer Law Journal* 1; Warren Pengilley, 'Why Not Reinstate Clearance of Restrictive Trade Practices as an Assistance to Small Business?' (2006) 14 *Competition & Consumer Law Journal* 53; Warren Pengilley, 'Section 45 of the *Trade Practices Act* – The Law and Administration to Date' (1976) 8 *Federal Law Review* 16.

Part IV *Competition and Consumer Act 2010* (Cth) ('CCA') and the RTA, the Doctrine continues to stand stoically; its ancient form dating back to the late 1800s following the ground breaking English decision in *Nordenfelt v The Maxim Nordenfelt Guns & Ammunition Co Ltd*.<sup>11</sup> The last formal review of the Doctrine by a Law Reform Commission in Australia was in 1970 by the New South Wales Law Reform Commission.<sup>12</sup> No other State or Federal Government has since commissioned a further review.

### THESIS PROPOSITION

Given the obvious difficulties that continue to be faced by the Australian public when contracting in RT and the lack of literature available on law reform options, the purpose of this thesis is to firstly identify and evaluate the existing deficiencies experienced by parties when entering into a RT contract. This analysis will extend from the common law to the unique statutory regime in the State of New South Wales. In addition, the author will explore the relationship between the operation of the Doctrine and the competition laws of Australia and critically assess how the competition laws encapsulated now in the CCA influence parties when they contract in RT.

Insofar as it does not relate to matters of employment, the thesis proposition advanced in this paper is that the Doctrine should be abolished in its entirety. Whilst admittedly a challenging proposition, particularly given the prominence of the Doctrine's history in the annals of common law, it is the author's conclusion through the body of this work that the Doctrine is no longer necessary or desirable for the legal protection of parties that contract in RT. This paper will argue that the Doctrine should not be concerned with the relative value or reasonableness of bargains

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<sup>11</sup> [1894] AC 535 ('*Nordenfelt*').

<sup>12</sup> New South Wales Law Reform Commission, *Covenants in Restraint of Trade*, Report No 9 (1970) ('LRC Report').

reached between willing and able parties that contract with each other and that by relinquishing the possibility of judicial oversight into a seemingly problematic and unnecessary incursion into RT contracts, society will stand to benefit both economically and socially from the ability to enjoy increased freedoms when contracting.

This proposition for abolition partly rests on the premise that contracting parties may be suitably protected through existing principles of misleading or deceptive conduct,<sup>13</sup> unconscionable conduct,<sup>14</sup> duress,<sup>15</sup> unfair terms,<sup>16</sup> undue influence,<sup>17</sup> illegality,<sup>18</sup> mistake,<sup>19</sup> and incapacity<sup>20</sup>. In addition, federal legislation such as the CCA<sup>21</sup> and state legislation regarding fair trading practices,<sup>22</sup> sale of goods<sup>23</sup> and minors and their capacity to enter into contracts<sup>24</sup> all exist today to provide contracting parties with the peace of mind that, should a contract fall foul of one or more of the above common law or statutory principles, remedies are adequately provided for in law

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<sup>13</sup> CCA s 18 sch 2.

<sup>14</sup> CCA ss 20(1), 21 sch 2.

<sup>15</sup> CCA s 50 sch 2.

<sup>16</sup> CCA ss 23-24 sch 2.

<sup>17</sup> See leading authority of *Johnson v Buttress* (1936) 56 CLR 113.

<sup>18</sup> See, eg, *Clay v Yates* [1856] 1 H&N 73 in relation to contracts to commit a crime or civil wrong; *Parkinson v College of Ambulance* [1925] 2 KB 1 in relation to contracts leading to corruption in public life; *Pearce v Brooks* [1866] LR 1 Ex 213 in relation to contracts promoting to sexual immorality; *Foster v Driscoll* [1929] KB 470 in relation to contracts that prejudice public safety; *Miller v Karlinski* (1945) 62 TLR 85 in relation to contracts that defraud the taxation office.

<sup>19</sup> See leading authority of *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377.

<sup>20</sup> See leading authorities of *Gibbons v Wright* (1954) 91 CLR 423; *Blomley v Ryan* (1954) 99 CLR 362; *Nash v Inman* [1908] 2 KB 1.

<sup>21</sup> CCA s 45 relates to contracts, arrangements or understandings that restrict dealings or affect competition, s 46 relates to misuse of market power and predatory pricing, s 47 relates to exclusive dealing that constitute anti-competitive conduct, ss 48 and 49 relate to resale price maintenance and the making of a dual listed company that substantially lessens competition and s 50 relates to mergers.

<sup>22</sup> *Fair Trading Act 1992* (ACT); *Fair Trading Act 1987* (NSW); *Consumer Affairs and Fair Trading Act* (NT); *Fair Trading Act 1989* (QLD); *Fair Trading Act 1987* (SA); *Fair Trading Act 1990* (TAS); *Fair Trading Act 1999* (VIC); *Fair Trading Act 1987* (WA).

<sup>23</sup> *Sale of Good Act 1954* (ACT); *Sale of Good Act 1923* (NSW); *Sale of Good Act* (NT); *Sale of Good Act 1896* (QLD); *Sale of Good Act 1895* (SA); *Sale of Good Act 1896* (TAS); *Goods Act 1958* (VIC); *Sale of Good Act 1895* (WA).

<sup>24</sup> *Age of Majority Act 1974* (ACT); *Minors (Property and Contracts) Act 1970* (NSW); *Age of Majority Act* (NT); *Age of Majority Act 1974* (QLD); *Age of Majority (Reduction) Act 1970* (SA); *Age of Majority Act 1973* (TAS); *Age of Majority Act 1977* (VIC); *Age of Majority Act 1972* (WA); *Molton v Camrous* (1848) 2 Exch 487; *Gibbons v Wright* (1954) 91 CLR 423.

which may be relied upon to protect the contracting party that has been wronged. For ease of use, future references to the above will be noted as ‘Recognised Contractual Wrongs’.

Abolishing an ancient common law doctrine that remains widely in use is no simple feat and one must recognise the enormity of the task even if one were to agree with the author’s assessment and recommendation for reform. It is with this in mind that the author will also present a number of alternative law reform options which take on a ‘gentler’ and more palatable form.

This paper will not examine the separate topic of employment restraints. Employee covenants have been treated as a distinct form of RT since the late 1800s and regarded by Courts with more suspicion than ordinary covenants in RT.<sup>25</sup> Professor Harlan Blake summarised the reason for their distinction as follows:

A transfer of goodwill cannot be effectively accomplished without an enforceable agreement by the transferor not to act so as unreasonably to diminish the value of that which he is selling. The same is true in regard to any other property interest of which exclusive use is part of the value. The restraint on the transferor in such a case necessarily runs concurrently with the use of the property by the covenantee...The essential purpose of the post-employment restraint is quite

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<sup>25</sup> See, eg, *Nordenfelt* [1894] AC 535, 543-44, 566; *Herbert Morris Ltd v Saxelby* [1916] 1 AC 688, 701; *Attwood v Lamont* [1920] 3 KB 571, 586; *E Underwood & Sons Ltd v Barker* [1899] 1 Ch 300, 305, 310; *Mason v Provident Clothing and Supply Co Ltd* [1913] AC 724, 734, 738; *North Western Sale Co Ltd v Electrolytic Alkali Co Ltd* [1914] AC 461, 471; *Great Western and Metropolitan Dairies (Ltd) v Gibbs* (1918) 34 TLR 344, 345; *Ronbar Enterprises Ltd v Green* [1954] 2 All ER 266, 270; *English Hop Growers v Dering* [1928] 2 KB 174, 180; *Lindner v Murdocks Garage* (1950) 83 CLR 628, 641-42; *Butt v Long* (1953) 88 CLR 476, 486; *Escott v Thomas* [1934] NZLR 1046; *Maguire v Northland Drug Co Ltd* [1935] SCR 412, 416; *Elsley v J G Collins Ins Agencies Ltd* [1978] 2 SCR 913, 924; *Gallagher Group Ltd v Walley* [1999] 1 ERNZ 490, 497. See also, C J W Farwell, ‘Covenants in Restraint of Trade as between Employer and Employee’ (1928) 44 *Law Quarterly Review* 66; C E Carpenter, ‘Validity of Contracts Not to Compete’ (1928) 76 *University of Pennsylvania Law Review* 244; Andrew Stewart, ‘Drafting and Enforcing Post-Employment Restraints’ (1997) 10 *Australian Journal of Labour Law* 181; A Brooks, ‘The Limits of Competition: Restraint of Trade in the Context of Employment Contracts’ (2001) 24 *University of New South Wales Law Journal* 346; D J Ingram, ‘Covenants Not to Compete’ (2002) 36 *Akon Law Review* 49.

different, however. Its objective is not to prevent the competitive use of the unique personal qualities of the employee - either during or after the employment - but to prevent competitive use, for a time, of information or relationships which pertain peculiarly to the employer and which the employee acquired in the course of the employment. Unlike a restraint accompanying a sale of goodwill, an employee restraint is not necessary for the employer to get the full value of the thing being acquired – in this case, the employee's current services. The promise not to act in certain ways after terminating employment is something additional which the employer may or may not feel to be important and worth bargaining and paying for, depending on the circumstances. A sale of goodwill implies some obligation to deliver the thing sold by refraining from competition, just as an employment contract implies some obligation not to impair the value of the services rendered by competitive activity during the period of employment. But no such commitment not to compete after employment can be implied from an ordinary contract.<sup>26</sup>

The principle of Blake's reasoning is based on the inherently unequal bargaining positions between an employer and employee. The consequences of employees entering into restraints may be such that the employee, upon the termination of his or her employment, is left powerless to obtain gainful employment in the employee's profession or trade. When as is commonly the case, the restraint is coupled with a lack of separate consideration passing between the employer and employee on account of the employee entering into the restraint, it is right that Courts should be wary of endorsing restraints in the context of employment. Given these unique characteristics, the continuing operation of the Doctrine in matters involving employment is necessary. This is not to suggest, however, that the state of RT laws in employment cannot be improved. As one will observe, evolution of the Doctrine in the field of employment is ongoing and with the advent of the information age, new challenges surrounding the test of reasonableness will continue to arise as traditional barriers of time and space are distorted through the increasing globalisation

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<sup>26</sup> Harlan Blake, 'Employee Agreements Not to Compete' (1960) 73 *Harvard Law Review* 625, 646-48.

and international reach of businesses. Such an analysis however, is best left as the subject for another discourse.<sup>27</sup>

Before departing from the issue of employment restraints, it is noteworthy that in certain cases, the categorisation of a restraint as an ordinary RT as opposed to an employment RT can be difficult and what appears to be an employment restraint may in substance, be a common restraint between a purchaser and vendor in a sale of business. In these circumstances, Courts have adopted the position that such restraints were to be:

tested by the principles applicable as between vendor and purchaser since the covenant had been...taken for the protection of the goodwill of the business sold to the plaintiffs by the defendant, rather than for the protection of the plaintiff's present and future business as employer.<sup>28</sup>

It would be incumbent on a Court when faced with these matters to examine the circumstances giving rise to the parties entering into the RT. The employee covenant is therefore not looked at in isolation and it is irrelevant whether the restraint is contained in an employment contract or the sale of business contract.<sup>29</sup>

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<sup>27</sup> See generally, Joellen Riley, *Employee Protection at Common Law* (Federation Press, 2005) for an overview of the Doctrine in the context of employers and employees; See also, Christopher Arup et al, 'Restraint of Trade: The Legal Perspective' (2013) 36 *University of New South Wales Law Journal* 1 for an excellent synopsis of Australian RT employment litigation and its analysis of law reform; See also, David Cabrelli and Louise Floyd, 'New Light through Old Windows: Restraint of Trade in English, Scottish, and Australian Employment Laws – Emerging and Enduring Issues' (2010) 26(2) *International Journal of Comparative Labour Law* 167-91 for an interesting comparative analysis of Australian employment RT laws to that of England and Scotland.

<sup>28</sup> *Allied Dunbar (Frank Weisinger) Ltd v Weisinger* [1988] IRLR 60, 64.

<sup>29</sup> *Dawnay, Day & Co Ltd v d'Alphen* [1997] IRLR 442, 446-47; *TSC Europe (UK) Ltd v Massey* [1999] IRLR 22, 26; *Pioneer Concrete Services Ltd v Galli* [1985] VR 675, 693.



## METHODOLOGY

The methodology used throughout this paper will be derived from two modes of analysis; law and economics, and historical analysis. The author will chart the reasons that gave rise to the development of the Doctrine and its evolution over time. Historical analysis is important as the Doctrine has been remodeled and refined since its earliest days in line with the changing needs of society. Through the identification of seminal events which contributed to the Doctrine's evolution, much can be synthesised to explain the present state of the Doctrine.

The historical analysis will take the form of an assessment of available primary materials. Insofar as the primary materials are pertinent, the author will present and critically examine Australian case law that has fundamentally shaped the dimensions of the Doctrine and its interaction with relevant legislation. The cases of *Nordenfelt* and *Quadramain Pty Ltd v Sevastapol Investments Pty Ltd*<sup>30</sup> will feature heavily in their relevant chapters. The historical analysis will also feature coverage of the *TPA/CCA* with respect to the influence of competition law upon RT contracting. Additionally, an historical overview of the *RTA* and its impact upon RT contracting will be examined. Foreign cases from the United Kingdom, United States of America, Canada and Singapore will likewise be reviewed in critiquing the use of cascading clauses as an accepted technique of contract drafting in Australia when implementing restraints.

The overriding purpose of adopting an historical analysis methodology is to evaluate the long and continuing difficulties that contracting parties have experienced throughout the evolution of the Doctrine. This form of analysis will show that many of the commercial exigencies which fueled this evolution are no longer imperatives which require the protection of this ancient, obsolescent

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<sup>30</sup> (1976) 133 CLR 390 (*'Quadramain'*).

Doctrine thanks to developments in the conduct of modern commerce and to advances in law that protect contracting parties that enter into covenants in RT.

Examination of the Doctrine would not be complete without a study of the fundamental role that economic theory has had on its development. The law and economics analysis will also be pursued through the review and critique of secondary materials. Aided by relevant secondary materials, the author will approach the subject of law and economics from a mixed market economy perspective. In short, a market economy is an economy in which decisions regarding investment, production and distribution are based on supply and demand and the prices of goods and services are determined in a free pricing system without external interference.<sup>31</sup> The defining characteristic of a free market economy is that decisions on the allocation of resources are made through market forces.<sup>32</sup> In a mixed market economy, supply and demand are modulated by fiscal or monetary policy and by law which combine to correct the free market economy from recognised forms of inefficiency.<sup>33</sup>

The Australian economy is a typical form of a mixed market economy. Discussions of the perfectly competitive model and the externalities associated with RT contracts will feature in theories posited by respected jurists including Frank Easterbrook,<sup>34</sup> Robert Bork<sup>35</sup> and Learned Hand.<sup>36</sup> The author will also draw upon the works of Maureen Brunt<sup>37</sup> and D A Walsh,<sup>38</sup>

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<sup>31</sup> See generally, Robin Malloy, *Law and Market Economy: Reinterpreting the Values of Law and Economics* (Kluwer Academic Publishers, 2000); Maureen Brunt, 'Economic Overview – Trade Practices Lectures No. 11' (Speech delivered at Monash University, Clayton 1975); F M Scherer, *Industrial Market Structure and Economic Performance* (Rand McNally, 1970).

<sup>32</sup> Ibid.

<sup>33</sup> Ibid.

<sup>34</sup> See generally, Frank Easterbrook and Daniel Fischel, *The Economic Structure of Corporate Law* (Harvard University Press, 1991).

<sup>35</sup> See generally, Robert Bork, *The Antitrust Paradox* (Free Press, 2<sup>nd</sup> ed, 1993).

<sup>36</sup> See generally, *United States v Aluminum Co. of America et al*, 148 F.2d 416 (2d Cir, 1945).

particularly in the examination of competition law and its relationship to the Doctrine. Such an analysis will provide the backdrop to law reform recommendations which in turn can be justified from a law and economics perspective. By focusing a key thrust of this paper on law reform, the author will embrace a normative approach through the making of recommendations aimed at promoting economic efficiency and certainty when parties contract in RT.

## OBJECTIVES & FRAMEWORK

In this thesis, the author's objectives are set out as follows:

- (a) Trace the evolution of the Doctrine from its earliest days and identify the milestones which helped shape the Doctrine;
- (b) Apply a law and economics methodology to the Doctrine by using theories of the mixed market economy, perfectly competitive model and positive/negative externalities;
- (c) Critique the reasonableness between the parties test, the public interest test and the use of cascading clauses in Australia;
- (d) Analyse and trace the history of the *RTA* and its effect on RT contracts;
- (e) Evaluate using a law and economics methodology, the need for government intervention in RT contracts through the use of competition legislation;
- (f) Critically examine the relationship between the Doctrine and the *TPA/CCA*; and
- (g) Propose and justify the abolition of the Doctrine and alternative options for law reform.

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<sup>37</sup> See generally, Maureen Brunt and P H Karmel, *The Structure of the Australian Economy* (F W Cheshire, 1966); Maureen Brunt, *Economic Essays on Australian and New Zealand Competition Law* (Kluwer Law International, 2003).

<sup>38</sup> See generally, D A Walsh, 'Authorization and Clearance – Trade Practices Lectures No. 7' (Speech delivered at Monash University, Clayton 1975).

The framework of this thesis will be divided into 4 chapters.

Chapter 1 is entitled ‘History, Business, Economics and the Law’. This chapter will trace the Doctrine back to its origins and establish the reasons for its earliest existence. It will then analyse the evolution of the Doctrine and identify the key moments in history during which the emerging and increasingly sophisticated commercial and social requirements of society contributed to the reform of the Doctrine. Chapter 1 will then launch into a law and economics discussion of RT contracting. It will demonstrate that in a mixed market economy, governments and Courts have to intervene and disrupt certain RT arrangements to encourage economic efficiency.

The contribution of Chapter 1 to the thesis can be divided into two parts. The first part is to demonstrate through historical analysis that the imperatives which launched the earliest forms of the Doctrine into existence are no longer relevant. Historically, the Courts have been rigorous in maintaining a flexible approach to the question of RT contracts. This was necessary, in part, to maintain relevance of the law in the face of society’s historical commercial and social needs. It is argued that the same flexibility must be adopted in the law reform process. If it is demonstrated that society’s commercial and social needs are now best met through the abolition of the Doctrine, it should be incumbent on law makers and the Courts to consider such an approach. The second part is to demonstrate through a law and economics analysis that maximum economic efficiency is generally achieved through minimal legal interference in a party’s freedom to contract. Thus the proposition will be advanced that RT contracts ought to be upheld unless a party to the contract can establish a Recognised Contractual Wrong.

Chapter 2 is entitled ‘Common Law Deficiencies, Legislative Remedies and the Use of Cascading Clauses’. This chapter will examine the current operation of the Doctrine in Australia. Extended commentary and critical analysis will be provided in respect of the test of reasonableness between

the parties and the public interest test which form the backbone of the Doctrine. The *RTA* that is unique to NSW will then be introduced and a historical account including the reasons for the introduction of the *RTA* will follow. Chapter 2 will conclude by showcasing the drafting technique of cascading clauses and the relative advantages and disadvantages of its use. The cascading clause is a unique form of drafting technique formulated in an attempt to overcome common problems associated with the test of reasonableness pursuant to the Doctrine. Nevertheless inherent in the use of the cascading clause is a lack of certainty when parties contract which inevitably increases the potential for future litigation.

The contribution of Chapter 2 to the thesis is to examine the present workings of the Doctrine and pinpoint its problems, which will in turn establish the framework for suitable law reform proposals. Critical analysis and data from secondary sources evidence the persisting complications associated with the test of reasonableness and the difficulty in determining what is reasonable and unreasonable in the eyes of the Doctrine. Observations are also made in relation to the defunct test of public policy which, for all intents and purposes, is not applied to cases in any substantive or meaningful manner. Chapter 2 then seeks to demonstrate that whilst the *RTA* does go some way in alleviating the problems associated with the Doctrine, it nevertheless falls short of establishing a satisfactory premise for future contracts that seek to implement RT. It also argues that the use of cascading clauses remains very much an artificial technique born of a need to overcome the inherent difficulties associated with the Doctrine. The author is highly critical of their use. By establishing the framework for law reform in this chapter through the identification and analyses of problems associated with the Doctrine, the *RTA* and the use of cascading clauses, the author is then able to propose suitable law reform recommendations in line with an established framework.

Chapter 3 is entitled ‘The Relationship Between Competition Legislation and the Restraint of Trade Doctrine’. This chapter will consider the effect of the *CCA* on RT contracting. Whereas the common law and the *RTA* are interested in the reasonableness of a restraint and to a limited degree, the application of the public interest test, the premise behind the *CCA* is, unlike the common law and the *RTA*, to promote competition and prohibit restrictive agreements which seek to restrain trade that substantially lessens competition. Insofar as agreements in RT can be challenged under the Doctrine and the *RTA*, such agreements may also be challenged through the *CCA*. Accordingly, proposals for law reform will be amiss without due consideration of the *CCA* and its impact on RT contracting.

Chapter 3 will begin by adopting a law and economics analysis of the impact of competition legislation upon agreements in RT. It will then examine the difficulties of maintaining a working relationship between the Doctrine and the *CCA* and how these difficulties were overcome through legislation. Chapter 3 will conclude by reviewing the process of Authorisations and the potential merits of reinstating the now defunct Clearance procedures for contracts that purport to engage in RT.

The contribution of Chapter 3 to the thesis is to question whether from a law and economics methodology, government intervention in RT contracts by way of legislation (such as the *CCA*) is warranted. The author concludes in this chapter that intervention is not only desirable but necessary for the proper function of markets in Australia. A number of observations are made throughout the chapter on the nature of the relationship between the Doctrine and the *TPA/CCA*. The author will also establish that under the existing legislative framework, the reinstatement of the now defunct Clearance procedure for contracts that engage in RT is desirable and should be considered as a future subject for law reform.

Chapter 4 is entitled ‘Propositions of Law Reform’. This chapter will use the frameworks established in the preceding Chapters 1-3 as a set of normative and practical criteria for the evaluation of law reform options in RT contracting. It will present the author’s principal argument that the Doctrine should be abolished in its entirety. The author will then review the analyses made in Chapter 3 and conclude that RT contracts that have the effect of substantially lessening competition should be ordinarily invalidated unless such a contract receives Authorisation under the *CCA*. The proposal for resurrecting Clearances is revisited and affirmed as a further point of law reform consideration.

The contribution of Chapter 4 to the thesis is primarily through the presentation of the author’s thesis statement that the Doctrine should be abolished. Additional arguments are presented that competition laws are necessary for a working economy and Clearances should be resurrected as an option for contracting parties. As alternatives to abolishing the Doctrine, other law reform recommendations include:

- (a) Providing parties with the option to obtain independent legal advice prior to the execution of RT contracts;
- (b) Empowering Courts to award a sum of compensation to covenantees that lose the protection of a restraint should the restraint be unenforceable to prevent inequitable windfall gains; and
- (c) Creation of federal legislation mirroring the *RTA*.

This paper will conclude by making some observations about the difficult nature of law reform, particularly with respect to the author’s subject matter. Notwithstanding those difficulties, it is the author’s contention that the present state of society, commerce and law do not justify the ongoing operation of the Doctrine and it should accordingly be abolished.

## **CHAPTER 1: HISTORY, BUSINESS, ECONOMICS AND THE LAW**

Many of the current problems with the Doctrine are rooted in its history and these problems have echoed through its evolution down to the present day. In particular, the reverberations can still be felt of the *Nordenfelt* case which established the foundation for the Doctrine and the RTA. To fully appreciate these problems, the panorama must also include the economic theories that have contributed to the common law interpretation and application of the Doctrine in Australia with a particular focus on the positive and negative externality effects of RT contracts.

### **1.1 FROM GENERAL RESTRAINTS TO CASCADING CLAUSES**

The Doctrine was developed between the 1600s and mid-1800s.<sup>39</sup> In its earliest form, the common law had resented the notion of all RT. The judiciary's ideology behind this severe and uncompromising position was derived from the perception that the importance of maintaining a free labour market was paramount to all other private and public interests.<sup>40</sup> Coke CJ stated the following back in 1614:

...at the common law, no man could be prohibited from working in any lawful trade, for the law abhors idleness, the mother of all evil...and therefore the common law abhors all monopolies, which prohibit any from working in any lawful trade...<sup>41</sup>

In the early 18<sup>th</sup> century, the Courts began to recognise the benefits of permitting certain restraints.<sup>42</sup> For example, a restraint voluntarily entered into by a vendor pursuant to a sale of

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<sup>39</sup> See generally, Trebilcock, above n 8, 3-14.

<sup>40</sup> See *Ipswich Tailors' Case* (1614) 77 ER 1218, 1219.

<sup>41</sup> Ibid 1219-220.

<sup>42</sup> See *Mitchel v Reynolds* (1711) 24 ER 347 ('*Mitchel*').



business may not necessarily be detrimental to the proper functioning of society as it provided the purchaser with an opportunity to establish itself without undue competition from the vendor.<sup>43</sup> During this period, the Doctrine was segregated into restraints formed via Guild Rules or Crown Patents (termed involuntary restraints) and restraints involving the use of contracts (termed voluntary restraints).<sup>44</sup>

The position of the common law was such that all involuntary restraints were void with the exception of Crown grants for patents.<sup>45</sup> In the case of voluntary restraints however, a distinction was drawn between ‘general restraints’ in which the restraint extended across the entire geographical borders of England, and ‘partial restraints’ where the restraint extended to only a part of the geographical borders of England.<sup>46</sup> All general restraints were void *per se*. The primary reason for the prohibition of general restraints was that such restraints were viewed as contrary to the public interest in that they discouraged gainful employment whilst depriving society of the benefits associated with such employment.<sup>47</sup> In addition, by their very nature, general restraints were viewed as being far wider than could possibly be necessary for the reasonable protection of legal interests.<sup>48</sup> It was uncommon, for example, to see businesses at that time with commercial ties that stretched across the whole of England. Most commercial activities then were in that sense, limited and localised to one or several small geographical regions in England. On the other hand, partial restraints might be valid if supported by consideration.<sup>49</sup> The partial restraint also had to be no greater than was necessary for the

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<sup>43</sup> Ibid.

<sup>44</sup> Trebilcock, above n 8, 3-14.

<sup>45</sup> Ibid.

<sup>46</sup> Ibid.

<sup>47</sup> See *Mitchel* (1711) 24 ER 347.

<sup>48</sup> Ibid.

<sup>49</sup> Trebilcock, above n 8, 3-14.

protection of the party seeking it, including that of geographical limitations imposed by the restraint.<sup>50</sup>

By the mid-1800s, the English commercial world was burgeoning as industrialisation and long distance transportation made real, the notion of a national market which foreshadowed the beginnings of an international market for goods and services under the Pax Britannica. During the period between 1800 and 1850, the population of England and Wales doubled from 9 million to 18 million.<sup>51</sup> This increase in population also saw huge scale migration from rural England to metropolitan England and in particular, to the new factory cities such as Manchester, the centre of England's cotton industry.<sup>52</sup> London more than doubled in population between 1800 and 1850 (from 1 million to 2.36 million) such that by 1851, the urban population of England and Wales was greater than the rural population.<sup>53</sup> Between 1830 and 1850, in the second wave of the English industrial revolution, the production of coal and iron tripled in volume and a steel industry was created to supply the rapidly expanding railways of England.<sup>54</sup> The combination of innovative mass production technology, large urbanised workforces and mass transit produced enormous industrial output enabling trading entities to expand their commercial reach across the entire geographical borders of England and beyond.

In response to industrial and commercial advancement, the English equity Courts reconceptualised the Doctrine by diverging from the previous distinction between general and partial voluntary restraints.<sup>55</sup> Rather than mandating that all general restraints were void *per se*,

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<sup>50</sup> Ibid.

<sup>51</sup> Carlo Cipolla, *Before the Industrial Revolution* (W. W. Norton & Company, 1994) Introduction.

<sup>52</sup> E J Hobsbawm, *Industry and Empire* (Hammondsworth: Penguin, 1977) 56.

<sup>53</sup> Ibid.

<sup>54</sup> Ibid 35.

<sup>55</sup> David Meltz, 'Happy Birthday Mr Nordenfelt – the Centenary of the Nordenfelt Case' (1994) 2 *Trade Practices Law Journal* 149.

the Courts instead held that all restraints irrespective of whether they were general or partial were void and in violation of public policy unless they were reasonable for the protection of the parties in dealing with the subject matter of the contract.<sup>56</sup> In adopting the reasonableness test when determining the enforceability of all voluntary restraints in the contractual context, the Courts again widened their powers to review contracts which contained a general restraint rather than mechanically rejecting such restraints, as was previously the case.<sup>57</sup>

The reasonableness test was framed extremely elastically: a contractual restraint was enforceable so long as it did no more than protect an interest that the law was prepared to recognise as being protectable in the circumstances. This principle was classically spelt out in the frequently quoted judgment of Lord Macnaghten in *Nordenfelt*.<sup>58</sup> Lord Macnaghten's reasoning has subsequently proved to be the cornerstone of the Australian statutory and common law approach to the Doctrine and thus *Nordenfelt* warrants examination so as to establish a starting point for this thesis.

Mr. Nordenfelt was an inventor of an early form of machine gun. He incorporated a company to take over his business and contracted not to compete with that company whilst it carried on business as a gun manufacturer. In 1888, negotiations were entered into with the Maxim Gun Company, a competitor which had also made significant advances in rapid firing guns. As part of the negotiations, Mr. Nordenfelt entered into a further non-compete contract for 25 years for the benefit of the Maxim Gun Company. He then proceeded to breach the contract by entering into commercial dealings with a Belgian company. In his defence, Mr. Nordenfelt argued that the

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<sup>56</sup> Ibid.

<sup>57</sup> Ibid.

<sup>58</sup> *Nordenfelt* [1894] AC 535, 565.

restraint was a general restraint and thereby void as the restraint prohibited him from carrying on business throughout the whole of England.

On face value, it was clear to the House of Lords that the construction of the restraint was that of a general restraint. The difficulty faced the Lord Justices was that by recognising it as a general restraint, their Lordships would be ousting the jurisdiction of the Courts' powers of review with respect to the merits of the restraint. In justifying the expansion of the Courts' powers of judicial review into the field of general restraints, Lindley LJ had pointed out in the earlier decision of the Court of Appeal that the distinction between a general restraint and partial restraint in the 1700s had been drawn because there had been at that time, no concept of a national or international market.<sup>59</sup> A general restraint therefore would have always gone beyond providing a necessary and reasonable protection envisaged by such restraints. Upon appeal to the higher Court, Lord Herschell LC further suggested that the distinction between general and partial restraints would not have been so developed in the first place if national and international markets had existed at the time of its formulation.<sup>60</sup>

The House of Lords in *Nordenfelt* proceeded to dissolve the traditional distinction between general and partial restraints and mandated an alternative approach enabling Courts to uphold restraints should the restraint in question be reasonable and not offend public policy. By removing the distinction between general and partial restraints, Courts were free to contemplate much broader considerations in deciding the validity of restraints. In the famous words of Lord Macnaghten who summarised the new *ratio* of the law as it stood post *Nordenfelt*:

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<sup>59</sup> Ibid 559.

<sup>60</sup> Ibid 546-47.

The true view at the present time I think is this: The public have (sic) an interest in every person's carrying on his trade freely: so has the individual. All interference with individual liberty of action in trading, and all restraints of trade of themselves, if there is nothing more, are contrary to public policy, and therefore void. That is the general rule. But there are exceptions: restraints of trade and interference with individual liberty of action may be justified by the special circumstances of a particular case. It is a sufficient justification, and indeed it is the only justification, if the restriction is reasonable – reasonable, that is, in reference to the interests of the parties concerned and reasonable in reference to the interests of the public, so framed and so guarded as to afford adequate protection to the party in whose favour it is imposed, while at the same time it is in no way injurious to the public. That, I think, is the fair result of all the authorities.<sup>61</sup>

Lord Macnaghten's limber expression of principle demonstrated the supple ability of the House of Lords to recognise the necessity for change in the application of the Doctrine to accommodate the expansion of commerce nationally and internationally. The principles elucidated by Lord Macnaghten were deliberately wide to allow scope for the judiciary to examine the nature of the restraint in light of its reasonableness with reference to both the interests of the contracting parties and the interests of the general public. It may be said that such tests, by the nature of their framing, enable contemporary conditions of commerce and the needs of the public to be imported into judicial decision making and allow the law, at least in theory, to keep up with commercial developments and business strategies of the day.

The obvious difficulty with this formulation however, is its indeterminate and subjective nature which, without further guidance in its application, may result in a miscellany of decisions with no precedential value. It is noteworthy on this point that the House of Lords avoided giving any

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<sup>61</sup> Ibid 565.

guidance in determining what and how the public interest test was to be applied and moreover, their Lordships added very little, if anything at all, as to how to construe the meaning of reasonableness with reference to the interests of the parties. The House of Lords also omitted to state how the relationship, if any, between the interests of the contracting parties and the interests of the public were to be balanced in the event of a conflict being perceived between the two.

On review, it appears from an English and Australian historical overview of cases subsequent to *Nordenfelt* that very few cases have declared a contract containing a restraint void on the grounds of public interest where such a restraint had been found to be reasonable and in the interests of the parties.<sup>62</sup> With the clear exception of the common law's long-standing axiom of a person's right to earn a living as an employee despite any restraint which may be imposed by an employment agreement, the public interest test was largely left untouched since *Nordenfelt*. In part, this was due to the judiciary's reluctance to be seen as consciously making public policy which it saw as the primary function for the legislature.<sup>63</sup>

In seeking to crystallise the concept of reasonableness with reference to the interests of the parties, early Australian decisions revealed that Courts were prepared and willing to provide suitable geographical and temporal restraints in appropriate circumstances.<sup>64</sup> Trade secrets, business assets and the goodwill attached to a business were all legal interests which Courts were prepared to protect by way of a restraint where such a restraint was held to be within reasonable limits. However, should a restraint be found by a Court to have strayed beyond the appropriate bounds of reasonableness, the restraint was held to be void unless it could be read down under the

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<sup>62</sup> Meltz, above n 55, 153-54.

<sup>63</sup> See, eg, Heydon, above n 1, 22- 32, 272-78; *Wilkinson v Osborne* (1915) 21 CLR 89, 97.

<sup>64</sup> See, eg, *Fleming Bros (Monaro Agencies) Pty Ltd v Smith* (1983) ATPR 40-389 ('*Fleming Bros*').

doctrine of severance. Additional considerations to this general rule apply only in New South Wales under the *RTA*, the subtleties of which will be discussed in Chapter 2.

The flexibility in the application of the Doctrine decreed by the House of Lords in *Nordenfelt* continues to prevail and Australian Courts have been loath to articulate clearly, whether in *rationes decidendi* or *obiter dictum*, any fixed or clear notion of what is an appropriate restraint, preferring instead to deal with such matters on a case by case basis. Holland J in *Fleming Bros* observed that the reasonableness of restraints was often determined by the Courts ‘on a common sense basis and on impression for the simple reason that the issue is not capable of determination by precise calculation. There are too many intangibles involved.’<sup>65</sup>

It is fair to conclude from the historical account above that the origins and early development of the Doctrine in England provided Australian Courts with a wide discretion when faced with deciding the validity of such restraints, particularly in relation to the reasonableness test. Unfortunately, as Chapter 2 will show, Australian Courts have applied this discretion rather liberally and over time, have created a medley of legal precedents that fail to enlighten contracting parties who seek to engage in RT contracting.

Even more alarmingly, rather than addressing this concern by seeking to increase certainty through judicial or legislative intervention when contracting in RT, the Australian jurisprudence has dug itself a deeper hole by adopting the convenience of scalable RT clauses. Such clauses are commonly known as ‘cascading clauses’. In simple form, a cascading clause is a contractual clause that utilises a matrix of restraints with respect to time, geography and other variables from which a Court may configure a restraint that it deems reasonable with reference to the interests of

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<sup>65</sup> Ibid 44, 571.

the parties in the event of a dispute. An example is provided below of such a clause in a business sale agreement the subject of which is an internet café:

1.1 This clause shall have effect as if it were several separate covenants consisting of each separate covenant set out in clause 1.2 with each separate period of time set out in clause 1.3 and of each such separate combination with each separate area set out in clause 1.4 and if any of the said several separate covenants shall be or become invalid or unenforceable for any reason then such invalidity or unenforceability shall not affect the validity or enforceability of any of the other separate covenants.

1.2 In consideration of the purchaser entering into this contract and to reasonably protect the goodwill of the business, the vendor agrees that it will not for the period and within the area hereinafter specified without the prior written consent of the purchaser:

- (a) carry on or be engaged in or concerned with directly or indirectly or otherwise engage in the business of an internet café of any description or any other business of a similar nature;
- (b) procure or solicit or encourage any other person to procure or solicit the custom of any former customer of the business; or
- (c) hold or beneficially own whether directly or indirectly and whether absolutely or contingently or hold options over shares in or be an adviser to any corporation doing any of the things referred to above in 1.2(a) and 1.2(b).

1.3 The period of time hereinbefore referred to are:

- (a) during the period of 3 years from and after completion;
- (b) during the period of 2 years from and after completion;
- (c) during the period of 1 year from and after completion;



1.4 The areas hereinbefore referred to are:

- (a) within the political border of the Commonwealth of Australia;
- (b) within the political border of the State of Victoria;
- (c) within a 5km radius from the place of business.

From the above cascading clause, it is possible to configure the restraint in no less than 27 different variations. It should therefore be of no surprise that parties can be uncertain of the precise extent of the restraint upon execution of an RT agreement, even when advised by competent lawyers. It is commonly the case that the most restrictive restraint is elected by the covenantee as the applicable restraint even though it may manifestly infringe the test of reasonableness. Ordinarily then, it would be up to the covenantor to challenge the reasonableness of such a restraint. Such uncertainty encourages litigation and parties are then often faced with a dispute as to which of the host of restraints conjured from the cascading clause are in fact enforceable. Moreover, their acceptance by Australian Courts is evidence of those Courts' acknowledgement of the high levels of uncertainty when lawyers are faced with the task of advising their clients on the perils of RT contracting.<sup>66</sup> The very fact that Courts are presented with this myriad of options from a restraint clause is indicative of the unacceptable difficulties faced by parties when contracting in RT. A detailed discussion of the above will be presented in Chapter 2.

## 1.2 THE BUSINESS OF ECONOMIC THEORY

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<sup>66</sup> See, eg, *JQAT Pty Ltd v Storm* [1987] 2 Qd. R 162 ('*JQAT*').

Earlier in this paper, the proposition was made that the advancement of industry and commerce was pivotal to the evolution of the Doctrine. Such a proposition would not be robust without elaborating on the influence of economic theory to the evolution of the Doctrine.

In its raw form, a contractual RT is an agreement between two or more parties to carry out or refrain from carrying out an action or set of actions. From an economic perspective, the existence of a contractual mechanism to make such promises binding typically maximises welfare because it enables cooperation between parties which would otherwise be uncertain.<sup>67</sup> The upholding of contractual mechanisms is therefore of paramount importance to a proper functioning of a mixed market economy. However, this theory presumes, amongst other things, that the obligations and effects created by the contracts are captured in its entirety by the contracting parties.<sup>68</sup> The theory is complicated in RT cases as the agreed restraints may also impact upon third parties, whether they are individuals, groups of individuals or an entire population.

This impact on a third party, if positive, is known in economic terms as a positive externality.<sup>69</sup> If, on the other hand, the impact is negative, it is known as a negative externality.<sup>70</sup> In most private RT contracts, the number and effect of the externalities or the combination of them is negligible in reference to the interests of the wider public. In these circumstances, maximum efficiency will dictate that the States or Courts should uphold the sanctity of contracts wherever possible.<sup>71</sup>

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<sup>67</sup> Kevin Marshall, 'Product disparagement under the *Sherman Act*, Its nurturing and Injurious Effects to Competition, and the Tension Between Jurisprudential Economics and Microeconomics' (2006) 46 *Santa Clara Law Review* 237.

<sup>68</sup> Ibid.

<sup>69</sup> B Taylor, *Positive Externality* (2006) Economics Fundamental Finance <<http://economics.fundamentalfinance.com/positive-externality.php>>.

<sup>70</sup> B Taylor, *Negative Externality* (2006) Economics Fundamental Finance <<http://economics.fundamentalfinance.com/negative-externality.php>>.

<sup>71</sup> Steven Shavell, *Foundations of Economic Analysis of Law* (Harvard University Press, 2004) 297-99.

This argument is founded upon the assumption that one sets out to achieve a perfectly competitive model of maximum efficiency in consumption, production and allocation.<sup>72</sup> The above assumption forms the basis of what is known economically as the perfectly competitive model.<sup>73</sup> Through the creation of efficiencies, the perfectly competitive model offers the greatest social opportunity for wealth creation and greater output at lower prices.<sup>74</sup> Economically speaking, the perfectly competitive model exists when the following characteristics occur simultaneously:

- (a) There are numerous buyers and sellers, each acting independently and rationally;<sup>75</sup>
- (b) Each buyer and seller consumes or produces such a negligible amount of the total output such that no one buyer or seller can influence price by the amount they either consume or produce;<sup>76</sup>
- (c) There are no barriers to entry or exit with respect to consumer or product markets;<sup>77</sup>
- (d) All buyers and sellers are fully informed of relevant economic and technological data;<sup>78</sup>
- (e) All products are homogeneous, or rather, constitute interchangeable substitutes for each other;<sup>79</sup> and
- (f) The forces of supply and demand are free to determine the quantity of output in a relevant market as well as determine a competitive price with respect to that output.<sup>80</sup>

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<sup>72</sup> David Colander, *Microeconomics* (McGraw-Hill Education, 5<sup>th</sup> ed, 2004) 242.

<sup>73</sup> The perfectly competitive model is a well understood and often used economics model of assessing efficiency in consumption, production and allocation. It is normative in nature and thus, in reality, very few markets (if any) are in fact perfectly competitive. As a normative model, it is used in this thesis with an acknowledgment of its inherent economics and social imperfections and limitations.

<sup>74</sup> Marshall, above n 67, 231, 233.

<sup>75</sup> Robert Pindyck and Daniel Rubinfeld, *Microeconomics* (Prentice Hall, 5<sup>th</sup> ed, 2001) 327.

<sup>76</sup> Steven Landsburg, *Price Theory & Applications* (Cengage Learning, 6th ed, 2005) 634.

<sup>77</sup> Pindyck and Rubinfeld, above n 75, 253.

<sup>78</sup> Ibid 595.

<sup>79</sup> Ibid 252.

<sup>80</sup> Ibid 55.

It therefore follows that if any contractual activity threatens any one or more of the necessary characteristics, they must be discouraged or altogether eradicated through legislative and judicial intervention to maximise the ability of the market to achieve a perfectly competitive equilibrium.

With the raft of legal mechanisms available to protect contracting parties in the event of misleading or deceptive conduct, unconscionable conduct, duress, unfair terms, undue influence, illegality, mistake and incapacity, contracting parties are to a large extent, protected against the vagaries of events (a), (d) and (f) with respect to their ability to be informed of relevant facts and to act independently, rationally and freely.<sup>81</sup> In addition, ss 45-50 of the *CCA* seeks to regulate events (b), (c) and (e) for the benefit of the wider public in the maintenance of a free market.<sup>82</sup>

Taking the above into account, it is logical that contracting activity which does not impinge upon any of the 6 necessary events should not be interfered with because unnecessary interference typically results in less than optimal efficiency with respect to the allocation and use of resources. It should be the default position that, unless justifiable reasons exist to interfere with a private contract, (whether those reasons are social, economic, political or otherwise), society is best served by the legal recognition of that contract.

In a contracting situation of negligible externalities, events (b), (c) and (e) can be largely ignored as the contracting parties cannot be influential enough to materially affect the market. By way of clarification, it is noted here that RT contracting with negligible externalities typically involves a

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<sup>81</sup> With reference to characteristic (b), anti-competitive conduct will have an effect on prices in a manner that is usually adverse to the consumers' interests.

<sup>82</sup> With reference to characteristic (e), it may be overstating the effects of the *CCA* if one was to argue that the legislation directly promotes the production of homogeneous products or interchangeable substitutes, however, by promoting competition and free trade and regulating against actions that substantially lessen competition, the *CCA* has an indirect effect on the market by encouraging the production of homogeneous products and interchangeable substitutes which in turn creates competition.

private contract between two or more parties in a free market where the effects of their contracting efforts will have a minimal or negligible impact on society or trade due to the availability of substitute goods and services within that society. In this light, and in the absence of misleading or deceptive conduct, unconscionable conduct, duress, unfair terms, undue influence, illegality, mistake and incapacity (which threaten events (a), (d) and (f) and the presence of anti-competitive behaviour contrary to ss 45-50 of the *CCA* (which threaten events (b), (c) and (e)), this thesis argues that in order to achieve maximum economic efficiency, RT contracts should be recognised and enforced when called upon, notwithstanding that they may be outside the boundaries of what is objectively reasonable to protect the interests of the contracting parties.

In a broader sense, it is important to note that in an economic context, the application of the Doctrine does not always promote free trade. It may inhibit or even strangle free trade contrary to the aims and goals of the Doctrine. Lord Peace recognised this in *Esso* in which he stated ‘Undue interference, though imposed on the ground of promoting freedom of trade, may in the result hamper and restrict the honest trader and, on a wider view, injure trade more than it helps it.’<sup>83</sup> The above quotation arose from his Lordship’s reflections upon the reasonableness of restraints. It may also be considered equally apt in demonstrating that economics is best served by the law upholding bargains and enforcing RT contracts other than those which clearly jeopardise any of the 6 events or which are contrary to public policy. In other words, to achieve maximum economic efficiency, a party which seeks to break a RT arrangement ought to be obliged to show that the contract was tainted by a Recognised Contractual Wrong.

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<sup>83</sup> [1967] 1 All ER 699; see also, *Esso* [1967] 1 All ER 724.

What position should be adopted with respect to RT contracting that creates a negative externality? Reference has previously been made to the proposition that, if an RT creates a negative externality, the performance of such a contract can often decrease economic efficiency and social welfare.<sup>84</sup> The mere existence of a negative externality however, is insufficient to render the transaction economically inefficient *per se*. Inefficiency in this instance is properly defined as occurring when the net harm exceeds the net benefits provided by the RT.<sup>85</sup> The law should theoretically be positioned to facilitate the distribution of resources and the balancing of negative externalities created by RT contracting so as to maximise the net benefits for society. In this respect, RT laws are designed to ordinarily protect the competitive market with respect to events (b), (c) and (e) in an attempt to preserve, to the extent that it is able to, the perfectly competitive model. This is especially relevant to 2 types of conduct that are ordinarily deemed to be economically inefficient.

Firstly, RT contracts among competitors that increase the barriers of market entry and RT contracts which create barriers for others to competitively market goods and services are generally viewed as anti-competitive.<sup>86</sup> These types of RT are agreed by most economists to be harmful to the economy as the negative externalities created by the RT typically outweigh the positive externalities.<sup>87</sup>

Secondly, RT laws are concerned about the creation and maintenance of illegal monopolies.<sup>88</sup> In general terms, monopolies are viewed as destructive to competition when they are realised or

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<sup>84</sup> Thomas Piraino, 'Identifying Monopolists' Illegal Conduct under the *Sherman Act*' (2000) 73 *New York University Law Review* 809.

<sup>85</sup> *Ibid.*

<sup>86</sup> Herbert Hovenkamp, 'Antitrust's Protected Classes' (1989) 88 *Michigan Law Review* 1, 6.

<sup>87</sup> *Ibid.*

<sup>88</sup> Piraino, above n 84, 814-16.

maintained by means unrelated to merit (i.e. via illegal RT operations or contracts).<sup>89</sup> As monopolistic entities typically exert a significant degree of control over the pricing of goods or services by changing the quantity supplied in the face of little or no competition, their existence create a deadweight loss through their ability to reduce production levels to less than the equilibrium level.<sup>90</sup> This also has the effect of reducing consumer choice which can stifle incentives for development.<sup>91</sup> A monopoly will therefore generally create inefficiency in the allocation of resources and is viewed by economists as a form of market failure, hence the need for law to correct such failure.<sup>92</sup> This view is subject to certain exceptions which may warrant the existence of a monopolistic industry (e.g. postal, money printing and defense) although modern trends in Australia have seen the deregulation of many previous monopolistic industries (e.g. telecommunications and utility service providers) based on competition arguments even if some deregulated monopolistic industries remain monopolistic by nature.<sup>93</sup>

Some commentators have asserted that monopoly power is simply a reflection of a business successfully meeting consumer demand in quantity and price.<sup>94</sup> It is obvious to state that businesses will gain market share only at the expense of another. The gaining of market share typically occurs because a business is able to offer a product or service that is similar or superior in quality to a rival product or service at a more competitive price. On this subject, the American legal scholar Robert Bork commented that ‘if consumers choose to purchase more from one

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<sup>89</sup> Ibid.

<sup>90</sup> Ibid.

<sup>91</sup> Ibid.

<sup>92</sup> Ibid. See generally, Jodi Beggs, *The Economic Inefficiency of Monopoly* (2015) About Education <<http://economics.about.com/od/monopoly-category/ss/The-Economic-Inefficiency-Of-Monopoly.htm>>.

<sup>93</sup> See generally, Peter Ross ‘The Deregulation of the Australian Telecommunications Sector: Workforce restructuring and employment relations (ER) at Telstra in a deregulated environment’ (2004) *Association of Industrial Relations Academics of Australia and New Zealand* 1; Alan Moran, *Power to the People: Privatisation and Deregulation of the Electricity Industry in Australia* (2002) Institute of Public Affairs <<https://www.ipa.org.au/library/amsafrica.pdf>>.

<sup>94</sup> John McGee, ‘Why Not “Deregulation” for Antitrust?’ (1977) 46 *Antitrust Law Journal* 777, 785.

company than from its rivals, that firm is, precisely to that degree, the most efficient in the market.’<sup>95</sup> Similarly, the well-respected American jurist, Frank Easterbrook stated that ‘the more successful a firm is at reducing the cost of its product or making that product more attractive to consumers, the more it sells. In the end, a very successful firm will wind up with the whole market.’<sup>96</sup> These comments reflect the well-established principle in both Australia and the United States that RT laws do not prohibit the acquisition of market power *per se*. Nor do RT laws prohibit a monopoly where such market power has been achieved legitimately by outcompeting other market players. To allow the reverse would be to pervert fundamental principles established under a democratic mixed market economy which Australia and the United States reflect in their systems of government, commerce and law. In illustrating this point, Justice Learned Hand famously stated back in 1945, ‘The successful competitor, having been urged to compete, must not be turned upon when he wins.’<sup>97</sup> This statement remains true today through the legal accounting of dynamic efficiency together with allocative efficiency when modern Courts consider the merits of RT arrangements. Democratic mixed market economies therefore do not generally seek to destroy monopolies unless predatory and unlawful conduct is established.<sup>98</sup> Furthermore, specific types of efficiency prohibiting conduct such as exclusive dealing, price discrimination and tying are not prohibited in every instance. A further example of this tolerance lies in restrictive licensing arrangements and unilateral refusals to deal being generally permitted despite their RT characteristics.

To use a simple analogy, the owner of a new software technology can exclude others entirely from access to the software. They can also sell the software, license the software, form a joint

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<sup>95</sup> Robert Bork, ‘Antitrust and the Theory of Concentrated Markets’ (1977) 46 *Antitrust Law Journal* 873, 878.

<sup>96</sup> Frank Easterbrook, ‘On Identifying Exclusionary Conduct’ (1986) 61 *Notre Dame Law Review* 972, 973.

<sup>97</sup> *United States v Aluminum Co. of America et al*, 148 F.2d 416 (2d Cir, 1945).

<sup>98</sup> *Ibid*.



venture to exploit the software or do nothing with the software. Moreover the owner may supply the software to another under an exclusive dealing arrangement, engage in a cost cutting strategy against competitors or tie the sale or license of the software to an ongoing maintenance contract. All of the above examples on their own or as a combination may restrain trade and hence be contrary to RT laws but insofar as they do not restrain competition unreasonably, such arrangements may be permitted under Australian law.

That such legal leeway should exist is not without economic merit. For example, some markets exist due to the increased economies of scale created by RT arrangements. This is particularly true in advanced network environments whereby technology exists to facilitate the exchange of goods or services such as computer operating systems, stock exchanges and credit card facilities.<sup>99</sup> When a single or a few network units are able to dominate the market, they can establish uniform standards of exchange which are followed by all other network players. In this manner, efficiencies are created by users being able to utilise existing systems. Examples of this include Visa and Mastercard credit networks, Microsoft Windows operating system, Apple and Android mobile platforms and Sony's Blu-Ray optical digital storage system.

Where efficiencies are created by RT arrangements, there is also some evidence to suggest that pricing does not always correspondingly increase.<sup>100</sup> In some cases, these RT arrangements may result in a price reduction of goods and services as the savings created from increased efficiencies are passed onto consumers either in full or in part.<sup>101</sup> Correspondingly, when the economies of scale are high in advanced commercial network environments, it is argued by some economists

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<sup>99</sup> See generally, Thomas Piraino, 'A Proposed Antitrust Approach to High Technology Competition' (2002) 44 *William and Mary Law Review* 65.

<sup>100</sup> Lawrence Sullivan, 'Monopolization: Corporate Strategy, the IBM Cases, and the Transformation of the Law' (1982) 60 *Texas Law Review* 587, 616 and Harold Demsetz, 'The Trust Upon Which Antitrust Stands' (1977) 46 *Antitrust Law Journal* 818, 821.

<sup>101</sup> *Ibid.*

that an aggressive and restrictive RT policy may result in higher compliance costs and hence, higher consumer prices.<sup>102</sup>

The potential benefits encapsulated by monopolies are reinforced by the existence of patent systems across the world. In simple terms, a patent is an RT arrangement between a government/s and a patentee.<sup>103</sup> Despite the negative implications asserted by economists regarding the existence of monopolies and RT arrangements, the legal protection granted to patentees upon the successful registration of a patent is evidence of governmental recognition that in some circumstances, the benefits attached to RT arrangements outweigh the economic costs of creating and maintaining these RT arrangements. In the case of patents, governments across the world recognise that incentives backed by law are needed by some businesses to enable them to continuously invest in innovation. Pharmaceutical companies, for example, would have little incentive to spend the considerable resources necessary to innovate and create new ground-breaking medicines if government-backed patent systems were not made available to them. Joseph Schumpeter noted that the potential for superior returns and monopolistic status (at least until the expiry of the patent/s) gives businesses the necessary incentive to develop new products.<sup>104</sup>

Chapter 1 sought to demonstrate that in RT contracting with negligible externalities, the most economically efficient manner is to let parties freely contract so long as the act of contracting does not impinge upon any of the 6 events which will disrupt the model of perfect competition. In situations where RT contracting will result in negative externalities, this chapter addressed how

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<sup>102</sup> Ibid.

<sup>103</sup> David Balto and Andrew Wolman, 'Article: Intellectual Property and Antitrust: General Principles' (2003) 43 *IDEA: The Journal of Law and Technology* 405-09.

<sup>104</sup> Joseph Schumpeter, *Capitalism, Socialism, and Democracy* (Harper Perennial Modern Classics, 3<sup>rd</sup> ed, 1950) 100-06.

economic inefficiency will only occur where the net harm exceeds the net benefits resulting from the RT contract. In these situations, it becomes economically efficient for governments and Courts to intervene to disrupt or eradicate the RT arrangement in order to preserve economic efficiency. Notwithstanding the need to restore economic efficiency, the method and degree of intervention is difficult to measure because intervention without appropriate economic justification may actually result in decreased efficiency. Legislating for RT laws and thereafter providing for their enforcement therefore presents a significant challenge to any government and accordingly history has witnessed a continuing evolution of RT laws in an attempt to address the economic and social challenges of the epoch.

## **CHAPTER 2: COMMON LAW DEFICIENCIES, LEGISLATIVE REMEDIES AND THE USE OF CASCADING CLAUSES**

In February 1969, the Honourable K M McCaw, the then New South Wales Attorney-General commissioned the New South Wales Law Reform Commission ('Commission') to review the common law relating to the validity and enforcement of covenants in RT.<sup>105</sup> A Working Paper was released in the same year and comments were invited from the public.<sup>106</sup> In June 1970, the LRC Report was finalised and tabled at the Office of the Attorney General.<sup>107</sup> No action was taken by the Parliament of New South Wales until September 1976 when the then Attorney-General, the Honourable Frank Walker, introduced the *Restraints of Trade Bill*<sup>108</sup> in the New South Wales Legislative Assembly ('First Reading Speech').<sup>109</sup> In the First Reading Speech, the purpose of the legislation was summarised by reference to paragraph 47 of the LRC Report. It is reproduced below:

We are concerned...to see that, so far as consistent with the public policy against undue restraint of trade, the law should give effect to the reasonable expectations of the parties to a contract rather than let legitimate interests be imperiled by inartificialities of expression.<sup>110</sup>

The Second Reading Speech of the *RTA Bill* ('Second Reading Speech') was read in the same month and the *RTA Bill* received Royal Assent on 15 November 1976 which gave birth to the

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<sup>105</sup> LRC Report, above n 12.

<sup>106</sup> New South Wales Law Reform Commission, 'Covenants in Restraint of Trade' (Working Paper No 4, New South Wales Law Reform Commission, May 1969) ('Working Paper').

<sup>107</sup> LRC Report, above n 12.

<sup>108</sup> *Restraints of Trade Bill 1976* (NSW) ('*RTA Bill*').

<sup>109</sup> New South Wales, *Parliamentary Debates*, Legislative Assembly, 8 September 1976, 735-36 (Frank Walker).

<sup>110</sup> Ibid, quoting LRC Report, above n 12, 47.

existing RTA.<sup>111</sup> The RTA is unique in Australia and should be examined in any proposal for law reform. No other State or Territory in Australia has enacted similar legislation. Chapter 2 will therefore examine the rationale behind the RTA and comparatively review the common law against the New South Wales legislative approach with respect to RT. It will then dissect the history behind cascading clauses and critically analyse the advantages and disadvantages of their use.

## 2.1 THE COMMON LAW ISSUE OF REASONABLENESS BETWEEN THE PARTIES TEST

It was noted in the Working Paper that the subject matter was first brought to notice by judicial comments made regarding the inequitable consequences which have resulted from the inability of the Courts to properly enforce covenants in RT under the common law position.<sup>112</sup> The first of these judicial comments came from the decision in *Mertel v Rigney*.<sup>113</sup> The facts are straightforward. The defendant vendor sold his business to the plaintiff purchaser with a covenant that neither he or his wife will for a period of 5 years, carry on or be employed in a business of a similar nature within a radius of 3 miles. The vendor subsequently, within the 5 year period, entered into a similar business less than half a mile from where the subject business was being carried out. Justice Nicholas found that a radius of 3 miles was unreasonable and beyond the interests of the parties. His Honour said:

I have come to the conclusion, having regard to the nature of the business, to the evidence that was given of the way in which it was carried on, very slight evidence, the figures of population that were put in, and the number of shopping centres within the prescribed area, that this covenant is

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<sup>111</sup> New South Wales, *Parliamentary Debates*, Legislative Assembly, 29 September 1976, 1179-186 (Frank Walker).

<sup>112</sup> Working Paper, above n 106, 1.

<sup>113</sup> (1939) 56 WN 122 (*'Mertel'*).

too wide, and I can only say that any judge coming to such a conclusion on facts such as these does so with great regret because he is allowing a man to recover for himself property for which he has been paid without himself repaying any of the purchase money. That is an act which I have to sanction until the legislature amends the law in this respect, so that a covenant is enforceable to the extent necessary to protect the purchaser.<sup>114</sup>

These comments were later echoed in the decision of Isaacs J in *Papastavrou v Gavan*.<sup>115</sup> In that case, the subject was a hairdressing business sale agreement which carried a restraint of 3 years within a radius of 3 miles. His Honour, in his decision, referred to the decision of Nicholas J in *Mertel* and stated that a radius of 3 miles is effectively a circle with a diameter of 6 miles which covers an area of 28 square miles. He further noted that very few businesses in a business sale agreement would warrant the protection of a 3 mile geographic RT.<sup>116</sup>

These above examples reflect a curious result of the evolving common law where a judge, when requested by a plaintiff to enforce an RT covenant, must dismiss such a request if the covenant is deemed too wide and accordingly unreasonable and unenforceable. The unedifying consequence of this is a vendor who provides an RT covenant that is too wide and accordingly unreasonable and unenforceable, can establish a competing business next to the business that it sold at any time and thus, steal back the custom or goodwill which it has purported to sell to the purchaser without any form of compensation to the purchaser. Such a possibility offends public policy whereby a person receives consideration pursuant to a contract and the value of that contract is wholly or partly dependent on an RT clause which is subsequently held to be unenforceable, that the consideration should then be allowed to be retained by the party benefiting from the

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<sup>114</sup> Ibid 123.

<sup>115</sup> (1968) 2 NSW 286 ('*Papastavrou*').

<sup>116</sup> Ibid 288, see also, *Commercial Plastic Ltd v Vincent* [1965] 1 QB 623; *SW Strange Ltd v Mann* [1965] 1 WLR 629, 642; *Lyne-Pirkis v Jones* [1969] 1 WIR 1293, 1299.

unenforceable RT. This punishment, if it may be stated as such, contradicts the basic principles of equity and, disappointingly, the failure of the common law to correct such an inequity presents a continued reflection of bad law. This system in short, sits diametrically opposed to the doctrine of unjust enrichment;<sup>117</sup> not only can it cheat a person in the non-enforcement of contractual promises, it also adds salt to the wound by allowing the escaping party to retain the consideration provided for an unenforceable RT.

This problem extends to numerous other RT scenarios including but not limited to exclusive licensing contracts, sale of technology contracts, sole distribution agreements, supply agreements, partnership agreements etc. The long tentacles of the Doctrine may be underestimated by many and the example below is a case in point. A garage is in financial distress and is in need of a loan. An oil company wishes to expand its customer reach by appointing additional garages to sell its fuel. The two parties negotiate and a loan agreement coupled with the relevant security and interest payments are agreed to. Key to the deal for the oil company is the exclusive sale of its fuel by the garage. Given that the loan repayment period was 21 years, it would seem to make commercial sense that any sales exclusivity would also extend to 21 years. This deal would ensure the survival of the garage and the expansion of the oil company's customer base. To an outsider, this appears to be a win-win arrangement. It is plausible to suggest that if the sales exclusivity was not a part of the agreement, the oil company will have minimal benefit to gain from the contract.

These facts are a recital of the background leading up to the *Esso* case. Given that the Court determined in *Esso* that 5 years was a reasonable restraint, it would have been highly unlikely for

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<sup>117</sup> See generally, *Pavey & Matthews v Paul* [1987] 162 CLR 221 in which the High Court of Australia acknowledged that unjust enrichment encompassed an obligation of restitution based on *quantum meruit* on the part of a defendant to make fair and just restitution for a benefit derived at the expense of a plaintiff.

*Esso* to assist a similar garage in financial distress post the *Esso* decision unless the benefits of exclusivity are justifiable in a 5 year time frame. Whilst this decision is isolated to the evidence presented within the case and does not reflect an attempt to establish any particular standard for the test of reasonableness (other than within the circumstances presented in *Esso*), it is useful to illustrate that in this example, if the 5 year period was an insufficient incentive for the oil company, the garage may fall into further financial distress and eventually go into liquidation. Such closure would be detrimental to the community being serviced by that garage as the supply of fuel is diminished in that local community and competition amongst garages decrease. The gravity of harm will be exponentially more if the garage is located in a rural area and is the only garage in the local community. In determining the issue of reasonableness therefore, the *Esso* case provides an example of the RT anomaly: the decision to categorically state that 5 years is an appropriate RT period and that 21 years is inappropriate despite the geographic restraint being limited to the single garage represents nothing but a counterproductive situation which may very well carry negative social and economic consequences for the local community.

Similarly, in the decisions of *Mertel* and *Papastavrou*, the issue before the Court was that of a geographic restraint. On the facts presented, the Court assessed that a reasonable restraint would have been less than 3 miles from the place of business in both cases. Meltz observed that Australian cases of RT have appeared to disregard the parties' opinions at the time of contracting and instead have looked for an objective connection between the area of operation and goodwill.<sup>118</sup> By eliminating or at the very least diminishing the value of opinions from consenting contracting parties, the Courts inevitably force parties to consider, at the time they

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<sup>118</sup> See generally, Meltz, above n 9, 121-35.



enter into the contract, the issue of what is reasonable from an objective perspective when contracting in RT.<sup>119</sup>

In *Mertel* for example, the Court regarded as relevant facts, the nature of the business, the population size and the number of shopping centres within the geographical restraint area.<sup>120</sup> In consideration of those facts, the Court held that a 3 mile radius was too wide a restraint. Fortunately for the Court, the matters in *Mertel* were straightforward and based on simple facts. It was also an easily identifiable subject matter capable of being restrained, i.e. the business. This poses the question of how a Court would decide if the facts were more complex. What if the facts involved future events and business planning decisions, which despite not having eventuated at the time of contracting, were key contributing factors for a purchaser or licensee to enter into a contract? Moreover, what if the subject matter of the contract was intellectual property, for example, an intangible property capable of deployment across the globe unrestrained by physical limitations (i.e. information, formulae, technological devices and certain patentable inventions)? Suppose that a licensor company contracted to licence the intellectual property subject to an RT proviso that, during the period of the licence and within the restrained territory, the licensor must not grant another licence to a third party without the licensee's consent. Suppose further that the intellectual property is novel and untested but bears great commercial potential and the licensee is interested in developing and selling this intellectual property across Australia, United States and United Kingdom. The licensor on the other hand, would not have sufficient resources to develop the intellectual property without the assistance of the licensee. On the request of the licensee, the parties agree to a 20 year exclusive licensing arrangement within the countries of Australia, United States and United Kingdom which incorporates an RT proviso giving effect to a restraint

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<sup>119</sup> Ibid.

<sup>120</sup> *Mertel* (1939) 56 WN 123.

upon the licensor from further licensing the intellectual property within a 20 year period in those specified countries.

In such an example, according to the *ratio decidendi* established in *Esson*, it would seemingly be unreasonable to restrain any party to a 20 year restraint period across a geographic region that covers a restraint area not measured by how many kilometers or miles but by how many countries. Such a combination of restraints would appear to be so wide as to render the restraint unreasonable from any perceivable angle of the existing common law. Nevertheless, if one dispenses with this analysis and perceives the issue through a commercial prism, one will quickly appreciate the practical necessity for the licensee to obtain such a restraint term because, only by means of the restraint, will the licensee benefit sufficiently to render the contract worthwhile.

Finally, where a restraint is predicated upon future events and matters that have not yet eventuated, the Court is placed in yet another difficult position of deciding how much weight to place on the likelihood of those events coming to pass. For example, if at the time of the dispute arising, the licensee had only developed and sold the intellectual property in Australia and not the United States or the United Kingdom, should the Court determine that the reasonableness of the geographic restraint lies within only the borders of Australia? Relevant to this matter is also the question of how much weight should be placed on the passage of time. By way of a further example, if the licensee had not commercialised the intellectual property after 5 years out of a 20 year RT term, what weight should be placed on this knowledge when determining the issue of reasonableness? What if 10 years or 15 years had lapsed out of the 20 year RT term instead? Furthermore, what weight should be placed on the stages of development and commercialisation? If the intellectual property was only developed and commercialised in Australia after 5 or 10 or 15 years, should a Court hold at a certain point in time that further restraint regarding licensing within the United States and United Kingdom would objectively offend against the concept of

reasonableness? Should the test depend on the relative success of the development and commercialisation measured partly against the amount of time it has taken to capture a certain market share?

These questions may become increasingly relevant and are indicative of the questions that Courts currently face and will increasingly face in light of the growing uncertainties involved when contracting in RT, particularly in the context of advancements in commerce and the globalisation of trade. It would not be unreasonable to conclude that what is reasonable between the parties is a complex question which cannot be determined with an acceptable level of clarity in the common law system today especially when such an assessment is based on an objective test. An overriding question arises from this dilemma as reflected on by the Honorable Tim Moore, Member for Gordon in the Second Reading Speech of the Act: 'I question whether the Supreme Court is the appropriate tribunal to deal with the matter...'<sup>121</sup> He then cited the remarks of Lord Bramwell in the case of *Manchester, Sheffield & Lincolnshire Railway v Brown*.<sup>122</sup> His Lordship said:

It seems to me perfectly idle, and I cannot understand how it could have been supposed necessary, that is should be referred to a judge to say whether an agreement between carriers, of whose business he knows nothing, and fishmongers, of whose business he equally knows nothing, is reasonable or not.<sup>123</sup>

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<sup>121</sup> New South Wales, *Parliamentary Debates*, Legislative Assembly, 29 September 1976, 1184 (Tim Moore).

<sup>122</sup> (1882-83) LR 8 App Cas 703.

<sup>123</sup> Ibid.

The commentary by Lord Bramwell in 1883 is remarkably insightful in its day and continues to hold true, if not with increased emphasis given the discussions above.<sup>124</sup> It succinctly summarises a persuasive argument that a judge, when required to obtain a proper understanding of what should be considered reasonable and in the interest of the parties, is commonly placed in a difficult situation due to the increasing complexity involved in reviewing the possibilities in each and every RT. The example in *Pyle v Sharpe Bros. Pty Ltd*<sup>125</sup> is a case in point. In *Pyle*, the New South Wales Court of Appeal considered the reasonableness of an RT covenant. Walsh J observed that reconciling the historical authorities on the issue of reasonableness was difficult.<sup>126</sup> Most notably, his Honour commented that, in the case before him, it was feasible that different judges may very well reach different conclusions on the issue of reasonableness.<sup>127</sup> This comment begs the obvious question: if the Courts cannot determine the issue of reasonableness with an acceptable level of certainty and consistency and past cases do little to shed light on the issues faced by contracting parties, how does the legislature or judiciary expect the business community to contract with an acceptable level of certainty?

## 2.2 THE COMMON LAW ISSUE OF THE PUBLIC INTEREST TEST

The public interest test, as introduced in Chapter 1 is considered by the common law as subordinate to the test of reasonableness between the parties.<sup>128</sup> It is a generally accepted view amongst legal academics and practitioners of the law that, from a historical perspective, judges

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<sup>124</sup> See generally on the subject of whether judges are best placed to make decisions about complex business dealings, John Wade 'Judicial Decision-Making in Australia: Critique and Redemption' (2009) 15 *The National Legal Eagle*; Roman Tomasic and Brendan Pentony 'Judicial Technique in Takeover Litigation in Australia (1989) 12 *University of New South Wales Law Journal*; Margaret Davies, *Asking the Law Question: The Dissolution of Legal Theory* (Lawbook Co, 2002); See historically, Roscoe Pound 'Mechanical Jurisprudence' (1908) 8 *Columbia Law Review* 605.

<sup>125</sup> [1968] 2 NSW 511 ('*Pyle*').

<sup>126</sup> *Ibid* 513.

<sup>127</sup> *Ibid* 514.

<sup>128</sup> Heydon, above n 1, 184-87, 272-78.

have taken a cautious view when considering the effect of the public interest test with respect to RT cases.<sup>129</sup> Parke B, noted for his influence on future generations of the judiciary, observed some 150 years ago that ‘we are not authorised to establish as law everything we may think for the public good, and to prohibit everything which we think otherwise.’<sup>130</sup>

Heydon J of the High Court of Australia commented that in practice, most restraints held to be reasonable between the parties are not harmful to the public interest and the burden of establishing the issue of public interest will ordinarily lie with the party claiming the existence of the public interest concern.<sup>131</sup> It was further noted that issues arising in considering the public interest test can be manifestly difficult to adjudicate and are so different from those usually determined by judges thereby justifying their treatment of caution in the Courtroom.<sup>132</sup>

The prospect of defining the issue of the public interest should accordingly never be narrow and closely defined. Ungood-Tomas J in *Texaco Ltd v Mulberry Filling Station Ltd*<sup>133</sup> warned specifically that the public interest should refer to ‘interests as recognisable and recognised by law.’<sup>134</sup>

Traditionally, the legitimate body to determine issues relating to the public interest should be none other than the legislature because the body of the legislature is resourced and qualified to consider social and economic data and empowered to make decisions in the interests of advancing the social and economic good of society. The vast public resources which are available to

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<sup>129</sup> See generally, *Richardson v Mellish* [1824-34] All ER Rep 258 (‘Richardson’); *Hilton v Eckersley* (1855) 6 E&B 47 (‘Hilton’); *Egerton v Earl of Brownlow* (1853) 4 HL Cas 1 (‘Egerton’); *Hibblewhite v M’Morine* (1839) 5 M&W 462 (‘Hibblewhite’); *Re Mirams* [1891-94] All ER Rep 370 (‘Mirams’).

<sup>130</sup> *Fender v St John Mildmay* [1938] AC 1, 23 (‘Fender’).

<sup>131</sup> Heydon, above n 1, 36.

<sup>132</sup> See generally, *Richardson* [1824-34] All ER Rep 258; *Hilton* (1855) 6 E&B 47; *Egerton* (1853) 4 HL Cas 1; *Hibblewhite* (1839) 5 M&W 462; *Mirams* [1891-94] All ER Rep 370.

<sup>133</sup> [1972] 1 WLR 814.

<sup>134</sup> *Ibid* 526-27.

Parliament in the process of law-making in comparison to the generally more limited private resources of litigants also marks a fundamental difference. The determination of issues relating to the public interest will frequently require significant time and resources involving extensive consultation with the public, academia, related industries and interest groups. Experts will be commonly engaged, statistics gathered and subcommittees formed. Most importantly, the angle of approach from the legislature is crucially different to that of the judiciary. Whilst the legislature is or at least, should be concerned with the making of laws for the advancement of society, the judiciary's role is primarily that of dispute resolution, protection of legal rights and the interpretation of laws. Such a forum, with respect to the judiciary, is not the most appropriate forum to determine issues of the public interest. Best CJ perhaps summarised this view most succinctly, 'let that doubtful question of policy be settled by that high tribunal namely, the legislature, which has the means of bringing before it all the considerations that bear on the question.'<sup>135</sup>

The cautionary approach to public policy is necessary because an ill-defined set of public policies will only prompt additional uncertainty in the already confused RT contracting world. Burrough J noted that the issue of public interest is similar to that of an unruly horse – 'when once you get astride it, you never know where it will carry you. It may lead you from sound law.'<sup>136</sup> Lord Campbell CJ also pointed out over 150 years ago that his reluctance to consider the issue of public policy arose 'when I think how different generations of judges, and different judges of the same generation, have differed in opinion upon questions of (the) political economy.'<sup>137</sup> Moreover, Alderson B noted that 'an active imagination may find a bad tendency arising out of

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<sup>135</sup> *Richardson* [1824-34] All ER Rep 258, 262.

<sup>136</sup> *Ibid* 266.

<sup>137</sup> *Hilton* (1855) 6 E&B 47.

every transaction between imperfect mortals; and to use this as a criterion for determination would make every case depend on the arbitrary caprice of an acute judge.’<sup>138</sup>

Whilst it has been demonstrated that the issue of the public interest cannot be easily and succinctly defined, it is key to note that at the very foundation of the law of contracts is the maintenance of contractual promises. It would therefore be a perversion of the law to invoke the issue of public interest to invalidate contracts without good cause. To do so is to create a dangerous precedent as it is fundamental to a functioning and efficient society to maintain the public faith in the enforceability of contractual promises. On this subject, Sir George Jessel MR commented as follows:

...if there is one thing which more than another public policy requires, it is that men of full age and competent understanding shall have the utmost liberty of contracting, and that their contracts when entered into freely and voluntarily shall be held sacred and shall be enforced by Courts of Justice.<sup>139</sup>

Holmes J also stated, ‘the most enlightened judicial policy is to let people manage their own business in their own way, unless the ground for interference is very clear.’<sup>140</sup> Such grounds and causes for interference will typically arise with respect to the matters of Recognised Contractual Wrongs. In light of the above, the usefulness of this secondary test of public interest must be questioned. Why, if given the unchanging historical and current approach to the issue of the public interest over the centuries, should this secondary test remain as a possible means to invalidate an RT if an RT is found to have passed the test of reasonableness? Do the existing

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<sup>138</sup> *Egerton* (1853) 4 HL Cas 1, 109.

<sup>139</sup> *Printing and Numerical Registering Co v Sampson* (1875) LR 19 Eq 462, 465.

<sup>140</sup> *Dr Miles Medical Co v John D Park & Sons Co*. 220 US 373, 411 (1911).

laws whether through common law or statute not recognise and address Recognised Contractual Wrongs? The answer to this rhetorical question is, of course, that the existing laws through various common law and statutory mechanisms do already provide extensive protection and coverage against such concerns.<sup>141</sup>

This does not equate to the author suggesting that the existing solutions provide a perfectly acceptable mechanism. However, the argument can be put that if the existing laws fail to sufficiently protect relevant parties, it may be those laws whether in the form of common law or statute, which should be reviewed.

To present a balanced view of the issues, it must be said that the author's perspective on the role of the public interest test is not shared unequivocally. It would be an incomplete analysis without recognising and addressing another explanation for the continued existence of the public interest test. To summarise this view, some believe that Courts have an increasingly important role to concern themselves with issues of the public interest and consequently the mandate of judicial intervention is given to Courts to enable them, in limited circumstances to accept evidence sufficient to invalidate RT clauses in the name of the public interest.<sup>142</sup> This explanation is widely expressed to duly cover all avenues of enquiry which a Court may deem relevant in its investigation of what is in the public interest.

The author disagrees with this view for the reasons outlined below. As noted previously, it is difficult to refute the argument that Courts are an inappropriate forum to consider issues of public interest. Moreover, unlike an inquisitorial judicial system such as the system established in the German judiciary, judges in Australia's common law system lack the resources, experience,

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<sup>141</sup> The author will provide an in-depth discussion in Chapter 4.1 of this paper.

<sup>142</sup> Heydon, above n 1, 276.



professional training and active inquisitorial and investigative power to order and request assistance either from the litigious parties or via independent means throughout the process of decision making.<sup>143</sup> Thus the rationale of leaving matters of public interest to Parliament is well founded and generally accepted. However, Roche J stated that the problem is sometimes that Parliament, from time to time, lacks the willingness or time to intervene when an issue of the public interest arises.<sup>144</sup> This may be particularly the case if the necessary action is not politically advantageous and will unlikely attract more votes or coverage on the evening news.

A prime example is the time taken by Parliament to action the LRC Report by introducing the *RTA Bill* in the New South Wales Parliament 6 years after the LRC Report was tabled. It should be further noted that despite the recommendations of the LRC Report, no other State or Territory has debated or enacted similar legislation or commissioned an investigation into RT contracting and the same may be said of the Government at the federal level. It may therefore be a valid argument to suggest that, if Parliament cannot or does not act where such action is clearly in the interests of the public, the Court ought to step in and not decline to act on the ground that it is not perfectly equipped to act. According to Heydon J, the Court, as a judicial body, ‘must do the best it can’.<sup>145</sup> In line with this argument, it was further suggested that judges often have to consider issues of public policy when directed to do so by statute.<sup>146</sup> It was also suggested that judges have frequently held other administrative or political posts prior to their judicial post and may possess, at a basic level, the skills and experience to consider issues of public policy.<sup>147</sup>

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<sup>143</sup> See generally, Mary Glendon, Paolo Carozza and Colin Picker, *Comparative Legal Traditions* (West Academic Publishing, 3<sup>rd</sup> ed, 2008).

<sup>144</sup> *Fender* [1938] AC 1.

<sup>145</sup> Heydon, above n 1, 276, quoting *Egerton* (1853) 4 HL Cas 1, 151 (Pollock CB).

<sup>146</sup> Heydon, above n 1, 276.

<sup>147</sup> *Ibid*.

By the same token, there is an acknowledgement by Heydon J that historically, where the Courts have discarded the cautionary approach and entertained arguments of public policy, they have done so in a salutary manner.<sup>148</sup> For example, in *Esso*, the House of Lords was only able to discuss the issue of public interest because a report by the Monopolies Commission had been published earlier on the subject matter of the restraint.<sup>149</sup> To this, the author adds that the Court, if called upon to entertain material submitted on the question of public policy, may create a dangerous process whereby it may rely on incomplete and skewed information drawn for the purpose of litigation to make decisions regarding the public interest. In addition, the rules of evidence will generally render inadmissible, extrinsic evidence which may otherwise be reviewed and utilised in the legislative process.<sup>150</sup>

Lastly, the author notes that where evidence is drawn upon to argue the issue of the public interest, the complexity of litigation, length and cost will also substantially increase for both the Courts and the litigating parties. This is predictable as the burden of proof is substantial to justify a Court's decision to invalidate a restraint where the restraint is considered to be reasonable and in the interests of the parties. On this issue, Frankfurter J stated from a United States perspective with regards to cases on the validity of RT contracts in the petrol industry:

...to demand...evidence as to what would have happened but for the adoption of the practice that was in fact adopted or to require firm prediction of an increase of competition as a probable result of abandoning the practice, would be a standard of proof if not virtually impossible to meet, at least ill-suited for ascertainment by Courts...judges (are) unequipped for (the task) either by experience or by the availability of skilled assistance.<sup>151</sup>

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<sup>148</sup> Ibid.

<sup>149</sup> Ibid.

<sup>150</sup> See generally, Heydon, above n 1, 276-78.

<sup>151</sup> *Standard Oil Co of California v US* 337 US 293, 309-10 (1948).

Despite the numerous issues raised by the author with respect to the test of the public interest, it is interesting to note that the Working Paper, LRC Report, First Reading, Second Reading and Explanatory Memorandum of the *RTA* all displayed no interest in the issues surrounding the public interest test. It appears that the parliamentary focus was wholly on the issue of reasonableness between the parties. This may be the result of the vector of law reform established by the Courts in the decisions of *Mertel* and *Papastavrou*. Given that the issue of the public interest has always remained out of the limelight, it has, since the time of *Nordenfelt*, limped along the RT scene with minimal objective criticism from either the Courts or other interested parties as to its continuing role. The investigation into the test of reasonableness between the parties was therefore sufficiently concerning on its own for the Commission to take issue with it in its LRC Report and hence the test of reasonableness became the focus of the Commission and the Parliament of New South Wales at the time of the enactment of the *RTA*.

### *2.3 RESTRAINT OF TRADE ACT 1976 (NSW)*

The *RTA* was passed in 1976 with little opposition from the shadow government of the day. Parliamentary debate with respect to the *RTA* was generally limited to questions regarding its operation and administrative concerns. The Deputy Leader of the Opposition in the Second Reading Speech stated the following in support of the *RTA Bill*:

The Opposition supports this measure basically for the reasons outlined by the Attorney General. Certainly what is proposed here brings great satisfaction to the commercial community involved often in contracts dealing with covenants in restraint of trade...Honourable members of this side of

the House agree that it is high time the matter was determined by legislation and that the public interest would be better served by this measure than has been the case without it.<sup>152</sup>

This following section will discuss the operative parts of the *RTA* and critically assess its merits. It is well recognised at the time the *RTA* was passed that the *RTA* is a product of law reform designed to combat the clear deficiencies of the common law as they were then perceived.<sup>153</sup> Since the *RTA*'s passage and with the flow of time over the past 30 years, one can, with the benefit of hindsight, comment on and critique its robustness with respect to today's commercial and social needs.

Section 4(1) of the *RTA* provides, 'A restraint of trade is valid to the extent to which it is not against public policy, whether it is in severable terms or not'.<sup>154</sup> Public policy is defined as 'public policy in respect of restraint of trade'.<sup>155</sup> By defining public policy in this manner, Parliament was able to avoid the provision of a strict definition, effectively avoiding the very question which the Court sought to place on the shoulders of the legislature. The term 'Restraint of Trade' is defined as meaning a 'restraint of trade created by contract, created by the rule of an association, or otherwise created'.<sup>156</sup> 'Association' includes a corporation.<sup>157</sup> 'Rules' includes a corporation's memorandum and articles of association and provisions of the constitution with reference to unincorporated associations.<sup>158</sup>

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<sup>152</sup> New South Wales, *Parliamentary Debates*, Legislative Assembly, 29 September 1976, 1182 (John Maddison).

<sup>153</sup> New South Wales, *Parliamentary Debates*, Legislative Assembly, 29 September 1976, 1179 (Frank Walker).

<sup>154</sup> *RTA* s 4(1).

<sup>155</sup> *Ibid* s 2(1).

<sup>156</sup> *Ibid* s 2(2).

<sup>157</sup> *Ibid* s 2(1).

<sup>158</sup> *Ibid*.

Section 4(2) provides that s 4(1) does not affect the invalidity of a RT by reason of any matter other than public policy.<sup>159</sup> The *RTA* therefore applies to validate a contract where the restraint is unreasonable insofar as it alters the rules of severance but does not step so far as to validate restraints which are against public policy or any other ground of invalidity, such as illegality or uncertainty.

Importantly and key to the operation of the *RTA* is s 4(3) which provides as follows:

Where, on application by a person subject to the restraint, it appears to the Supreme Court that a restraint of trade is, as regards its application to the applicant, against public policy to any extent by reason of, or partly by reason of, a manifest failure by a person who created or joined in creating the restraint to attempt to make the restraint a reasonable restraint, the Court, having regard to the circumstances in which the restraint was created, may, on such terms as the Court thinks fit, order that the restraint be, as regards its application to the applicant, altogether invalid or valid to such extent only (not exceeding the extent to which the restraint is not against public policy) as the Court thinks fit and any such order shall, notwithstanding subsection (1), have effect on and from such date (not being a date earlier than the date on which the order was made) as is specified in the order.<sup>160</sup>

The rationale behind s 4(3) is an echo of the LRC Report whereby the Commission's view was that a promise in RT must reflect at a minimum, a real attempt by the parties to provide a restraint which was reasonable as between the promisor and the promisee.<sup>161</sup> It was further commented on by the Commission that unless such an attempt is evident, the promise will fail to provide sufficient guidance to the Court to adjudicate the reasonableness of the restraint upon which the

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<sup>159</sup> Ibid s 4(2).

<sup>160</sup> Ibid s 4(3).

<sup>161</sup> LRC Report, above n 12, 44.

parties agreed.<sup>162</sup> However, this was not to be a hard and fast rule and the Commission noted that the above proposition was not intended to be wide or common in its operation. In the LRC Report, the following additional comments were made:

We do not consider that a flagrant violation of public policy should necessarily disentitle the promisee to any relief. The gravity of the harm which the promisee would suffer by a refusal of relief may be out of proportion to the gravity of the violation of public policy. Again, although the promisee has violated public policy, the promisor may be behaving outrageously. Consider these supposed facts. The promisor sells his business to the promisee. The promisor willingly gives a promise in restraint of trade which manifestly is absurdly wide. He does so knowing that the promise cannot be enforced according to its terms. Forthwith after completion of the sale the promisor opens a rival business next door and solicits his old customers. Should he not be restrained, even though the promise was not a real attempt to provide a restraint which was reasonable as between the promisor and the promisee?<sup>163</sup>

The Committee's answer to this question is that the Court should be empowered to refuse or restrict relief, regardless of the intention or lack of intention of the contracting parties.<sup>164</sup> It further commented that a case in which relief is refused will be exceptional but the power to refuse or restrict relief should be given to the Court regardless.<sup>165</sup> This recommendation was not entirely adopted by Parliament. Section 4(3) for example, only provides for an order of invalidity or limited validity. The Commission however, recommended that the Court be given the power to refuse relief or grant only limited relief.<sup>166</sup> It was felt by Parliament that the Commission's rationale should be applied but in a modified form to encourage a promisee to apply his mind to

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<sup>162</sup> Ibid.

<sup>163</sup> Ibid.

<sup>164</sup> Ibid.

<sup>165</sup> Ibid.

<sup>166</sup> Ibid.

what would be a reasonable restraint when contracting in RT.<sup>167</sup> Notably, the term ‘manifest failure’ was also inserted which was considered to be a condition precedent to the grant of relief pursuant to s 4(3).

If one were to comment that the *RTA* is convoluted and difficult to apply, it would not be far from the truth. For some time after the enactment of the *RTA*, Courts struggled with the application of the *RTA* and different interpretations and methods of application were canvassed.<sup>168</sup> In the 1980s, the correct approach to the application of s 4 was settled and continues to be accepted today as the appropriate application of the *RTA*.<sup>169</sup> The methodology is enumerated below:

1. The Court determines whether the alleged breach infringes the terms of the restraint;
2. If there is an infringement, the Court determines whether the restraint is against public policy. If the restraint is not against public policy, the restraint will be valid, subject to any s 4(3) order detailing the extent of the invalidity; and
3. If there is no infringement, the *RTA* will have no function.<sup>170</sup>

Where the extent of the invalidity is required to be determined subject to s 4(3) of the *RTA*, the decision of McLelland J in *Orton*<sup>171</sup> is the accepted test. The relevant part of that decision is repeated as follows:

Whether, and if so the extent to which, the Court will have to define the outer limits of validity of a restraint in a particular case, will depend upon the nature, and degree of generality, of the relief which in that case it is necessary or proper for the Court to grant. For example, where injunctive

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<sup>167</sup> *RTA* s 4(3).

<sup>168</sup> *Davis v Wood* [1979] ATPR ¶40-117; *Magna Alloys & Research Pty Ltd v Bradshaw* (1977) 3 TPC 71.

<sup>169</sup> *Orton v Melman* [1981] 1 NSWLR 583 (‘*Orton*’).

<sup>170</sup> *Ibid.*

<sup>171</sup> *Ibid.*

relief is granted, the duration of a valid restraint of any breach enjoined will have to be determined. In applying s 4(1) the Court should consider the circumstances of the particular case before it and determine the validity of the restraint to the extent that it purports to operate in those circumstances and it is unnecessary to consider its purported operation in other conceivable sets of circumstances. Other considerations may of course arise in an application under subsection (3) or s 4. In my opinion the enactment of s 4(1) has succeeded in requiring attention to be concentrated on 'the actual breach' rather than 'imaginary breaches' for the purpose of determining validity of a restraint.<sup>172</sup>

The significance of considering 'the actual breach' rather than the 'imaginary breach' is, of course, a comment with respect to the doctrine of severance and its peculiar application in common law. Criticism is centered on the fact that the doctrine of severance focuses on imaginary breaches and not actual breaches when applied in RT cases. By way of an example, assume that a vendor sells a pharmacy located in Ballarat to a purchaser. The vendor covenants not to establish a pharmacy within a 5 kilometre radius of the pharmacy he sold. The vendor subsequently establishes a pharmacy within 3 kilometres from the pharmacy. Instead of assessing whether the location of the vendor's new pharmacy will legitimately harm the interests of the purchaser (which is the approach dictated by the *RTA*), under common law the Court would instead determine the question of reasonableness without reference to the actual location of the vendor's new pharmacy. Rather, the Doctrine takes into account the entirety of the 5 kilometre radius and 'imagines' whether a vendor pharmacy located anywhere within that 5 kilometre radius will harm the legitimate interests of the purchaser. If the RT was expressed as a combination of several distinct restraints, the Court will determine (under the Doctrine) if the RT may be brought into the realm of reasonableness by deleting (otherwise known as blue penciling) the offending combination of restraints under the doctrine of severance without altering the nature

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<sup>172</sup> Ibid 587-88.



of the original agreement. If this cannot be successfully done (i.e. the RT is not expressed as a combination of restraints but rather, a single covenant and hence cannot be severed or where blue penciling the offending parts results in a fundamental alteration to the scope and intention of the contract), the vendor is legitimately able to operate the new pharmacy in direct competition with the purchaser.

This loophole is further capable of exploitation where the purchaser has mistakenly rather than maliciously drawn a covenant too wide to be considered reasonable. This is especially the case where lay persons draw up a covenant that is too wide. In the case of *Commercial Plastics Ltd v Vincent*,<sup>173</sup> the Court of Appeal said, 'it is unfortunate that a home-made provision, offered and accepted in good faith between commercial men and not in the least intended to be oppressive, has to be ruled out and declared void in a Court of Law for lack of the necessary limiting words.'<sup>174</sup> Differences in drafting technique to encapsulate the same restraint through the use of various forms of 'limiting words' can be shown by the following example.

Suppose a business only has goodwill in the States of Victoria, New South Wales and Queensland. Assume it is sold. An RT protecting the purchaser may be drawn up as follows. The first is an RT whereby the vendor agrees not to compete in the States and Territories of Tasmania, Victoria, Australian Capital Territory, New South Wales, Queensland, South Australia, Northern Territory and Western Australia. The second is an RT which is expressed simply as the whole of Australia. In both instances, the restraint is expressed to cover largely the same geographic regions. The promises are both unenforceable but the blue pencil rule may allow the first covenant to be partly enforceable as the unreasonable parts of the restraint may be severed by

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<sup>173</sup> [1965] 1 QB 623.

<sup>174</sup> Ibid 647.

the blue pencil rule. Given that 'Australia' cannot be crossed out, the second restraint is unenforceable and unfortunately, must be severed entirely under the Doctrine.

The clarity brought by the *RTA* with respect to area restraints unfortunately is not repeated where the issue of reasonableness lies in duration. In assessing cases of restraint by time, it is not possible to pick a single 'actual breach': the Court selects the maximum lawful period by practice. It therefore follows that an unreasonable restraint validated by the operation of the *RTA* must fall within conduct restrained by the covenant as actually drafted. According to Giles J in *Douglass Automated Laboratories & Allied Services Pty Ltd v Sonic Technology Australia Ltd*,<sup>175</sup> s 4(1) 'does not call for a re-writing of the restraints in the abstract...but looks to the postulated breach'.<sup>176</sup> Section 4(3) on the other hand, 'provide(s) a means by which the Court may be asked, in effect, to re-write restraints so as to overcome public policy invalidity.'<sup>177</sup> The relationship between s 4(1) and s 4(3) is a question of construction and whilst the two may appear to contradict each other, Giles J further commented on this as follows in the case of *Industrial Rollformers Pty Ltd v Ingersoll-Rand (Australia) Ltd*:<sup>178</sup>

(Section) 4(3) is in a sense complementary to s 4(1). Section 4(1) enables limited enforcement of the restraint to the extent to which it applies to the particular breach, on the application of the promisee and looking to the past and present...Section 4(3) enables a reading down of the restraint in the abstract, on the application of the promisor...The complementary operations of s 4(1) and s 4(3) are, however not complete. Because the promisee's application focuses on the particular breach, invocation of s 4(1) does not define the extent of validity and enforceability of the restraint – it may have validity wider than that necessary for enforcement in the face of the particular

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<sup>175</sup> [1994] NSWSC BC9402640 (8 June 1994) 68.

<sup>176</sup> *Ibid.*

<sup>177</sup> *Ibid.*

<sup>178</sup> [2001] Aust Contract Rep ¶90-129.

breach. Because the promisor's application requires a finding of manifest failure, a promisor may be able to resist the promisee's proceedings to enforce the restraint in the face of his breach on the ground that the restraint would to that extent be against public policy, even though the promisor could not successfully invoke s 4(3) to have the restraint found invalid or read down. There are other problems. It may be some time before the operation of s 4(3) of the Act is settled.<sup>179</sup>

In more recent times, a further and rather curious flaw in the *RTA* was discussed in the matter of *Spooner v Commonwealth Broadcasting Corporation*.<sup>180</sup> In *Spooner*, the plaintiff had entered into a contract with the defendant which provided for a post-employment RT as follows:

1. For 6 months after the plaintiff ceased working for the defendant, he would be restrained from contacting, personally or otherwise, or procuring or seeking to procure business from any person who is, or was in the last 6 months of the plaintiff's employment, a client of the employer; and
2. For 3 months after the plaintiff ceased working for the defendant, unless with the consent of the General Manager of the employer or Chief Executive Officer of the Australian Radio Network group of companies, he would be restrained from providing 'any services' (whether directly, indirectly or through any third party) to any operator or licensee of any commercial FM radio station [in Sydney], which are the same or similar to the services provided by [the plaintiff] to the employer.<sup>181</sup>

After receiving an offer of employment from a competitor to the defendant, the plaintiff tendered his resignation. He then proceeded to seek advice from the defendant regarding whether it would enforce the RT clause. The defendant responded by stating that it would seek to enforce the

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<sup>179</sup> Ibid ¶¶91-580.

<sup>180</sup> [2009] NSWSC 6063/08 (*'Spooner'*).

<sup>181</sup> Ibid.

restraint and that it would not pay any consideration for the restraint. By reason of the defendant's response, the plaintiff and his prospective employer postponed the plaintiff's employment until the restraint had expired.

The plaintiff subsequently issued proceedings for damages on the basis that the restraint clause imparted an unreasonable restraint and that s 4(5) of the *RTA* offered the prospect of compensation for losses sustained. Unfortunately for the plaintiff, the trial judge dismissed the matter pursuant to a Notice of Motion brought by the defendant on the grounds that s 4(3) of the *RTA* restrained the plaintiff from bringing a tenable cause of action. The trial judge ruled that s 4(3) of the *RTA* operated on the basis that the quantum of damages is assessed prospectively from the date of judgment and if the plaintiff fails to conclude the litigation prior to the expiration of the RT period, he or she will be deprived of any remedy which might otherwise be available whether the restraint was reasonable or not.

Since *Spooner*, it is now clear that in New South Wales, the time to challenge or negotiate the terms of a restraint is at the time of entry into the contract. This can of course, be unrealistic and difficult when business people get together to talk about potential contracts. Notwithstanding this difficulty, *Spooner* shows that once the period of potential redress has lapsed, s 4(3) of the *RTA* operates entirely prospectively so that an action cannot be instituted, nor maintained nor any damages awarded, irrespective of the reasonableness of the restraint. This has the effect of being contrary to the principle of law that a party ought not to have an interest in delaying proceedings such that the result of an entirely prospective nature of assessment as to damages is that RT clauses must also balance the likelihood of a challenge to the restraint against the time that it will take a Court to hand down its judgment. The operation of s 4(3) therefore results in a curious position whereby an unreasonable restraint, even if successfully litigated, will impose no liability upon the defendant if the judgment is handed down after the restraint period has expired.

Despite the continuing problems of interpreting and applying the *RTA*, its existence no doubt provides contracts that are subject to the laws of the State of New South Wales with a fallback position should the common law operate to invalidate a restraint based on unreasonableness. All the other States and Territories in Australia continue to suffer from the lack of statutory protection when parties covenant in RT. Common law contracts are therefore entirely reliant on the doctrine of severance and its RT protégé, the cascading clause. The following section will examine the use of this mechanism in more detail and critique the difficulties associated with its use.

#### 2.4 CASCADING CLAUSES AND THE ISSUE OF UNCERTAINTY

Cascading clauses appear to have been first encountered by the judiciary in Australia in the decision of *Austra Tanks Pty Ltd v Running*.<sup>182</sup> *Austra Tanks* dealt with a contract for the sale of a business where the vendor covenanted that he would ‘not for the stipulated period engage in the business of the Partnership or any aspect thereof in the stipulated area.’<sup>183</sup> The definition of ‘stipulated period’ and ‘stipulated area’ contained a large number of variables, some of which were overlapping.<sup>184</sup> Wootten J noted that the RT was seeking to ‘define the obligation through a series of enquiries as to what is enforceable’<sup>185</sup> and referred to the English Court of Appeal decision of *Davis v Davis*.<sup>186</sup> In *Davis*, there was a retiring partner who covenanted to ‘retire wholly and absolutely from the partnership, and so far as the law allows from the trade or business thereof in all its branches...’<sup>187</sup> The Court held these words were too vague to enforce.

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<sup>182</sup> [1982] 2 NSWLR 840 (*Austra Tanks*).

<sup>183</sup> *Ibid* 841.

<sup>184</sup> *Ibid*.

<sup>185</sup> *Ibid* 843.

<sup>186</sup> (1887) 36 Ch D 359 (*Davis*).

<sup>187</sup> *Ibid*.

Cotton LJ in *Davis* held:

A covenant in this form, indefinite as it is in my opinion, is one which neither a Court of Equity nor a Court of Law ought to enforce. The parties must make up their minds to say what they agree to as regards to the limits of time or space within which there is to be no trading.<sup>188</sup>

Bowen LJ and Fry LJ emphasised that the Court's duty is the interpretation of contracts which the parties themselves have agreed upon; not the duty to make the contract for the parties.<sup>189</sup>

Wootten J in *Austra Tanks* followed this line of reasoning in relation to the impropriety of leaving it to the Court to fix a valid restraint.<sup>190</sup> He went on to hold the restraint void for uncertainty:

The agreement only contemplates one covenant. Which one is intended? The problem is not to be solved by saying that the widest enforceable covenant is intended because in the absence of any statement as to the priority of application of the variables it is not possible to say which covenant is widest. Does a 100km radius for one year give a wider covenant than a 10km radius for five years?

I referred earlier to this covenant as malevolent because it makes no genuine attempt to define the covenantee's real need for protection, gives the covenantor no clear guide as to what he can or cannot do...<sup>191</sup>

Accordingly, the Court refused to exercise its power under s 4(3) of the *RTA* as it was found that the parties were guilty of a manifest failure to make the restraint a reasonable restraint.<sup>192</sup> In

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<sup>188</sup> Ibid 388.

<sup>189</sup> Ibid 389-98.

<sup>190</sup> Ibid 845.

<sup>191</sup> Ibid 846.

<sup>192</sup> Ibid.

contrast, the Full Court of the Queensland Supreme Court upheld the restraint in question in *JQAT*<sup>193</sup> by distinguishing the restraint from both *Austra Tanks* and *Davies*.<sup>194</sup> The restraint contained 18 restraint combinations but the effect of an 'instructional clause' made clear that the combinations were to operate as separate restraints, albeit cumulative and overlapping.<sup>195</sup> Moreover, the combinations were not inconsistent with one another and were capable of being simultaneously actioned. The instructional clause is repeated below:

The preceding sub-clause 6.2 of this Clause 6 shall be construed and have effect as if it were a number of separate sub-clauses which results from combining the commencement of sub-clause 6.2 with each sub-paragraph of paragraph (a) and combining each such combination with each sub-paragraph of paragraph (b) and combining each such combination with each sub-paragraph of paragraph (c), each such resulting sub-clause being severable from each other such resulting sub-clause, and it is agreed that if any of such separate resulting sub-clauses shall be invalid or unenforceable for any reasons, such invalidity or unenforceability shall not prejudice or in any way affect the validity or enforceability of any other such resulting sub-clause.<sup>196</sup>

The combination of restraints, when tempered with an instructional clause as the one above, was ruled in *JQAT* to provide sufficient certainty as to what obligation was being imposed.<sup>197</sup> Contrary to the primary judge's decision, the Full Court in *JQAT* held that the parties had demonstrated an intention that was sufficiently clear, namely, to impose 18 different restraints, of which some may be enforceable and others, unenforceable. Of the unenforceable restraints, the combination of their drafting and the instructional clause allowed the doctrine of severance to be employed to sever their connection to the contract, leaving the remaining restraints intact.

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<sup>193</sup> *JQAT* [1987] 2 Qd R 162.

<sup>194</sup> *Ibid* 167.

<sup>195</sup> *Ibid* 163.

<sup>196</sup> *Ibid*.

<sup>197</sup> *Ibid* 169.

This line of reasoning was applied by Spender J in the Federal Court decision of *Re Lloyd's Ships Holdings Pty Ltd and Queensland Merchant Holdings Limited v Davros Pty Ltd; Lloyd Corporation (A Firm); Keith Bernie Lloyd and Lloyd's Exclusive Charters Pty Ltd*.<sup>198</sup> This case will be analysed below in detail as it is a poignant example of the difficulties faced by contracting parties when contracting via cascading clauses. The case involved the sale of a ship-building business relating to the construction of luxury vessels. The sale agreement provided for the acquisition of goodwill and in particular, exclusive rights to use the name 'Lloyd's Ships' under which the business had established a substantial reputation. Consideration of \$6,000,000 was duly paid by the purchaser and the vendor covenanted to restrain itself according to the RT clauses below:

39(a) In consideration of the purchaser entering into this contract and to reasonably protect the goodwill of the business the vendor, the second vendor, the third vendor, the fourth vendor, the fifth vendor and the sixth vendor and each of them do jointly and severally agree with the purchaser that subject to cl 39(b):

- (i) This clause shall have effect as if it were several separate covenants consisting of each separate covenant set out in sub-clause (ii) of this cl 39(a) combined with each separate period of time set out in sub-clause (iii) of this cl 39(a) and of each such separate combination combined with each separate area set out in sub-clause (iv) of this clause 39(a) and if any of the said several separate covenants shall be or become invalid or unenforceable for any reason then such invalidity or unenforceability shall not affect the validity or enforceability of any of the other separate covenants.

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<sup>198</sup> [1987] FCA 70 ('*Re Lloyd's Ships*').



(ii) The vendor, the second vendor, the third vendor, the fourth vendor, the fifth vendor and the sixth vendor and each of them will for the period and within the area hereinafter specified without the prior written consent of the purchaser whether directly or indirectly by themselves or jointly with or on behalf of any other persons or corporation or trust on any account or pretext by any means whatsoever or though (sic) an agent or independent contractor:

- (a) carry on or be engaged in or concerned with directly or indirectly (whether as proprietor, employer, servant, agent, principal, partner or in any other capacity whatsoever) or otherwise engage in the business of shipbuilding of any description or any other business of a similar nature; or
- (b) procure or solicit or encourage any other person to procure or solicit the custom of any former customer of the business; or
- (c) hold or beneficially own whether directly or indirectly and whether absolutely or contingently or hold options over shares in or be an adviser to any corporation doing any of the things referred to in 39(a)(ii)(a) or 39(a)(ii)(b) above.

(iii) The periods of time hereinbefore referred to are:

- (a) during the period of ten (10) years from and after completion;
- (b) during the period of nine (9) years from and after completion;
- (c) during the period of eight (8) years from and after completion;
- (d) during the period of seven (7) years from and after completion;
- (e) during the period of six (6) years from and after completion;
- (f) during the period of five (5) years from and after completion;
- (g) during the period of four (4) years from and after completion;

- (h) during the period of three (3) years from and after completion;
  - (i) during the period of two (2) years from and after completion;
  - (j) during the period of one (1) year from and after completion;
- (iv) The areas hereinbefore referred to are:
- (a) within the United States, Canada, Australia and/or New Zealand;
  - (b) within Australia;
  - (c) within the East Coast of Australia

39(b) Nothing in sub-cl 39(a) shall prevent the sixth vendor from representing to any interested person or persons that he acts on behalf of the purchaser in pursuance of the commission agency agreement referred to in cl 40 hereof.<sup>199</sup>

After settlement of the contract, a dispute arose between the parties whereby the purchasers alleged that the vendors had continued to carry on the business of ship building and that the vendors' new business was situated within 1.5kms of the purchasers' business.<sup>200</sup> Moreover, the vendors advertised under their name under 'Lloyd Corporation' which conduct was alleged to be misleading and deceptive by the purchasers.<sup>201</sup> A number of causes of action were alleged against the vendors including an allegation that they were in breach of cl 39 of the sale agreement.<sup>202</sup> The vendors denied that the purchasers had a valid claim to relief and alleged that the RT clause was void either by way of uncertainty or in the alternative, it contravened public policy or is an unreasonable RT.<sup>203</sup>

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<sup>199</sup> Ibid 26.

<sup>200</sup> Ibid 11.

<sup>201</sup> Ibid.

<sup>202</sup> Ibid 16.

<sup>203</sup> Ibid 17.

The Court first addressed two inadvertent mistakes made in the drafting of cl 39 which may otherwise have rendered the contract uncertain. The first was in cl 39(a)(ii) whereby the Court accepted the purchasers' argument that the clause should be read as if 'not' appeared after the word 'will'.<sup>204</sup> The Court also accepted that the term 'and/or' in cl 39(a)(iv)(a) introduced a disjunctive element which the parties had not intended.<sup>205</sup> The term was therefore disregarded.

From the instructional clause in cl 39(a)(i), the Court was able to generate 120 restraints of which 30 were not restrained by area and thereby creating a world-wide restraint.<sup>206</sup> The 90 sub-clauses consisted of restraints defined by area and time. The Court began its analysis by stating that where goodwill is sold for consideration, a restraint on the vendor by way of an RT clause is proper.<sup>207</sup> The character of the business sought to be protected must remain however, the focus of any analysis by which the validity of the RT is to be judged.

On the subject of uncertainty, the Court drew an important distinction between a variable restraint clause which contemplates a single RT operating from different combinations of conduct, time and area which are generated and a series of clauses each operating cumulatively.<sup>208</sup> Where RTs are to operate as a single covenant, the Court was of the opinion that a means must be provided to determine which of the combinations will apply and how they will apply.<sup>209</sup> Such means may be provided by way of an instructional clause such as cl 39(a)(i). If the interpretation of an instructional clause however, is that the widest restraint is to apply, the RT may be uncertain in the absence of any guidance as to the priority of interpreting what is a wider RT when compared to another RT. In particular, if no guidance is provided as to what is the widest restraint and it is

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<sup>204</sup> Ibid 44.

<sup>205</sup> Ibid 45.

<sup>206</sup> Ibid 46.

<sup>207</sup> Ibid 29.

<sup>208</sup> Ibid 48.

<sup>209</sup> Ibid 48-49.

unclear as to what can be construed as the widest restraint, the RT clause will be void for uncertainty. For example, is a restraint of 50km radius for 5 years greater than a restraint of 100km radius for 1 year? On the other hand, if the variable RT clause contemplates all of the possible combinations applying cumulatively with severance of those found to be an unreasonable RT, then the RT will be sufficiently certain. Importantly, the overlapping of RT restraints is acceptable and not regarded as being inconsistent. Under this interpretation, an RT with a restraint of 5 years is not inconsistent with another RT with a restraint of 4 years.

The RT was ultimately found to be unenforceable due to the words ‘the business of ship building of any description or any other business of a similar nature’ which appeared in cl 39(a)(ii)(a).<sup>210</sup> The choice of terminology did not allow the Court to read down the clause to limit the restraint to one that would be reasonable and enforceable. As the clause purported to restrain the vendors from engaging in all forms of ship building (and therefore not limited to luxury vessels), many of which had never been undertaken by the business sold, it was held to be an unreasonable RT as it went beyond what was reasonable in protecting the interests of the purchasers.<sup>211</sup>

From the above example and through the analysis of case law throughout Chapter 2, several operational observations on the use of cascading clauses may be noted:

- (a) Conduct sought to be restrained, together with the geographical and temporal limits of that restraint cannot be determined in isolation by the contracting parties' desires. Instead, the RT must be determined in line with the character of the subject matter for which protection is sought.

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<sup>210</sup> Ibid 80-82.

<sup>211</sup> Ibid.

- (b) The variable restraint clause should reflect a series of separate independent restraints, each capable of being severed in the event that a Court finds the restraint to be unreasonable.
- (c) If a single covenant is to be drafted, it must provide a means through an instructional clause to enable interpretation and choice of how the combination restraint should be applied. The instructional clause must provide a statement of priority of application with respect to the variables in the covenant.
- (d) The greater the number of variables and possible combinations and the more indiscriminate those combinations are, the more likely it is that the Court will not view the RT as a genuine attempt by the parties to define the extent of the restraint needed for protection.
- (e) The *RTA* cannot save unreasonable RT clauses where the parties are guilty of a manifest failure to consider the reasonableness of a restraint and the restraint is subsequently found to be unreasonable.
- (f) The *RTA* cannot save RT clauses which are against the public interest.
- (g) In considering the issue of reasonableness, the RT clause must have regard to the following factors:
  - (1) Nature and range of activities carried on by the covenantee including any peculiarities of the industry in which the covenantee is involved in (i.e.

the pharmaceutical business with long research and product development times);

- (2) Geographical area in which the covenantee is involved and where appropriate, a reasonable geographic area where the covenantee may expand in the future;
  - (3) The nature of the covenantee's market, the covenantee's market penetration and the nature of competition within that market;
  - (4) The time it may take for the covenantor to lose contact with customers of the covenantee; and
  - (5) Whether a restraint against third party covenantors is necessary and reasonable to protect the legitimate interests of the covenantee. For example, in a sale of business, it may be reasonable and necessary to restrain the business' key personnel but unreasonable to restrain the husband or wife or children of the covenantor.
- (h) The *RTA* operates prospectively so that once the period of redress has lapsed, an action to challenge the restraint cannot be instituted, maintained, nor any damages awarded, irrespective of the reasonableness of the restraint.

The observations denote very clearly, the problems experienced by parties when contracting in common law. Whilst the *RTA* provides a level of certainty when parties contract in RT, it is plausible to suggest that the laws surrounding RT remain overly complex and remain guided by

antiquated laws such as the test of public policy which for all intents and purposes is long obsolete and not applied to cases of RT today.

The test of reasonableness fares no better with arguable propositions of what is on one hand, reasonable, and on another, unreasonable. Commentary from the Courts has gone as far to admit that different judges, when faced with the same set of facts, may very well determine the issue of reasonableness differently with respect to the criteria used and the outcome of the application of that criteria. Here, it is apt to note the words of Heydon J in the preface to his 2008 publication, the ‘Restraint of Trade Doctrine’:

Ten years have passed since the last edition was prepared. The period has seen no revolution, but it has generated quite a number of reported cases, and the great volume of unreported cases which have come into existence suggests that the subject retains considerable practical significance both for lawyers engaged in litigation and other lawyers.<sup>212</sup>

Moreover, with many cases resulting in what may be arguably correct as an application of black letter law, the resulting inequity from those decisions have been noted in numerous cases by judges who are forced to find in favour of a party that seeks to invalidate an RT clause due to such a clause being deemed unreasonably wide. The inequity of allowing a party to walk away from its restraint obligations whilst providing that party with a windfall gain by permitting that party to retain consideration paid by the opposing party is truly inequitable and is a regretful position in law.

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<sup>212</sup> Heydon, above n 1, xi.

Despite the increasing number of cases both reported and unreported in Australia, the legislature, aside from the State of New South Wales, has failed to enact any laws to protect contracting parties from the existing deficiencies of the Doctrine when they contract in good faith in RT. This result has created a void in the RT field of law which lawyers, with relative support from the Courts, have sought to mend via an expedient created to circumvent an otherwise intolerable and unacceptable position. However, the use of cascading clauses, with respect to their method of application, interpretation and judicial guidance over the years, remain very much an artificial technique derived to overcome the inherent deficiencies of RT contracting. Its artificiality creates problems for contracting parties through its intrinsic lack of certainty despite its being accepted in principle by the Courts of Australia. It should therefore not be surprising when clients ask their lawyers for an explanation as to why there are 5 different types of geographic restraints or 5 different time restraints and how these restraints should be applied. It is indeed an embarrassing situation when lawyers have to explain to bewildered clients the shortcomings of the law and why, in the current state of RT contracting, best practice dictates the use of cascading clauses notwithstanding that there will always remain an indisputable prospect of future litigation with respect to what constitutes a reasonable restraint. Such explanations do little to instill the sense of confidence that businesses require in their day to day dealings with one another.

The *RTA* does go some way to correct the problems of the common law. Its achievement in focusing the Courts of New South Wales on actual breaches rather than imaginary breaches is a significant breakthrough and one that is preferable to having no statutory protection at all. In providing Courts with a fallback position when the doctrine of severance would simply render an otherwise applicable restraint unenforceable, contracting parties are provided with greater flexibility to contract with each other. Unfortunately, a persistent threat remains in any RT litigation from the issues associated with time restraints and the ratio arising from the *Spooner*



decision not to mention the continuing difficulties of interpretation. These matters may well be suitable as subjects for future law reform.

### **CHAPTER 3: THE RELATIONSHIP BETWEEN COMPETITION LEGISLATION AND THE RESTRAINT OF TRADE DOCTRINE**

The principal federal legislation governing RT contracts prior to 1 January 2010 was the *TPA*. After 1 January 2010, the *TPA* was replaced by the *CCA*. Insofar as agreements in RT can be challenged under the provisions of the *RTA* and under the common law, it may also be challenged under the *CCA*. Accordingly, any analysis in relation to RT contracts would be incomplete without an examination of the impact of the *CCA* on RT contracts. Whereas the common law and the *RTA* are interested at a fundamental level in the reasonableness of a contractual restraint and to a limited degree, in the application of the public interest test, the premise behind the *CCA* differs from the common law and the *RTA* in its goal of promoting competition and prohibiting restrictive agreements that substantially lessen competition.

Despite the emphasis of the *CCA* being upon competition regulation, the importance of this piece of legislation and its shared role in the regulation of RT agreements should not be underestimated. It was suggested by David Meltz in 1995 that ‘it may be arguable that as a result of the enactment of the *Trade Practices Act 1974* (Cth) the common law doctrine of restraint of trade in Australia has been placed in the dustbin of legal history’.<sup>213</sup> In fairness, Meltz’s observation may be a slight exaggeration of the impact that the *TPA* has had with respect to RT agreements but it is an undeniable fact that the *TPA* has had a profound influence in hampering willing contracting parties to engage each other for gain where such engagement would or would have likely resulted in a substantial lessening of competition. To a large extent, the enactment of the *TPA* has created a marriage between common law principles and statutory intervention by separating the protection of an individual’s liberty to trade from the community benefit enjoyed by curtailing

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<sup>213</sup> Meltz, above n 9, 1.

potential economic serfdom arising from anti-competitive conduct. It may be further said that, whilst not a perfect solution, the hesitation of applying the common law public interest test by the Courts is now partly remedied by the CCA with respect to the public interest of preserving competition in the market.

It is worth noting at the outset of this chapter that the author does not intend to comment generally on the vast quantity of material already in existence with respect to restrictive trade practices under Part IV of the CCA. Much has already been written on this subject.<sup>214</sup> Chapter 3 will instead provide a law and economics analysis on the role of anti-competition legislation insofar as it relates to agreements in RT. It will also examine the difficulties of maintaining a workable relationship between the operation of the Doctrine and the CCA. Chapter 3 will conclude by reviewing the process of Authorisations and the potential merits of reinstating the now defunct Clearance procedure for contracts that purport to engage in RT.

### 3.1 THE ECONOMIC THEORY BEHIND THE NEED FOR ANTI-COMPETITIVE LEGISLATION

It was noted in 1975 at a Trade Practices Lecture at Monash University delivered by D.A. Walsh that the TPA is a governmental expression of economic policy and must be interpreted under the spotlight of economic policy objectives.<sup>215</sup> Its terms cannot be interpreted or applied accordingly in a ‘mechanical or legalistic fashion’ since the facts to which they relate will only assume

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<sup>214</sup> See, eg, Ian Wylie, ‘Not That Old Chestnut Again – Third Line forcing Under the *Competition and Consumer Act 2010*’ (2011) 19 *Competition & Consumer Law Journal* 18; Warren Pengilly, ‘Thirty Years of the *Trade Practices Act*: Some Thematic Conclusions’ (2004) 12 *Competition & Consumer Law Journal* 1; Frances Hanks and Philip Williams, *Trade Practices Act: A Twenty-Five Year Stocktake* (The Federation Press, 2001); or Russell Miller, *Miller's Australian Competition and Consumer Law Annotated* (Thomson Reuters (Professional) Australia, 34<sup>th</sup> ed, 2014).

<sup>215</sup> D A Walsh, ‘Authorization and Clearance – Trade Practices Lectures No. 7’ (Speech delivered at Monash University, Clayton 1975).

significance through economic analysis and argument.<sup>216</sup> Professor Maureen Brunt expounds on this fundamental view by suggesting that the aim of the *TPA* is the promotion of ‘workable’ or ‘effective’ competition (which were common terms used by industrial organisation economists to describe the nature and role of impersonal economic and competitive pressures aimed at encouraging society to function in a progressive manner towards the economic goal of Pareto efficiency).<sup>217</sup> Professor Brunt’s analysis is of interest in view of her distinguished membership of the Trade Practices Tribunal (‘TPT’) which had a significant influence on the development of policies in the Trade Practices Commission (‘TPC’). She was later recognised in 2007 by Professor Allan Fels who chaired the Australian Competition and Consumer Commission (‘ACCC’) from its inception in 1995 to 2003 as an individual who significantly contributed to the policy-making, the application and the development of competition law in Australia.<sup>218</sup>

In dissecting the premise behind a suitable definition of ‘workable or effective competition’, one will quickly recognise the somewhat nebulous and round-about notion that it represents. Notwithstanding this, the role of economic theory in the formulation and early development of the *TPA* can be traced back to Chapter 1 where the foundations of the perfectly competitive model were laid out. To recap, in Chapter 1, it was stated that for the perfectly competitive model to exist, the following events need to occur simultaneously to maximise economic efficiency:

- (a) There are numerous buyers and sellers, each acting independently and rationally;<sup>219</sup>

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<sup>216</sup> Ibid.

<sup>217</sup> Robert Baxt and Maureen Brunt, ‘Monash Trade Practices Lectures No. 11’ (Speech delivered at Monash University, Clayton 1975).

<sup>218</sup> Allan Fels, ‘Distinguished Fellow of the Economic Society of Australia, 2006: Maureen Brunt’ (2007) 83 *The Economic Record* 204.

<sup>219</sup> Pindyck and Rubinfeld, above n 75, 327.

- (b) Each buyer and seller consumes or produces such a negligible amount of the total output such that no one buyer or seller can influence price by the amount they either consume or produce;<sup>220</sup>
- (c) There are no barriers to entry or exit with respect to consumer or product markets;<sup>221</sup>
- (d) All buyers and sellers are fully informed of relevant economic and technological data;<sup>222</sup>
- (e) All products are homogeneous, or rather, constitute interchangeable substitutes for each other;<sup>223</sup> and
- (f) The forces of supply and demand are free to determine the quantity of output in a relevant market as well as determine a competitive price with respect to that output.<sup>224</sup>

It was previously argued that events (b), (c) and (f) are largely regulated by statute for the benefit of the wider public in the maintenance of a free market, with exceptions made for natural monopolies where such monopolies are established for the greater good. The regulation referred to is, of course, a reference to the *CCA*. From a law and economics perspective, the theories touched upon in Chapter 1 can now be expanded to include the economic reasons for legislative intervention in RT contracts. As a starting point, given static environmental and behavioural assumptions required in modelling perfect competition, the theoretical output is said to be economic efficiency. Realistically however, economic theorists recognise that these conditions are rarely fulfilled in the real world. To the extent that these events are not fulfilled, market power may arise which reflects in part, the absence of close substitutes for a product, either actual or potential within a reasonable time and geographic limitation.<sup>225</sup>

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<sup>220</sup> Landsburg, above n 76, 634.

<sup>221</sup> Pindyck and Rubinfeld, above n 75, 253.

<sup>222</sup> Ibid 595.

<sup>223</sup> Ibid 252.

<sup>224</sup> Ibid 55.

<sup>225</sup> Ibid.

At a theoretical level and purely based on economic concepts of market power, all businesses will possess some market power if only by virtue of their differing locations. Carl Kaysen and Donald Tuner noted that, 'a firm possesses market power when it can behave persistently in a manner different from the behaviour that a competitive market would enforce on a firm facing otherwise similar cost and demand conditions.'<sup>226</sup>

D A Walsh takes this analysis one step further by suggesting that market power may derive from legitimate sources but may also be manifested through restrictive agreements and other generally undesirable practices such as:

Price fixing, market-sharing, collective boycotts and collective resale price maintenance; or it may arise out of market dominance by a monopolist or oligopolist. Market power may also be inadvertently obtained through the facilitation of mergers, take-overs, monopolization, exploitative pricing, restriction of output, exclusive dealing, predatory price-cutting or price discrimination.<sup>227</sup>

Walsh also contends that market power is essentially a matter of structure; that is to say; its existence depends upon a favourable combination of structural elements.<sup>228</sup> In tying this summary to the above analysis, the reference to structural elements relates to events (b), (c) and (f) above. Accordingly, Professor Brunt's 'workable or effective competition' can otherwise be defined as the elimination or containment of market power by deliberate external intervention through the moulding of its structural elements into a competitive and economically acceptable common position. This, according to Frederic Scherer, in his publication of 'Industrial Market

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<sup>226</sup> Carl Kaysen and Donald Turner, *Antitrust Policy: An Economic and Legal Analysis* (Harvard University Press, 1959) 75.

<sup>227</sup> D A Walsh, 'Authorization and Clearance – Trade Practices Lectures No. 7' (Speech delivered at Monash University, Clayton 1975).

<sup>228</sup> Ibid.

Structure and Economic Performance',<sup>229</sup> may be defined under three categories: these being structure, conduct and performance.

Structure moulding denotes the following:

- The number of traders should be at least as large as scale economies permit;
- There should be no artificial inhibitions on mobility and entry; and
- There should be moderate and price-sensitive quality differentials in the products offered.

Conduct moulding denotes the following:

- Uncertainty should prevail in the minds of competitors as to whether price initiatives will be followed;
- Businesses should strive to achieve their goals independently, without collusion;
- There should be no unfair, exclusionary, predatory or coercive tactics;
- Inefficient suppliers and customers should not be shielded permanently;
- Sales promotion should not be misleading; and
- Persistent harmful price discrimination should be absent.

Performance moulding denotes the following:

- Production operations should be efficient;
- Promotional expenses should not be excessive;
- Profits should be at levels just sufficient to reward investment, efficiency and innovation;

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<sup>229</sup> Frederic Scherer, *Industrial Market Structure and Economic Performance* (Rand McNally, 1970).

- Output levels and the range of qualities should be responsive to consumer demands;
- Opportunities for introducing technically superior products and processes should be exploited;
- Prices should not intensify cyclical instability; and
- Success should accrue to sellers who best serve consumer wants.<sup>230</sup>

In Australia, the external intervention of market forces designed to regulate the structure, conduct and performance of businesses to maintain a workable or effective competitive market is enshrined in Part IV of the *CCA*. This next section will explore the historically troubled development of Part IV and the many twists and turns from its enactment in 1972 to its current modern day version.

### 3.2 SECTION 45 - *COMPETITION & CONSUMER ACT*

Part IV of the *CCA* prohibits anti-competitive practices that have the effect of substantially lessening competition in the market. The various forms of anti-competitive practices can be generally limited to a number of descriptions which include that of cartel conduct<sup>231</sup>, anti-competitive agreements, misuse of market power, predatory pricing, exclusive dealing, third line forcing and resale price maintenance.<sup>232</sup> Insofar as RT contracts are concerned, s 45 of the *CCA* is the basic starting point of the Australian legal system of trade practices control.

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<sup>230</sup> Ibid at 37.

<sup>231</sup> Cartel conduct includes price fixing, market division, restricting outputs and bid rigging.

<sup>232</sup> Price fixing, exclusionary conduct, third line forcing and resale price maintenance are *per se* prohibitions which would require Authorisation even if it could be shown that such conduct would not substantially lessen competition.



The author's intention for this chapter is to focus on s 45 of the *CCA*. As will be discussed below, s 45 is primarily concerned with contracts, arrangements or understandings that restrict dealings or affect competition. Due to the broad coverage of s 45, it can be viewed as the overarching provision of other anti-competitive sections within the *CCA*, specifically those within Part IV. The construction of s 45 prevents entities from engaging in conduct which will substantially lessen competition. The section's deliberately broad coverage captures any actions that are anti-competitive and are not exclusively covered by other sections of the *CCA*, such as misuse of market power under s 46, exclusive dealings as per s 47 or mergers under s 50.

Under s 46, a corporation that has a substantial degree of market power cannot take advantage of that power to eliminate or damage a competitor, prevent entry of an entity into that or any other market, or deter or prevent an entity from engaging in competitive conduct. The section also prohibits predatory pricing whereby an entity supplies goods or services for an extended duration below cost price. In addition to s 46, s 46A makes reference to misuse of market power within Trans-Tasman Markets.

Section 47 specifically relates to various forms of exclusive dealing that constitute anti-competitive conduct. This section focuses on two main types of behaviour between suppliers and retailers being:

- (1) Supplying or acquiring goods or services subject to a condition, including but not limited to exclusivity, pricing, re-supply or limiting other acquisition/supply arrangements; and
- (2) Refusing to supply or acquire goods or services to an entity for not agreeing to terms of a condition, including but not limited to exclusivity, pricing, re-supply or limiting other acquisition/supply arrangements.

Most forms of the above conduct are only in contravention of s 47 if they substantially lessen competition.<sup>233</sup> However, third line forcing, in which the supplier supplies goods or services on the condition that the customer purchase other goods or services from a third party, is strictly prohibited regardless of whether it is anti-competitive in nature.<sup>234</sup> Likewise, refusing to supply goods or services because a customer refuses to agree to a condition that they purchase other goods or services from a third party is also strictly prohibited.<sup>235</sup> Nevertheless, there is recognition that potential public benefits may arise in relation to exclusive dealing arrangements and thus Authorisations of such conduct are available under s 88.

In addition to ss 46 and 47, other provisions of the CCA that illustrate specific forms of anti-competitive conduct are ss 48, 49 and 50. Under ss 48 and 49, resale price maintenance and the establishment of a dual listed company that substantially lessens competition are prohibited. Furthermore, s 50 prohibits both direct and indirect acquisitions by persons or corporations of each other where the acquisitions will, or will likely, substantially lessen competition in a market.

The distinguishing element of s 45 from ss 46 through to 50 is that s 45 pertains to contracts, understandings and arrangements, whereas the other sections do not. It is reasonable to state that ss 46 to 50 focus on outcomes that are non-specific to contracts but have the concluding effect of anti-competitive conduct. As this paper is not centred on anti-competitive outcomes as its primary area of interest, the author will focus the history and operation of s 45 with emphasis on the historical and current parallels and distinctions between the operation of the legislative instrument and the common law Doctrine.

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<sup>233</sup> CCA s 47(10).

<sup>234</sup> CCA s 47(6).

<sup>235</sup> CCA s 47(7).

Section 45 of the *CCA* mirrors the old s 45 of the *TPA* which was in turn, modelled on the United States anti-trust legislation, namely s 1 of the *Sherman Anti-Trust Act*.<sup>236</sup> Section 45 of the *TPA* first came into effect on 1 October 1974 with respect to agreements that sought to fix the prices of goods. For all other anti-competitive and RT agreements, s 45 became effective on 1 February 1975. In summary form, the then s 45(1) provided that a contract in RT made before the commencement date is unenforceable. Section 45(2)(a) prohibited a corporation from making a contract or arrangement, or entering into an understanding in RT. Section 45(2)(b) prohibited a corporation from giving effect to a contract, arrangement or understanding to the extent that it is in RT, whether or not the contract or arrangement was made or the understanding was entered into before or after the commencement date.

To restrict the scope of its operation, s 45(4) provided that restraints of trade are not contrary to the *TPA* unless the restraint has or is likely to have a significant effect on competition between the parties to the contract, arrangement or understanding or on competition between those parties or any of them and other persons. This qualifying attempt on the ambit of s 45 ensured that the Doctrine remained alive and well especially in areas excluded from the operation of s 45 by virtue of s 51 of the *TPA*.

Of the ideologies carried over from the United States into the *TPA*, there were some significant differences which distinguished the Australian system from its American counterpart. In particular, the Australian legislature was concerned that an *in toto* importation of s 1 of the *Sherman Act* into the Australian economic environment would have at the time, resulted in an unacceptable level of insecurity for businesses.<sup>237</sup> Furthermore, in contrast to the American

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<sup>236</sup> 15 USC (1890) ('*Sherman Act*').

<sup>237</sup> Warren Pengilly, 'Section 45 of the *Trade Practices Act* – The Law and Administration to Date' (1976) 8 *Federal Law Review* 16.

model, it was also seen to be beneficial for businesses to be provided with an opportunity to have its agreements evaluated away from judicial bodies to avoid unnecessary adjudications that were costly and inefficient to run.<sup>238</sup> An administrative measure was therefore enacted via s 92(1) of the *TPA* to enable parties to apply to the TPC for Clearance of contracts, arrangements or understandings which may be prohibited by s 45.<sup>239</sup> Clearance may be applied for in respect of not only actual contracts, arrangements or understandings but also potential or proposed contracts, arrangements or understandings on the basis that the conduct or proposed conduct is not substantially anti-competitive. If clearance is granted by the TPC, then the relevant contract, arrangement or understanding cannot be challenged by the TPC for breach of s 45, subject to relevant parties' compliance in respect of any conditions or qualifications placed by the TPC.

A further important legislative refinement which distinguished the Australian approach from the American approach is the Authorisation procedure. It was here that the legislature recognised and accepted the economics argument that some restraints, irrespective of their anti-competitive nature, may result in an overall public benefit. In addition to the availability of Clearances, the *TPA* thus also created the instrument of Authorisations to sanction a contract, arrangement or understanding based on public benefit grounds (as opposed to Clearances, which was based solely on whether conduct was substantially anti-competitive). There was no definition of 'public benefit' but the TPC was not to grant an Authorisation unless it was satisfied that the:

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<sup>238</sup> Ibid.

<sup>239</sup> Earlier clearance procedures were ineffective as competition legislation introduced by the *Australian Industries Preservation Act 1906* (Cth) was successfully challenged on a constitutional basis. The second major attempt was the *Trade Practices Act 1965* (Cth), which was influenced by the United Kingdom's *Restrictive Trade Practices Act 1956* (UK). This act and its related successors (until the enactment of the *TPA*) were criticised as being inefficient, slow and costly. For more information, see Lee Boldeman, *The Cult of the Market: Economic Fundamentalism and its Discontents* (ANU, 2007). The European Community also had its own clearance procedures prior to the *TPA*. For more information, see Dermot Cahill, *The Modernisation of EU Competition Law Enforcement in the EU* (Cambridge, 2004).

...contract, arrangement, or understanding...to which the application relates results, or is likely to result, in a substantial benefit to the public, being a benefit that would not otherwise be available, and that, in all the circumstances, that result, or that likely result, as the case may be, justifies the granting of the authorisation.<sup>240</sup>

Similar to the operation of Clearances, Authorisations may also be applied for in respect of actual or potential contracts, arrangements or understandings. The inclusion of s 45 and the availability of Clearances and Authorisations was necessary partly because of the high inflationary problems faced in Australia during the mid-1970s. In an attempt to control rising inflation, the Whitlam government took it upon itself to enact legislation aimed at controlling and curtailing restrictive trade practices so as to maintain the government's economic credibility in its struggle over the country's fiscal woes.<sup>241</sup> Through the enactment of the *TPA*, the Whitlam Government sought to enhance the competitive nature of the private sector and to discourage certain practices which were antithetical to the promotion and advancement of market competition.<sup>242</sup>

In the Second Reading Speech at the House of Representatives, the then Minister for Manufacturing Industry, Mr Keppel Enderby noted that the *Trade Practices Bill* 1973 (Cth) (*'Trade Practices Bill'*) sought to provide on a national basis:

...long overdue protection for consumers against a wide range of unfair practices. Restrictive trade practices have long been rife in Australia. Most of them are undesirable and have served the interests of the parties engaged in them, irrespective of whether those interests coincide with the interests of Australians generally.<sup>243</sup>

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<sup>240</sup> *TPA* s. 90(5)

<sup>241</sup> Gough Whitlam, *The Whitlam Government 1972-1975* (Viking, 1985) 362.

<sup>242</sup> *Ibid.*

<sup>243</sup> Commonwealth, *Parliamentary Debates*, House of Representatives, 16 July 1974, 225 (Keppel Enderby).

This recognition of the need for legal protection of the greater economic interests of the Australian public was largely echoed by the Opposition who in principle supported the enactment of the *TPA*.<sup>244</sup> The choice of language and operational measures incorporated into the *TPA* however, were debated at length. For example, with respect to the drafting of the *Trade Practices Bill*, it was noted by the Government that:

...other provisions, particularly those describing the prohibited restrictive trade practices, have been drafted along general lines using, wherever possible, well understood expressions...Special provisions are included in the Bill for no other reason than to remove uncertainty. These are the provisions for clearances and authorisations. In the great majority of cases the applicability of the provisions in this Bill will be clear. In those cases where some uncertainty does arise, particularly during the early years of its administration, there will generally be opportunity for the uncertainty to be removed by seeking a clearance or an authorisation.<sup>245</sup>

The highly complex nature of the *Trade Practices Bill* resulted in a significant number of changes being made to it between the time of its original draft and the time of its Second Reading. The comments of Mr Robert Ellicott, the then Member for Wentworth, which was cited in the Second Reading Speech of the *Trade Practices Bill*, is telling:

Events have shown that the Opposition's refusal to be hurried into the passing of this legislation was completely justified because in March this year the Attorney-General brought the Bill forward again in the Senate with over 100 amendments...This experience should serve to warn the

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<sup>244</sup> Commonwealth, *Parliamentary Debates*, House of Representatives, 24 July 1974, 567 (Robert Ellicott).

<sup>245</sup> Commonwealth, *Parliamentary Debates*, House of Representatives, 16 July 1974, 228 (Keppel Enderby).

Government that it should not seek to push complex legislation through this House in haste and without sufficient time for debate and representation by interested parties.<sup>246</sup>

It was the view of the Opposition at the time of passage of the *Trade Practices Bill* that there remained a level of uncertainty in relation to how s 45 may be applied by the judiciary in the adjudication of any subsequent disputes. In particular, the drafting of s 45 contained prohibitions of contracts, arrangements and understandings ‘in restraint of trade or commerce’. In the Second Reading Speech of the *Trade Practices Bill*, the Opposition noted:

Of course, we have known a doctrine of restraint of trade in this country inherited from the common law and one of the problems with clause 45 and its interpretation will be whether the courts will apply to it the common law doctrine.<sup>247</sup>

In hindsight and with the passage of time, it is evident that the Opposition’s concerns were justified with respect to the uncertainty created when the judiciary was called upon to interpret the application of s 45, as will be demonstrated by the analysis below of the ground breaking High Court decision in *Quadramain*.

### 3.3 THE RELATIONSHIP BETWEEN S 45 AND THE COMMON LAW

*Quadramain* was the first decision of the High Court with reference to the *TPA* since its enactment. The decision was highly controversial at the time as a divided bench struggled to wade through the murky waters of clarifying the relationship between s 45 of the *TPA* and the Doctrine.

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<sup>246</sup> Commonwealth, *Parliamentary Debates*, House of Representatives, 24 July 1974, 567 (Robert Ellicott).

<sup>247</sup> *Ibid* 569.

The facts are relatively straightforward. The Berowra Heights Hotel Pty Ltd ('Berowra') owned two lots of land ('Lot 1 and Lot 2'). Lot 1 was used as the site of a hotel and Lot 2 was to be developed as a shopping centre. In 1969, Berowra transferred Lot 2 to Holloway Sackville (Australia) Pty Ltd ('Holloway'). As a condition of the transfer, Holloway covenanted for itself and its assigns that Lot 2 would not be the subject of an application for a liquor licence under the *Liquor Act 1912* (NSW). In 1972, Holloway transferred Lot 2 to Metropolitan Investments Pty Ltd which later leased part of Lot 2 to Sevastapol Investments Pty Ltd ('Sevastapol'). In 1974, Berowra transferred Lot 1 to Quadramain Pty Ltd ('Quadramain P/L'). In 1975, a notice of intention to apply for a conditional spirit merchant's licence in relation to a shop on Lot 2 was filed by Sevastapol. Proceedings were subsequently issued by Quadramain P/L to prevent the shop from being used to sell liquor which in effect was in competition with the hotel business at Lot 1. Sevastapol argued that the covenant was an unreasonable RT and therefore unenforceable under s 45 of the *TPA*. It further argued that the restraint was unenforceable as it infringed s 45(1) and s 45(4) of the *TPA*. Quadramain P/L responded by pleading that the defence failed to allege and demonstrate that the restraint had or was likely to have a significant effect on competition pursuant to s 45(4) and that s 45 was beyond the legislative power of the Commonwealth.

Amongst the numerous legal issues debated in *Quadramain*, one prominent issue was that of an appropriate definition for the term 'restraint of trade' pursuant to s 45(1) of the *TPA*. Some writers predicted that the High Court would be guided in its interpretation of the statute by the common law meaning of 'restraint of trade'.<sup>248</sup> It had been suggested that if a common law

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<sup>248</sup> John Heydon, 'The *Trade Practices Act*, 1974: Section 45: Agreements in Restraint of Trade' (1975) 3 *Business Law Review* 262.



approach was taken to interpret s 45(1), the most likely definition would stem from the definition Diplock LJ gave in *Petrofina*<sup>249</sup> as follows:

A Contract in restraint of trade is one in which a party (the covenantor) agrees with any other party (the covenantee) to restrict his liberty in the future to carry on trade with other persons not party to the contract in such manner as he chooses.<sup>250</sup>

This definition was applied by Joske J in *Top Performance Motors Pty Ltd v. Ira Berk (Queensland) Pty Ltd*<sup>251</sup> and Wootten J in *Hollywood Premiere Sales Pty Ltd v. Faberge Australia (Pty) Ltd*<sup>252</sup> and had been regularly referred to since.<sup>253</sup>

Others did not agree that a common law definition of RT should be imported into the TPA.<sup>254</sup> It was considered by some that if the common law Doctrine was read into s 45, the good intentions behind the *Trade Practices Bill* would be lost or at least restricted; firstly that the intentionally broad coverage of RT under s 45 would be unduly confined,<sup>255</sup> and secondly that a common law approach to s 45 would deter from the economic interpretation intended by Parliament.<sup>256</sup>

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<sup>249</sup> Trade Practices Act Review Committee, Parliament of Australia, *Report to the Minister for Business and Consumer Affairs* (1976).

<sup>250</sup> *Petrofina* [1966] 1 All ER 126, 138.

<sup>251</sup> (1975) 24 FLR 286.

<sup>252</sup> [1976] 2 NSWLR 144.

<sup>253</sup> See, eg, *Specialist Diagnostic Services Pty Ltd v Healthscope Ltd* [2012] VSCA 175; *Tullett Prebon (Australia) Pty Ltd v Purcell* (2008) 175 IR 414; *Cactus Imaging Pty Ltd v Peters* [2006] NSWSC 717; *Woolworths Ltd v Olson* [2004] NSWCA 372; *Williams v FAI Home Security Pty Ltd (No 5)* [2001] FCA 399; *Caerns Motor Services Ltd v Texaco Ltd* [1994] 1 WLR 1249; *Perceptual Development Corporation v Versi Pty Ltd* (1988) ATPR ¶40-837; *Trade Practices Commission v TNT Management Pty Ltd* (1985) 6 FCR 1; *Prudential Assurance Company Ltd v Rodrigues* [1982] 2 NZLR 54; *Clae Engine (Qld) Pty Ltd v Donaldson Australasia Pty Ltd* (1977) 14 ALR 697; *Amoco Australia Pty Ltd v Rocca Bros Motor Engineering Co Pty Ltd (No 2)* (1975) 133 CLR 331.

<sup>254</sup> Graeme Samuel, 'Contracts in Restraint of Trade – Trade Practices Lectures' (Speech delivered at Monash University, Clayton 1975).

<sup>255</sup> Bruce Donald, 'A General Prohibition of Trading Restriction' (1977) 8 *Sydney Law Review* 135.

<sup>256</sup> Pengilly, above n 237, 16.

The decision of the High Court was to apply the term ‘restraint of trade’ in accordance with its common law relative. The economic theory of law as it was first applied by the High Court was therefore one of reversion of s 45(1) to the ebbs and flows of the Doctrine, for good or for bad. Thankfully, the narrow *ratio decidendi* which may be drawn from the *Quadramain* decision is tangential to the general application of s 45(1) as the High Court ruled that s 45(1) does not apply to a covenant that runs with the land where the burdened and benefited land are adjoining and the parties seeking to enforce and escape the covenant are not the original parties to the covenant. Taken on face value, the *Quadramain* decision, on its own, did not represent a major direct inroad into the interpretation of s 45(1) due to its narrow application to land but instead, raised a broader and potentially serious issue by its *obiter dicta* as to the intended relationship between the Doctrine and its application to s 45(1). Indeed, if s 45(1) remained unamended after the *Quadramain* decision, it would appear that the application of s 45(1) would be interpreted in line with the Doctrine thereby significantly narrowing its application. Given that McTiernan, Gibbs and Mason JJ held that s 45(1) had the same meaning as its relative in common law while two judges held to the contrary and two judges expressed no view, it would appear that statistically, the probability that the High Court would eventually affirm the above *obiter dicta* in future matters was relatively high. Moreover, the danger of this interpretation did not end with s 45(1) but could potentially, as some legal commentators predicted, extend to s 45(2) which carried a much greater future relevance to the development of competition law in Australia.<sup>257</sup> Section 45(2) specifically spoke not only about contracts but about ‘contracts, arrangements or understandings’ in RT which, through their drafting methodology, were intended to apply to a much broader variety of formal and informal contractual arrangements.

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<sup>257</sup> Donald, above n 255, 135.

The impending threat of the common law Doctrine being read into and implied into ss 45 (1) and 45(2) after *Quadramain* was hence, very real. The gravity of the *Quadramain* decision was such that if the Doctrine was imported into s 45, all the defects of the common law as previously discussed would also be imported and read into s 45. Such a result would have severely crippled the government's legislative attempt to control anti-competitive conduct through the enactment of s 45 by disengaging economic theories of law which was the foundation upon which s 45 was built and replacing them with the common law hegemony in RT contracting.

It can therefore be surmised that, after *Quadramain*, s 45 was placed in a state of uncertainty and confusion until Parliament passed the *Trade Practices Amendment Act 1977* (Cth) to dispense entirely with the term 'restraint of trade' in s 45. In particular, the Swanson Committee in the 1976 Report of the *TPA*<sup>258</sup> noted that the *Quadramain* direction in law which had been established by the High Court had taken an 'unduly legalistic approach to the interpretation of this economic legislation'.<sup>259</sup> This, of course, served to highlight again, Walsh and Brunt's observations of the inherent problems of interpreting and applying the *TPA* mechanically or legalistically in contrast to the need to examine, interpret and apply the *TPA* through the broader perspective of economic analysis. However, the Swanson Committee's interpretation of the *TPA* did not suggest that it would be appropriate to eliminate or limit the common law application of the Doctrine. In fact, the Swanson Committee went to some pains to paint an environment whereby the economic application of s 45 and the Doctrine may co-exist although as mutually exclusive partners for the purposes of regulating RT contracts.<sup>260</sup>

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<sup>258</sup> Trade Practices Review Committee, Parliament of Australia, *Report of the Trade Practices Review Committee* (1976) ('the Swanson Report').

<sup>259</sup> *Ibid* 15.

<sup>260</sup> *Ibid* 18-19.

Specifically, the Committee recommended that the phrase ‘restraint of trade’ be replaced by a ‘notion or notions more closely related to the concept of competition without limiting common law connotations’.<sup>261</sup> In addition, the Swanson Committee also saw the *obiter dicta* in *Quadramain* as presenting an undesirable set of legal policies as it focused on the form and not the substance of the agreement reached between the contracting parties.<sup>262</sup> Accordingly, it was recommended that the *TPA* should extend to all property covenants with respect to any use of land which may have a substantial adverse effect on competition.<sup>263</sup>

The amended s 45(1) provided that if a provision of a contract made before the commencement of the section is an ‘exclusionary provision’ or has the purpose, or has or is likely to have the effect of substantially lessening competition, that provision is unenforceable insofar as it confers rights or benefits or imposes duties or obligations on a corporation. The amended s 45(2) provided a similar result by removing the term ‘restraint of trade’ and substituting it for the term ‘substantially lessening competition’. With respect to the *ratio* of *Quadramain*, the *Trade Practices Amendment Act 1977* (Cth) laid such matters to rest in the new s 45B. This provides that a covenant in relation to land, whether arising before or after the section commenced, is unenforceable insofar as it confers rights or benefits or imposes duties or obligations on a corporation or associated person. This will be the case where the covenant has, or is likely to have the effect of substantially lessening competition.

The removal of the reference to ‘restraint of trade’ and its substitution for ‘substantially lessening competition’ in ss 45(1) and 45(2) ensured that the *TPA* would develop independently from its common law counterpart as Parliament had originally intended. Section 4M of the *TPA* further

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<sup>261</sup> Ibid 15.

<sup>262</sup> Ibid 20.

<sup>263</sup> Ibid 20-21.

provided that the *TPA* does not affect the law relating to the Doctrine, thereby preserving its operation, insofar as the common law can operate concurrently with the *TPA*. Section 4M has subsequently been carried over into the new s 4M of the *CCA* and provides as follows:

This Act does not affect the operation of:

- (a) the law relating to restraint of trade in so far as that law is capable of operating concurrently with this Act...

The High Court of Australia considered whether s 45 was able to operate independently of common law in *Peters (WA) Ltd v Petersville Ltd and Another*.<sup>264</sup> In this case, Petersville had formed a partnership with QUF Industries Ltd in 1980 and manufactured ice-cream under the names of 'Pauls' nationally and 'Peters' nationally except for in Western Australia as Peters (WA) Ltd was selling its ice-cream under the same name already within that state. In 1983, Peters made a contractual agreement for the acquisition of the ice-cream business of Petersville and QUF Industries Ltd in Western Australia. An exclusive right was created for Peters to use the 'Pauls' trademark and that Petersville would not sell, supply or distribute to any person, frozen confections within Western Australia during the term of the agreement.

The initial judgement by Carr J, found that the agreement was unenforceable on the basis that it was an unreasonable RT. An appeal to the Full Federal Court was subsequently dismissed. On Appeal to the High Court, Peters claimed that the Doctrine had been overridden by the *TPA* and thus a ruling was unable to be made under the Doctrine. Gleeson CJ, Gummow, Kirby, and Hayne JJ found that the *TPA* was able to operate independently from the Doctrine. On this basis it can be understood that common law has the ability of striking down a RT even if it falls outside

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<sup>264</sup> [2001] HCA 45 ('*Petersville*').

the operation of Part IV of the *TPA*. This has now been carried over into s 4M of the *CCA* to prevent the common law from encroaching upon s 45 and other sections under Part IV *CCA*.

These legal developments, despite taking place over 30 years ago, were an important step in recognition of the need for an economic foundation in *TPA* evolution by preventing the Doctrine, together with its deficiencies and difficulties, from being imported into s 45. It also provided s 45 as amended, with genuine economic authenticity by removing the common law test of reasonableness and substituting it for one of competition which owed more to economic theory in comparison to the archaic legal concepts behind the Doctrine. This was in every possible manner, a triumph for the economic theory of law.

### 3.4 CLEARANCES AND AUTHORISATIONS OF ANTI-COMPETITIVE CONDUCT

As described in the introduction to Chapter 3, a general analysis and recommendation of reform with respect to the *CCA* in relation to anti-competitive conduct is not intended to be engaged in by the author. It is sufficient to state that, from the early days of the *TPA*, the legislation has been regularly reviewed and refined such that it now represents a culmination of over 35 years of critique and law reform. As with any important piece of legislative development, there is a vast amount of case law and academic legal commentary available to those who are interested.<sup>265</sup> Analysis of this material is simply beyond the scope of this thesis and largely irrelevant to the subject of RT contracts. Instead, the author will focus the next section on what appears to be a relatively neglected territory in RT contracting.

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<sup>265</sup> See generally, Alex Bruce, *Australian Competition Law* (LexisNexis Butterworths Australia, 2<sup>nd</sup> ed, 2013); Stephen Corones, *Competition Law in Australia* (Thomson Reuters, 5<sup>th</sup> ed, 2010); Russell Miller, *Miller's Australian Competition and Consumer Law Annotated* (Thomson Reuters (Professional) Australia, 34<sup>th</sup> ed, 2014).

Earlier in this chapter, the subject of Clearances was briefly mentioned. Clearances had been established by virtue of s 92(1) of the *TPA*. At its inception, the Whitlam Government hailed Clearances as an innovative and unique effort which would provide some respite and clarity to the operation of s 45 by offering businesses the ability to obtain approval of contracts, arrangements or understandings which may offend s 45.<sup>266</sup> Until 1 July 1977, the TPC could grant Clearance for a restrictive trade practice if, on application by a party, it believed that any RT or commerce did not have or would not be likely to have a significant effect on competition. It was therefore a surprise to some that less than 3 years after its initial debut, the entire operation of Clearances was abolished via the *Trade Practices Amendment Act 1977* (Cth). Previously granted Clearances were given public benefit status and converted to Part VII Authorisations. The reason for the abolition was characterised in a general manner by Mr John Howard, the then Minister for Business and Consumer Affairs during the Second Reading Speech of the *Trade Practices Amendment Bill 1977* as follows:

Whatever justification this may have had in the early days of the legislation has now disappeared.

To continue the clearance procedure would perpetuate unnecessary interference by government in the exercise of individual economic initiative.<sup>267</sup>

In abolishing the availability of Clearances, the government suggested that it was giving more responsibility back to businesses which were urged to take their own advice, make their own decisions and accept the attached risk as to the legality of their decisions without any support or clarification from any judicial or administrative body. The impact of these changes was aptly summed up by the TPC in the following words:

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<sup>266</sup> Commonwealth, *Parliamentary Debates*, House of Representatives, 16 July 1974, 228 (Keppel Enderby).

<sup>267</sup> Commonwealth, *Parliamentary Debates*, House of Representatives, 9 December 1976, 3532 (John Howard).

With the abolition of the clearance procedure, there is now no opportunity for companies to assume their position by seeking a ruling from the Commission that they are not substantially anti-competitive...they must assess their own position and take their own risk as to the competition issue...Authorisation cannot be granted unless the public benefit test is satisfied. However, the unavailability of authorisation for conduct where the only issue is the competition issue does not mean that the conduct is, therefore, illegal; it means that the businessman must face the competition issue himself.<sup>268</sup>

In a further clarification that Authorisations could not be regarded and relied upon as a substitute for the abolished Clearance procedure, the TPC also stated the following:

...there is now no opportunity for companies to assume their position by seeking a ruling from the Commission that their conduct is not substantially anti-competitive...it must be emphasised that the authorisation procedure should not be used for cases that would previously have been appropriate for clearance and not for authorisation. It was the deliberate policy of the legislation to abolish the clearance procedure and it cannot be restored under another name. Authorisation cannot be granted unless the public benefit test can be satisfied.<sup>269</sup>

The result of the 1977 amendment is that contracting parties have since become unable to obtain any comfort in what is an essential foundation for the nurturing and development of business relationships; that is, legal certainty. Authorisation procedures currently available to businesses are largely inadequate as they rest upon the ability of parties to satisfy the ACCC that the net public benefit of their anti-competitive conduct outweighs the net public detriment. These concepts, despite continuing assistance in their clarification from the judiciary, remain vague and

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<sup>268</sup> Trade Practices Commission, Parliament of Australia, *Third Annual Report – Year Ended 30 June 1977* (1977) ¶1.48-1.49.

<sup>269</sup> Ibid.



difficult to apply in practice.<sup>270</sup> Attempts to define the concept of public benefit as ‘anything of value to the community generally, any contribution to the aims of society’<sup>271</sup> have certainly not shed any useful light. This is partly the natural result of the necessity to maintain a pliable approach to Authorisations to enable its application across a broad spectrum of commercial situations. Unfortunately, this uncertainty also creates lengthy and costly applications as the measurement of public benefit necessarily involves a high degree of vagary and is often imprecise and difficult to quantify both conceptually and economically.<sup>272</sup> Such difficulty will then naturally transpire in the legal application of determining the issue of public benefits. The TPC, in the very first case to come before it under the *TPA* noted that ‘the policy of the Act is clearly opposed to arrangements in restraint of trade or other anticompetitive practices. An application for final authorisation has a substantial onus in satisfying (the public benefit test).’<sup>273</sup>

This statement of principle and the high bar which must be overcome to succeed in an Authorisation application has been often repeated.<sup>274</sup> When deciding whether to grant an Authorisation, the ACCC must identify the public benefits and anti-competitive detriments arising from the proposed contract, arrangement or understanding.<sup>275</sup> A proper delineation of the proposed market in which the public benefits and detriments will impact is also required.<sup>276</sup> The main principles of this assessment process are adequately expressed in the Australian Competition Tribunal’s (‘ACT’) decision *Re John Dee (Export) Pty Ltd*:<sup>277</sup>

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<sup>270</sup> See, eg, *Re Howard Smith Industries Ltd* (1977) 28 FLR 385 (‘Howard’).

<sup>271</sup> *Re 7 Eleven Stores Pty Ltd* (1994) ATPR ¶41-357 (‘7 Eleven’); see also, *Queensland Cooperative Milling Association Re Defiance Holdings Ltd* (1976) 8 ALR 481 (‘Queensland Cooperative Milling’).

<sup>272</sup> *Howard* (1977) 28 FLR 385.

<sup>273</sup> *Re Queensland Timber Board* (1975) 5 ALR 501, 507.

<sup>274</sup> Warren Pengilly, ‘Why Not Reinstate Clearance of Restrictive Trade Practices as an Assistance to Small Business’ 14 *Competition & Consumer Law Journal* 53, 57.

<sup>275</sup> Damien O’Brien, ‘Pleading s 45 *TPA* Claims: The Problems Continue’ (2009) 17 *Trade Practices Law Journal* 149.

<sup>276</sup> *Ibid.*

<sup>277</sup> (1989) ATPR ¶40-938 (‘John Dee’).

First, it is for the parties seeking authorisation to satisfy the tribunal that benefit to the public is likely and that there will be sufficient public benefit to outweigh any likely anti-competitive detriment; Second, since the likely benefit and detriments to be considered are those that would result from the proposed conduct, the Tribunal is required to consider the likely shape of the future both with and without the conduct in question; and Third, the task will generally entitle an understanding of the functioning of relevant markets with and without the conduct for which authorisation is sought.<sup>278</sup>

In a similar fashion to the lack of definition of what constitutes a public benefit, the meaning of anti-competitive detriment is also undefined; although it has been described in a number of early ACT decisions as any loss to the community generally, with an emphasis on gains and losses being measured in terms of economic efficiency.<sup>279</sup> The difficulty with such a definition was recognised by a member of the ACT, Professor David Round when commenting on the meaning and construction of the term ‘efficiency’:

Efficiencies come in all shapes and sizes. Real ones and pecuniary ones, scale and scope economies; technical and allocative efficiencies; dynamic efficiencies and x-efficiencies; short run and long run efficiencies; and productive, management, distribution, buying and retailing efficiencies. Some are harder to achieve than others...Some are easier to measure, some are not. Some are mere wealth transfers. Some are of more lasting value to society than others. Do we count them all equally? Should we? Are they all of equal value to society?<sup>280</sup>

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<sup>278</sup> *John Dee* (1989) ATPR ¶40-938, ¶50-206, cited in *Corones*, above n 265, Ch 3.

<sup>279</sup> See, eg, *7 Eleven* (1994) ATPR ¶41-357; *Queensland Cooperative Milling* (1976) 8 ALR 481.

<sup>280</sup> David Round, ‘Whither Efficiencies: What is in the Public Interest? A Commentary on “The Great Efficiencies Debate in Canadian Merger Policy: A Challenge to Economic Foundations of Canadian Competition Law or a Storm in a Teacup” by Michael Trebilcock’ (Paper presented at the Fifteenth Annual Workshop of the Competition and Policy Institute of New Zealand, Auckland, 13-15 August 2004) 2-3.

Further complications also arise from the application of the *John Dee* ‘future with and without’ test which requires a comparison of the present situation with and without the conduct for which the Authorisation is sought in order to determine not the present net public benefit and detriment but rather, the future net public benefit and detriment. This approach was confirmed by the ACT in the matter of *Qantas Airways Limited*<sup>281</sup> such that the difficulty of identification and quantification of the public benefit vs public detriment is compounded by the need to highlight not only present but future efficiencies that may flow into the delineated market.

In fairness however, the author recognises that despite the difficulties associated with the maintenance of a mechanism to recognise valid exceptions to the general ban on contracts, arrangements or understandings that are anti-competitive, it remains desirable both economically and socially from a public policy perspective for such exceptions to remain. Notwithstanding their existence being a somewhat vague and cloudy haze at the best of times, the removal of Authorisations would create an even greater loss for businesses. It may therefore be justifiable to view Authorisations as a necessary derivative of society’s need for competition law that by its very nature cannot be as clearly defined and straightforward to apply as one might like. That is not to suggest however that no reform or improvement to the Authorisation mechanism can be made.

Indeed, when one reviews the short history of Clearances, it may be feasible to consider the resurrection of this additional mechanism to supplement the Authorisation mechanism. This is, in part, due to the long recognised overlap between the tests of competitive impact and public benefit such that in Authorisations, a competition evaluation is almost always embarked upon

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<sup>281</sup> (2004) ACompT 9.

before any public benefit analysis.<sup>282</sup> In this respect, the competition evaluation and the public benefit analysis can be considered mutually exclusive and capable of being assessed separately. For example, in cases prior to the abolition of Clearances, applications to clear anti-competitive conduct were often made through both Clearances and Authorisations at the same time.

The statistics taken from the Third Annual Report of the TPC show that 3 Authorisations were granted in respect of s 45 restraints in 1975-1976 and 15 in 1976-1977 but 759 Authorisation applications were denied in 1975-1976 and 948 denied in 1976-1977 because Clearances had previously been granted based on a competition evaluation alone.<sup>283</sup> These statistics support the argument that during their short lifetime, Clearances were heavily utilised in the business community when the community faced the uncertainty of whether a particular conduct would amount to being anti-competitive and therefore, in breach of s 45. The result should not be surprising because, if an application for immunity can be decided at the competition stage, in almost all instances, the decision maker need not consider the more obscure concept of public benefit. Mr Ron Bannerman, the First Chairman of the TPC continued to recognise the importance of Clearances to the community some 25 years after the enactment of the *TPA*. In his article, 'Reflections on the Changing Role of the Commission', published in 2000, Bannerman noted:

Progressively since 1977, however, it has become more obvious that companies do not wish to carry their own risk in major cases under any of the sections if they can get from the Commission the comfort of what amounts to a 'non-statutory clearance' ...<sup>284</sup>

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<sup>282</sup> Trade Practices Commission, Parliament of Australia, *Third Annual Report – Year Ended 30 June 1977* (1977) ¶1.57.

<sup>283</sup> *Ibid* Table 3.

<sup>284</sup> Ron Bannerman, 'The *Trade Practices Act*, Reflections on its Twenty-Fifth Anniversary' 8 *Trade Practices Law Journal* 166, 168.

This argument is further supported by the fact that, since the abolition of Clearances, the TPC and ACCC have concluded that the public benefit criterion of Authorisations may be satisfied through contracts, arrangements or understandings that ‘assist the competition process’.<sup>285</sup> This approach to the grant of Authorisations is clearly founded upon and couched as a competition evaluation. Conceptually, it would seem that legislative policy surrounding Authorisations are somewhat irregular given that the ACCC is mandated with power to approve anti-competitive conduct based on public policy (and in turn, based on competition benefits) but it cannot grant approval based on findings that a proposed contract, arrangement or understanding did not have or would not be likely to have a significant effect on competition.

A prime example of this shortfall was the ACCC’s own observation in its Authorisation Paper on Collective Bargaining and Boycotts<sup>286</sup> in which a number of industries were noted as having been granted Authorisations. These ACCC decisions involved collective bargaining arrangements by chicken growers, dairy farmers, sugar cane growers, lorry owner drivers, TAB agents, hotels, newsagents and small private hospitals.<sup>287</sup> In reaching a decision to authorise the collective bargaining practices relating to the above industries, the ACCC found in every decision in which Authorisation was granted that the competitive detriment was negligible. This observation lends support to the argument that a public benefit analysis is not necessary except perhaps in the most unusual of cases. In ordinary terms, a competition analysis is all that is required. Clearances therefore remain as a more logical, efficient and manageable tool in comparison to Authorisations when dealing with the bulk of applications for immunity from the CCA. The case for the resurrection of Clearances to address potential s 45 infringements is compelling. Indeed, it may

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<sup>285</sup> *Foodland Group, Super Value Group, Speedy Family Fare Group, Cut Price Stores Group, Four Square Group, Nifty Thrifty Low Price Stores Group* (1978) ATPR 17089.

<sup>286</sup> Australian Competition and Consumer Commission, Parliament of Australia, *Authorizing and Notifying: Collective Bargaining and Boycott Issues* (2004) 9.

<sup>287</sup> *Ibid* 8.

seem counterproductive for legislative policy not to sanction contracts, arrangements or understandings which are not illegal on face value. Surely, so the question goes, the legislative purpose of an ACCC application should be to apply first for sanction of conduct which runs the risk of breaching the *CCA*. It therefore makes little sense that the administrative exemption is not based on the same test as that of infringement.

The author is not alone in making the case for the resurrection of Clearances. The Former Commissioner of the TPC, Dr Warren Pengilley, argued in a 2006 publication of the *Competition & Consumer Law Journal*:

Because of the abolition of clearance and the inability, in the vast majority of cases, to demonstrate public benefit, the result of the 1977 amendments is that parties are presently generally unable to obtain what they most require in the interest of certainty, ie, a ruling that their conduct does not breach the *TPA*.<sup>288</sup>

Pengilley's argument for reinstatement of Clearances was largely centred on its perceived benefit to the business community. He noted that above and beyond the provision of certainty to businesses, the effect of allowing Clearances would extend to encourage pro-competitive activity that would otherwise not have been engaged in to the detriment of the community:

The argument in this opinion piece is that consideration should be given to the reinstatement of a clearance procedure for restrictive trade practices. Abolition of the clearance procedure previously available was effected on the basis that the then TPC was perpetuating 'unnecessary interference by government'. I have never seen any evidence of this. To the contrary, I have seen evidence that significant pro-competitive activity has not taken place because of the inability to

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<sup>288</sup> Pengilley, above n 274, 57.

have an administrative procedure available which would give business certainty. The arguments for reinstating Clearances are, in my view, persuasive...<sup>289</sup>

As an illustration of the above, certain joint activities engaged in by businesses to enable them effectively to compete against larger corporate entities may serve to increase competition and stimulate the provision of a greater variety of goods or services.<sup>290</sup> The benefits of these joint activities may otherwise not be available to the consumer if businesses did not have the certainty of Clearances.

From a cost-benefit analysis point of view, Pengilley made a further observation that reinstatement of the Clearance procedure is unlikely to result in a burdensome administration exercise for the Government. His observations are noted as follows:

The Clearance procedure, if reinstated, would in all likelihood be sparingly used. We must adapt to the times. Competition is better understood now than in 1974. An analogy can be drawn with the still available s 47 competition clearance procedure. The automatic legality of exclusive dealing arrangements subject to a competition test on mere lodgement of a clearance application has resulted in recent times in very few clearance lodgements despite the legal protection such lodgement gives.<sup>291</sup>

If legislators remain unconvinced that, if resurrected, the Clearance procedure would not result in a significant resource drain, it is also possible to create a deterrent to prevent businesses from seeking Clearances without due consideration and need by imposing a cost for the lodgement of

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<sup>289</sup> Ibid 62-63.

<sup>290</sup> See, eg, *Pharma Buy* (1975) C4272; *Magnetic Electric Application* (1975) C939; *Donlan Liquor Market* (1975) C763.

<sup>291</sup> Pengilley, above n 274, 63.

every Clearance application. The formula to determine an appropriate cost structure can take several forms and account for various considerations (e.g. the number of Clearance applications received, resources required to determine a Clearance application, concessions that may be provided to small businesses, turnover or profitability of the parties seeking Clearance, the nature of the industry for which Clearance is sought and the appropriateness of a tiered cost structure). Certain exemptions to pay an application cost may also be created for organisations such as charities, not for profit entities, community based organisations, schools and religious institutions. If the application cost is seen to be overly burdensome, consideration may be given to the possibility of refunding the cost in full or in part where Clearance is ultimately granted. It is therefore evident from the great many possibilities noted above that the expected limited drain of resources to resurrect Clearances can be largely mitigated.

As an alternative to the proposed method of reinstating Clearances, one additional possibility is to reform Authorisations by separating the steps that are required to successfully obtain Authorisation. If the process of Authorisations were divided into a two-step process whereby the former step involves a consideration of the competition test and the latter step involves a consideration of the public benefit test, one may find that the benefits associated with Clearances may be carried over and into Authorisations without the direct need to reinstate Clearances. Operationally then, the second step will only be required if adjudication of the competition test reveals a contract, arrangement or understanding that has the purpose, or has or is likely to have the effect of substantially lessening competition. Accordingly, if the proposed contract, arrangement or understanding does not fall foul of the competition test, there is no further need to invest the time, effort and resources of parties to investigate the more complex matter of public benefit.



Adoption of the alternative approach may also be desirable as historically most Authorisations were coupled with a Clearance application or vice versa which, in effect, resulted in the unnecessary and onerous administrative burden of processing 2 independent applications. Given that Authorisations were historically placed on hold pending the outcome of the Clearance determination, one can logically conclude that the process of law reform to combine the first and second steps described above may be sensible and economically desirable.

By re-implementing the Clearance procedure in relation to s 45 into the CCA, many benefits can be grasped. Take for instance a fictional example that involves Pfizer Australia ('Pfizer'), one of Australia's largest pharmaceutical researchers, developers and manufacturers of pharmaceutical products. If Pfizer contracted with Queensland Health to provide all pharmaceutical products in relation to surgeries at a discounted rate on the basis that Queensland Health was unable to obtain any product from a Pfizer competitor, prima facie it would be in contravention of s 45. This is because Queensland Health operates over 60% of hospitals in Queensland and other companies would be unable to sell their surgically-related pharmaceutical products to these hospitals.<sup>292</sup> In applying for Clearance of this agreement, consideration could be given to the proposition that, whilst Pfizer has an exclusive agreement to supply to over 60% of hospitals in Queensland, it will not be substantially lessening competition because in 2010-11 there were 440,566 surgeries being conducted in Queensland, of which more than 65% were to be found within private hospitals, and thus Pfizer will only have an exclusive agreement to supply to 35% of the market for surgical equipment.<sup>293</sup> Consequently, other major companies with substantial market share, such as AstraZeneca, Aspen Asia Pacific, GlaxoSmithKline and Merck Sharp & Dohme will be able to continue supplying products to a significant market requiring surgically-related pharmaceuticals products. While Pfizer may or may not be ultimately successful (much of which would depend

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<sup>292</sup> Australian Institute of Health and Welfare, *Australian Hospital Statistics 2010-11*, Report No 43 (2011).

<sup>293</sup> Ibid.

on whether the proper delineation of the market is determined to be the hospital market or the market for surgical equipment), the Clearance process can assist in an early resolution of such competition issues.

Chapter 3 has introduced an additional complexity to RT contracts whereby contracts, arrangements or understandings may be unenforceable if they have the purpose or have or are likely to have the effect of substantially lessening competition. This is an entirely separate legislative regime to the common law Doctrine and founded upon economic principles of workable or effective competition. The historical intervention by Parliament to separate the Doctrine from the legislative operation of s 45 following the High Court's decision in *Quadramain* was a correct and economically justifiable approach which cemented all future interpretation of s 45 through economic theories of law. Indeed, had Parliament decided not to amend the original wording of s 45, the likely result would be the reading into s 45 of all the defects of the Doctrine. Such a result would have severely crippled the government's legislative attempt to control anti-competitive conduct in Australia. The separation of the Doctrine from s 45 therefore served as an important milestone by providing genuine economic authenticity to the *TPA* through the substitution of the common law test of reasonableness for one of competition.

As an additional exception mechanism and to provide the business community with a greater sense of certainty when contracting, the author also recommended the reinstatement of the now defunct Clearance procedure for s 45 contracts, arrangements and understandings that do not have or are not likely to have, a significant effect on competition. This was argued to be beneficial as there is a long-recognised overlap between the tests of competitive impact and public benefit such that in almost all Authorisations, a competition evaluation is embarked upon before a public benefit analysis. The author concludes that, if reinstated, Clearances will act as an efficient

instrument in combination with Authorisations when dealing with applications for immunity from anti-competitive conduct.

Chapter 4 will now present the thesis statement and in doing so, bring together the various common law and legislative commentaries, case law analysis, historical observations and economic theories which were covered in Chapters 1 to 3.

## **CHAPTER 4: PROPOSITIONS OF LAW REFORM**

The evolution of the Doctrine has taken place over the last 400 years as the common law attempted to maintain its relevance in significant periods of societal and economic advancements, from the age of the guilds through the age of the industrial revolution and now the age of information. As the guild systems broke down, the English Courts remolded the Doctrine in its highly restrictive form to recognise the appropriateness of enforcing certain restraints in circumstances where an RT contract was, for example, associated with the sale of businesses or incorporated into employment contracts. Tests of reasonableness and public policy were devised to provide contracting parties with an increasingly complex and finite balance between the freedom to contract vs the freedom to trade. In more recent times, many distinguished commentators have expressed ongoing dissatisfaction at the present state of the Doctrine in its application to modern day challenges. The use of cascading clauses to address the uncertainties of RT contracts did little to advance the agenda of maximising certainty. Against the backdrop of the numerous difficulties currently faced by the operation of the Doctrine in Australia, the author will now present a combination of possibilities for law reform.

### **4.1(a) ABOLISHING THE RESTRAINT OF TRADE DOCTRINE**

In its most radical form there is merit in the argument for the abolition of the Doctrine in its entirety. With the advent of technology and the globalisation of industry and commerce, the reasons for the continuing operation of the Doctrine have diminished to such a degree that one may be justified in purging it from the common law. By abolishing the operation of the Doctrine, contracting parties would be capable of entering into restraints knowing that the enforcement of restraints cannot be thwarted by the test of reasonableness.

At its heart, concerns associated with the abolition of the Doctrine stem from the uneasiness and possible inequity of enforcing RT contracts which contain an unreasonable restraint. However, the concept of reasonableness, as it is applied in RT contracts, was critiqued in Chapter 2 and found to be a most unsatisfactory test, the jurisprudence of which is largely comprised of indeterminate references from judgment to judgment, thereby providing no more than an opportunity for a value judgment on the facts of each case. The current methodology of observing general behavioural patterns in a social context to assess whether a restraint is reasonable often turns on what strikes the judge as being what can be loosely termed as judicial common sense. The tasks of finding intangible elements of reasonableness of duration or the geographic extent of a tie, amongst other considerations, is often so lacking in probative value such that a cursory review of Australian decisions may leave the reader more confused than enlightened about the likelihood of a particular restraint being upheld. Much of what is expressed here was demonstrated in Chapter 2 to the extent that even members of the judiciary have frequently been cited as finding the difficulties insurmountable and open to conflicting outcomes.

This argument alone cannot sound the death-knell of the Doctrine as the author recognises that much of what the judiciary is engaged to do is to find on difficult matters of fact. Often, the law in litigation is clear but it is the application of law to the facts that is the more difficult task. Indeed, more will be required and may be capable of being better justified by striking at the heart of the Doctrine through an examination of the rationale of the Doctrine's principal concern that a covenantor in an RT contract may suffer from some species of 'unfairness' that is somehow unique to the Doctrine and therefore deserves separate recognition and treatment in law. The question of fairness may be better explained in colloquial terms whereby concern arising from the abolition of the Doctrine arises when a covenantor is bound to continue with a contract in which a restraint is unduly wide such that by enforcing the restraint, the Court will render the covenantor 'unprofitable'. In other words, the test of reasonableness can be also loosely expressed as a

concept of fairness which dictates that the common law is required in RT contracts, to assess the fairness of the bargain reached between parties to ensure that the covenantor is not rendered ‘unprofitable’ by entering into an unduly wide restraint. ‘Profitability’ is given a wide meaning by the author and may encompass monetary, non-monetary and opportunity based gains or losses. It can also extend to the gains or losses outside of the contracting parties’ direct grasp and into the field of externalities, whether positive or negative.

On this subject, it has often been expressed that the law is not concerned with the adequacy or relative value of consideration reached between parties to a contract. In the leading case of *Chappel v Nestle*,<sup>294</sup> Nestle advertised that it would supply a music record to anyone who sent it a sum of money and 3 chocolate wrappers. Nestle had engaged in this advertising campaign in a bid to increase sales of its chocolates. The central issue for the House of Lords was whether the wrappers could constitute proper consideration for the sale of the music record. Lord Somervell of Harrow noted in his judgment:

A contracting party can stipulate for what consideration he chooses. A peppercorn does not cease to be good consideration if it is established that the promisee does not like pepper and will throw away the corn.<sup>295</sup>

The law of the land in relation to consideration is clear. The law is not traditionally concerned with the relative value of bargains. Its role is not to assess the commerciality of bargains reached or the consideration given in exchange of such contracts in the absence of a Recognised Contractual Wrong.

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<sup>294</sup> [1959] 2 All ER 701.

<sup>295</sup> Ibid 712.

In the absence of a Recognised Contractual Wrong, if Joe Bloggs wishes to sell his house to John Doe for \$500,000 when the true value of his house is \$750,000, the law is not concerned and will not interfere with such a contract purely on the basis of what appears to be an uncommercial decision on the part of Joe Bloggs. Similarly and by extension of this example, if Joe Bloggs wishes to contract with John Doe to restrain himself from competing against John Doe in a location and for a duration that is agreed to by both parties, it would seem to be at odds for the law to interfere with such a restraint in the absence of a Recognised Contractual Wrong, despite the potential gravity of such a decision on the part of the contracting parties.

In addition, the fact that an RT contract may restrain a party for an extended period of time and across a great geographic region and therefore requires intervention is equally unconvincing. Many examples can be provided in contracts outside of RT whereby parties sign up to obligations that are extended in geography or time<sup>296</sup> to the extent of having the effect of permanency. In fact, with the exception of matters engaging in RT, almost all contracts can be extensive in its coverage of geography or time if parties so wish. The sale of property from Joe Bloggs to John Doe is, for example, a decision of a permanent nature. If a principle of law is questioned on the basis of the extent of time or geography during which parties are bound or by the gravity of their decisions, the law of contracts will suffer from a fundamental breakdown in functionality. The continuing operation of the Doctrine therefore cannot be justified on the basis of time, geography or gravity of the subject matter either.

On the public interest limb of the Doctrine, it was demonstrated in Chapter 2 that historically, Courts are not interested in the entertainment of protracted debate on the said subject in deciding

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<sup>296</sup> Eg, licenses of pharmaceutical products, leases of residential crown land in the Australian Capital Territory, settlement agreements reached between litigating parties, sale of business agreements and residential domestic waterfront licences.

the enforceability of a restraint. Ordinarily, private contracts between parties do not create a negative externality to such an extent that law should be interested in regulating these contracts. As most private contracts affect only the parties that are contracting, the argument that public policy is normally best served by the legal recognition and enforcement of contracts that are duly formed is persuasive. A real question therefore needs to be asked as to whether there is any ongoing purpose in the continuing operation of this limb of the Doctrine, especially in the face of a substantial amount of jurisprudence that points to the redundancy of the public interest limb.

The answer to the above question partly lies in the observation that, in the modern world of contracts, recognition has to be given to matters of law and public policy that are well developed in comparison to the times during which the Doctrine was originally formulated. For example, the principles behind competition law and the economic necessity for its existence and ongoing operation as it relates to RT contracts are well recognised. Indeed, the relevance of the limited role that public interest has in RT contracts may be generally condensed to matters of Recognised Contractual Wrongs. Insofar as existing laws provide for causes of action and remedies for the same, it is fair to state that, at the time the Doctrine was conceived, the Recognised Contractual Wrongs were either limited in their development or altogether non-existent. It is therefore an understandable position for the Doctrine to have been developed with a second limb of public policy which then provided, at least theoretically, the Courts with discretion to adjudicate and strike down restraints by reason of public policy.

It is perhaps an obvious matter but one that should be noted for completeness that matters of public policy, as they are applied to RT contracts, are generally also applicable to other forms of contracts that are not related to RT. In line with this observation it is expected that general matters of public policy will continue to be refined by the legislature or common law as the need arises and will have ongoing application to contracts in RT as well as other forms of contracts



generally. If this argument is accepted by the reader, it will also be logical to conclude that the specific limb of public interest in the Doctrine is obsolete and should be abolished in practice.

In considering the abolition of the Doctrine, two other questions that should be asked are whether the Recognised Contractual Wrongs are sufficient in protecting contracting parties that seek to contract in RT if the Doctrine was abolished and also, whether the abolition of the Doctrine will adversely result in a loss of rights to parties that seek to contract with each other. A number of observations may be made in relation to the above.

As a starting point, when one examines the breadth of factual situations in which the Recognised Contractual Wrongs provide coverage and protection for, one will recognise that from a timing perspective, contracting parties are protected from a myriad of issues from pre-contractual dealings all the way through to post-termination of an RT contract. At every stage of the contract (including pre-contract and post-contract), parties are subject to the scrutiny of the Courts in such an extensive manner against wrongs that may be committed in the contracting process. Many of the Recognised Contractual Wrongs are focused specifically on the process of contract formation and the principles that govern the relationship between parties including their representations and actions. It also extends to the relative bargaining positions of the parties at the time they contracted with each other as well as their capacity to enter into contracts. Its catchment extends yet again to regulate against technical irregularities and also the protection of fair trading practices.

Insofar as competition is concerned, ss 45 to 50 of the *CCA* provide a comprehensive suite of statutory protection in the name of the public interest with coverage for matters that include contracts, arrangements or understandings which restrict dealings or affect competition, misuse of

market power, predatory pricing, exclusive dealing, third line forcing, resale price maintenance, mergers and cartels.

There is therefore no denying that the tentacles of the law are already far reaching and provide legal coverage across a wide set of conceivable issues that may arise in private between contracting parties and also in public matters of competition and market maintenance. This thesis however, does not suggest that Recognised Contractual Wrongs can operate as a substitute for the Doctrine. After all, the Doctrine operates in an isolated corner of the law of contracts and stands alone in its principles. The subject matter in which it seeks dominion is also isolated and not directly impacted by the application of Recognised Contractual Wrongs to RT contracts. Despite working hand in hand with other doctrines such as the doctrine of severance and the blue pencil rule, if the Doctrine were to be abolished, the proper form of examination of its effect is not whether the Recognised Contractual Wrongs can supplement or substitute the Doctrine but whether contracting parties in RT will be adversely affected.

In short, as the modern Doctrine is not interested in matters of competition, the obvious answer as it is applied to matters of competition is that abolition of the Doctrine will have no significant impact to contracting parties that seek to contract in RT. It is less simple however, when decoding the effect of abolition on the private rights of contracting parties. When considering whether a contracting party will lose a right that it would otherwise enjoy, there is no denying that abolition of the Doctrine will take away and fundamentally change the landscape of RT contracting in Australia. For starters, the shortcomings of the cascading clause need no longer be tolerated. Parties will be able to contract freely and without interference from an antiquated Doctrine that is at its core, economically inefficient. Problems of decoding what is a reasonable restraint vs. an unreasonable restraint can be avoided and parties can finally be certain that RT clauses which are agreed to will be enforceable and upheld. Issues associated with considering

actual breaches vs imaginary breaches will no longer arise and the age old enigma of the profiteering usurper of RT promises will finally be cast into the pages of legal history. In the eyes of the law, these fundamental changes to the RT contracts landscape can only result in a better outcome for those that seek to contract in RT. The reasons for the abolition far outweigh the reason or reasons for the maintenance of the Doctrine, the analysis of which was considered earlier in this chapter. Whilst it is beyond the scope of this thesis to extend the analysis into addressing the specific nuances of each and every Recognised Contractual Wrong, what is important and useful to remember in the back of ones' mind when questioning the adequacy of protection proffered by the Recognised Contractual Wrongs is that the law is not static. The law of each and every Recognised Contractual Wrong is ever-evolving to match the challenges brought by society and the needs of contracting parties. What this chapter has sought to establish thus far, is that a significant collection of laws already protect private and public interests when parties contract in RT. They are by no means perfect but they are comprehensive and extend across the time spectrum from the pre-contractual to the post-contractual. In themselves, the Recognised Contractual Wrongs do not render the Doctrine redundant. Indeed, as pointed out before, the subject matter of the Doctrine and the subject matter of each of the Recognised Contractual Wrongs (including that of competition) deal with different matters and interests. To suggest that the Recognised Contractual Wrongs render the Doctrine redundant would be overstepping the boundaries of the Recognised Contractual Wrongs. The proposal for abolition of the Doctrine stands on its own merits for the reasons given throughout Chapters 1, 2 and 3. The contribution brought about by the Recognised Contractual Wrongs is that if the Doctrine is abolished under its own merit, there is an existing and workable legal structure protecting parties that engage with each other and this set of legal structures may provide the appropriate causes of action against those that seek to breach any recognised legal obligations under the contract. Change is never easy and abolishing a law that has its roots as deeply entrenched as the Doctrine

will require a mountain of determination but one that this thesis argues will benefit contracting parties in future years to come.

#### 4.1(b) RESTRAINT OF TRADE AND COMPETITION LAW

The historical reasons for the creation of the Doctrine were associated with the social and economic problems of the day. Three reasons for the creation of the Doctrine may be identified. The first reason was to prevent traders from having exclusive economic control over the pricing of goods.<sup>297</sup> Law makers were particularly interested in the pricing of food which may be aptly put as being a greater concern at a time when food supplies were scarce and the possibility of famine was a common fact of life. The second reason can be associated with the stifling of guild powers which existed to protect its members through the reduction of competition from foreigners and strangers to the guild.<sup>298</sup> The third reason concerned itself with royal grants of monopolies.<sup>299</sup>

Over 400 years later, much can be said about the ongoing need for economic regulation despite the changing nature of what is regulated. One might add that the role of economic regulation to prevent anti-competitive conduct is even more prominent today in an advanced network economy than the more traditional localised economies of medieval times. This is particularly so as contracts that affect competition have an increasingly national, international or even global reach which may affect literally billions of people. Examples of competition cases such as the

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<sup>297</sup> Robert Wilberforce, Alan Campbell and Neil Elles, *The Law of Restrictive Trade Practices and Monopolies* (Sweet & Maxwell, 2<sup>nd</sup> ed, 1966) 115-124.

<sup>298</sup> Heydon, above n1, 3-5.

<sup>299</sup> Ibid 6-7.

European Union's investigation into Google's Android licensing practices,<sup>300</sup> the United States Department of Justice's case against Apple's e-books pricing strategies<sup>301</sup> and the United States Department of Justice's case against Microsoft's bundling of its operating systems with its web browser<sup>302</sup> have the potential to globally affect the masses. Much can therefore be said of the need and place of competition law in society.

Economic analysis undertaken of the effects of anti-competitive RT contracts in Chapter 3 focused on the positive and negative effects of externalities when parties contract. It was noted that if society desired the maintenance of a mixed market economy, it was necessary for law to intervene in circumstances where the negative externality of an RT contract is so great as to cause a significant reduction in competition. It may be further said that accordingly, whilst not a perfect solution, the hesitation of applying the common law public interest test by the Courts is partly remedied by the CCA with respect to the public interest of preserving competition in the market.

Whilst the majority of RT contracts do not have the potential to impact on competition as understood pursuant to the CCA, contracts, arrangements or understandings that have the effect of substantially reducing competition in the market continue to have a place under the microscope of the CCA. Despite the tumultuous history of the development of s 45 of the CCA through the times of *Quadramain* and the *Trade Practices Amendment Act 1977* (Cth), s 45 remains a cornerstone of competition law in Australia and for the purposes of this thesis, the author sees no justifiable reason as to why it should not continue to operate to invalidate RT contracts that have the effect of substantially lessening competition.

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<sup>300</sup> Stuart Dredge, *Google Facing European Antitrust Scrutiny of Android Device Deals* (31 July 2014) The Guardian <<http://www.theguardian.com/technology/2014/jul/31/google-european-antitrust-android-regulators>>.

<sup>301</sup> *United States v Apple Inc et al* (12 CIV 02826, 5 September 2012).

<sup>302</sup> *United States v Microsoft Corporation*, 253 F 3d 34 (2001).

On a point of law reform however, Chapter 3 outlined the history and premise behind Clearances. At the time when Clearances were abolished it was said that the government was giving more responsibility back to businesses. In reality, businesses were forced to accept the competition risks associated with contracting and in the event that they were to misjudge those risks, severe and costly penalties would be imposed. The continued availability of Authorisations partly offsets this heavy burden but remains insufficient as the only instrument upon which businesses may rely to protect themselves from anti-competitive contracts, arrangements or understandings.

In this light, the arguments for the resurrection of Clearances for s 45 infringements are compelling. Logical argument dictates that contracts which are not anti-competitive should be sanctioned and upheld. It was noted by the author that if the legislative purpose of an application to the ACCC was to apply to sanction conduct which ran the risk of breaching the CCA, the test which should be applied by the ACCC should also be based on that of infringement so as to invalidate contracts only if they are an actual infringement of the CCA.

The principal benefit brought about by resurrecting Clearances as they relate to RT contracts is clear. On the one hand, the Australian public requires the protection of s 45. Certain RT contracts which are entered into between parties may breach the section but the application of the competition criterion to RT contracts is often difficult to decide with precision when parties are forced to take their own advice. On the other hand, businesses need clarity capable of being produced in a cost efficient, timely and effective manner. If the proposed conduct which they wish to engage in does not create an anti-competitive outcome, Clearances may provide the balancing instrument capable of bringing the interest of businesses and the Australian public closer to equilibrium.

An alternative method of achieving the same purpose (and arguably a simpler and cheaper method to oversee administratively) is to amend the existing Authorisation procedure by dividing it into a two-step process. The first step would involve a formal consideration of the competition test and the second step would involve consideration of the public benefit test, if warranted. By amending the Authorisation procedure instead of resurrecting Clearances, the benefits associated with Clearances may be carried over into Authorisations. From an operational perspective, the public benefit test (which is a more difficult test to adjudicate and one that requires a significant devotion of resources) will only be required if adjudication of the competition test results in the effect of substantially lessening competition.

#### 4.2 ALTERNATIVES TO ABOLISHING THE RESTRAINT OF TRADE DOCTRINE

As with most matters involving law reform, evolution of law is generally far easier for law makers to digest when compared with a legal revolution, and law reform of the Doctrine is no exception. In the context of this paper, a revolution in the field of RT would be to abolish the Doctrine. Notwithstanding its merits, the abolition of the Doctrine is perhaps a pill that many law makers will find difficult to swallow, especially given the long and rich history that the Doctrine has enjoyed in the common law. This remaining chapter will therefore recommend law reform from a softer and perhaps more palatable angle in the spirit of continuing law reform from an evolutionary perspective.

##### 4.2 (a) INDEPENDENT LEGAL ADVICE

Lessons may be learnt from other areas of law in matters whereby the common law or statute have identified certain contracts that may be particularly prejudicial if parties were to execute them without being legally advised. One such category of contract that may be cited is financial

agreements under s 90 of the *Family Law Act 1975* (Cth) ('FLA'). Provision is made pursuant to the FLA for parties in a marriage or in a de facto relationship to enter into an agreement about financial arrangements between the contracting parties should the marriage or de facto relationship break down. Financial agreements may be made before, during or after a marriage / de facto relationship. However, for a financial agreement to be legally binding, the contracting parties must receive independent legal advice before executing the agreement. Section 90(g)(1b) of the FLA provides as follows:

...a financial agreement is binding on the parties to the agreement if, and only if before signing the agreement, each spouse party was provided with independent legal advice from a legal practitioner about the effect of the agreement on the rights of that party and about the advantages and disadvantages, at the time that the advice was provided, to that party...<sup>303</sup>

This prerequisite to the finding of finality and binding nature of financial agreements is founded on the concept of 'informed consent' which aims to put persons in a position whereby an objective degree of information is imparted to a contracting party before consent is given through the act of executing a contract.<sup>304</sup> By requiring parties to obtain independent legal advice pursuant to s 90(g)(1b), Parliament expressly carried over the concept of informed consent into financial agreements.

By extension of the common law, the concept of informed consent has also featured in matters involving mortgages, loans and guarantees. In this context, a prerequisite of many lenders in Australia before a loan is approved is for borrowers or guarantors to obtain independent legal advice prior to execution of relevant security contracts. In the leading case of *Commercial Bank*

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<sup>303</sup> FLA s 90(g)(1b).

<sup>304</sup> Jessica Berg et al, *Informed Consent* (Oxford University Press, 2001) 41-75.



of *Australia v Amadio*,<sup>305</sup> the High Court held that an elderly, unsophisticated migrant couple who agreed to give security over their home for what they understood to be a limited sum over a short time to assist their son were themselves persons that were subject to a special disadvantage which was or ought to have been known to the bank, given their dealings with the couple. As the loan documents involved liability for an unlimited time and amount and this was not made known to the couple, the High Court decided that it was unconscionable for the Bank to rely on the security and to enforce the mortgage.

In the years following the High Court's decision in *Amadio*, lenders sought to transfer the risks associated with the enforcement of a mortgage or other security in the event of a default to the borrower and the borrower's solicitor.<sup>306</sup> The question of whether the borrower has had the benefit of (or at least has been offered the opportunity to obtain) independent legal advice is especially important for third party guarantors who often obtain no tangible financial benefit under the loan, despite incurring substantial risks. Unlike financial agreements, this form of practice has become prevalent in the banking and finance industry despite there being no legislation requiring borrowers or guarantors to obtain independent legal advice prior to the execution of contracts.<sup>307</sup> This obligation therefore arises purely from contract alone. In that respect, it has become an industry standard in comparison to a standard mandated by legislation. Notwithstanding this, various law societies in Australia have issued guidelines and recommendations over the years to assist lawyers in carrying out the advisory component of these contracts. In addition, the Law Society of New South Wales has not only issued guidelines for best practice but also made provision for rules of professional conduct.<sup>308</sup> Rule 45 covers,

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<sup>305</sup> (1983) 151 CLR 447 ('*Amadio*').

<sup>306</sup> Brian Horrigan, *Focus: Unconscionability Breaks New Ground – How the ACCC Test Cases Affect Banks* (15 October 2001) Allens Linklaters <<http://www.allens.com.au/pubs/baf/banking2.htm>>.

<sup>307</sup> *Ibid.*

<sup>308</sup> *Revised Professional Conduct and Practice Rules 1995* (NSW) r 45.

amongst other matters, issues relating to the nature of advice that solicitors must provide, contents of the certificate being provided to the lender, the form of acknowledgement by clients that advice has been received, identification of proposed signatories of documents and the independence of the certifying solicitor. This comprehensive framework seeks to ensure that clients are in a position whereby they are objectively better informed through a prescribed and highly regulated procedure prior to their execution of contracts involving a borrower or third party mortgagor, guarantor, surety mortgagor or indemnifier providing security for the borrower.

The final example which the author will draw upon concerns certificates issued for the purpose of franchise agreements. The Franchising Code of Conduct requires that before a franchise agreement is entered into, the franchisor must receive from the prospective franchisee, a signed statement that the prospective franchisee acknowledges in writing that they have received advice or elected not to seek advice.<sup>309</sup> The standard of informed consent is, from this perspective, more relaxed in comparison to financial agreements under the *FLA* whereby parties must receive advice in order for the financial agreement to be binding. In addition, the Franchising Code of Conduct allows the advice to be rendered by an independent legal advisor, business advisor or accountant, thereby lowering again the standard required.

The importation of the concept of informed consent into RT contracts may be a desirable but partial solution which may reduce the number of contracting parties from successfully arguing that they were uninformed, misinformed or simply ignorant of the burdens that come with signing such contracts. Whilst it does not present a full and unequivocal solution to the problems faced between contracting parties, it does allow parties to position themselves one step closer to the goal of increasing certainty when parties contract in RT. By turning attention to better balancing

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<sup>309</sup> *Trade Practices (Industry Codes – Franchising) Regulations 1998* (Cth) ('Franchising Code of Conduct').

the competing needs of contracting parties whilst preserving the overriding goal of contract legitimacy and enforcement, it may be suggested that the need to obtain independent legal advice for the covenantor is a welcome form of protection for all parties that enter into a restraint.

Whether this recommendation is adopted as a statutory requirement in order for an RT contract to be enforceable however, is a more difficult proposition. It would defeat the purpose of promoting contract legitimacy if parties that entered into a restraint without independent legal advice were able to absolve themselves from the restraint by reason of not obtaining the advice prior to the execution of that contract. Such a result would be regrettable and therefore the strict hurdles that are applied by statute with respect to financial agreements under s 90 of the FLA would not be advisable in this instance. Instead, where a restraint has been entered into after independent legal advice is obtained, the law may extend to recognise that restraint as being reasonable even if the restraint is unreasonable pursuant to the ordinary application of the Doctrine. For the conservatives amongst us that do not agree with abolishing the Doctrine, the independent legal advice option may be coupled with the existing Doctrine so parties remain able to contract with each other on subjects of restraints without independent legal advice. Such contracts however, remain open to scrutiny under the present Doctrine and may be invalidated if they do not pass the test of reasonableness. If this approach is adopted parties may then be free to enter into wider than reasonable restraints which, in the ordinary sense, would otherwise be invalidated by the common law. In return, covenantors may enjoy greater consideration or increased flexibility and creativity when dealing with covenantees in exchange for agreeing to restraints that are wider or of longer duration.

#### 4.2 (b) ALTERNATIVES TO ABOLISHING THE RESTRAINT OF TRADE DOCTRINE –

##### PREVENTION OF WINDFALL GAIN

The author observed in Chapter 2 that covenantors who enter into an unreasonable restraint will, in effect, obtain a windfall gain as that party is not required by the Doctrine to reimburse the value of goodwill lost due to competition created by the breaching covenantor. This inequitable position should be rectified so that Courts are empowered to award a sum of compensation to covenantees that lose the protection of a restraint should the restraint be deemed unreasonable under the Doctrine. Instead of promoting what appears to be an equitable outcome, the current state of law runs contrary to all theories of civil compensation, both with respect to traditional notions of restitution for wrongs (whereby wrongs can arise by way of a tort, equitable wrong, breach of contract or criminal offences) and restitution to reverse unjust enrichment. This inequity is one of the greatest failures of the current state of the law in RT as it promotes, albeit passively, the breach of covenants entered into by covenantors since no compensation or restitution is available to the covenantee if a restraint is deemed unreasonable.

Legal recognition and rectification of this conundrum by way of statutory intervention is necessary and highly desirable to better balance the bargains reached between parties even if a restraint is found to be unreasonable and hence, unenforceable. One would expect that with the passage of legislation to curtail this problem, the number of litigious RT matters will diminish as covenantors are forced to weigh up the potential costs of paying the covenantee even if they were successful in litigating to render a restraint unenforceable. Such a result may be achieved by assessing the goodwill or value of what is lost and applying that or a proportion of that amount as compensation for the unenforceable RT clause. The burden of proof to establish the amount of compensation should rest with the covenantee and expert evidence allowed where a contract does not stipulate the amount of goodwill or value to be attributed to the restraint.

Alternatively, it may be feasible for law makers to allow a Court to appoint an expert to jointly assess the value of the loss on behalf of both the covenantor and covenantee to minimise the

duration and complexity of litigation with respect to the examination of expert testimony. There is no getting away from the fact that such a procedure will result in an increased burden on the decision making process of the Courts when deciding RT cases. Nevertheless the expected drop in the volume of litigation once this measure is implemented would justify these changes from a public resources efficiency perspective.

4.2 (c) ALTERNATIVES TO ABOLISHING THE RESTRAINT OF TRADE DOCTRINE –  
PASSING FEDERAL LEGISLATION MIRRORING *Restraint of Trade Act 1976* (NSW).

Much was said in Chapter 3 about the history and development of the *RTA* since its enactment in 1976. Through the passage of time, flaws relating to the definition of RT as it is applied in s 4(3) were overcome. A further alternative to the abolition of the Doctrine may be to pass federal legislation which mirrors the operation of the *RTA*. Such a function may fall into the legislative powers of the Commonwealth through the operation of s 51(i) of the *Commonwealth of Australia Constitution Act* (Cth) which provides that the Commonwealth Parliament shall have power to make laws for the peace, order and good government of the Commonwealth with respect to trade and commerce with other countries, and among the States. It was held in the matter of *Redfern v Dunlop Rubber Australia Ltd*<sup>310</sup> that the power of the Commonwealth under s 51(i) extends to coverage of both interstate and intrastate activities where they are inseparably connected. Notwithstanding this, if the author is incorrect and the Commonwealth Parliament does not have the requisite legislative power, it would fall to the State Parliaments to enact appropriate legislation to mirror the *RTA*. Such an outcome, of course, will be manifestly more difficult due to the need to obtain legislative input from not one government but many state governments.

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<sup>310</sup> [1964] HCA 20.

On the subject of s 4(3), the curious case of *Spooner* as discussed in Chapter 3 highlighted what appears to be an anomaly in the construction of that section. The retrospectivity of damages was first raised when the *RTA Bill* was read by the Attorney General in the Second Reading Speech. It was contended then by the opposition that s 4(3) should be amended to allow damages to be calculated from at least the date on which the lodgment of the application was first made to the Court as opposed to a date not being earlier than the date on which the order was made. The Attorney General rejected this contention for reason that being certain of the future conduct of the parties was paramount to the Act, whereas retrospectivity could encourage promises to be unduly wide and reckless.<sup>311</sup> The Attorney General concluded the second reading with the following:

I think the best thing to be done about this is to give it further consideration, perhaps in the light of the practical operation of the legislation. If the fears expressed by the honourable members opposite become a reality, and I do not discount that as a possibility, undoubtedly I shall have to come back to this place with my tail between my legs and seek to amend the legislation.<sup>312</sup>

For the reasons espoused in *Spooner*, it appears now that the fears of the opposition have become a reality and contrary to the principle of our law that a party ought not to have an interest in delaying proceedings, the result of the entirely prospective nature of the assessment of damages under s 4(3) is that defence lawyers are encouraged to delay or prolong proceedings through the use of various litigation tactics to defeat the Court's power to award damages through the operation of s 4(3).

With respect, the author does not agree with the current state of the law nor the opposition's argument entirely as expressed during the passage of the *RTA*. It is a peculiar position for a Court

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<sup>311</sup> New South Wales, *Parliamentary Debates*, Legislative Assembly, 29 September 1976, 1189 (Frank Walker).

<sup>312</sup> *Ibid.*

to certify the legality of a restraint but then be itself constrained from making the usual remedial Orders for damages. It is the author's contention that full retrospectivity of damages should be made available if the restraint is found to be enforceable by operation of the *RTA*. If the problem associated with this position lies in the possibility of awarding significant damages for breaches in an inherently uncertain area of law, then Parliament may concede to sanction the remedy of damages calculated only from the date of the application to the Court, as previously recommended by the opposition.

#### 4.3 THE USE OF CASCADING CLAUSES

The use of cascading clauses remains a conundrum and it is a difficult point to consider for the purposes of law reform. Cascading clauses were discussed in Chapters 1 and 2 and the author acknowledges the benefits that they bring to contracting parties. On the other hand, much has also been said about the deficiencies of cascading clauses and the numerous problems that they bring in their wake. One may surmise from reading Chapters 1 and 2 that cascading clauses are a necessary evil given the state of uncertainty in RT contracting today. The author is sympathetic to this view. The well respected academic commentator Andrew Stewart stated back in 1997 (note in reading below that 'step clauses' are the same as cascading clauses and these terms may be used interchangeably. Also, whilst relating to employment, the comments of Stewart are equally applicable to non-employment restraints):

In (my view) all step clauses should be struck down on the ground of uncertainty. Employers and other covenantees should be compelled to be clear as to what activities they wish to restrain, in what location and for what period. If they exceed the limits set by the law, and find that they cannot enforce the restraint in the face of conduct that could on any basis have been the subject of a reasonable covenant, then so be it. That is the price to be paid for taking insufficient care or

being overly ambitious as to the scope of the restraint. The risk of losing out in that way does no more than balance the natural advantage that most employers enjoy through superior resources, access to legal advice and the intimidatory effect of the mere presence in a contract of a restraint, valid or not. [However], it would be a foolish lawyer who failed to at least consider using a step clause when drafting a post-employment restraint especially outside New South Wales. Given the current state of the authorities, properly constructed step clauses confer an advantage on employers that is hard to resist.<sup>313</sup>

Several comments can be made in relation to the above. First and foremost, through the research and materials available to the author at the time of writing, it is evident that cascading clauses are used and judicially recognised as being a proper form of contract drafting technique only in Australia. No other country appears to have adopted this form of drafting technique and commentary from various common law countries that have examined Australia's use of cascading clauses are generally critical of its use.

There have been no cases in the United Kingdom that have considered such clauses to date. The closest that United Kingdom Courts have come to considering a cascading restraint was in *Seabrokers Ltd v Ridell*<sup>314</sup> where a discretionary sliding scale was used. The covenant purported to enable an employer to select a period of anything up to 12 months in a non-compete covenant. The election of time was to be made by the employer when the employee was terminated from employment. The Court of Session found that the discretionary sliding scale as envisaged by the contract was not properly applied as the employer had not elected a period of restraint at the time of the termination of employment. As the Court did not have to consider the validity of such a

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<sup>313</sup> Andrew Stewart, 'Drafting and Enforcing Post-Employment Restraints' (1997) 10 *Australian Journal of Labour Law* 19.

<sup>314</sup> [2007] CSOH 146.



restraint given that the employer had failed to apply the restraint correctly, the Court had nothing further to say about the general enforceability of discretionary sliding scales.

In Singapore, the Court of Appeal in *Smile Inc Dental Surgeons Pte Ltd v Lui Andrew Stewart*<sup>315</sup> specifically noted in its *obiter dicta* the practice of cascading clauses in Australia. Whilst not commenting decisively on its views of cascading clauses, the Court of Appeal felt that the reasons adopted by the Supreme Court of Canada in *Shafron v KRG Insurance Brokers (Western) Inc*<sup>316</sup> were insightful and persuasive. In *Shafron* the Court held that there is no objective bright-line rule that can be applied in all cases to render the restrictive covenant reasonable; applying notional severance simply amounts to the Court rewriting a covenant in a manner that it subjectively considers reasonable in each individual case and creates uncertainty as to what may be found to be reasonable in any specific case. The Court commented further that notional severance invites the covenantor to impose an unreasonable restrictive covenant on the covenantor with the only sanction being that if the covenant is found to be unreasonable, the Court will still enforce it to the extent of what might validly have been agreed to between the parties.<sup>317</sup>

These observations from other foreign jurisdictions demonstrate what appears to be a universal concern about the operation of cascading clauses. Because cascading clauses can blur the line between the traditional blue pencil form of severance and the notional form of severance, Australia may very well remain the only country that expressly recognises its use, at least in the foreseeable future. If some of the earlier recommendations for law reform are accepted, such law reform may have the effect of increasing certainty in contracting and thereby rendering cascading

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<sup>315</sup> [2012] SGCA 39 (*'Smile'*).

<sup>316</sup> (2009) 301 SLR 522 (*'Shafron'*).

<sup>317</sup> *Smile* [2012] SGCA 122.

clauses obsolete. If law reform is not on the agenda however, the author must reluctantly continue to acknowledge the place that cascading clauses will continue to have in Australian law.

## CONCLUSION

This thesis reviewed the Doctrine using a historical methodology with the intention of identifying the reasons for the creation of the Doctrine and the key events which helped to shape the Doctrine as we know it today. Through the analysis in Chapter 1, the author noted that the historical reasons for the creation of the Doctrine were associated with social and economic phenomena that existed in the 1600s. Taken in their earliest form, the judiciary was scathing of any restraints as they were perceived to be inimical to the proper functioning of society.

In the 1700s however, the Courts relaxed the strict approach to the law of restraints as they began to recognise the benefits of expressly permitting limited restraints. Through the segregation of restraints into voluntary and involuntary restraints, the Courts began to draw a distinction between voluntary restraints entered into via contract and general restraints. By changing the approach of the Courts from the earliest days of the Doctrine and permitting certain voluntary restraints, persons who entered into RT contracts with each other to restrain or to be restrained were able to have such restraints upheld if the geography of the restraint extended to a locality that was no greater than was necessary for the protection of the party seeking it. General restraints which extended across the entirety of England however, remained unenforceable.

By the mid-1800s, amidst the dawn of the industrial revolution and mass production, the Courts further extended the concept of enforceable restraints to such extent that even general restraints were capable of being enforced if they did no more than was reasonably necessary to protect the covenantee in dealing with the subject matter of the restraint. By adopting a test of reasonableness when determining the enforceability of a restraint, the Courts effectively widened their power to review and uphold some general restraints. The radical decision of the House of Lords in *Nordenfelt* in 1894 provided the foundation of the Australian approach to the Doctrine.

It was demonstrated through the historical analysis in Chapter 1 that an ongoing commitment was engaged in by the judiciary to review and recast the Doctrine over time to enable contemporary conditions of commerce and social needs to be recognised by law. However, the process of evolution since *Nordenfelt* has been retrograde. After *Nordenfelt*, with the exception of limited law reform in New South Wales through the introduction of the *RTA*, no other evolutionary attempts have been undertaken to align the Doctrine with the advancements of society and commerce in Australian jurisprudence. In particular, the growth of e-commerce, information technology industries and globalisation of businesses all contributed to an undeniable conclusion that commercial capabilities today are vastly different when compared to those of the late 1800s. Through this historical analysis, the author concluded that the present state of the law of restraints is misaligned with the current commercial and social needs of society.

The early conclusions that may be drawn from Chapter 1 may be summarised as follows:

- (a) Historically, the Doctrine has evolved over time to suit the needs of society and commerce.
- (b) The Doctrine has failed to continue its trajectory of evolution since the late 1800s after the pivotal *Nordenfelt* decision and is out of touch with society's present commercial and social needs.
- (c) Law reform of the Doctrine should aim to minimise legal intervention into RT contracts to maximise economic efficiency.
- (d) Legal intervention into RT contracts is only required if RT contracts are tainted with Recognised Contractual Wrongs.
- (e) Competition laws have a place in a mixed market economy but not all monopolistic behaviour should be outlawed.

The legal analysis which followed in Chapter 2 examined the present application of the Doctrine through its tests of reasonableness and public policy. The basic premise for the test of reasonableness rests on the requirement that an RT covenant must be reasonable in the interests of the contracting parties such that the restraint does no more than is necessary to protect that interest. If the restraint goes beyond what is necessary, then it will not be considered reasonable and will be rendered unenforceable.

It was noted that in assessing the question of reasonableness, the Courts adopt an objective assessment rather than a subjective assessment. Such method disregards or at least diminishes the weight of evidence given to reasons provided by contracting parties when they enter into contracts. By adopting an objective approach, the test of reasonableness encroaches into one's freedom to contract and opens up the complex question of how a judge determines what is objectively reasonable. This is particularly so if a restraint extends to future events thereby necessitating an objective assessment of a future restraint. The lack of certainty in contracting and the constant fluxion in the determination of what is reasonable or unreasonable results in a fundamental problem of uncertain outcomes in RT contracting and inconsistency of judgments which gives rise to increasing litigation amongst parties.

The public interest test fares no better and is altogether, an undeniably redundant test that is given little attention in the determination of RT matters. Judges have historically taken a cautious view when applying the public interest test. This has been so for good reason. In practice, most reasonable restraints are not harmful to the public interest. Moreover, a fundamental pillar of the public interest is the Court's recognition of the sanctity of contracts and, in order to maintain a functioning and efficient society, it is necessary to maintain the public faith in the enforceability of contractual promises. The true usefulness of the public interest test is hence, questionable. Given that current laws through common law or statute already recognise and address what

appears to be the underlying concerns of the public interest test, it would appear entirely justifiable to conclude that our system of laws do already provide extensive protection and coverage on account of the public interest.

The application of the Doctrine and in particular, the uncertainty caused to contracting parties through the indeterminate references as to what is a reasonable restraint, led to the passage of the *RTA* in 1976 in the State of New South Wales. The *RTA* partly corrected certain deficiencies of the Doctrine, specifically in relation to the operation of the test of reasonableness. In New South Wales, as a result of the *RTA*, the Courts are empowered to modify a restraint to what it believes is a reasonable restraint rather than being forced to simply render an unreasonable restraint unenforceable. This has the additional effect of curing a further anomaly of the Doctrine by requiring attention to be concentrated on the actual breach instead of the imaginary breach for the purpose of determining the validity of a restraint. The *RTA* is not a perfect solution to the problems engendered by the Doctrine but it is a step in the right direction by providing contracts with a fall back position should the common law operate to invalidate a restraint based on unreasonableness. All other States and Territories in Australia continue to suffer from a lack of statutory protection and are therefore entirely reliant on the doctrine of severance and the use of cascading clauses.

Chapter 2 then moved to critique the use of cascading clauses. Although it is well established that cascading clauses are a legitimate form of drafting technique in Australia, the complexity associated with their use have frequently resulted in decisions from Courts rendering them to be unenforceable. The artificiality of cascading clauses as a method of overcoming some of the problems associated with the present exposition of the Doctrine cannot be understated. The creation of multiple restraint periods, geographic regions and actions of restraint contribute to an increasing lack of certainty when contracting in RT despite its essential acceptance by the Courts

of Australia. Instead of determining whether a single restraint is reasonable based on clauses which are not cascading in style, Courts may be frequently asked to examine the reasonableness of more than 100 restraints in modern cases as evidenced in the example of *Re Lloyd's Ships*. The sense of uncertainty created through the use of cascading clauses permeates the majority of contracts that specify a restraint given its widespread use. While attempting to adopt an expedient for the problems created by the Doctrine through the use of cascading clauses, another problem arises from their use through the indirect promotion of litigation as no contracting party is able to articulate which precise restraint from the combination of restraints will apply to their set of facts. Even if cascading clauses was drafted perfectly and found to be enforceable, the determination of what is an acceptable restraint can only be resolved through the adjudication of the combination of restraints by the Courts at the present time.

The conclusions that may be drawn from Chapter 2 may be summarised as follows:

- (a) The majority of cases in RT before the Courts are fundamentally due to the uncertainty of application surrounding the test of reasonableness. Reconciling the historical authorities on the issue of what is a reasonable restraint and what is an unreasonable restraint is difficult. It is entirely plausible that judges will reach different conclusions on the issue of a restraint's reasonableness despite the same set of facts being presented before them, partly due to the frequent use of cascading clauses in Australia.
- (b) The public interest test is generally accepted as being a redundant test that is given symbolic attention in the determination of RT matters. Judges have historically taken a cautious view of this test as matters of the public interest are said to be ordinarily best determined outside of the judicial environment. Moreover, the fundamental reason for

the existence of this limb of the Doctrine is questionable today given that the public interest is now better protected by existing statutes and common law.

- (c) The *RTA* is a positive instrument that empowers the Court to amend an unreasonable restraint to what it considers to be a reasonable restraint rather than simply rendering an unreasonable restraint unenforceable. The *RTA* is not without its problems but there is no doubt that contracting parties are better off with such an instrument rather than being solely reliant on the doctrine of severance and the use of cascading clauses.
- (d) Cascading clauses are an inappropriate expedient to the problems associated with the test of reasonableness. By requiring Courts to determine the reasonableness of a combination of restraints, the inevitable result is a further erosion of certainty in RT contracting. Cascading clauses also have the effect of encouraging litigation as contracting parties cannot assess for themselves with any acceptable degree of certainty, the reasonableness of one combination of restraint over another.

Chapter 3 examined the relationship between the *TPA/CCA* and the Doctrine. The paper first applied a law and economics analysis to the question of whether society is benefited by maintaining competition regulations that restrict the freedom of contracting parties when they engage in anti-competitive behaviour. The perfectly competitive model of analysis which followed showed that competition legislation is essential to maximise economic efficiency for 3 reasons. The first reason related to the ability of buyers and sellers to influence the pricing of goods and services. The second reason related to the barriers of market entry and exit and the third reason related to the presentation of relevant and accurate data to consumers. Through this analysis, the author concluded that a system of ‘workable or effective competition’ was necessary to eliminate or contain behaviour that substantially lessens competition. Such a system exists in



Australia with respect to RT contracts through the operation of s 45 of the *CCA* which is broadly concerned with contracts, arrangements or understandings that restrict dealings or affect competition.

The early historical account of the development of the present s 45 of the *CCA* and its relationship to the Doctrine saw a perilous position being adopted by the High Court in the decision of *Quadramain*. By importing the common law definition of RT into the interpretation of s 45, many of the economic considerations and imperatives behind competition regulation would be lost. The Swanson Report and passage of the *Trade Practices Amendment Act 1977* (Cth) was therefore a welcome move which realigned the economic foundations of the *TPA* with the ongoing application of s 45.

The author then turned attention to the subject of Clearances. Analysis of Clearances in academic literature is limited as it was a procedure extinguished in 1977, 3 years after its initial debut. The author recommended the reinstatement of the now defunct Clearance procedure as it was argued to be beneficial to contracting parties through the ability for these parties to seek approval and therefore certainty in their proposed RT actions.

The conclusions that may be drawn from Chapter 3 may be summarised as follows:

- (a) A law and economics analysis supports a system of workable or effective competition through government intervention. The purpose of such intervention can be theoretically linked back to the perfectly competitive model and, more practically, to the elimination or containment of anti-competitive actions.

- (b) After the decision of *Quadramain*, it was necessary for s 45 of the *TPA* to be realigned with the economic foundations which underpinned its statutory formulation. If the *Trade Practices Amendment Act 1977* (Cth) had not been passed, the present application of the competition legislation might have become disengaged from its economic foundations and suffered from the defects of the Doctrine. The *Trade Practices Amendment Act 1977* (Cth) and the decision of the High Court in *Petersville* cemented the independence of the competition laws of Australia from the operation of the Doctrine by substituting the tests associated with the Doctrine for one of ‘substantially lessening competition’.
- (c) Clearances should be reinstated or amalgamated into the Authorisation procedure to provide contracting parties with increased certainty through the parties’ ability to seek permission to engage in a contract, arrangement or understanding and in a form of restricted trade practice if they are able to establish that the proposed action did not or would not have the effect of substantially lessening competition.

Chapter 4 presented the thesis statement. The principal contribution of this thesis to the jurisprudence of RT is in its proposal and justification for the abolition of the Doctrine. Through the process of charting the historical development of the Doctrine from its earliest days in England and the law and economics methodology adopted in the assessment of RT in various contexts, several conclusions may be drawn.

Firstly, the improvements and increasing capabilities of industry and commerce reduces the ongoing need for the Doctrine. Secondly, the advancements of law in the areas of Recognised Contractual Wrongs may sufficiently protect contracting parties. Thirdly, the *CCA* has displaced many of the public policy concerns that gave rise to the creation of the Doctrine at its time of formation. Fourthly, the current test of reasonableness and its past applications has failed to

provide contracting parties with an appropriate yardstick by which they may determine if their conduct or proposed conduct is reasonable or not. This is unlikely to change as industry and commerce continue to advance into a world where market borders become increasingly vague. Fifthly, the redundancy of the public interest test has the effect of rendering that limb of the Doctrine as a symbolic test without real substance in matters of contested RT. Finally, the use of cascading clauses does not improve certainty in RT contracting and instead, encourages litigation among contracting parties.

Through these observations, it would seem that the arguments for the abolition of the Doctrine are numerous and persuasive. In order to present a complete perspective, the author also considered the possible reasons against the abolition of the Doctrine. The fundamental argument against abolition stems from the unfairness of enforcing an RT contract which contains an unreasonable restraint. This argument was found to be unmeritorious as RT contracts do not present a different species of unfairness that is somehow unique and distinct from other forms of unfairness when parties contract with each other. It was demonstrated that the law is not concerned with the relative values of bargains *per se* and contracting parties are free to contract notwithstanding that a bargain struck may be more advantageous to one and less advantageous to another. Another argument against abolition is that RT restraints may extend for a significant period of time or geography. The author also found this argument lacking as any ordinary contract may contemplate for an extended duration or geography as part of its terms.

In addition to the main proposition of abolishing the Doctrine, the author recommended several alternative law reform possibilities. These are summarised below:

- a) Independent legal advice

The importation of the concept of informed consent into RT contracts may be a partial solution to reduce the number of RT matters before the Courts. By recognising an RT as being reasonable once independent legal advice is sought and received even if the restraint is *prima facie* unreasonable pursuant to the Doctrine, contracting parties are able to achieve greater certainty when engaging in RT contracts. It also opens the possibility of parties entering into wider than reasonable restraints where it is agreed between the covenantor and covenantee without fear of its unenforceability.

b) Prevention of windfall gain

Statutory intervention is highly desirable to prevent covenantors from being able to enjoy a windfall gain if an RT is found to be unenforceable. At present, covenantors who enter into a restraint will obtain a windfall gain if the restraint is deemed unenforceable by the Courts as they are not required to reimburse the value of consideration lost on account of the restraint. Such a result may be achieved by assessing the value of what is lost and applying that or a portion of that value as compensation for the unenforceable RT. A Court appointed expert may jointly assess the value of loss to minimise the duration and complexity of litigation before the Courts.

c) Passing federal legislation mirroring *Restraint of Trade Act 1976* (NSW)

The *RTA* is not a perfect solution but its existence in the State of New South Wales contributes to greater flexibility for the Courts in making decisions on RT contracts. Passing of federal legislation mirroring the *RTA* would be a significant inroad into this field of law. In addition, full retrospectivity of damages should be made available if a restraint is found to be reasonable. If the concept of awarding significant damages for

breach is unacceptable, Parliament may mandate that the damages should be calculated only from the date of the application to the Court.

d) The use of cascading clauses

From an objective perspective, cascading clauses must be acknowledged to bring certain benefits to parties when they engage in RT contracts. Their use however, contributes to increasing uncertainty despite judicial recognition of the validity. If some of the recommendations for law reform are adopted, it may have the effect of rendering cascading clauses obsolete. However, in the absence of law reform, the use of cascading clauses currently represents best practice for the drafting of RT contracts.

Law reform is neither straightforward nor painless and lawmakers are generally loath to hastily adopt law reform of established doctrines for good reasons. The abolition of the Doctrine would amount to a revolution in this field of law. Nevertheless, in the current state of affairs, and given the slow but evolving history of the Doctrine over the centuries, it is realistic to acknowledge that few law makers will have sufficient reason to criticise so strongly, the operation of the Doctrine and advocate for its abolition. Such a revolution may very well prove to be stillborn. Nonetheless, if the Doctrine were to continue on its evolutionary trajectory, there is some hope that the arguments proposed in this thesis may yet see the light of day.

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