Federal Court of Australia

Australian Competition and Consumer Commission v Baxter Healthcare Pty Ltd [2005] FCA 581 (16 May 2005)

Last Updated: 15 July 2005

FEDERAL COURT OF AUSTRALIA

Australian Competition and Consumer Commission v Baxter Healthcare Pty Ltd [2005] FCA 581

AUSTRALIAN COMPETITION AND CONSUMER COMMISSION v BAXTER HEALTHCARE PTY LTD AND ORS
N 1153 of 2002

ALLSOP J
16 MAY 2005 (CORRIGENDUM 2 JUNE 2005)
SYDNEY

IN THE FEDERAL COURT OF AUSTRALIA
NEW SOUTH WALES DISTRICT REGISTRY **NSD 1153 of 2002**

BETWEEN:	**AUSTRALIAN COMPETITION AND CONSUMER COMMISSION** **APPLICANT**
AND:	**BAXTER HEALTHCARE PTY LTD** **FIRST RESPONDENT**
	THE STATE OF WESTERN AUSTRALIA **SECOND RESPONDENT**
	THE STATE OF SOUTH AUSTRALIA **THIRD RESPONDENT**
	THE STATE OF NEW SOUTH WALES **FOURTH RESPONDENT**
JUDGE:	**ALLSOP J**
DATE OF ORDER:	**16 MAY 2005 (CORRIGENDUM 2 JUNE 2005)**
WHERE MADE:	**SYDNEY**

CORRIGENDUM

To conclude that the interference with the State tender process substantially affects or is likely to affect competition is not to undermine my earlier conclusion that the PD market is an Australia wide one. Rather, though the States are of varying sizes, to affect each State tender process was, in my view, to lessen competition or be likely to do so in a meaningful way for the Australian market. This can be seen either by reference to the meaningful number of PD patients in each State (including in South Australia, though not a huge number there) or as affecting tender processes in sovereign States within the Australian market.

IN THE FEDERAL COURT OF AUSTRALIA
NEW SOUTH WALES DISTRICT REGISTRY **N 1153 of 2002**

BETWEEN:	**AUSTRALIAN COMPETITION AND CONSUMER COMMISSION** **APPLICANT**
AND:	**BAXTER HEALTHCARE PTY LTD** **FIRST RESPONDENT**
	THE STATE OF WESTERN AUSTRALIA **SECOND RESPONDENT**
	THE STATE OF SOUTH AUSTRALIA **THIRD RESPONDENT**
	THE STATE OF NEW SOUTH WALES **FOURTH RESPONDENT**
JUDGE:	**ALLSOP J**
DATE:	**6 MAY 2005 (CORRIGENDUM 2 JUNE 2005)**
PLACE:	**SYDNEY**

REASONS FOR CORRIGENDUM

1 Since handing down my reasons in this proceeding on 16 May 2005 I realised that I overlooked inserting in the final draft a paragraph, which I had intended for some time to include. During the final preparation of the reasons for judgment and the proofing, which took some time, I overlooked the inclusion of this paragraph. The paragraph can probably be recognised as implicit in my reasons in any event. Nevertheless, I think it important to explain to the parties the fact that I neglected to include the paragraph.

2 This explains the nature of the corrigendum today.

I certify that the preceding two (2) numbered paragraphs are a true copy of the Reasons for Corrigendum herein of the Honourable Justice Allsop.

Associate:

Dated: 2 June 2005

Counsel for the Applicant:	Mr A I Tonking
Solicitor for the Applicant:	Australian Government Solicitor
Counsel for the First Respondent:	Mr I S Wylie
Solicitor for the First Respondent:	Blake Dawson Waldron

Counsel for the Fourth Respondent: Ms K Kerr (Slr)

Solicitor for the Fourth Respondent: NSW Crown Solicitor

Date of Corrigendum: 2 June 2005

FEDERAL COURT OF AUSTRALIA

Australian Competition and Consumer Commission v Baxter Healthcare Pty Ltd [2005] FCA 581

TRADE PRACTICES – ss 46 and 47 – tendering for supply of sterile fluids for State and Territory health facilities

STATUTORY CONSTRUCTION – CROWN IMMUNITY – extending to protect conduct of third party (first respondent) with respective State and Territory executive governments

Trade Practices Act 1974 (Cth) Part IV ss 46, 47, 76, 80, 83

ASX Operations Pty Ltd v Pont Data Australia Pty Ltd (No 1) (1990) 27 FCR 460 referred to
Australian Gas Light Company v ACCC [2003] ATPR 41-966 referred to
Bass v Permanent Trustee Co Ltd (1999) 198 CLR 334 referred to
Boral Besser Masonry Ltd v ACCC (2003) 215 CLR 374609 referred to
Bradken Consolidated Ltd v BHP (1979) 145 CLR 107 applied
Bropho v Western Australia (1990) 171 CLR 1 referred to
Burgundy Royale Investments Pty Ltd v Westpac Banking Corporation (1987) 18 FCR 212 referred to
China Ocean Shipping Co v South Australia (1979) 145 CLR 172 referred to
Commonwealth v Rhind (1960) 119 CLR 584 referred to
Davis v Commonwealth (1980) 166 CLR 79 referred to
Dowling v Dalgety Australia Limited (1992) 34 FCR 109 referred to
Doyle v Edwards (1898) 16 NZLR 572 referred to
Lower Hutt City v Attorney-General [1965] NZLR 65 referred to
Eastern Express Ltd v General Newspapers (1992) 35 FCR 43 referred to
Melway Publishing Pty Ltd v Robert Hicks Pty Ltd (2001) 205 CLR 1 referred to
Monroe Topple & Associates Pty Ltd v Institute of Chartered Accountants in Australia (2002) 122 FCR 110 referred to
NT Power Generation Pty Ltd v Power and Water Authority (2004) 210 ALR 312 discussed and applied
Queensland Co-operative Milling Association (1976) ATPR 40-012 referred to
Queensland Wire Industries Pty Ltd v Broken Hill Proprietary Co Ltd (1989) 167 CLR 177 referred to
Re Telephone Apparatus Manufacturers' Application [1963] 1 WLR 463 discussed
Rural Press Ltd v ACCC (2003) 216 CLR 53 203 ALR 217 referred to
Stirling Harbour Services Pty Ltd v Bunbury Port Authority (2000) ATPR 41-752 referred to
Tillmanns Butcheries Pty Limited v Australasian Meat Industry Employee's Union and others (1979) 42 FLR 331 referred to
Universal Music Australia Pty Ltd v ACCC (2003) 131 FCR 529 referred to and applied
Wellington City Corporation v Victoria University of Wellington [1975] 2 NZLR 301 referred to

Wynyard Investments Pty Ltd v Commissioner of Railways (NSW) (1955) 93 CLR 376 discussed

Nalebuff, B (2000) "Competing against bundles" in *Incentives, Organisation, and Public Economics*; Peter Hammond & Gareth Myles, eds, Oxford University Press.)

Seddon *Government Contracts: Federal State and Local* (3rd Edn)

AUSTRALIAN COMPETITION AND CONSUMER COMMISSION v BAXTER HEALTHCARE PTY LTD AND ORS
N 1153 of 2002

ALLSOP J
16 MAY 2005
SYDNEY

IN THE FEDERAL COURT OF AUSTRALIA
NEW SOUTH WALES DISTRICT REGISTRY **N 1153 of 2002**

BETWEEN:	**AUSTRALIAN COMPETITION AND CONSUMER COMMISSION** **APPLICANT**
AND:	**BAXTER HEALTHCARE PTY LTD** **FIRST RESPONDENT**
	THE STATE OF WESTERN AUSTRALIA **SECOND RESPONDENT**
	THE STATE OF SOUTH AUSTRALIA **THIRD RESPONDENT**
	THE STATE OF NEW SOUTH WALES **FOURTH RESPONDENT**
JUDGE:	**ALLSOP J**
DATE OF ORDER:	**22 JUNE 2005**
WHERE MADE:	**SYDNEY**

THE COURT ORDERS THAT:

1. the reasons published on 16 May 2005 no longer be or remain confidential and may be distributed.

THE COURT NOTES THAT:

Note: Settlement and entry of orders is dealt with in Order 36 of the Federal Court Rules.

IN THE FEDERAL COURT OF AUSTRALIA
NEW SOUTH WALES DISTRICT REGISTRY **N 1153 of 2002**

BETWEEN:	**AUSTRALIAN COMPETITION AND CONSUMER COMMISSION** **APPLICANT**
AND:	**BAXTER HEALTHCARE PTY LTD** **FIRST RESPONDENT**
	THE STATE OF WESTERN AUSTRALIA **SECOND RESPONDENT**
	THE STATE OF SOUTH AUSTRALIA **THIRD RESPONDENT**
	THE STATE OF NEW SOUTH WALES **FOURTH RESPONDENT**
JUDGE:	**ALLSOP J**
DATE OF ORDER:	**16 MAY 2005**
WHERE MADE:	**SYDNEY**

THE COURT ORDERS THAT:

Note: Settlement and entry of orders is dealt with in Order 36 of the Federal Court Rules.

IN THE FEDERAL COURT OF AUSTRALIA
NEW SOUTH WALES DISTRICT REGISTRY **N 1153 of 2002**

BETWEEN:	**AUSTRALIAN COMPETITION AND CONSUMER COMMISSION** **APPLICANT**
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	THE STATE OF NEW SOUTH WALES **FOURTH RESPONDENT**
JUDGE:	**ALLSOP J**
DATE:	**16 MAY 2005**
PLACE:	**SYDNEY**

REASONS FOR JUDGMENT

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Introduction and summary of my conclusions

1 The Australian Competition and Consumer Commission (the "ACCC") has brought an application under Part IV of the *Trade Practices Act 1974* (Cth) ("the Act") against Baxter Healthcare Pty Ltd ("Baxter"), a manufacturer and supplier of sterile fluids. It seeks declarations that there have been various contraventions by Baxter of ss 46 and 47 of the Act, It also seeks injunctions under s 80 of the Act, pecuniary penalties under s 76 of the Act and an order that there be findings of fact pursuant to, and for the purposes of, s 83 of the Act.

2 The conduct of Baxter was at all times undertaken with New South Wales, Queensland, South Australia, Western Australia and the Australian Capital Territory in connection with the supply to the health authorities of those States and that Territory of fluids and products for use in hospitals. I have come to the view that the Act does not apply to, or operate in respect of, the conduct complained of. The reasons for this conclusion, which are set out later in these reasons, are that (to use a convenient shorthand) the principles of Crown immunity or derivative Crown immunity mandate that result.

3 I have otherwise dealt with the matter on the assumption that I am wrong in that conclusion. Approaching the matter on that basis, I would find that there has been one contravention of s 46 of the Act, and that there have been a number of contraventions of s 47 of the Act.

4 A significant amount of the evidence in the proceeding was said to be confidential. Given the extensive evidence of contract negotiation and bid assessment, that was readily understandable. In order that the hearing might proceed with some despatch, in making orders under s 50 of the *Federal Court of Australia Act 1976* (Cth), I relied, in significant part, on the careful and commonsense treatment of confidentiality claims by the practitioners involved. It became impractical to express my reasons without dealing expressly with confidential documents. I propose to allow the ACCC and the legal advisers of the parties some time to examine the relevant parts of my reasons and identify any parts that should be placed in a confidential part of the reasons or which can be expressed differently to convey the same idea or fact. This is the explanation for orders 3, 4 and 5 made today.

5 From time to time in these reasons in recounting factual material, I have used the present tense. I have generally done so because of the terms or context of admissions or evidence. Where this appears, unless the context makes the contrary clear, it should be taken as relevant to the period in question, 1998 to 2001.

Background facts

6 Baxter was incorporated as Travenol Laboratories Pty Limited on 26 April 1962 and changed its name to Baxter Healthcare Pty Limited on 18 November 1987. It is the Australian operating subsidiary, and, effectively, the Australian division, of Baxter International Inc ("BI Inc"), a global medical products and services company incorporated in the United States of America (the "US"), which specialises in critical therapies for life threatening conditions. BI Inc has three divisions, namely, BioScience (products related to blood), Renal (dialysis products) and Medication Delivery (intravenous products), and Baxter supplies products for each of these divisions in Australia.

7 Although BI Inc has manufacturing plants in over 20 countries, Baxter manufactures the majority of its Australian products at a plant in Toongabbie, New South Wales. According to Mr Brian Lee (Baxter's former Managing Director), that plant commenced producing intravenous ("IV") solutions in 1973 and peritoneal dialysis ("PD") solutions in 1980. Baxter began its compounding centre (pharmacy) at the Toongabbie plant in the early 1980s and since that time has manufactured parenteral nutrition ("PN") products there. Compounding centres have also been established at St Vincent's Hospital (1994), in Brisbane (1997/1998) and in Melbourne (1998). In the past, Baxter also produced blood bags and blood and solution sets, but these are now generally imported. I will explain the nature of these products shortly.

8 The conduct complained of in these proceedings is connected with Baxter's negotiation of, entering into, and giving effect to, five long-term contracts between 1998 and 2001 with State and Territory

authorities concerned with the organisation and conduct of purchasing commodities. The authorities which are variously named, but were described generically in the proceedings as State Purchasing Authorities ("SPAs"). The authorities with whom Baxter contracted were within New South Wales ("NSW"), the Australian Capital Territory ("ACT"), Western Australia ("WA"), South Australia ("SA") and Queensland ("QLD"). Each was part of the executive arm of government of the respective polity. I will refer to these contracts by their State or Territory. The contracts with NSW, ACT, SA and WA provided, in substance, for the supply of the entire requirements of each for certain sterile fluids and 90 per cent of their PD fluids, for the periods 18 May 1998 to 30 April 2003, March 1999 to April 2003, 1 April 2001 to 30 March 2006 and 1 March 2001 to 28 February 2006, respectively. The contract with QLD provided for the supply of the State's entire requirements for certain sterile fluids (excluding PN fluids) and 92.5 per cent of its PD fluids for the period 1 June 2001 to 31 May 2004.

9 The context in which the alleged conduct took place involved State-wide tenders issued by each of NSW, QLD, WA and SA (but not the ACT) for the supply of certain sterile fluids to public hospitals. Baxter ostensibly had a similar response to each State tender request. It was said that Baxter would make an offer to supply tender items on an item-by-item basis at so-called high "cherry pick" prices, and it would also make an offer to supply the same items on an exclusive sole supply basis for substantially lower prices. This sole supply included PD products.

10 The products that were affected by the various State contracts were irrigating solutions ("IS"), large volume parenteral ("LVP") fluids, PN fluids and PD fluids and products. The nature and function of the first three products were set out in the uncontested affidavit evidence of Dr David McWilliam, the Director of Intensive Care at the Royal Prince Alfred Hospital in Sydney. Similarly, the nature and function of PD and haemodialysis and related treatments ("HD") were set out in the uncontested affidavit evidence of Dr Jeremy Chapman, the Director of the Renal Unit at Westmead Hospital and of Mr Trevor Garland, who was formerly a Clinical Nurse Consultant at St Vincent's Hospital in Sydney and who is now a consultant with Fresenius. Dr Ashley Irish, the Director of the Renal Unit at the Royal Perth Hospital, also gave some evidence about PD and HD, and although he was cross-examined, he was not questioned on the evidence that he gave in this regard. There was no relevant issue litigated concerning the nature of the products and fluids.

11 LVP fluids are sterile fluids that are administered intravenously by slow infusion therapy for the purpose of re-hydration, the administration of drugs, resuscitation, and fluid and electrolyte replacement in human patients. They are typically solutions of water, electrolytes and dextrose, and are divided into crystalloid and colloid solutions. Colloid solutions contain larger molecules which will not pass through semi-permeable cell membranes. Crystalloid solutions are those that contain smaller molecules, which can pass through semi-permeable cell membranes for the maintenance of patient daily fluid requirements. LVP fluids are used where the amount of fluid required is greater than 250 ml. LVP fluids are used to treat approximately 80 per cent of all patients admitted to hospital. There are no products that are substitutable for any or all LVP fluids.

12 LVP fluids are to be distinguished from small volume parenteral fluids ("SVP fluids"), which are fluids used to perform or facilitate injections and reconstitute pharmaceuticals. SVP fluids are stored in volumes of 250 ml or less in vials, ampoules and small bags. They are administered intravenously, but not by slow infusion therapy.

13 There is, and was at all relevant times, an established and entrenched demand for LVP fluids from public hospitals, clinics and other facilities funded by the States and Territories (to which I will refer as "Health facilities", being a phrase also used in the semi-capitalised form in the evidence), private hospitals, medical practices and ambulance services.

14 At all relevant times, the largest purchasers of LVP fluids were the relevant SPAs on behalf of their respective Health facilities.

15 The demand for LVP fluids has not increased rapidly since January 1997, and is unlikely to do so.

16 The various types or categories of LVP fluids used in Health facilities are used in different volumes. Some are heavily used, some are not.

17 PN involves the provision of nutrition by intravenous sterile solutions formulated to provide all or part of a patient's nutritional requirements, in circumstances where the patient is unable to digest food. PN fluids are produced by dissolving water soluble ingredients such as amino acids, salt or glucose in water, and then placing the solutions in containers. There are approximately 30 types of PN fluid used by hospitals (public and private) and nursing homes. PN differs from enteral nutrition ("EN"), which is the provision of food to the patient via the digestive tract, either by mouth, or by a tube inserted into the stomach or small bowel. PN and EN fluids are produced in separate facilities so as to avoid cross-contamination due to their different properties. EN is less expensive than PN, and is also safer because there is less risk of infection. EN also maintains the nutrition of the gut mucosa better than PN and as a result, PN is only utilised where EN is not feasible. PN and EN are substitutable, unless the patient's gastro-intestinal tract is not functioning.

18 There is an established and entrenched demand for PN fluids. At all relevant times, the largest purchasers of PN fluids were the relevant SPAs on behalf of their respective Health facilities.

19 IS are aqueous based-products that are used generally in hospitals for a number of purposes, including washing or cleaning wounds or in surgery. Although they are sterile, they are not suitable to perform the function of LVP fluids. As a result, they cannot be substituted for LVP fluids. It might be possible to use an LVP as an IS although it would not be optimal because the packaging is not designed for easy pouring. In that sense, LVP fluids are also not properly substitutable for IS. On the pleadings, it was admitted by Baxter that there are no products substitutable for IS.

20 There is an established and entrenched demand for IS. They are used in almost every operation or surgical procedure. They are used by hospitals (public and private), medical practices and ambulance services. At all relevant times the largest purchasers of IS were the relevant SPAs on behalf of their respective Health facilities. The demand for IS has not increased rapidly since January 1997, and is not likely to do so.

21 PD is a form of dialysis treatment for chronic renal failure. Renal failure can also be treated with HD or a kidney transplant. PD removes waste products from the blood by osmosis using the peritoneum, which is the membrane covering the intestinal organs located in the abdominal cavity, as a filter. The process involves using a surgically implanted catheter and a sterile dialysis solution which is introduced into, and removed from, the patient's peritoneal cavity several times a day. Most PD treatments are self-administered by patients at home. There are two kinds of PD treatment: continuous ambulatory PD ("CAPD") and automated PD ("APD"), which can operate while the patient sleeps. CAPD does not require a machine, APD does.

22 "PD products" is a phrase used in the evidence and can be taken as a reference to PD fluids and ancillary PD products used to perform PD, such as APD machines, lines for fluid connection, locks for the connectors and bags for fluids.

23 HD treatment involves the patient's blood flowing outside the body through disposable bloodlines into a specially designed filter: the dialyser. The dialyser assumes the function of an artificial kidney and the dialysis solution carries away waste products. The whole process is controlled by an HD machine and is usually required by a patient three times per week. Whilst it is unnecessary to canvas in any detail, there are a number of different types of excorporeal dialysis treatments. HD, itself, does not involve the use of sterile fluids. The dialysis fluid passes on the other side of a membrane within the dialyser. Treatments related to haemodialysis proper, haemofiltration and hameodiafiltration, do involve some intravenous introduction of sterile fluids. It is sufficient for present purposes, however, simply to use the initials "HD" to cover all these treatments.

24 PD and HD, subject to certain medical conditions on the part of the patient, are not mutually exclusive and as a result, some, but not all, patients have a choice of treatment. Patients who have had extensive abdominal operations or who have a colostomy, or who are incapable of strict hygiene are not suitable for PD. Patients who have vascular problems or diabetes are usually not suitable for HD, because the removal of blood during the HD process places a strain upon the heart. The advantage of PD is that it is portable and easily administered at the patient's home or workplace. PD is often recommended for patients who have residual renal function because it maintains that function for a longer period than HD. The disadvantage of PD is that it can only be used in a patient who has a functioning peritoneal membrane. There is also a risk of infection (peritonitis) by the use of PD. Indeed, patients are often forced to move from PD to HD because of infection or the failure of the peritoneal membrane, which failure will eventually occur after about five to eight years through the undertaking of the PD process. Unless contra-indications appear, and unless peritonitis develops, PD patients can thus remain on PD for five to eight years.

25 Where a patient is physically able to have either PD or HD treatment there are various factors that may influence the decision as to the choice between PD or HD treatment. These include age, health, residual renal function, convenience, the desire for more intermittent treatment (in HD), body image, diet and other lifestyle factors.

26 In Australia in 2001, there were approximately 5,000 HD patients and 1,915 PD patients. The location of the PD patients was as follows:

- NSW/ACT 700
- Victoria 380
- QLD 520
- WA 175
- SA 80
- Tasmania 30
- Northern Territory 30

27 As at 2002, the annual treatment cost for PD was between $20,000 and $25,000 per patient, and for HD was between $24,000 and $55,000 per patient.

28 There is an established and entrenched demand for PD products. The purchasers of these products are the Health facilities (in the States and Territory dealt with in these proceedings, through the SPAs) and a very small number of private hospitals. From the nature of the treatment involved, the demand for PD is generated by patients with chronic renal failure caused by kidney disease. Kidney disease in Australia is increasing at a rate of 6-7 per cent per annum. The number of patients requiring dialysis is increasing by about 7-10 per cent per annum. The major cause of these increases is the rise in the number of patients with diabetes and hypertension. The demand for PD products is increasing for these reasons.

29 At all relevant times, the largest purchasers of PD products were the relevant SPAs on behalf of their respective Health facilities. Historically, PD has been provided to patients through the public hospital system.

30 Though PD can be, and is, administered by the patient otherwise than in hospital, the PD patient requires regular appointments and monitoring by trained nursing and medical staff, which is only available at major public hospitals with renal units.

31 Patients with kidney disease are usually treated within their State or Territory of residence.

32 In relation to the States and Territory dealt with in these proceedings, decisions about the

purchasing of PD products are made by the SPAs in relation to the total needs of all PD patients within the State. PD products are purchased separately by each State to treat the number of patients in the State. The prices paid for PD products vary between States.

33 Historically, in Australia PD products have generally been provided by Health facilities.

34 In the early 1980s, PD first became available for home-based patients. From then, and until Gambro commenced supplying PD products in 1990, Baxter was the only supplier of PD fluids in Australia.

35 Subject to patients in the ACT not infrequently being treated in NSW and NSW patients not infrequently being treated in the ACT, it was common ground on the pleadings that patients with kidney disease are usually treated within their State or Territory of residence. This is so for two reasons, it was agreed. The first was that funding for Health facilities is State or Territory based and consequently it is more difficult for patients to gain access to treatment out of the State or Territory in which they are resident. Secondly, a patient undergoing PD treatment requires regular appointments and monitoring, which is only available at major public hospitals with renal units.

36 One matter of terminology which should be noted at this point relates to the expression "sterile fluids". The phrase could be used to refer to LVP fluids, IS, PN fluids and PD fluids. All are required to be sterile. However, the ACCC conducted the case using the phrase to mean only LVP fluids, IS and PN fluids. There is an issue as to markets to which this question might relate. In order that terminology not confuse substantive issues, I will use the phrase in a manner not to be taken as a reference to PD fluids, unless the context makes clear the contrary.

The ACCC claims

37 I will deal in more detail with the products, their manufacturing and distribution and market shares in due course. At this point, however, it is convenient, with the above background, to examine the claims of the ACCC.

38 The ACCC submitted that, broadly speaking, the sterile fluids other than PD, and perhaps PN, fluids can be viewed as bulky water-based items in respect of which Baxter has the only manufacturing plant in Australia. The products could also be described as "high volume low value" and were to be compared to PD products which were of lower volume and higher value. Thus, it was said, Baxter has a significant competitive advantage in the manufacture and sale of these "high-volume-low-value" sterile fluids. Importation costs of carrying "water on water" made import competition in relation to sterile fluids very difficult. The ACCC's case was that, effectively, a monopoly existed for sterile fluids. PD fluids, on the other hand, were of lesser volume or bulk and of higher value than sterile fluids. Taken as an individual group of products, the local manufacture by Baxter of PD did not give it as significant an advantage as it enjoyed in respect of sterile fluids. Import competition was real in relation to PD products.

39 The impugned approach of Baxter was said to be the "bundling" of the PD products with the "monopoly" sterile fluid products, thereby eliminating, it was said, the effectiveness of any competition from rival PD suppliers who could not, and in most cases did not want to, compete with Baxter in the supply of sterile fluids.

Section 46 claims

40 The ACCC, in its s 46 claims, says that Baxter took advantage of what was said to be its substantial market power in the sterile fluids market or markets for the purpose of harming competitors or preventing competitive conduct in the PD products market. Such claims have been characterised in the US as antitrust violations under s 2 of the *Sherman Act* and s 3 of the *Clayton Act* are known as "monopoly leveraging" or "exclusionary bundling": *Smith Kline v Eli-Lily* 575 F 2d

1056 (1978); *Ortho Diagnostic Systems v Abbott Laboratories* 920 F Supp 455 (2003); *Le Page Inc v 3M* 324 F 3d 141 (1996); and *North Pacific Railway v United States* 356 US 1 (1958).

41 In essence, the complaint was that Baxter offered prohibitively high item-by-item prices (the so-called "cherry pick" prices) so as to compel the States to agree to exclusive supply contracts for the supply of sterile fluids (being products over which it has a monopoly and being products which constitute a market or markets in which it allegedly has substantial power), bundled with PD products, for lengthy periods. This arrangement allegedly took advantage of Baxter's market power in the sterile fluids market or markets, because it would not or could not have been able, under competitive conditions, to force the States to take the bundled offer by threatening prohibitive prices for sterile fluids. This arrangement also allegedly harmed both actual and potential competition in the PD products market, namely two foreign concerns through their Australian subsidiaries, to which I will generally refer without any greater specification of corporate form, except where necessary, as Fresenius and Gambro, because these companies were unable to compete in the markets for LVP, PN and IS fluids.

42 To be successful, the ACCC had to demonstrate that Baxter had substantial power in the relevant sterile fluids market or markets, that Baxter took advantage of that power and that Baxter had the requisite subjective purpose.

43 The ACCC pleaded a number of alternative contraventions under s 46.

44 The alleged contraventions of s 46 were put in eight alternative ways depending on the definition of the market in which Baxter was said to have a substantial degree of power and of the market to which the relevant purposes were said to be directed. In all cases the relevant purposes were said to be the same. Those purposes were:

(a) eliminating or substantially damaging its competitors, Fresenius and Gambro (being the two relevant Australian subsidiaries of the German and Swedish groups) in the respective PD markets (s 46(1)(a)); and
(b) deterring or preventing Fresenius and Gambro and other potential competitors from engaging in competitive conduct in the respective PD markets (s 46(1)(c)).

45 The first market (being the market in which Baxter was said to have a substantial degree of power) was said, alternatively, to have been:

(a) separate national wholesale markets for LVP fluids, PN fluids and IS fluids, or
(b) a combined national wholesale sterile fluids market.

46 The second market (being the market to which the relevant purposes were said to be directed) was said, alternatively, to have been:

(a) separate State-based geographic markets for PD products, or
(b) a combined national PD products market.

47 In each case, the conduct said to be the taking advantage of the relevant power was in negotiating and entering into five agreements with NSW, ACT, SA, WA and QLD requiring the relevant State or Territory to require LVP fluids, PN fluids (except in QLD) and IS exclusively from Baxter and between 90 to 100 per cent of its PD products, on the basis that the prices under those agreements would be significantly lower than they would be in the absence of the effective sole supply requirement. Thus, it was said, to obtain the significantly lower price for sterile fluids the SPA was required to buy all products exclusively from Baxter. This, it was said, tied or bundled PD products to sterile fluids and their significantly lower prices.

48 A tabular break up of the s 46 claims is as follows:

Paragraphs of application	Asserted market where Baxter is said to have taken advantage of substantial degree of power	Conduct (taking advantage)	Market(s) to which purpose directed
[1]	Wholesale LVP Fluids	Negotiating and entering into supply agreements with NSW, ACT, SA, WA & QLD	NSW, SA WA & QLD PD Products
[2] (Alternative to [1])	Wholesale LVP Fluids	Negotiating and entering into supply agreements with NSW, ACT, SA, WA & QLD	National PD Products
[3] (Alternative to [1] – [2])	Wholesale PN Fluids	Negotiating and entering into supply agreements with NSW, ACT, SA & WA	NSW, SA & WA PD Products
[4] (Alternative to [1] – [3])	Wholesale PN Fluids	Negotiating and entering into supply agreements with NSW, ACT, SA & WA	National PD Products
[5] (Alternative to [1] – [4])	Wholesale IS	Negotiating and entering into supply agreements with NSW, ACT, SA, WA & QLD	NSW, SA WA & QLD PD Products
[6] (Alternative to [1] – [5])	Wholesale IS	Negotiating and entering into supply agreements with NSW, ACT, SA, WA & QLD	National PD Products
[7] (Alternative to [1] – [6])	Wholesale Sterile Fluids (LVP, PN & IS)	Negotiating and entering into supply agreements with NSW, ACT, SA, WA & QLD	NSW, SA WA & QLD PD Products
[8] (Alternative to [1] – [7])	Wholesale Sterile Fluids (LVP, PN & IS)	Negotiating and entering into supply agreements with NSW, ACT, SA, WA & QLD	National PD Products

Australia-wide wholesale LVP market

49 The first and second claims posit an Australia-wide market for the supply at wholesale level of LVP fluids to, amongst others, public hospitals, private hospitals, medical practices and ambulance services. This market was denied.

Asserted market power of Baxter in the wholesale LVP market

50 It was claimed (and was not in dispute) that since at least January 1997 Baxter manufactured a full range of LVP products and supplied almost 100 per cent of the LVP fluids at a wholesale level to public and private hospitals, medical practices and ambulance services in Australia.

51 It was claimed that since at least January 1997, 90 to 100 per cent (and it was admitted as to 80 per cent) of the LVP fluids supplied by Baxter to Health facilities in NSW, QLD, SA and WA have been supplied under contracts which provide for the supply of LVP fluids, together with PN fluids (except QLD), IS and PD products.

52 It was claimed that, at least since January 1997, there were significant barriers to entry into the wholesale LVP market or expanding supply if it were entered. These matters were said to be:

(a) the necessity to register and the time and expense in registering LVP fluids with the Therapeutic Goods Administration ("TGA");
(b) the requirements of States in the analysis of tenders, in particular in relation to quality assurance and local purchasing preference schemes;
(c) difficulties and costs associated with importing LVP fluids, in particular based on the asserted low margins and high water volume;
(d) the existence of long term exclusive supply contracts with Baxter;
(e) the need for significant investment to manufacture and distribute LVP fluids in Australia;
(f) the reasonably stable demand for LVP fluids;
(g) the costs to Health facilities in changing supplier, because of requirement to implement new systems and new equipment; and
(h) the demand from customers other than Health facilities, that is, private hospitals, medical practices and ambulance services, is insufficient to support a minimum efficient scale of production of LVP fluids in the market.

Australia-wide wholesale PN fluids market

53 The third and fourth claims assert (and Baxter denies) an Australia-wide PN fluid market at wholesale levels to, amongst others, public and private hospitals and nursing homes.

Asserted market power of Baxter in the PN fluids market

54 It was asserted that since at least January 1997 Baxter manufactured a full range of PN fluids in NSW and supplied between 80 per cent and 90 per cent of the PN fluids in the PN fluids market. The only substantial competition being an importer, Fresenius-Kabi AG which has supplied up to 10 per cent of the market. (Aspects of these assertions were denied.)

55 It was asserted (and admitted) that since January 1997 approximately 90 to 100 per cent of PN fluids supplied by Baxter to Health facilities in NSW, WA, QLD and SA have been supplied through contracts which provide for the supply of PN fluids, together with LVP fluids, IS and PD products.

56 It was claimed that since January 1997 there have existed significant barriers to entry in the PN fluids market or expanding supply if it were entered. These matters were said to be of a character the same as matters [52(a)] to [52(f)] above.

Australia-wide wholesale IS market

57 The fifth and sixth claims assert (and Baxter denies) an Australia-wide market for the supply at a wholesale level of IS to, amongst others, public and private hospitals, medical practices and ambulance services.

Asserted market power of Baxter in the IS market

58 This was put in similar fashion to the earlier asserted markets: that since January 1997 Baxter has manufactured in NSW a full range of IS products, that it supplied between 70 per cent and 80 per cent

of the IS supplied in the IS market, that it was the only supplier able to supply IS products that are sold in large volumes and that its competition Pharmacia Australia Pty Ltd ("Pharmacia"), Astra Zeneca Pty Ltd ("Astra Zeneca") and Briemar Nominees Pty Ltd ("Briemar") have only supplied "specialist" IS products from their approximate 25 per cent of the market.

59 The asserted barriers to entry since January 1997 were matters said to be of a character the same as the matters referred to at [52(a)] to [52(f)] above and that there were significant costs and perceived risks in Health facilities changing suppliers because, it was said, of the need for new systems and equipment and the untested quality and reliability of competitors.

Australia-wide sterile fluids market and asserted market power theories

60 The seventh and eighth claims assert a combined Australia-wide market for sterile fluids being LVP fluids, PN fluids and IS to, amongst others, public and private hospitals, nursing homes, medical practices and ambulance services.

61 The asserted market power in this market was by reference to the previous allegations.

The PD markets claims

62 The affected market in each of the claims was the PD market. It was asserted to be either State based or Australia-wide. The following wholesale supply markets were pleaded:

(a) NSW PD products (including the ACT);
(b) QLD PD products;
(c) SA PD products;
(d) WA PD products; or
(e) National PD products.

63 It was claimed that since at least 1997 Baxter has manufactured a full range of PD products and supplied them in each PD market; that the Australian subsidiary of the German group, Fresenius Medical Corp Australia Pty Ltd ("Fresenius") and the Australian subsidiary of the Swedish group, Gambro Pty Ltd ("Gambro") have supplied or sought to supply PD products in each of the PD markets; that Baxter has supplied between 90 per cent and 95 per cent of PD products in each of the PD markets; between 90 per cent and 100 per cent of those products were purchased at wholesale level pursuant to contracts with State authorities providing for supply of PD products, together with LVP fluids, PN fluids (except QLD) and IS.

64 It was also asserted that the demand of PD products from private hospitals, medical practices and ambulance services (that is, other than Health facilities) is insufficient to support a minimum efficient scale of production of PD products in any of the PD markets.

The asserted "strategy" of Baxter for supply arrangements

65 The ACCC asserted that since about 1990 Baxter employed various practices in dealing with the purchasing authorities for NSW, ACT, QLD, WA and SA. Those "practices" (identified in paragraph 45 of the statement of claim) were:

(a) to seek to enter supply agreements which had the following characteristics:

(i) at least a two year term;
(ii) sole or substantially sole supply of Health facility requirements of sterile fluids and PD products;
(iii) at prices representing a substantial discount in the price of sterile fluids (especially

LVP fluids) when compared with offers on an item-by-item supply basis without the two year exclusive supply characteristics of (i) and (ii);

(b) to tender on the basis of two or more alternative offers at least one of which had the characteristics of (a)(i) to (a)(iii) above and at least one of which included item-by-item prices;

66 The particulars to these allegations were that this had occurred on the following occasions:

- NSW tenders 1992 and 1997
- QLD tenders 1991, 1997 and 2001
- WA tenders 1991, 1995 and 2001
- SA tenders 1992, 1995 and 2001

67 The asserted relevant contraventions in respect of which relief was sought were, however, more narrowly framed in time. The asserted relevant contraventions were in respect the negotiations and entering into the following agreements:

• the 1998 NSW Supply Agreement between Baxter and the State Contracts Control Board on behalf of NSW made in June 1998 for the period 18 May 1998 to 30 April 2003 (the "1998 NSW Agreement")

• the ACT Health Agreement between Baxter and the Department of Health and Community Care of the ACT made on or about March 1999 that the terms of the NSW Agreement would apply (the "ACT Agreement")

• the 2001 South Australia Supply Agreement between Baxter and SA made on or about 1 May 2001 for the period 1 April 2001 to 30 March 2006 (the "2001 SA Agreement")

• the 2001 Western Australia Supply Agreement between Baxter and WA made on or about 2 May 2001 for the period 1 March 2001 to 28 February 2006 (the "2001 WA Agreement")

• the 2001 Queensland Supply Agreement between Baxter and Qld made on or about 17 April 2001 for the period 1 June 2001 to 31 May 2004 (the "2001 QLD Agreement")

The 1998 NSW Agreement

68 The relevant conduct was said to be constituted by the submission by Baxter on 30 October 1997 of its tender response to the invitation to tender by the State of New South Wales on 8 October 1997 and its revision thereof in February and March 1998, for the supply from 1 April 1998 to 31 March 2000 of a range of LVP fluids, PN fluids, IS and PD products for use in NSW by Health facilities; and the entry into the agreement with the State Contracts Control Board on behalf of the State of New South Wales in June 1998.

The ACT Agreement

69 The relevant conduct was said to be constituted by the agreement between Baxter and the Department of Health and Community Care of the ACT ("ACT Health") that the term of the 1998 NSW Supply Agreement would apply to the ACT. In June 2001, Baxter alleged that ACT Health was in breach of its agreement and in July 2001 it purported to amend its prices higher than existed under the exclusive arrangement.

The 2001 SA Agreement

70 The relevant conduct was said to be constituted by the submission by Baxter on 1 September and 24 November 2000, including variations thereafter, of a response to the invitation to tender by SA for the supply for a two year period (with an option to extend for one year) of a range of LVP fluids, PN fluids, IS and PD products; and by the entry into a contract from 1 May 2001 for the supply of LVP and PN fluids, IS and PD products from Baxter for five years from 1 April 2001 to 30 March 2006.

The 2001 WA Agreement

71 The relevant conduct was also said to be constituted by the submission by Baxter and subsequent variation in response to an invitation to tender in October 1999 from WA for the supply for five years from 1 October 2000 to 30 September 2005 for a range of LVP fluids, PN fluids, IS and PD products for use by Health facilities in WA; and by the entry into a contract in May 2001 with WA for the supply of LVP and PN fluids, IS and PD products by Baxter for five years from 1 March 2001 to 28 February 2006.

The 2001 QLD Agreement

72 The relevant conduct was also said to be constituted by the submissions by Baxter and subsequent variation in response to an invitation to tender in January 2000 from QLD for the supply for three years of a range of LVP fluids, IS, PD and haemodialysis products (not PN fluids) for use in QLD by Health facilities; and by the entry into a contract from 17 April 2001 with QLD for the supply of substantially all LVP fluids, PD products and IS from 1 June 2001 to 31 May 2004.

Section 47 claims

73 The substantially identical body of conduct (with one additional aspect) is said to give rise to contraventions of s 47 of the Act. The additional aspect of conduct relied upon is that from 18 May 1998, 1 April 2001 and 1 March 2001, Baxter has supplied LVP fluids, PN fluids, IS and PD products to NSW, SA and WA, respectively, under the relevant agreements and that from 1 June 2001 Baxter has supplied LVP fluids, IS and PD products to QLD under the relevant agreement. This conduct was said to be, the offering to supply, or the supply, of goods (LVP fluids, IS, PN fluids (except for QLD) and PD products) or the supply of those at a particular price on condition that the State or the ACT will not, or will not to a limited extent, acquire such goods from a competitor of Baxter, thereby satisfying s 47(2) of the Act.

74 The various claims under s 47 of the Act were framed in the alternative by reference to various markets for PD products LVP fluids, PN fluids, IS and sterile fluids. In each case the underlying conduct was the same: negotiating, entering into and supplying pursuant to each of the five impugned agreements.

75 The above conduct by reference to the five impugned agreements was said to be for the purpose, being a substantial purpose, of substantially preventing, hindering or lessening of competition in:

(a) the separate State-bound geographic markets for PD products,
(b) a combined national PD products market,
(c) the separate national wholesale market for LVP fluids, PN fluids and IS fluids, or
(d) a combined national wholesale sterile fluids market.

76 The above conduct by reference to the five impugned agreements was also said to have had the effect or likely effect of substantially preventing, hindering or lessening competition in those markets.

77 The above conduct by reference to two or more of the impugned agreements was said to have been done for the above purpose and with the above effect or likely effect in relation to the above markets.

78 A tabular break up of the s 47 claims is as follows:

Paragraphs of application	Exclusive dealing	Effect/Purpose	Affected market
[9]	By negotiating, entering into and supplying under each of the agreements with NSW, ACT, SA, WA & QLD	Purpose of	NSW, SA WA & QLD PD Products
[10] (Alternative to [9])	By negotiating, entering into and supplying under each of the agreements with NSW, ACT, SA, WA & QLD	Purpose of	National PD Products
[11]	By negotiating, entering into and supplying under each of the agreements with NSW, ACT, SA, WA & QLD	Effect or likely effect of	NSW, SA WA & QLD PD Products
[12] (Alternative to [11])	By negotiating, entering into and supplying under each of the agreements with NSW, ACT, SA, WA & QLD	Effect or likely effect of	National PD Products
[13]	By negotiating, entering into and supplying under 2 or more of the agreements with NSW, ACT, SA, WA & QLD taken together	Effect or likely effect of	NSW, SA WA & QLD PD Products
[14] (Alternative to [13])	By negotiating, entering into and supplying under 2 or more of the agreements with NSW, ACT, SA, WA & QLD taken together	Effect or likely effect of	National PD Products
[15]	By negotiating, entering into and supplying under each of the agreements with NSW, ACT, SA, WA & QLD	Purpose of	LVP Fluids, PN Fluids and IS markets
[16] (Alternative to [15])	By negotiating, entering into and supplying under each of the agreements with NSW, ACT, SA, WA & QLD	Purpose of	Sterile Fluids market (LVP, PN & IS)
[17]	By negotiating, entering into and supplying under each of the agreements with NSW, ACT, SA, WA & QLD	Effect or likely effect of	LVP Fluids, PN Fluids and IS markets
[18] (Alternative to [17])	By negotiating, entering into and supplying under	Effect or likely effect of	Sterile Fluids market (LVP, PN & IS)

	each of the agreements with NSW, ACT, SA, WA & QLD		
[19]	By negotiating, entering into and supplying under 2 or more of the agreements with NSW, ACT, SA, WA & QLD taken together	Effect or likely effect of	LVP Fluids, PN Fluids and IS markets
[20] (Alternative to [19])	By negotiating, entering into and supplying under 2 or more of the agreements with NSW, ACT, SA, WA & QLD taken together	Effect or likely effect of	Sterile Fluids market (LVP, PN & IS)

Further factual background

Relevant Participants

79 A number of companies other than Baxter participate, and have participated in the past, in the manufacture, importation and selling of products in and into Australia which bear upon the issues in these proceedings. The major competitors or potential competitors of Baxter in the sale of sterile fluids in Australia are Gambro, Fresenius, B. Braun AG and Abbott Laboratories.

Gambro

80 Gambro is the Australian subsidiary of Gambro AB, a Swedish company. Since its inception in 1964, Gambro AB has been involved in renal dialysis. Its three major corporate arms (Gambro, Cobe and Hospal) are concerned with dialysis, blood component technology, the cardiovascular area, and acute therapy and critical care. To a significant degree, and certainly in Australia, Gambro is a specialist renal and dialysis company. Gambro commenced business in Australia and New Zealand in 1975.

81 Gambro considers Baxter and Fresenius to be its two main competitors in the global dialysis industry. The worldwide market shares of Gambro, Baxter and Fresenius for HD products were in 1998-2001 in the order of 20 per cent, 7 per cent and 30 per cent, respectively. For PD products they were 2 per cent, 70 per cent and 17 per cent, respectively, and for Renal Intensive Care they were 54 per cent, 14 per cent and 12 per cent, respectively.

82 Gambro manufactured haemofiltration fluids in Australia from 1985, initially through the manufacturing plant of a company called Delta West (up to 1987) and then at a plant of another company, Kendall-McGraw (up to 1989). Gambro began selling imported HD fluids in Australia in 1986. In 1990 Gambro purchased the Kendall-McGraw sterile fluids plant in Dandenong. From 1990, Gambro began manufacturing PD fluids and haemofiltration fluids at this plant. In 1991, this plant also commenced producing HD fluids.

83 Mr Stokoe, the managing director of Gambro in Australia, gave evidence that the acquisition of the Dandenong plant was part of an overall strategy to expand Gambro into new product areas. From the evidence, including Confidential Exhibit JTKS-2, it is apparent that in the early to mid-1990s Gambro was making a concerted effort to gain HD and PD business in Australia.

84 Today, Gambro supplies, and provides support for, renal equipment, owns and operates dialysis clinics, and manufactures HD concentrates and solutions for PD and haemofiltration. Renal related products constitute 93 per cent of its Australian business.

85 As to HD products, Gambro offers complete HD systems, including dialysis machines, dialysers, blood lines, powder concentrate, concentrate solutions, catheters and needles, water treatment systems, machine disinfection products and technical and educational support. Gambro manufactures its HD and HF equipment overseas. Only its sterile and non-sterile dialysis fluids are produced in Gambro's Australian plant at Dandenong.

86 In mid-1991 a major dialysis clinic in Sydney, the Sydney Dialysis Centre (the "SDC") began to use Gambro PD products. By 1992, the SDC was using Gambro PD products for 150 of its 460 PD patients and by 1993 Gambro PD products had become well received in other major hospitals such as St Vincents in Sydney.

Fresenius

87 Fresenius AG is a publicly listed German company which in 2001 (through its various subsidiaries) employed more than 60,000 people worldwide, with a turnover in excess of USD 4.2 billion. There are three corporate divisions of the group – Fresenius Medical Care specialising in dialysis products and services and related treatments; Fresenius Kabi specialising in intravenous products, including infusion therapy, PN, EN and related treatments; and Fresenius ProServe GMBH which is involved in the ownership of health care facilities and the construction of production facilities.

88 Fresenius Medical Care is the largest of the three divisions and is the only division which operates in Australia. In 2002, the Australian subsidiary had 102 employees and sales of $43 million. Fresenius Medical Care is a worldwide specialist dialysis group whose products treat more than 100,000 patients in more than 1,400 clinics around the world. It has 30 manufacturing plants in 15 countries, each plant manufacturing different products. For example, an Australian plant and a UK plant produce only HD fluids, a Spanish plant produces PD fluids only, a German plant produces a full range of PD products.

89 Fresenius Kabi manufactures (though not in Australia) a comprehensive range of LVP fluids and PN and EN fluids. It does not supply, and has not supplied, LVP fluids and EN fluids in Australia, but does supply some PN fluids through a supply arrangement with Baxter. In 1998, Fresenius Kabi acquired the PD fluids business of two companies and Baxter began distributing those PN fluids for Fresenius Kabi. In 2000, Fresenius Kabi PN fluids constituted 18 per cent of PN fluids sold in Australia.

90 Fresenius sought to enter the HD and PD markets in Australia in about 1995. In 1996, Fresenius Medical Care set up its headquarters for the South East Asia region in Sydney. In 1996, Fresenius began offering HD and PD products around Australia. In 1996, Fresenius purchased a production plant in Smithfield in Sydney from Ajax Chemicals at which it commenced to manufacture HD fluids. The plant did not, and does not, make PD fluids.

91 Mr Mechtersheimer, the Vice-President, South Asia Pacific of Fresenius Medical Care, said that in Australia in 1996, Gambro was the dominant HD supplier with a small share of the PD market and Baxter was the dominant PD supplier with a small share of the HD market. Since entry into the Australian market, it would appear that Fresenius has increased its market share of HD products to over 50 per cent; though its share of the PD market has not risen above 5 per cent. Fresenius' turnover in Australia had increased from $7 million in 1996 to $30 million by 1 January 2002.

92 Fresenius imports its HD equipment, though it produces HD fluids at its Smithfield plant. It also imports its PD products including fluids. Fresenius largely contracts out the distribution of its products, with the exception of NSW where it has its own warehouse, staff and trucks for the performance of this function.

93 The ACCC's case was that the inability of either Gambro or Fresenius to make headway in the PD

market was a result of the impugned agreements and their predecessors.

Abbott

94 Abbott Laboratories is a US health care products and services company. Worldwide it operates 54 offices, sells in more than 130 countries and employs over 70,000 employees. Its sales in 2002 exceeded USD 17.6 billion. Abbott Laboratories, through a subsidiary company, Abbott Australasia Pty Ltd ("Abbott"), has been in Australia since 1937. In 1970, Abbott acquired intravenous fluid manufacturing plants in Sydney, Adelaide and Perth. The Perth plant was closed in 1980. A new plant was built in Adelaide. Up until 1992 (when the Adelaide plant closed), Abbott manufactured and supplied LVP in Australia. Abbott continues to supply EN feeds and products. They are manufactured overseas. Abbott, however, no longer manufactures and supplies LVP fluids in Australia, having left the market in circumstances to which I will come.

95 Abbott supplied PN fluids manufactured in the US to Australia in 1987 for 1 year, but discontinued that supply because of the complexities of TGA registration. Mr Baker, who is a Program Manager Class A and Demand Manager with Abbott, said that Abbott does not consider the supply of PN fluids in Australia to be in its strategic objectives, because the number of patients is static and the capital cost of building a compounding plant are prohibitive.

96 From 1985 to 1992 Abbott's share nationally of the LVP market fluctuated from 10 per cent (to Baxter's 90 per cent) to 44 per cent (to Baxter's 56 per cent). This fluctuation was, to a significant degree, a result of the success or otherwise of these companies in winning large scale State tenders.

B. Braun

97 B. Braun Melsungen AG ("B. Braun AG") is a multinational health care organisation based in Germany. It has a turnover of EUR 2.6 billion, employs over 28,000 employees and operates in almost 50 countries. B. Braun AG supplies approximately 40 per cent of each of the North American and German IV fluids markets. B. Braun AG provides all products utilised in intravenous therapy, as well as critical care products. It has manufacturing facilities in 25 countries.

98 B. Braun Australia Pty Ltd ("B. Braun") was established in Australia in 1982 and employs 70 employees. It supplies a certain intravenous therapy, a colloidal volume replacement and surgical instruments.

99 B. Braun AG does not manufacture any products in Australia. It manufactures sterile fluids and PD fluids in Germany and Malaysia. B. Braun currently has a full range of IV products, haemodialysis products and some PD products registered with the TGA. It spends approximately $15,000 per year to maintain these registrations and has approximately 80 per cent of LVP fluids required by NSW registered. B. Braun has registered with the TGA 80 per cent of the LVP fluids that were sought in the 1997 NSW request for tenders to supply IV fluids and IS. However, it does not have any PN products registered in Australia. At one time, it did have PD products registered, but it did not sell them in Australia. It should be noted at this point that registration of a company's product with the TGA does not mean that company can sell product which may be imported or manufactured in Australia. In either case, the manufacturing plant in Australia or overseas must meet specified requirements.

Other companies

100 Other companies participate and have participated in Australia in the selling of relevant or cognate products. Tyco Healthcare Australia Pty Limited ("Tyco Healthcare") is a subsidiary of Tyco International which is a diversified manufacturing and service company that operates in over 100 countries. Tyco Healthcare's business includes medical, surgical, respiratory, imaging, pharmaceutical and retail products. It sells saline solutions in Australia largely to pharmacies, and in

the main they are utilised as lens cleaners. Its Gelflex Normal Saline holds a 40 per cent market share within the normal Saline category.

101 Whilst Tyco Healthcare's saline solutions could be utilised as IS, Tyco Healthcare does not market its products under that banner. Tyco Healthcare has decided not to market a full range of saline solutions to hospitals because it perceives the margins to be too low and it believes the business not to be profitable. Tyco Healthcare is a pure sales organisation in Australia. It does not manufacture any products here.

102 Other companies manufacture or sell IS in small quantities: Pharmacia Australia, Promedica, Briemar, Orion and De Fries. Delta West was a significant local manufacturer of IS, at least in the late 1980s and early 1990s.

103 Astra Zeneca is the Australian subsidiary in a British based multinational group. It is one of Australia's leading suppliers of pharmaceuticals. Its product range has in the past included SVP fluids and IS. It has a manufacturing plant at North Ryde where a range of products, including SVP (but not IS) are made. It ceased manufacturing of sterile fluids by 1999.

104 Even though Astra Zeneca has dedicated machinery for the manufacture of SVP fluids, this equipment cannot be utilised for producing LVP fluids because of added complexities and unsatisfactory results. As a result if Astra Zeneca were to produce LVP fluids, an investment of approximately $10 million in suitable equipment would be required. However, since this would only permit a modest production of LVP fluids and a low return on investment, LVP fluids are not strategically important to Astra Zeneca, and for these reasons, Astra Zeneca does not intend to enter the LVP market in Australia.

105 As to IS, Astra Zeneca discontinued all such production, with the exception of one particular product, by 1997. Production of this product ceased in 1999.

The manufacturing processes involved and the history of production in Australia by Baxter

106 The General Operations Manager of Baxter, Mr John Bragg, gave evidence which included descriptions of the manufacturing processes of LVP fluids, PN fluids, IS and PD fluids and of the history of production by Baxter in Australia. He was not cross-examined on these matters. I was able to observe Mr Bragg in court when he was cross-examined on other aspects of his evidence. He gave evidence in a straightforward and open fashion. He appeared to answer questions put to him without prevarication. I found him to be attempting to be of assistance.

107 After commencing operation in 1963 in a joint venture with a local company, manufacturing a small range of products, Baxter, in 1973, in its own right, established a manufacturing facility in Toongabbie, in Western Sydney. In 1980, Baxter produced various products at the Toongabbie plant: IV fluids, PN fluids, PD fluids, IS, blood collection packs and some associated components. At this stage PD was in its infancy in Australia.

108 The Toongabbie plant was expanded in 1982 to include a new compounding facility in which PN fluids and other drugs could be mixed.

109 In 1985, through a takeover of a corporation in the US (American Hospital Supply Corporation ("AHS")) by BI Inc, manufacturing operations were acquired at Balgowlah in Northern Sydney, and in New Zealand. The Balgowlah operations were incorporated into the Toongabbie plant and the plant at Balgowlah was closed. After a time, the New Zealand plant was also closed and supply was made to New Zealand from the Toongabbie plant.

110 In the mid 1990s, Baxter launched major PD products in Australia which had been developed in

Europe and the US: "Freeline Solo" (for CAPD) and "HomeChoice" (for APD).

111 Baxter has invested not insignificant amounts of capital in the Toongabbie plant.

112 During the relevant period, the operation of the Toongabbie plant can be described as follows. It has five fluid manufacturing lines: two are for high volume IV and PD and are highly automated, two are for smaller volume IV, PN and PD fluids and are more manually run, and one line is for IS and various glass bottle products which may be PN and IV fluids.

113 Finished goods are produced on a batch basis. Fluid bags, tubes and wrappers are made. Chemicals are weighed according to the type of fluid to be produced. Chemicals are mixed in the mixing facility using high grade water. The same stainless steel vats are used for the production of all fluids. After testing the fluid is released to the filling lines for filtration and pumping. The bags are labelled, filled, sealed and placed into a pouch. The pouch is sealed, steam sterilised and placed into cartons.

114 The production process is the same for IV, PD and PN fluids and IS with the following qualifications:

(a) obviously each has a different chemical formulation;
(b) different tubing lengths and types of connecting apparatuses are used for PD and IV fluid bags;
(c) IS are contained in plastic bottles not PVC bags;
(d) the machine used to assemble bags for the Freeline Solo PD product is a dedicated machine; and
(e) some IS and PN fluids use glass bottles.

115 Though the fluids are sterile, this is because of the need for the solution container system to be sterile. The production is in a clean, but not sterile, environment in accordance with the relevant Australian manufacturing code and guide adopted by the TGA.

116 Dedicated production facilities are not required for the manufacture of PD and PN fluids.

117 Since 2003, the Toongabbie plant has also produced HD fluids.

118 Appropriate scheduling of production enables minimisation of down-time in the production of different types of fluid. It takes approximately 20 to 40 minutes to clean and flush equipment for the next solution and to set up different labelling.

119 Output and capacity are flexible to meet demand.

120 The evidence disclosed that in other countries where the market volume may be greater than in Australia, specific plants often specialise in a more limited range of these fluids.

Capital costs associated with manufacture

121 The investment required to develop, plan and construct a sterile fluid plant in Australia was estimated variously by witnesses as $10 million to set up a PD plant in Darwin (Mr Mechtersheimer); $20 million and two years to complete as a manufacturer in the IS market (Mr Anderson); $40 million to set up a plant such as Baxter's plant in Toongabbie (Mr Stokoe); $40 million to set up a medium size PN and LVP manufacturing plant (Mr Bhargava). I need not decide this issue, save to say that building such a plant would involve the likely expenditure of millions of dollars in the order of amounts identified by these witnesses.

122 The evidence as to capital expenditure by Baxter on the Toongabbie plant was not clear, but it is a fair inference that since 1992 some millions of dollars have been invested in capital equipment and the plant.

The distribution of sterile fluids and PD products

123 The shelf-life of different products varies. LVP fluids and IS have a shelf life of around two years. Standard PN fluids with amino acids and fat emulsions last 18 to 24 months, others up to five years. Some customised PN products may only last a few days. PD products have a shelf-life of about 18 months to two years.

124 The supply of sterile fluids requires local or State warehouses to support distribution which can originate from one production facility (such as Baxter's at Toongabbie) or from one port of entry if importation were to be undertaken (say by B. Braun). Head office facilities would not need to be duplicated and transport would be subcontracted.

125 The supply of PD products requires not just a local or state warehouse but also locally based support staff to assist patients and hospitals. For the home administration of PD products, distribution systems are required which take fluids and product not just to the renal units at hospitals, but also to patients at their homes. Fresenius, for instance, operates warehouses in WA, QLD, SA, NSW and Victoria, employing local drivers on contract to service patients at home, several nurses in each state and a PD therapy manager. (See generally Mr Hand's affidavit.) Baxter has similar arrangements.

Market shares

126 Since at least January 1997, Baxter has supplied almost 100 per cent of LVP fluids at the wholesale level to public hospitals, private hospitals, medical practices and ambulance services in Australia. B. Braun supplied in the relevant period one "niche" LVP product into Australia. Baxter was the only local manufacturer of LVP fluids since 1993.

127 There are numerous local producers and suppliers of SVP fluids. Given their nature and use SVPs can be seen to be in a different market to LVP fluids.

128 Baxter was during the relevant period the largest supplier of IS – about 95 per cent of sales.

129 Baxter was the only local manufacturer of PN fluids, though it distributes Fresenius Kabi product.

130 The market shares of PD were described by Mr Stokoe and Mr Hand in evidence that was not seriously challenged. Mr Stokoe set out Gambro's worldwide shares of HD and PD markets as at March 2002 as follows:

Region	HD	PD
Worldwide	19%	2%
Europe	39%	4%
United States of America	15%	0%
Asia excluding Japan	20%	6%
Canada	41%	0%
France	49%	7%
Germany	33%	6%
Korea	45%	10%
Australia	33%	1-2%

131 Mr Stokoe set out Baxter's PD market shares as follows:

Region	1996	1998	2000
Worldwide	78%	76%	77%
Europe	73%	71%	74%
USA	79%	79%	76%
Asia (excluding Japan)	78%	76%	77%
Australia	<90%	<90%	<90%

132 Mr Hand set out Fresenius' HD and PD market shares as at December 2001 as follows:

Region	Haemodialysis	Peritoneal Dialysis
Worldwide	30% +	16%
New Zealand	30%	20%
Australia	58%	5%

133 Mr Leyland, a senior executive of BI Inc, confirmed the accuracy of the worldwide market shares table in Mr Stokoe's affidavit, with the exception of Baxter's market share for PD, which he says is 5% - 6% higher. He also agreed with tables setting out Gambro's market shares and Baxter's market shares that appear in Mr Stokoe's affidavit, as well as a table that sets out Fresenius' market shares in the affidavit of Mr Hand.

The history of State contracts for the supply of LVP, PN and PD fluids and IS (up to the impugned conduct)

134 Baxter submitted, correctly, that its conduct between 1998 and 2001 which is impugned by the ACCC must be evaluated in the context of what occurred before, and, if probative, after, such conduct: *Boral Besser Masonry Ltd v ACCC* (2003) 215 CLR 374at [34] and [273].

135 This background is particularly important in understanding the extent to which the impugned conduct of Baxter can be characterised as the reasonably anticipated response to invitations by the respective States and Territory in the conduct of their affairs. As will be seen in due course this is important for the application of the principle of construction which can be referred to by shorthand as "Crown immunity" or "derivative Crown immunity".

136 During the 1980s, there were four manufacturers of IV solutions in Australia, namely Baxter, Delta West, Kendall and Abbott. By the late 1980s, Kendall had closed its manufacturing facility, and in 1990, Gambro purchased Kendall's plant at Dandenong. Gambro has never sought to manufacture sterile fluids at that plant (which is possible) because it purchased the plant for the purpose of manufacturing PD solutions. Delta West continued to manufacture some IV fluids (mainly minibags and IS) until 1993 and sold them until 1996. As discussed earlier, Abbott manufactured sterile fluids in Australia until it closed its Adelaide plant in 1992.

137 Until the mid-1980s, no company had an exclusive supply agreement with any of the States. In about 1983, Baxter successfully tendered for a sole supply agreement with Queensland for the supply of IV and PD fluids and IS for hospitals for a two year period. Shortly after this, NSW awarded a sole supply contract to Abbott for IV fluids. In 1985, NSW entered into contracts with both Abbott and Baxter for the supply of IV fluids, and between 1985 and 1992, Baxter supplied 85 per cent of the volume of these fluids.

138 Prior to about 1990, by reason of Commonwealth State funding arrangements, not a great deal of PD products, including fluids, was sold directly to the States. A change to funding arrangements in about 1990 saw States funded by the Commonwealth purchase PD products in their own right.

Queensland 1987 and 1990

139 In 1987, Baxter made various bids to the Queensland State Supply Board for a tender covering IV, IS and PD solutions. Four offers were made – two on the basis of item-by-item prices for all products covered by the tender, and two based on guaranteed sole supply for all items covered by the tender. The prices in the latter two offers were significantly below the first two. No analysis was made in the proceedings of these prices or of the comparison between them. There is a similarity between this tender and the impugned tender. But it is important to recall the limited purchasing of PD products by the States at this time. Baxter won the bid on a sole supply basis to Queensland.

140 In 1990, Baxter once again made bids on a Queensland tender which had an item-by-item offer, and two sole supply offers (one for two years and one for three). The third offer, for three years sole supply, was accepted. Again, there was no analysis in these proceedings of the comparative prices in respect of the tender. Indeed, the prices in the tenders were not in evidence.

141 Mr William Kelly, who was the Manager of Queensland State Stores Board ("QSSB") between 1988 and 1996 and then the Director of Queensland Health Services Purchasing & Logistics Group ("QHSPLG") between 1996 and 2002, was called by the first respondent to give evidence in this proceeding. He was forthright and straightforward, highly experienced and down to earth. I accept his evidence in full in relation to all tenders. Mr Kelly noted that between 1996 and 2002, he was responsible for the operation of approximately 90 different standing offer arrangements. The applicant called a Mr William Stewart (Manager of QHSPLG) to give evidence, and his affidavit was not contested.

142 Mr Kelly recalled that in or about August or September 1991, he and his staff held discussions in relation to consolidating the 330 separate period contracts that were then in existence for the supply of pharmaceuticals and other medical products to the State of Queensland. In Mr Kelly's view, this number of contracts had become too time consuming and cumbersome to administer. As a result, IV fluids and IS were at that time consolidated into the one contract. HD and PD fluids, however were not part of this contract because of perceived different organisational requirements related to the negotiations in respect of these two products (i.e. in terms of the clinical consultation required).

South Australia 1991

143 From May 1991 to April 1993, Baxter had a sole supply agreement with SA in relation to sterile fluids and PD fluids. Mr Horstmann, a former employee of "Supply SA", gave evidence that before

1995 (and it can be inferred, as early as 1991) LVP, PN and PD fluids and IS were linked both in supply by Baxter and in the same contract. He recalled that Baxter tenders before 1995 generally included a higher item-by-item price compared to a sole supply price.

Western Australia 1991

144 In October 1991, Baxter made five separate and contemporaneous offers in respect of a proposed contract with the State Supply Commission of Western Australia for products which included IV fluids, IS, PN and PD fluids. The structure of the offers was made clear in evidence. Offer 1 was an item-by-item bid for two years with a CPI adjustment after one year. All other four bids were sole supply bundled arrangements: two years, two years with a one year option, five years for all but PD fluids and two years plus a one year option for PD fluids, and five years.

145 The bid letter stressed the importance of total volume through the facility.

146 Though individual pricing was not in evidence, the bid letter did contain the relevant savings said to be made. The evidence does not permit a comparative analysis to assess the cost of acceptance of an item-by-item offer for all but PD and another supplier's PD products. But it is fair to say that the saving over five years between the item-by-item offer and the five year exclusive bundled offer was not insignificant: in the order of $2.25 million, based on an expenditure over five years in the bundled offer of $12.9 million.

147 It should be noted that at a time when Abbott was a domestic manufacturer of IV fluids Baxter did not put forward a bid for sole supply of LVP fluids and PN fluids, separating out PD fluids.

148 The two year offer with a one year option was accepted and the contract was extended to November 1994.

New South Wales 1992 and 1993

149 Before the process for the establishment of what became contract no. 938/904, the NSW Department of Health ("NSW Health") received pre-tender submissions, first (on 16 March 1992) from a consortium of Abbott, Delta West and Gambro, and later (on 7 April 1992) from Baxter.

150 The submission of the consortium was expressed as an attempt to provide competition to Baxter over all the relevant market "segments" (being the term used in the submission) which were identified in the covering letter to the submissions on Abbott letterhead as, broadly, LVP fluids, IS, PN and PD fluids (though these four categories were broken up into seven segments). The submission noted that in the 12 to 18 months prior to March 1992 SA, WA, Tasmania and QLD had accepted tenders from Baxter. It stated that the tenders were *constructed* to favour the supplier with the broadest range of product. The submission pointed out what were seen to be the anti-competitive consequences of such exclusive tenders. The submission also made the point that the cost structures of high volume LVP products were particularly sensitive to volume throughput. The letter also stated:

> *...We are penalised by:*
>
> *1. Bidding practices and tender construction which encourage bundling and a sole supplier situation.*
> *2. Artificially low prices in competitive areas of the market, compared to world parity.*
> *3. Resulting lower volume which drives unit costs up versus competition.*
>
> *Failure to gain an assured unit volume at realistic prices raises the dilemma of whether to discontinue operations as there is a disproportionate rise in costs for small-run*

production.

151 This letter highlights the fact that one element of Baxter's competitors' difficulties was the way that the tender processes were constructed. To this point this had not been dictated by Baxter but decided by the States. That remained the position up to and during the relevant period.

152 The submission of the consortium was an attempt to meet the product coverage of Baxter and involved an attempt to persuade NSW not to concentrate its purchasing and not to award the contract to Baxter. The submission included the following (the abbreviation "TPN" referring to Total Parenteral Nutrition):

> *• That NSW Supply and Department of Health consider a separate proposal for TPN products in the new supply period to reduce the opportunity for bundling, and list all supply requirements on a "line-by-line" basis, with no provision for the pricing tactics discussed above.*
> *• That the joint submission will indicate the minimum volume and price required in each segment to remain viable.*
> *• That NSW Supply and Department of Health consider awarding supply of sterile fluid segments or items to specified suppliers for particular Area Health Boards. Management of the Supply Agreement is facilitated and this option is logistically practicable.*
> *• That this Supply Agreement have a term of 3-5 years, with CPI price mechanism incorporated.*

153 In a contemporaneous document sent to NSW Health, Abbott stated that the Adelaide sterile fluid manufacturing plant was not viable at the then current utilisation level. Abbott stated that to continue manufacturing LVP fluids it required a guaranteed minimum volume, representing 45 per cent of the NSW LVP market and higher pricing than currently obtained. It made clear that it could not wait for the expiry of the next tender process later that year. It needed a decision virtually straight away.

154 In April 1992, an officer of one of the Area Health Services sent a memorandum to NSW Supply which was critical of the consortium proposal. The price suggested by Abbott was said to be a 25 per cent increase on current prices. The memorandum set out clear reasons for the rejection of the proposal and reflected a clear recognition of the consequences thereof. It stated, amongst other things, the following:

> *There is absolutely no guarantee they will not, in 3 to 5 years at contract termination close their plant and withdraw from the market.*
>
> *Missing, is a stated and detailed investment plan.*
>
> *A plan to expand capability, improve efficiency, reduce costs, and generally become permanently more competitive. A plan to set up a manufacturing base capable of ensuring an economically sustainable market share into the next century.*
>
> *Without this why should the Department of Health, here or elsewhere in Australia, concede or agree to this proposal.*
>
> *If Abbott and their alliance partners submit a detailed investment plan with irrevocable commitment to that plan their request should be considered, probably favourably. Otherwise, I would strongly recommend outright rejection.*
>
> *NOTE: Rejection would create a monopoly for Baxter and a vacuum for another competitor to fill. The importance of these products to the Australian Health Service, the Federal Government's ability to change qualification requirements if forced, and availability of large offshore suppliers would ensure Baxter remained competitive. What*

Company would want to lose a monopoly by stupid pricing.

155 The consortium proposal was rejected in May 1992. An invitation was made for the members of the consortium or Abbott to put forward a more detailed business plan.

156 Meanwhile, Baxter had submitted a pre-tender proposal. This did not contain specific pricing, but it was an offer for a five year contract (with an option to extend), with firm prices for 12 months, and CPI adjustments thereafter, based on a sole supply arrangement for NSW public hospitals and guaranteed supply. The proposal contained the following assertion made in reference to Baxter's cost structure:

> *Baxter's range of sterile fluids are produced in a single facility at Toongabbie, N.S.W., with common equipment, staff and technology. The most important factors in achieving* ***low cost*** *product, and therefore* ***low price*** *products, is having a guaranteed unit volume to utilise and absorb our common investment in sterile fluid production; and having a continuing commitment to supply our broad range of products.*
> [emphasis in original]

157 The reference to "sterile fluid production" in this document was to the production of IV solutions, IS, PN and PD fluids (and others).

158 The contents of the above assertion can be accepted as containing propositions of general validity. These were matters stressed by Abbott as important in connection with the continued existence of the Adelaide factory. They were matters referred to in the proposal by Baxter to Queensland in 1987.

159 On 11 June 1992, Abbott (apparently now on behalf of itself) put forward another quotation and business plan for IV and PN fluids. The author of the letter (who was not a witness) referred to the "seven-segment sterile fluid market in Australia".

160 A further pre-tender submission was then received from Baxter on 15 June 1992. It contained three pricing options, which were all on a sole supplier basis. The evidence does not disclose what Abbott and Baxter knew about the timing of these respective events. However, shortly after this, some time prior to 30 June 1992, Abbott decided to close its manufacturing plant. The news of this became public by early July 1992.

161 With the apparent withdrawal of one of the two local IV fluid manufacturers, NSW Supply took the view that steps should be taken to secure the long term supply of sterile fluids on appropriate terms by negotiating a "strategic relationship" with Baxter. A negotiating team, which comprised Messrs Houghton, Kinkade and Hawkins, was formed to that end. This can be seen as a commercial response to the reality that the closure of Abbott's facility left only one local manufacturer of LVP fluids and the bulk of sterile fluids. The approach to Baxter was aimed at obtaining for the State such advantages as could be negotiated in respect of prices, investment and quality of product.

162 This negotiating team met Mr Lee and others from Baxter in the second half of 1992 and early 1993. Early in the negotiation, Mr Lee was challenged about prices and, in particular, why Queensland had better prices than NSW. Mr Lee responded that Queensland had given Baxter three years' exclusive supply. At this point, one of the NSW negotiating team specifically sought five, seven and ten year exclusive bids for "IVs, irrigating solutions and PDs". Baxter later declined to offer pricing for ten years, and indicated that they would tender for five years. At one meeting in December 1992, during negotiations about price escalations, discussion became forceful, if not acrimonious. Mr Kinkade said to Mr Lee:

> *This is ridiculous. It does not matter how long it takes. We'll sponsor another company to come in and we'll get you.*

(Mr Lee's affidavit referred to this conversation in December 2002. In its context, that was plainly a typographical error.)

163 The evidence reveals that the parties continued thereafter to negotiate.

164 These events in 1992 after the withdrawal of Abbott reflect two important facts. First, the NSW government wanted a long term contract and one in which there was an exclusive supply arrangement covering sterile fluids and PD products. They saw the ability to lock in a negotiated position as advantageous in dealing with Baxter (which had a significant advantage of being the only local manufacturer). Secondly, the NSW government did not see its position as powerless, by any means. Though it certainly needed to buy the products in question, it had a power to assist entrants into the market and to do great harm to Baxter's investment in Australia. The evidence above reveals that not only did the negotiating team realise that, it used that threat in the 1992 negotiations.

165 On 21 October 1992, Baxter had put in a further proposal signed by Mr Lee. It contained three price options. The first, Schedule A Offer, was an item-by-item offer based on no guarantee of supply. The second, a five year offer based on current market share. The third was also a five year offer based on exclusive supply. The effect that each offer would have, if taken up, was summarised in a confidential memorandum dated 4 November 1992 produced by NSW Supply Services. That memorandum suggested that the Schedule A Offer contained an "excessive" price escalation and could be "read as a threat". It also said that the Schedule B Offer called for guaranteed market share and that the Schedule C Offer called for "a guaranteed monopoly position".

166 Though this was not one of the impugned agreements, the references by the person who prepared the memorandum to "excessive" price escalation and that the offer could be "read as a threat" were stressed by the ACCC. To a degree, certainly in respect of the consideration of Baxter's offers in its various tenders and the assessment of Baxter's purposes in making these offers, one can draw conclusions about the offers without the need for rigorous mathematical or theoretical assessment by reference to posited economic models. I will deal with the expert evidence in due course. It suffices at this point to say that there were a number of cotemporaneous assessments by persons in the SPAs whose judgments and comments on the offers are of particular assistance in understanding both the effect and the purposes of the offers in question. These comments in relation to the 1992 offers, in particular given the pattern of continuing events into the 1990s and up to 2001, set a helpful context in the understanding of the structure of the impugned tenders.

167 Even though the negotiating team continued its discussions with Baxter, Mr Houghton explained in his affidavit that because there was still no agreement between NSW and Baxter as at November 1992, it was decided that a public tender should be held. In addition to this, Mr Kinkade in his evidence suggested that because none of the submissions from Baxter had been satisfactory the purpose of the tender was to test the market.

168 On 11 January 1993, NSW Supply issued an invitation to tender for the supply contract (938/904) for sterile fluids in NSW for a period of three years, with an option to extend for a further two years (clause 2.2). The invitation sought the supply of IV, IS, PN and PD solutions (Annexure 2 to section 2), and it allowed tenderers to tender for one or more of the products (clause 1.4) at constant or variable prices (clause 1.21). It also envisaged alternative bids along the following lines:

> *Tenderers are in the first instance required to tender in accordance with the tender requirements. Alternative tenders may be considered but must meet the objective and intent of the tender requirement" (*clause 1.14)

Thus, as to whether Baxter's alternative bids answered the tender depends upon whether its objective and intent were met.

169 Tenders were received from Baxter, Gambro, Astra Zeneca and Clifford Hallam Pharmaceuticals

Pty Ltd ("Clifford Hallam"). NSW Supply, however, continued to negotiate with Baxter. Gambro tendered for both IS and PD products, Astra Zeneca tendered for a small number of LVP and IS fluids, and Clifford Hallam tendered for a range of LVP and IS fluids. Baxter was the only company to tender for all products.

170 Baxter's tender included an item-by-item offer, which had a total cost of $11,385,230, and a bundled offer that envisaged Baxter being the exclusive supplier of the items tendered for. The second offer had a total cost of $10,525,537. On 5 January 1993, NSW Supply sent a counter-submission to Baxter, and on 21 January 1993, Baxter responded to the counter-submission.

171 Meanwhile, the negotiating team met with Baxter in January and February 1993. Baxter submitted revised special conditions to NSW Supply. A further proposal was also submitted by Baxter in March 1993, which envisaged a five year supply contract, bundling IV, IS and PN fluids with PD fluids. The cost of this proposal was only $9,620,625.

172 An analysis of all of the tenders was then carried out by NSW Supply. A submission to the State Contracts Control Board ("SCCB") recommended the approval of negotiating a five year contract with Baxter. Ultimately, the SCCB accepted this recommendation on 23 March 1993. Further negotiations ensued and enabled the insertion of a "best price clause" and the removal of CPI increases. On 29 April 1993, a contract was entered into between Baxter and SCCB for the supply of sterile fluids and PD fluids to the NSW public health sector.

173 Mr Kinkade, who was involved in the events of 1992, gave the following evidence as to the recollection of his views at the time. This evidence included the following:

(a) NSW Health did not view Abbott's proposal as satisfactory.
(b) The negotiating committee had technical assistance from a specialist renal physician.
(c) The key areas on which the negotiating committee focused in the negotiations with Baxter were price and price escalation, delivery of service, quality of product, guaranteed supply, management information exchange and local manufacturing. During these negotiations, the negotiating committee extracted from Baxter a "best price" clause, guaranteed supply, a commitment to manufacture within Australia for the term of the contract, and a number of other value-added services.
(d) The negotiating committee considered that Baxter had a long history of quality accreditation in Australia and an excellent manufacturing plant in Sydney. It was Mr Kinkade's experience that Baxter maintained high manufacturing standards and an on-going commitment to upgrade its plant whenever necessary or desirable to improve quality and efficiency.
(e) Mr Kinkade was concerned, given previous rationalisation and, in particular, Abbott's exit, that Baxter, too, might quit local manufacture.
(f) Mr Kinkade was concerned, given previous rationalisation and, in particular, Abbott's exit, that Baxter too might quit local manufacture.
(g) The negotiating committee believed that it always had the option of sourcing supplies of sterile fluids from overseas. This option to import products, although not as appealing as a sustainable Australian manufacturer of sterile fluids, was a source of bargaining power in negotiations with Baxter. Mr Kinkade recalled that sterile fluids could be imported from a couple of different sources.
(h) The negotiating committee took into consideration the possibility that after five years there would be no other suppliers around and NSW would be locked into purchasing sterile fluids only from Baxter. However, the negotiating committee considered it had an option to purchase internationally after five years if that was the case.

(i) Mr Kinkade considered that if Baxter, as the sole supplier of sterile fluids, sought prices which were uneconomical, the State could import products as an alternative, and the threat of doing so would prevent Baxter from raising prices inappropriately.

(j) Although negotiations between the State and Baxter prior to the signing of the 1993 contract were protracted, ultimately the NSW Department of Health achieved the deal on pricing, supply and other terms, and the strategic long-term partnership that it wanted.

(k) Mr Kinkade considered the signing of the 1993 contract to be a "fabulous result" not only for the public health system in New South Wales, but also across Australia, because of the:

(i) costs savings, the contract prices being lower than they previously were;

(ii) guaranteed supply;

(iii) guaranteed local manufacturing; and

(iv) the State's greater influence on development of quality products and technology if a manufacturer was based in Australia.

(l) The negotiating committee felt that it had secured the sustainability of the supply of sterile fluids to New South Wales for a period of five years with Baxter's commitment to the Australian market with low prices, price and service guarantees and a commitment from Baxter to upgrade its Sydney manufacturing plant.

(m) As a result of the 1993 tender, it was clear to the negotiating committee that no supplier could meet the needs of New South Wales for the provision of sterile fluids in the way that Baxter was able to do. There were distinct advantages to the State in terms of value for money and certainty of supply, in sourcing all sterile fluids from the one supplier.

174 There was some challenge to this evidence in cross-examination. However, I accept the above evidence of Mr Kinkade.

175 It is worthwhile at this point to say something further about overseas supply. The NSW negotiating team recognised the strength of Baxter's position with the withdrawal of Abbott. Baxter was the only local manufacturer of most sterile fluids. That was an advantage. However, it is important to understand the capacity (though not at short notice) for importers of LVP products to provide a degree of real competition. Mr David Crawford, the managing director of B. Braun swore an affidavit which set out the various commercial factors concerning Baxter's advantages. In his affidavit, and in cross-examination, Mr Crawford made clear that B. Braun could land LVP products in Australia at competitive prices, though, the fact of importation would reduce its flexibility to discount. Shipping costs must be borne; but production costs may be lower in the place of manufacture than in Australia. He said that was the position in 1997 and remains the position today. He also agreed that overseas manufactured PD fluids and products could be landed at competitive prices in 1997 and onwards. There was, however, no real impairment to discounting imported PD fluids because of their higher price and larger margin.

176 This evidence clearly underpins the approach of Mr Kinkade and the negotiating committee in NSW in 1992 that they were not entirely without bargaining power merely because Baxter was the only domestic manufacturer of IV fluids. The negotiating committee also perceived as a significant factor of advantage the retention of a local manufacturer (constrained to a degree by the threat of import competition), in particular in not being entirely reliant on foreign importers from year to year.

Monitoring the 1993 NSW Agreement

177 Shortly after the entering into the contract 903/904, a Contract Monitoring Committee, chaired by Mr Hawkins, was set up to monitor the contract. It was made up of representatives from NSW Supply, the Sydney Dialysis Centre, Baxter and various hospitals and area health services. The

Monitoring Committee created a procedure to review Baxter's level of service. A number of servicing issues were raised throughout the life of the contract.

178 Mr Bruce Kemp (of NSW Supply) said in his affidavit evidence that the Committee also considered the health system's compliance with the sole supplier condition. In this respect, it emerged at a meeting on 21 October 1993 that St Vincent's Hospital had not been switching to Baxter PD products, because they were perceived by the hospital as too expensive. At that Committee meeting, Mr Hawkins said that this was unacceptable, since no clinical reason had been provided. The Eastern Suburbs Area Health Service was informed of this.

179 Mr Kinkade gave some affidavit evidence concerning the Contract Monitoring Committee meetings and he recalled that Mr Garland had voiced his concern that there was a lack of clinical consultation and a lack of clinical choice arising from the 1993 NSW Agreement. In Mr Kinkade's view, Mr Garland's criticisms were not valid, because clinicians had been invited by the negotiating committee to participate in the process (and Dr John Mahoney and Mr Mark Tudehope, both from Royal North Shore Hospital, did participate). Furthermore, Mr Kinkade believed that Mr Garland's opinions were not representative of the broader community of clinicians, particularly as he had received positive feedback in relation to the contract from a Dr John Horvath. In cross-examination, Mr Kinkade refused to resile from his view that Mr Garland's concerns were irrational and unjustified. It is unnecessary to decide whether Mr Kinkade was correct in that view. I accept however, that he had that view and that he himself was not acting irrationally in holding that view. (I will come to Mr Garland's evidence in due course.) He said that the Contract Management Committee had evaluated these clinical concerns and then decided that, overall, they did not "hold water per se". It is sufficient, at this point, to say that there was a difference of opinion expressed after the NSW 1993 contract was entered into as to the wisdom, in particular from a clinical perspective, of entering into the contract and undertaking a sole supply arrangement for PD fluids.

South Australia 1993

180 On 18 May 1993, Baxter was awarded a sole supply agreement for two years from 1 May 1993 to 30 April 1995. Prior to then Baxter had made offers to SA for all items that were the subject of the contract, which included LVP, PN and PD fluids and IS.

181 After the award of that two year contract, SA Supply came to the view that two years may be too short a period. It wrote to Baxter in August 1983 and stated the following:

> ...
> *In the course of the continuous review to improve our operations, a study of the period contract system is being conducted.*
>
> *It has been generally suggested that the length of period contracts may be too short i.e. normally 2 years, and that by extending their duration, there may be benefits to all parties, specifically these are viewed as:*
>
> • *Greater market security*
> • *The opportunity for public and private sector to undertake cooperative measures*
> • *The incentive for suppliers to make offers containing more than price*
> • *The duration may be long enough to amortise the cost of any investment by suppliers.*
>
> ...

182 Baxter was asked to respond and did so. It is unnecessary to examine the detail of the response. It involved sole supply of all the items the subject of the then existing contract. Pricing was said to be dependent on "volume and mix".

183 The SA sole supply arrangement was extended to 30 September 1995 and then to 28 February 1996.

184 At this point, it is worthwhile making one point from the terms of the letter from SA Supply to Baxter just referred to. In dealing with the Crown immunity issue later the issue arises whether the States' legal rights would be prejudicially affected by Baxter being required to provide fluids and products on terms identical to the impugned contracts but without any restriction on sourcing supply from others. The above letter illustrates that the contracts entered into with Baxter involved an inter-related body of rights and obligations reached after and through a process of bargaining, which should be viewed as an integrated whole. This, perhaps, is to state no more than the obvious in most contractual relationships. To remove a right of Baxter does not necessarily advantage the State by lessening in equal terms the correlative obligation of the State, because that right of Baxter, and the correlative obligation of the State, may be part of a wider fabric of mutual perceived advantage and its removal may ultimately be to the disadvantage of the State when the totality of economic, administrative and clinical factors are considered.

Queensland 1993

185 In October 1993 the QHSPLG issued separate requests for offers for IV, IS and injections on the one hand, and HD and PD on the other. Baxter made four separate bids, three of which were bundled, including a bid for a three year sole supply contract for all of QLD's IV, IS and PD requirements. Baxter also put in a five year bid for an exclusive supply agreement that included PN (which had not been requested). That latter offer was rejected because PN fluids were not part of the request and because Mr Kelly said that he had a strict policy of not allowing five year agreements where no competition existed. The three year bundled bid for IV, IS and PD was accepted. Mr Kelly gave evidence that he and others had the view that the offer from Baxter that was accepted represented the best value for money for those products over three years. He also said that his view at the time was that the Gambro tender for PD was inferior to that of Baxter by reason of considerations of product support including clinician training. I accept that evidence. Also, as part of the evaluation process Baxter gave assurances, which were important to Queensland, about commitment to manufacture sterile fluids in Australia, about a commitment to technological development and about other service issues.

186 The above episode with QLD illuminates the ability of the States to formulate important elements of the competitive process. QLD refused to include PN fluids in the relevant tender. No bundling was therefore permitted by QLD in relation to PN fluids. The same approach could have been taken by QLD (or indeed any other State) in relation to PD products.

Western Australia 1994

187 In September 1994, before the expiry of the extended 1991 contract, WA Health Supply Services considered the market and the position of WA in the market. The market was described by the author of a paper prepared for the purpose of dealing with the next contract as follows:

> *...Baxter Healthcare has in recent years moved to a dominant position with the Australian sterile fluids market. The smaller manufacturers Delta West and Gambro, have been unable to compete with Baxter Healthcare and are restricted to isolated pockets of the market.*
>
> *Baxter Healthcare has successfully negotiated 5 year sole supply contracts with Victoria and New South Wales. Queensland and South Australia have called 3 year and 2 year public tenders respectively, however Baxter Healthcare has dominated the contract award.*
>
> *The market situation is poised to change with the entry of B. Braun, the world's largest*

> *manufacturer of sterile fluids, into the Australian market. B. Braun has successfully listed part of its imported range of sterile fluids with the Therapeutic Goods Administration and is awaiting registration for their full range. However it is unlikely that the full range will be available before the end of 1995.*

188 It should be noted that the author (Mr Morrissey, who did not give evidence) described the "sterile fluid" market as one including PD. Consideration was given to delaying tenders until B. Braun was in the market. The recommendation, however, was not to wait for this to occur and was expressed as follows:

> *It is recommended that bids be sought for a two year contract period with a 12 month option and a five year fixed contract period. This will allow Health greater flexibility in approaching this procurement requirement.*

189 Baxter bid on 9 November 1994. Three offers were made: an item-by-item bid for two years with a 12 month option; a bundled sole supply (covering IV, IS, PN and PD) bid for two years and a 12 month option; and a similarly bundled sole supply bid for five years.

190 On 1 December 1994, the Western Australian Pharmaceutical Advisory Committee recommended the five year bid of Baxter. There were opposing views expressed by clinicians, who considered a two, not a five year contract was more appropriate, particularly because of the commencement of Fresenius in selling PD products. The offers were analysed by WA Health Supply Services. Some of Baxter's prices on PN were thought to be too high. Negotiations with Baxter took place. Baxter made some concessions. In February 1995, Baxter's five year sole supply offer was accepted, operative from 31 January 1995.

191 The above decision was made with an appreciation and consideration of the costs, and the benefits that might accrue if a two year contract were chosen to allow Fresenius to participate in the supply of PD, and to allow B. Braun to participate in large volume sterile fluids two years hence. But it was decided that these considerations would not predominate.

192 Once again, though not an impugned contract, this episode reveals the capacity of the States to choose, to a degree, the terms on which they would deal with Baxter and to choose aspects of the market structure insofar as the tender structure may be seen to affect that market structure.

South Australia 1995

193 Prior to the 1995 South Australian tender process, dialysis fluids were separated from pharmaceutical supplies, on the advice of a pharmaceutical supplies contract committee. A separate dialysis fluid committee was established. Pharmaceutical supplies included LVP and PN fluids and IS.

194 The pharmaceutical supplies tender was released in or before June 1995 for the period 1 October 1995 to 30 April 1997, with a further one year option. The dialysis fluid tender was released in December 1995 for the period 1 March 1996 to 30 April 1997, with a further one year option.

195 As to the pharmaceutical supplies tender, various companies including Baxter tendered. Baxter made three offers: an item-by-item offer for all items in the tender; an offer for all items in the tender on a sole supply basis; and an additional offer for sole supply to 30 April 1998 for all items in the tender and all products in the pending dialysis fluids tender.

196 As to the dialysis fluids tender, Baxter, Gambro and a Fresenius company offered to provide PD and HD products. Baxter's offer consisted of an item-by-item bid and a bundled offer, being the third alternative in the pharmaceutical supplies tender referred to above.

197 All these tenders were evaluated by a committee which included, in respect of the dialysis tender, a significant number of clinicians. The Baxter offer which bundled both tenders was accepted. The recommendation of the relevant committee (in Confidential Exhibit RPH 8 p 6) was:

> ...
> *Baxter be selected as sole supplier for its complete fluid product range due to the significant cost savings available and the inability of wholesalers to be competitive in the fluids area.*
> ...

198 Mr Horstmann, who gave evidence, was one of the people at SA Supply who analysed the pharmaceutical supplies tenders. In his analysis (confidential Exhibit RPH-9) the considerable savings by acceptance of Baxter were noted, and the following was stated:

> ...
> *Large volume sterile fluids are, by their bulky nature, not ideally suited for wholesale distribution due to the higher costs of warehousing and distribution. In addition to this the current major supplier of these items in Australia, Baxter Healthcare, already performs with short lead times and high service efficiency. Sterile fluids offered by Baxter Healthcare have therefore been considered as a separate issue in this tender, particularly in light of Baxter's bid for sole supplier status.*
>
> *Appendix 3A compares the aggregate annual cost of Baxter's Offer 1 (item by item acceptance) with its Offer 2 (sole supplier for all items bid) against the lowest tender (including Baxter Offer 1) for each item.*
>
> *It is clearly demonstrated that significant savings will result from acceptance of Baxter's Offer 2 ($174,000 per annum). The main competitors to Baxter (albeit with much less product coverage), Astra and Delta West, also tendered package offers across their respective product ranges but do not offer significant cost savings over and above item-by-item acceptance.*
>
> ...

199 In respect of the dialysis fluid tender, analysed separately, Baxter's tender was priced below Gambro and Fresenius.

200 The contract was awarded up to 30 April 1998.

Queensland 1997

201 By 1997, Mr Kelly said that he had decided that QHSPLG should issue a combined tender for PD, HD, IV and IS fluids. His reasons were that the administrative convenience, complementarity of products, the similarity in the clinicians being consulted and the stronger bargaining power that it gave to QHSPLG rendered separate tenders unnecessary. This evidence was confirmed by Mr Stewart's affidavit evidence which also explained that administrative efficiency compelled the use of one tender for all of these products. PN fluids were not included because Mr Kelly considered those products to have a different function from other sterile fluids and in cross-examination he confirmed that PN products required consultation with nutritionists, whereas PD, IV and IS products only required consultation with clinicians. Once again, the power of the States, for their own reasons and to their own perceived advantage, to influence the structure of the tender process and so, at least at one level, the competitive process, can be seen.

202 On 16 April 1997, a tender was issued for IV fluids, IS, injections and dialysis fluids for 12 months, with an option to extend for 24 months. Tender responses were received from Baxter,

Gambro, Fresenius and Astra Zeneca. Mr Kelly said that Baxter's offers followed a similar pattern to previous tenders. Offer 1 was an item-by-item bid for the one year plus two years; Offer 2 was a bundled bid on a sole supplier basis for the same period; Offer 3 was a bundled bid on a sole supplier basis for three years.

203 Mr Kelly recommended Baxter's Offer 3 for the reasons set out at paragraphs 40 to 44 of his affidavit. He was cross-examined about this. Mr Kelly was of the view that Baxter's price and product quality made Offer 3 the best available. He and his colleagues considered that there was not likely to be any realistic increase in competition in the coming three years and there was no good reason not to give Baxter a three year contract. Moreover, at the time, Mr Kelly was comfortable with this decision as to three years because Baxter had not in the past sought price rises during the contract term and had a history of high quality and performance. In cross-examination, Mr Kelly denied that Baxter's bundled offer gave Queensland little alternative but to accept it, even though he agreed that importing IV and irrigating solutions was not viable in the short term. Rather, he said that it was only after Baxter had "won fair and square on a line item by line item basis" that Offer 3 became the obvious alternative to accept.

204 On 12 August 1997, Baxter was requested to agree to having a 10 per cent allowance for the trialling of products from other PD companies. Baxter agreed to a five per cent allowance on 18 August 1997, and a contract with this condition was ultimately agreed to. Although Mr Kelly said that he would have preferred 10 per cent (because that would have allowed more meaningful trials), he said that he thought that five per cent was sufficient for this purpose, despite the advice of others. In cross-examination, he again denied that Queensland's inability to negotiate a better allowance meant that it lacked bargaining power. He also said that clinicians always had the ability to obtain other products if an individual patient genuinely required it. When it was then put to him that if this was true, no allowance was required, he responded by stating that a principle was at stake. I accept Mr Kelly's evidence. He did not consider that Queensland lacked bargaining power. His view is entitled to considerable weight.

205 Finally, in relation to the 1997 contract, Mr Kelly agreed that Baxter would be and was responsible for monitoring compliance with the contract.

206 Baxter's sole supply agreement applied to all health care facilities under the control of Queensland Health from 1 October 1997 to 30 September 2000.

The history of State contracts for the supply of LVP, PN and PD fluids and IS (the impugned conduct)

The negotiation of the 1998 NSW Agreement

207 In March 1997, NSW established a Contract Management Committee to negotiate and enter into a new sterile fluids and PD fluids supply contract. The Committee was chaired by Mr Graham Hawkins and comprised representatives from NSW Health, NSW Supply and various clinicians (including renal specialists and nurses). On 27 June 1997, a Request for Expressions of Interest for the supply of sterile fluids and PD fluids was issued by NSW Supply, and responses were received from Baxter, Fresenius, Gambro and B. Braun. B. Braun indicated that it was prepared to enter the market for intravenous fluids and IS.

208 The Gambro and Fresenius expressions of interest were restricted to PD products. Though, it should be noted that Fresenius stated that it had a medium term capacity to import IV solution from Europe and a long term capacity to do the same from a proposed Asia Pacific manufacturing plant. The B. Braun expression of interest stated a capacity to supply IV, PN and PD fluids and IS.

209 At a meeting of the Management Committee on 5 August 1997, a letter from Sandra Campbell of an organisation called Peritoneal Dialysis Support Services dated 17 June 1997 was considered. That

letter raised a concern that although Baxter's overall prices might be lower, its PD products were more expensive and less technologically advanced (in terms of their connection systems) than those of its competitors. At that meeting, the Committee decided that there was not enough information in the Expressions of Interest to determine whether a sole supplier contract would be beneficial. Accordingly, on 8 October 1997, NSW Supply released its Request for Tenders for the supply of LVP, PD and PN fluids and products and IS (clause 1.01(a)) for a two year period, although tenderers were asked to submit prices on the basis of a one year contract as well (clause 1.01(b)). As with the NSW tender request in 1993, tenderers were permitted to submit alternative tenders so long as they met "the objective and intent of the tender requirements" (clause 2.14). Furthermore, the request specifically envisaged and allowed the submission of bundled offers. Clause 4.32 of the Request said:

> *Tenderers are at liberty to submit special offers contingent upon specified groups of items being accepted in their entirety. ... Tenderers are also at liberty to submit special offers contingent upon being accepted on sole supplier either for a category of products or across all categories of products within this contract.*

210 Mr Kemp gave evidence, which I accept, to the following effect:

(a) It had been his experience, including as at 1997, that if New South Wales could establish a contract with a single supplier for a range of products over a term of years then that would yield better results in the tender process.
(b) In 1997, New South Wales had a leaning towards reducing the number of suppliers acting on its contracts.
(c) When the tender was issued in 1997 a contract for five years in which the supply of sterile fluids was bundled together was an acceptable option.

211 Tenders were received from Baxter, Fresenius, Gambro and B. Braun. Gambro offered to supply PD products, and its bid contained a volume discount of 2.5 per cent if it received 100 patients. Fresenius tendered for PD products. B. Braun tendered for LVP, PN and PD fluids and products and IS, though its tender did not cover some of the lower volume products. Baxter submitted five offers and tendered for all products. Offer 1 was an item-by-item bid for IV for one year, with an option for a 12 month extension; Offer 2 was an item-by-item bid for IV for two years; Offer 3 was an item-by-item bid for IS, PN and PD for two years; Offer 4 was a bid for all items tendered as a bundled, exclusive supply basis for two years; and Offer 5 was a bid for all items tendered on a bundled, exclusive supply basis for five years.

212 At this time B. Braun had registered with the TGA approximately 80 per cent of the range of LVP fluids in the specification in the 1997 NSW request for tender. These included the products that the SPAs would require in large numbers and volume. Mr Crawford also stated, and I accept, that B. Braun would, subject to importing PD, IS and PN products, have been able to link IV solutions with those products.

213 It is important to understand what the evidence revealed about what Baxter knew about B. Braun's capacity to compete at this time in respect of IV fluids. This is relevant to the assertion that Baxter took advantage of its posited market power. One aspect of that analysis is whether Baxter could or would have behaved as it did if in fact there had been what was referred to as a workably competitive sterile fluids market. Notwithstanding Baxter's position as sole domestic manufacturer, its own perceptions of import competition are relevant to that analysis.

214 Baxter knew that B. Braun did not manufacture locally. It knew that B. Braun was a major worldwide sterile fluid producer with a manufacturing plant in Penang. Mr Lee, the former managing director of Baxter in Australia who approved the various offers in 1997 gave evidence by affidavit that at the time that Baxter submitted its five offers he thought the following to be the case:

• I expected Fresenius and Gambro to bid on PD.
• I understood that Braun was registered with the TGA for all of the 8 major IV codes as well as several minor codes.
• I expected that Braun would bid for IV products but probably on the 8 major IV codes. (I do not know to this day if Braun did bid or not.)
• Those 8 major codes made up 80 per cent of Baxter's plant's IV volume.
• I expected that only Baxter would bid for ISs and PNs.
• I expected that NSW would not accept any of Baxter's 5 offers.
• Instead, I expected NSW to respond to our offers and seek to negotiate an arrangement.
• I considered offer 5 to be an ambit claim.
• This is because I expected that offer 5 would not be accepted, not because of the unattractiveness of Baxter's pricing, but because I expected that nephrologists would contend that there would be a lack of clinical choice if Baxter was the sole supplier of PD products.
• I considered that there was a risk that Braun would have some success in any IV bid by it.
• I expected that Baxter would probably eventually win an exclusive contract for IV fluids and ISs and about 80 per cent of the PD business, through post-tender negotiations.
• I thought Baxter would be listed for IV fluids at least in part on the 1998 contract, even if Baxter's prices were higher than Braun, because NSW could not risk Braun as a sole supplier of IV Products.
• I thought therefore that 40-60 per cent loss of the major IV codes was the most realistic worst-case scenario for IV codes.
• I thought that if Braun won 40-60 per cent of the major IV codes, it would import those products from its manufacturing plant in Penang, Malaysia.
• I also expected that Braun would bid at relatively low prices in order to capture initial business in Australia. I expected that these prices would be below Braun's (and Baxter's) average cost to make and sell.
• I thought that IV fluids represented about 80 per cent of Baxter's total sterile fluids volume.
• Having regard to these matters, for the "cherry pick" offers I assumed the following loss of volumes:
(i) 40 per cent of major IV codes across Australia; and
(ii) 40 per cent of PD codes across Australia.

215 Mr Lee accepted in cross-examination that he expected to win the LVP and IS tender for NSW. He agreed that between 1992 (with the exit of Abbott) and 1996 (with the apparent entry of B. Braun thereafter) he would have expected to be an exclusive supplier. The expectation of winning the LVP and IS tender in NSW in 1997 and 1998 does not deny that Mr Lee believed that B. Braun was a commercial threat in that tender to a degree.

216 In fact, B. Braun did not have, and was unable to obtain, TGA approval for its manufacturing plant in Penang. It was unclear on the evidence, and I am unable to make a clear finding about the issue, whether Baxter was aware of this during 1997 and 1998. I cannot conclude that it was so aware. From the above evidence of Mr Lee (and whilst I have grave reservations about other parts of Mr Lee's evidence, to which I will come) I accept that he saw B. Braun as a competitive threat for this NSW tender, though he did anticipate winning the sterile fluids contract.

217 The tenders were then summarised by Ms Margaret Fulham in respect of their pricing and non-pricing aspects. The Management Committee reviewed this summary on 27 November 1997. It appears that there was a substantial difference in cost between Baxter's item-by-item offers (with so called "cherry pick" prices) and Baxter's bundled offers. For example, total IV solutions under Offer 1 would cost $7,764,024 in the first year whereas under Offer 5 they would only cost $5,011,764. Moreover, Offer 1 represented an increase over the current prices of 58.5 per cent (the current IV cost was $4,892,634). The Committee therefore decided to seek further information, particularly in

relation to the clinical implications of the tenders.

218 The pricing spreadsheets prepared in the analysis of these tenders demonstrate with clarity the financial consequences of not taking Baxter's bundled bid. No complex modelling is required. Of course, Baxter did not have available to it the competing bids, However, it understood (if its item-by-item prices were taken seriously) that unless a new importer (B. Braun) was to take the bulk of the sterile fluids contract (which Mr Lee did not expect) the financial pressure on NSW to take Baxter's PD fluids and products was enormous. For PD to be purchased from Gambro or Fresenius effectively required NSW to abandon the local manufacturer (Baxter) for foreign made and imported sterile fluids.

219 A subcommittee was also formed to review the tender. In the minutes of this Contract Management Subcommittee dated 9 December 1997, it was said that:

> *The subcommittee expressed its disappointment at the overall financial implications of accepting the offer of any other supplier given that Baxter would still be accepted at most items but their non sole supplier pricing rates would apply. This would potentially cost the NSW Public Health system approximately $5 million extra per annum. It was agreed that this was unacceptable.*

220 The Contract Management Subcommittee also expressed concern over the level of technology supplied by Baxter and the questions of competition raised by a five year tender. The minutes of the meeting recorded the following:

> *Further consideration was given to the two Baxter offers which offered prices on a sole supplier basis. The subcommittee unanimously agreed that the 5 year sole supplier offer was not acceptable and recommended the two year sole supplier option for the following reasons:*
>
> *- There is a good deal of evidence, albeit largely anecdotal, which suggests that the PD solutions offered by Baxter are technologically and technically inferior to the products offered by alternative suppliers.*
> *- With acceptance of another 5 year sole supplier contract, there would be almost no incentive for alternative PD suppliers to persist in the Australian market. Such acceptance would also form a significant barrier to entry for potential suppliers to the IV and Irrigating Solutions markets.*
>
> *The subcommittee took the view that although a two year sole supplier contract was far from ideal it would at least provide alternative suppliers such as B.Braun and Fresenius with some encouragement to stay involved in the Australian market. It would also provide those suppliers with a definite timeframe to ensure that they met TGA requirements and were capable of producing a full range of solutions prior to the implementation of the next contract.*
>
> *Indicative pricing supplied by alternative suppliers such as B.Braun had shown that there is the potential to generate significant cost savings for the Public Health system in the long term by keeping the contract term less than five years.*
>
> *A two year sole supplier contract instead of a five year contract should send a significant message to Baxter to improve their technology and pricing if they wish to remain competitive in the longer term.*
>
> *The subcommittee was of the opinion that during the current 5 year contract, Baxter has made little effort to implement technological advances in their products and currently lag*

> *behind alternative products. The subcommittee felt that this situation would be exacerbated should Baxter be awarded sole supplier status on another long term contract.*

221 At the Contract Management Subcommittee meeting on 18 December 1997, it was resolved by seven votes to two that Baxter's two year combined offer would be recommended and that a negotiating team would be formed to extract further concessions from Baxter. The concessions that were envisaged included the ability to purchase 30 per cent of the five litre PD bags and 5 to 10 per cent of other PD bags "off contract", a commitment by Baxter to advances in connectology, a per patient treatment cost (as opposed to per item) and other issues. The SCCB approved this recommendation to engage in post-tender negotiations with Baxter. It is important to note, however, that despite this recommendation, both Mr Hawkins and Mr Kemp preferred a five year agreement because of the cost savings that it would bring.

222 At a meeting on 12 February 1998, Baxter was told by Mr Kemp that clinicians' concerns as to clinical flexibility meant that NSW required concessions if it was to enter into a five year agreement. Mr Wallace (General Manager Sales and Marketing of Baxter) said that Baxter would be unlikely to invest in Freeline Solo if there was only going to be a two year agreement (because it would not provide sufficient time to recoup its investment). On 23 February 2004, however, Baxter put in two further offers, namely Offer 5a (which was the same as Offer 5 except to the extent that it permitted 10 per cent of PD products to be sourced from other suppliers in years three to five) and Offer 5b (which was the same as Offer 5 except to the extent that it permitted 10 per cent of PD products to be sourced from other suppliers and had slightly higher prices). The 10 per cent allowance was actually a 5 per cent plus 5 per cent arrangement whereby authorisation from NSW Health was required if any hospital wished to exceed 5 per cent.

223 Negotiations then took place. On 27 February 1998, Baxter was advised that the Committee wanted the prices in Offer 5b to be the same as those in Offer 5a. On 2 March 1998, Baxter amended its Offer 5b to reflect this desire. Then on 7 April 1998, Baxter offered to further reduce its price for Freeline Solo. At the meeting of the Management Committee on 9 April 1998, it was decided that a recommendation be made that Baxter's Offer 5b be accepted, that is a five year bundled contract. Mr Kemp said that the overriding motive behind accepting Baxter's Offer 5b and not entering into multiple contracts was the additional cost that would have been borne by the public health system. The recommendation was approved by the SCCB on 28 April 1998. In cross-examination, Mr Kemp agreed that an agreement for a five year period at the agreed prices was an acceptable result.

224 It should be noted that beyond 31 March 1998, Baxter continued to supply products at the prices under the former contract (which by then had expired).

South Australia 1998

225 Meanwhile, in South Australia, the existing contract was due to expire on 30 April 1998. From February to November 1998, SA Supply explored the possibility of a new contract negotiated directly with Baxter. SA Supply, through Mr Horstmann, consulted with other SPAs about the merits of their long term supply agreements. Meanwhile the existing contract was rolled over on a monthly basis.

226 On 18 May 1998, Baxter made two bundled offers for IV fluids, IS, PN and PD fluids, the first for one year with a one year option, and the second for five years. These were not taken up and the existing sole supply contract was extended up to the 2000 tender at the request of SA.

ACT transaction (1998 onwards)

227 Mr Bonato, the supply Manager, Supply Services, Business Services Bureau, ACT Department of Health and Community Care gave affidavit evidence regarding the relationship between Baxter and the ACT. During his time as Supply Manager, Mr Bonato said that the ACT Health Department had

no formal standing agreements with companies that supplied medical and related consumables. Instead, suppliers were chosen on the basis of product availability and price, and indeed Baxter was the only company from which intravenous fluids could be purchased. However, Mr Bonato was of the belief that Baxter supplied products to the ACT at the same prices that NSW received, although he was not aware of the terms of the NSW Agreement. The only conditions imposed upon the Department by Baxter were those relating to delivery conditions, minimum order quantities and a returned goods policy.

228 During the 1990s, responsibility for the supply of PD and LVP fluids and IS in the ACT was assumed by Supply Services. PN fluids, however, continued to be purchased by Canberra Hospital's pharmacy. Also, throughout the 1990s, IV fluids were supplied exclusively by Baxter, and PD fluids were supplied by both Baxter and Gambro.

229 On 2 November 1998, after the securing of the NSW contract, Ms Jenny Spink of Baxter sent a letter to the ACT Health Department in which the Department was invited to formalise the basis upon which IV fluids, dialysis fluids and IS were purchased from Baxter. The main condition proposed was that Baxter be accepted as the sole supplier across all categories within the contract. At the time, in Mr Bonato's view, such formalisation was not necessary.

230 In successive conversations between Mr Bonato and Ms Spink, the latter said words to the effect that "if the ACT does not sign the contract with Baxter, then Baxter will not continue to give the ACT a good deal". Ultimately, on 17 March 1999, Mr Bonato signed an acceptance of Baxter's offer. At that time, Mr Bonato said that he did not think that the agreement meant that the ACT Health Department could no longer purchase products from other suppliers, particularly as Ms Spink had noted in a letter to Mr Bonato that the arrangement was "not intended to encourage Australian Capital Territory Public Hospitals to purchase products that do not meet its price and quality requirements".

231 On 19 August 2000, Supply Services advertised a request for proposals for the provision of dialysis fluids to Canberra Hospital on a price per treatment basis for both PD and HD. It was noted that the contract could be awarded to either a sole supplier or panel of suppliers. Proposals were received from Baxter, Fresenius and Gambro, although Baxter's offer did not address PD fluids. On 24 May 2001, Fresenius was awarded the contract to supply dialysis products, with the result that Baxter was no longer the exclusive supplier of PD fluid products to Canberra Hospital.

232 Correspondence between Baxter and the Canberra Hospital then took place and despite Baxter's assertions to the contrary, Mr Bonato expressed the view in the correspondence that the Fresenius contract did not breach the existing agreement with Baxter. Mr Bonato also recalled that during a meeting at Canberra Hospital, Baxter threatened to charge higher prices unless the dispute was resolved to its satisfaction.

233 On 12 September 2001, Supply Services received a facsimile transmission from Baxter that returned Supply Services' order of the previous day with a statement that Baxter was no longer prepared to supply the products at the prices sought. Baxter did, however, ultimately supply the products, although it claimed an entitlement to be paid prices that were in line with the price list that had been sent to Mr Rayment of Supply Services by Mr Browne of Baxter on 26 July 2001. The Department refused to pay those prices, and only paid the NSW contract price. The Department and Baxter remain in dispute about the additional prices.

QLD transaction (2000 onwards)

234 Before the expiry of the 1997 contract and the issue of the next tender, Mr Kelly and his staff sought information as to the performance of suppliers under the 1997 contract. Mr Kelly's recollection was that Baxter's performance under the contract was reported to have been satisfactory in relation to product quality, availability of products and training such that there was no reason why Baxter should not participate in the new tender.

235 On 3 May 2000, QHSPLG issued its 2000 tender request for IV fluids and dialysis fluids. The tender request excluded PN fluids, and was only in relation to IV, PD and HD fluids and IS. It envisaged a contract term of 12 months with the option of extending it twice each extension being for a period of 12 months. The request noted that no more than 7.5 per cent of patients would be involved in dialysis trials at any one point in time (clause 7.1). This increase to 7.5 per cent from the five per cent in the existing contract as an allowance for alternative PD suppliers was inserted after consideration of the question by the relevant multi-disciplinary advisory committee which included clinicians and health professionals.

236 Mr Kelly consulted with his staff and they reached the view that there was no reason to change the product mix covered by the tender. In particular, there was no perceived need to split the various products into different tenders. Mr Kelly had the view, supported by his staff, that the product mix in the tender was "optimal" in order to obtain value for money.

237 The tenders invited the submission of the tenderer's "best offers": clause 1.1; it was stated that post-offer negotiations were a "prospect": clause 20.1; it was stated that the main objective would be to obtain the "best ultimate value for Queensland Health": clause 5.3. Queensland reserved the right to select one or more offeror: clause 17.4.

238 Baxter put in its tender on 30 May 2000. It contained three offers namely, Offer 1, which was for an "item-by-item" contract for 12 months with two options; Offer 2, which was for an exclusive supply agreement for all products for one year (with an option for a further two periods of one year); and Offer 3, which was for an exclusive supply agreement for all products (plus PN fluids) for a period of three years.

239 Fresenius and Gambro also put in tenders for the supply of HD and PD products. Gambro's offers comprised item-by-item bids through to bundled bids with successively lower prices. However, the bids of Fresenius and Gambro were not for all PD products.

240 Evaluation of the offers took some time (from June 2000 to April 2001).

241 In relation to dialysis fluids a special advisory committee was convened to evaluate the offers. This committee only evaluated Baxter's unbundled bid. Baxter was recommended in relation to PD. Similarly Baxter's LVP and IS offers were assessed on an item-by-item basis. Subject to a recommendation for negotiation as to price, Baxter was recommended.

242 It is sufficient to say that the 2000 tenders were evaluated in such a way as to permit the clear conclusion that the impugned bundling had no effect whatsoever on the awarding of the tender to Baxter.

243 On 1 May 2001, Queensland accepted Baxter's offer to supply IV fluids, IS, and PD fluids on a sole supply basis (subject to a 7.5 per cent allowance for PD) for three years. Pricing terms were as in Offer 3. The contract commenced on 1 June 2001.

244 Mr Kelly referred to Mr Stewart's affidavit and said that he did not consider that Baxter was using bundling of IV and IS fluids at lower prices to guarantee its being awarded the PD business. He considered that Baxter had simply tendered with competitive pricing to ensure that it gave itself the best possible opportunity of winning as much of the tender as possible. As to the three year term, as opposed to one year plus option for a further two one year periods, Mr Kelly considered that this saved on administrative expenses.

245 In cross-examination, it was put to Mr Kelly that Queensland's failure to obtain a 10 per cent allowance in bargaining with Baxter in 2000 (notwithstanding the form of the tender in this respect) and the fact that Queensland took a three year contract was again evidence of a lack of bargaining power. Although Mr Kelly's preferred position was not a three year contract, he denied that there was

a lack of bargaining power. Indeed, in his affidavit, he had said that there was no imbalance of bargaining power between Baxter and the State, because the contract terms were relatively short and the volume was not high.

246 Mr Kelly, particularly throughout the 1997 to 2000 period, was impressed by Baxter's service and the quality of its products. In both the 1997 and 2000 tenders, he was concerned that other suppliers were not able to meet this level of quality and service. Accordingly, he regarded Baxter's bundled offer as the best value for money where there was a good record of quality and service. This was particularly so because he thought that Gambro and Fresenius were not particularly competitive with Baxter across IV and IS, and even PD fluids. Furthermore, Mr Kelly was of the view that Fresenius did not match Baxter in service, and given that neither Gambro's nor Fresenius' prices were as good as Baxter's, there was no point in appointing more than a single supplier for those products.

247 Mr Kelly also said that QHSPLG often encouraged suppliers to put in their best possible offers and to be creative. As to the three year term in 1997 and 2000, Mr Kelly took the view that this would not prevent QLD from accessing new technology, because three years was not a prohibitively long period.

248 It is important to appreciate the degree to which QLD perceived its position as one embodying real bargaining power, deployed in its own interests. This not only affects the analysis of "power" for the purpose of s 46 of the Act, but also illuminates for the purpose of the "Crown immunity" argument, the substantive nature of the affectation of the legal interests of a State if it has its contracts interfered with by orders granted by the Court.

Western Australian transaction (2000)

249 The Health Supply Services Division ("HSS") is the administrative arm of the WA Government Health Supply Service ("GHSC"), which is an advisory body that reports to the Minister for Health on supply-related matters. The HSS performs three functions: namely, health supply policy, health contract and tendering, and health supply chain management. It is responsible for all sterile fluids tenders in Western Australia (which includes PN, LVP and PD fluids, and IS), and it evaluates tenders by having regard to value for money, probity, confidentiality, fair-dealing and accountability.

250 A tender process had been in place since 1991, WA had previously had supply contracts with Baxter in 1991 and 1995, with the latter being for five years. In 2000, the tender process commenced six months prior to the conclusion of the contract that was then in place. The Evaluation Committee for this tender comprised six members of the Pharmaceutical Advisory Group (including the Chief Pharmacist at each of the five metropolitan teaching hospitals), a contracts manager, Associate Professor Mark Thomas (a renal specialist), Ms Mary Russell (Renal Nurse Manager at Sir Charles Gairdner Hospital) and Mr Bycroft, who was a senior contracts consultant with HSS, and who gave evidence in this proceeding.

251 During the preparation of the tender, the issue of whether PD fluids would remain part of the sterile fluids tender was raised. A group of renal clinicians (including Professor Thomas) called the Western Australian Dialysis Reference Group, advised that PD should remain in the tender. One reason was to encourage bidders to take a "value added" approach. It was felt that the competitive pressure from HD as an alternative treatment would assist in the inclusion of APD machines at no extra costs. There was a shortage of APD machines in Perth at the time.

252 Another issue for the tender was its proposed length. Based on the practice of the relevant Department, Mr Bycroft determined that the tender should be for a five year supply arrangement.

253 The Department, in submitting the procurement plan to the Minister for Health, expressed the following views:

> *• The current contract has proved very successful in establishing procurement arrangements that have met the needs of Western Australian public hospitals and eliciting significant potential savings on prices being paid for these products.*
> *• Baxter had supplied products in a prompt and efficient manner and had satisfied the Department of Health's requirements.*
> ***• It was noted that the proposers will also be requested to bid on a sole contractor and panel basis, and encouraged to offer discounts if awarded items as sole supplier.***
> *• This contract is not thought to place Health or suppliers in a position of undue risk. It is aimed to establish uniform, optimal pricing available to all Western Australian Public Health Care Units.*
> *• A period of five years has been determined as appropriate for the proposed new contract given the nature and relative stability of the products and the market. This term has worked well for the current contractual arrangement.*
>
> [emphasis added]

254 Thus, once again, a State was of the view that a sole supplier arrangement (thereby creating the tie or bundle) was in its interest.

255 On 26 May 2000, HSS issued a request for tender.

256 In response, three offers were received from Baxter, namely, Offer 1, which was on an item-by-item basis for a five year period; Offer 2, which was a combined bid for all items with a volume discount for three years; and Offer 3, which was a combined bid for all items with a volume discount for five years. The difference in price for each of Offers 1, 2 and 3 was substantial. For example, in respect of intravenous fluids, the five year cost under Offer 1, which had item-by-item prices, was $17,001,628.13 which represented a 65.6 per cent increase over current cost ($10,266,763.20). However, under the bundled offers, namely Offers 2 and 3, which contained lower prices, the five year cost was $13,558,052.78 and $11,558,052.78 respectively. In respect of the cost for provision of all sterile fluids and PD products, Offer 1 cost $40,396,625.97, Offer 2 cost $33,261,076.93 and Offer 3 cost $30,257,847.18, whereas the then contract cost was $28,196,621.45 for five years.

257 Offers were also received from Fresenius and from Gambro in relation to PD products. The detail in the tenders was confidential, but it can be said that the Baxter prices, including in its Offer 1, compared favourably with prices for PD products put forward by Fresenius and to a lesser degree Gambro. A brief confidential summary is as follows. Gambro's offer on PD products had a five year cost of $12,134,172 and Fresenius' offer on PD products had a five year cost of $12,985,071. Bearing in mind that Gambro and Fresenius did not bid for all PD products, this compared to Baxter's total five year PD cost of $13,222,985.92.

258 Once again, an appreciation of these figures made plain to those contemporaneously involved that the cost or "price" of not taking a Baxter sole supply arrangement for all products was huge, unless sterile fluids could be sourced elsewhere.

259 In response to the proposals, Mr Bycroft received correspondence from a number of clinicians expressing their concerns over a bundled contract. The views reflected fears held by some that patients and clinicians would not have access to new technology.

260 After receipt of the tenders, an "Evaluation Strategy" was formulated which directed attention to value for money. On 20 July 2000, the Evaluation Committee met. Two groups, namely the Pharmacy Group and the Renal Group were formed to analyse different aspects of the tenders. On 3 August 2000, the Pharmacy Group met and decided to recommend Baxter's third offer, although it also thought it appropriate for the Health Department to negotiate with Baxter to limit its guarantee of market share for PD products to 90 per cent.

261 On 15 August 2000, the Renal Group met and decided that the Health Department should attempt to negotiate only to guarantee a 60 per cent PD market share for Baxter, so as to allow Health facilities the freedom to experiment with new products. The Renal Group also wanted to negotiate a three year contract for PD products (with two 12 month extensions) with a price per patient treatment. After further discussion with those charged with the responsibility of negotiations, the Renal Group agreed that a 10 per cent allowance for other suppliers was satisfactory, although 20 per cent was preferred.

262 Negotiations then began with Baxter. On 4 December 2000, Baxter amended its Offer 3 to allow 5 per cent to other PD suppliers, with a further 5 per cent upon approval. On 13 December 2000, Mr Bycroft responded with concerns that the 5 per cent plus 5 per cent arrangement did not leave Health facilities with sufficient clinical choice. Accordingly, on 15 December 2000, after Baxter had been convinced that the 5 per cent plus 5 per cent arrangement would have been cumbersome to administer, Ms Karen Carty of Baxter wrote to Mr Bycroft, advising that a 10 per cent "leakage" would be allowed. On 2 May 2001, Baxter's amended Offer 3 was accepted.

263 Dr Irish an experienced nephrologist practising at Royal Perth Hospital gave oral evidence that Baxter's PD products and services as an entire therapeutic system were at least the equivalent of, or probably superior to, the alternatives in PD. Minds might differ about this. But this was a view held by an influential and respected Western Australian clinician.

South Australian transaction (2000 onwards)

264 In mid-2000, a new tender for pharmaceutical products, including LVP, PD and PN fluids and IS was called in South Australia. The Strategic Procurement Unit ("SPU") consulted a number of clinicians and pharmacists for the purpose of this tender, and an acquisition plan was drafted by Mr Battersby (Manager, Strategic Contracting in SPU). In his affidavit filed in the proceedings, Mr Battersby said that he had envisaged that tenders would be sought for a two year period with the option of a one year renewal.

265 Mr Battersby also said that the length of time that had passed since the last tender in 1995 was inconsistent with the State's policies on "open and fair competition". He also said that this had meant that South Australia had not benefited from any price reductions during that time, and that from discussions that he had in December 2000 with Christine Odgers (Chief Pharmacist at Flinders Medical Centre) he had learnt that hospital pharmacists thought Health facilities were paying more for pharmaceuticals than they should be. In addition to this, and prior to the release of the invitation to tender, Mr Battersby received an email from Chris Doeke, Director of Pharmacy Services, Royal Adelaide Hospital on 23 May 2000 expressing nervousness with respect to a five year contract. Mr Battersby responded the same day and noted that the base tender would still be for two years.

266 In July 2000, the Department of Human Services ("DHS") issued a public request for tenders in respect of various pharmaceutical products for a period of two years with the option of a one year renewal. The invitation noted that the DHS could elect to offer exclusive contracts as a panel arrangement. Tenderers were also given the option of making alternative offers to the base offer for overall terms of "2 + 2 years", so long as it provided the "most cost effective and practical solution, taking into account the totality of the requirement". There was no clause requesting offers over a range of product groups.

267 On 25 July 2000, the DHS released a Corrective Circular and it clarified the point that tenderers did not have to be able to supply both intravenous fluids and PD fluids. Another Corrective Circular was released on 18 August 2000. Then, after consultation with renal clinicians, Mr Battersby decided to withdraw certain renal fluids (PD and HD) from this tender, so a third Corrective Circular was issued on 24 August 2000 to this effect. However, after receiving Baxter's interest in tendering for HD fluids, and after further discussions with renal clinicians, a fourth Corrective Circular was issued which listed amendments in respect of the dialysis products that were included in the tender.

Expressions of interest for renal fluids were nonetheless still sought.

268 Thus, although renal fluids were for a time taken out of the tender, they were brought back into the tender. It is also fair to say that after all these steps were taken a bundled exclusive supply bid was not disconformable with the parameters of the tender.

269 Tenders were received from Baxter, Gambro and Fresenius. Fresenius tendered for dialysis products, as did Gambro. Gambro made offers on a bundled and unbundled basis in relation to HD and haemofiltration products. Baxter's tender was for all products and its Offer 1 was an item-by-item bid to supply all items for a period of two years (with options for two 12 month extensions), and its Offer 2 was a combined bid for all items on an exclusive basis for a period of five years with volume discounts. After a meeting on 5 December 2000 between Mr Chris Browne of Baxter, Mr Battersby, and the SPU's probity auditors, Mr Battersby requested a revised Offer 1 (to be called Offer 1A) which consisted of a five year term for the products in the tender but excluding those renal products the subject of a supplementary tender. Baxter responded with an Offer 1A on 11 December 2000. The request was, in effect, for an offer for sole and exclusive supply of sterile fluids, not including PD fluids or production. Thus, a volume discount was sought in exchange for sole and exclusive supply of sterile fluids.

270 The delivery of Offer 1A is a matter emphasised by the ACCC. It was said to be the epitome of the impugned conduct. The request for a further offer was made on 5 December 2000. It was specifically for a total bundle excluding renal products for a five year term and implicitly on a sole supply basis. As is apparent from the recitation thusfar of the history of the tenders and contracts in the various States, this was the first time that any SPA or State agency had asked for such a broken down, PD excluded, tender on a sole supply and long term basis.

271 The response of Baxter was to offer no discount whatsoever from the item-by-item prices in Offer 1.

272 Mr Browne who was primarily responsible for the SA bid said that he was not happy to lose 40 per cent of his revenues (PD) and did not feel inclined to give SA good pricing for this alternative. This evidence must be seen in the context of other evidence of Mr Browne that the only part of the business where he thought that there was a realistic threat to Baxter was PD. (Though said in evidence in the context of the WA bid, the comment had an equal relevance to SA.) I will return to this in due course in respect of issues as to "purpose" and "taking advantage" under s 46. It is sufficient to note at this point that Mr Browne's lack of inclination was informed by his recognition that Baxter would obtain the non-renal fluids business as there was no known competitive tenderer in respect of this business.

273 Mr Battersby's staff then generated comparisons of the tender offers and Mr Battersby himself had discussions with clinicians. Mr Battersby said that renal physicians consistently raised the concern that the specific market shares sought by the tenderers would limit flexibility. A summary sheet of Baxter's offers 1, 1A and 2 was prepared on 1 February 2001. Offers 1 and 1A (when PD products were taken into account) would both cost $5,914,291, whereas Baxter's bundled Offer 2 would cost $4,501,053. Importantly this revealed that Baxter's bundled offer for IV fluids and PD fluids ($4,501,053) was cheaper than Baxter's item-by-item offer for IV fluids alone in Offer 1 ($4,523,125). Moreover, this schedule also demonstrated that Baxter was not prepared to give a discount for exclusivity on IV fluids if there was no exclusivity for PD, given that Offer 1A prices matched those in Offer 1.

274 In the light of these issues, Mr Battersby emailed Chris Browne on 5 February 2001, and raised concerns that he had about Baxter's conduct by reference to the Act. Specifically, Mr Battersby said:

> *It is not clear that Baxter Healthcare is able to offer a pricing structure of this kind without being in breach of the misuse of market power provisions of the Trade Practices*

> *Act (s 46). In effect, unless the prices offered in Offer 1 for IV fluids are not real market prices, the combined offer price for PD solutions is at, or approaches, zero cost, thereby (in the terms of the Act) potentially 'eliminating or substantially damaging' the competition for PD solutions*

Mr Browne responded by stating that Baxter had sought legal advice to the effect that there would be no breach of the Act. He was not able to provide a copy of that advice. In particular, Mr Battersby was concerned that the restrictive conditions in Baxter's offer meant that Baxter had not made its best possible offer. Accordingly, he contacted his Western Australian counterpart, Mr Bycroft, to seek his view, and was informed of the 10 per cent limit on sourcing PD products from other suppliers that Baxter had allowed.

275 On 21 February 2001, a minute was sent from the SPU to Brendon Kearney, the executive director of a division within DHS responsible for policy and funding, which requested a policy decision on whether a cost premium was acceptable to achieve a future competitive market and clinical flexibility. Professor Kearney concluded that whilst in a strategic sense there would be merit in following the clinical advice, the payment of a cost premium of this magnitude for clinical flexibility was not sustainable for South Australia if it acted alone to change the market. On 22 February 2001, a Purchase Recommendation was sent to Dr Tom Stubbs of the panel advising on the tenders upon the direction of Professor Kearney.

276 At that point, Baxter put in Offer 4 which was a three year option. After further discussion and review, on 16 March 2001 the State Supply Board endorsed the purchase recommendation to accept Baxter's five year offer with the 10 per cent allowance for purchasing PD products from other suppliers.

277 On 25 March 2001, Mr Battersby also wrote to the ACCC to advise it that South Australia was about to enter an agreement with Baxter, and then on 26 March 2001, emailed Michael Kiley of the ACCC to advise him that South Australia was going to proceed with the contract.

278 The following should be noted as to the Purchase Recommendation referred to above. The Gambro offer in relation to PD was limited and not compliant. The Fresenius offer was limited, but was otherwise compliant and was a reasonable alternative to Baxter in respect of the products the subject of the offer. Clinical advice was that there was no particular reason to choose one brand over another. Whilst competition dangers were perceived, it was stated that in ordinary circumstances, Baxter, as the dominant supplier with a significant local manufacturing presence would be the supplier of choice. Mr Battersby, as the author of the Purchase Recommendation, expressed a recognition in the weakness of SA's position:

(a) In dealing with IV fluids he said:

> *The intravenous fluids market in Australia is largely controlled by one supplier, Baxter Healthcare, who has the only local (NSW) manufacturing facility for these products.*
>
> *Baxter Healthcare continue to push for long-term contracts – typically 5 years for most State Governments – to ensure continuity of production for the facility. From a production planning perspective, this provides a reasonable time horizon to introduce new capital investment into the plant. From a strategic perspective, it also limits the opportunity for potential competitors to gain a significant foot-hold in the Australian market.*
>
> ...
>
> *Given that the SA requirement is less than 8% of the national requirement, there is little*

bargaining possible in such a monopoly supply situation, but there are some opportunities to work the margins through product rationalisation and added-value arrangements. There may be longer-term strategies that will improve leverage through multi-State cooperative arrangements.

In these circumstances, SA has little choice to opt for a 5 year term for IV fluids and it is recommended that approval be given to enter into a contract on this basis, *with the understanding that this represents a worst case scenario. Any continuing negotiations during contract formulation (such as Offer 4) and contract term will be to improve SA's position, particularly on modifying terms and conditions and to extract added value considerations (such as improving supply chain economics).*
[emphasis in original]

(b) In dealing with PD solutions he said:

Baxter has linked the lower-priced offer for IV fluids (in ***Clause 4.3.2*** *above) with a mandatory purchase of not less than 95% of the requirement for PD fluids within the contract arrangements – thereby effectively cutting out the smaller competitors, Fresenius and Gambro.*

A series of negotiations has occurred based on an attempt to break the nexus between the product groups and to reduce the contract period, in order to introduce clinical flexibility and competitiveness in the market place. ***Whilst some minor gains have been achieved (and a late Offer 4 received that provides a 3 year term), Baxter is resolute in dictating long term and linked product group contract arrangements.***

...

To achieve the clinicians' future flexibility will come at a significant cost (~$1.2m per annum for total flexibility – Offer 1 or ~$0.3m per annum for 3-year term and 95% market share only – Offer 4). These premiums increase further year by year, as negotiated fixed price advantages disappear. The acceptance of that cost is a policy issue compared with competing demands in the health system.

This cost premium has been determined to be not acceptable on policy grounds. ***It is therefore recommended that Baxter be nominated as the principal supplier (90% share) of APD and CAPD fluids for a 5 year term.*** *This recommendation is again on the understanding that this represents a worst case scenario and that continuing negotiations will be held during the contract term to better SA's position, possibly in cooperation with other States and noting that the ACCC may yet make a determination.*
[emphasis in original]

279 In cross-examination, Mr Battersby did concede that tenderers were told that the department might elect to offer exclusive contracts for particular items, and indeed, that such an arrangement may have been in its interest at the time.

NSW & Vic Agreement 2003

280 During the 1990s, and up until 2003, the supply of IV fluids and PD products to Victorian public hospitals were on separate contracts and not made through centralised purchasing. Often, the contracts for PD products were negotiated and entered into with separate public hospitals. There was no detailed examination of the Victorian position in the proceeding, though there was evidence to indicate that Gambro and Fresenius had been able to achieve a greater market share in PD products in Victoria than in other States. This assists in understanding and illuminating to a degree, the fact that the States have some power in determining the structure of the market and thus the structure and form

of the competitive process. This is perhaps best illustrated by a letter written by Mr Lee, the then Managing Director of Baxter, to the Chairman of the ACCC on 7 April 2004 in which the following was stated:

> *The relevant markets (however defined) are, if anything, more competitive now than they were before the challenged conduct. For example, the contracts being challenged are generally less exclusive than those which preceded them, and the largest contract has now been superseded by a contract let by Victoria and New South Wales on a totally non-exclusive unbundled basis for over 60% of the Australian market.*

281 On 9 May 2003, the NSW Department of Commerce issued a tender on behalf of the NSW SCCB and Health Purchasing Victoria for the supply of IV, PD and PN solutions and IS for a period of one year. The tender request invited responses on an item-by-item basis, and Baxter put in a tender on 25 June 2003 along those lines. At a meeting on 18 August 2003 at the NSW Department Commerce, NSW and Victorian representatives said that Baxter's prices were unacceptable. By way of response, Mr Lee wrote to Mr de Lapp on 26 August 2003 and indicated that Baxter was still keen to pursue a volume discount contract.

282 After further discussions, Baxter submitted a further offer on 10 October 2003 which contained more favourable pricing based upon volume discounts for total usage of IV and PN solutions and IS, and a minimum of 80 per cent of the available PD market. Through further correspondence, NSW and Victoria indicated that this offer was acceptable, although they were not prepared to guarantee supply. It should be noted, however, that a circular was sent on or about 13 November 2003 to chief executive officers of Area Health Services to advise them it was important to maintain Baxter's share of the PD market at 80 per cent, because prices were based upon Baxter's expectation that this would be the case.

283 Mr Lee, through his staff, protested in relation to the lack of a volume guarantee. Ultimately, however, in view of a threat from NSW that Baxter might be delisted from the contract for PD (with the market then being supplied by Fresenius and Gambro), Mr Lee said that he thought that Baxter had no alternative but to accept the contract. Accordingly, Baxter no longer has a guaranteed exclusive supply agreement with NSW and has not been able to charge the "cherry pick" prices.

284 Once again events reveal a real capacity in the States to decide upon the structure of the market and so, to a degree, upon the nature and form of the competitive process.

Evidence of Baxter's Competitors

285 The applicant filed affidavit evidence of representatives from companies which could potentially compete with Baxter in its markets for LVP and PN fluids and IS. Its thrust was that none of these companies sees entry into those markets as profitable or likely.

286 Mr Anderson who was employed by Astra Zeneca in Australia said that there are three difficulties to overcome before a company can supply IS in Australia. First, such solutions must be registered with the TGA, which is a process that is complex, time consuming and costly. Secondly, there are potential importation costs due to high freight costs arising from IS being bulky items. Thirdly, there is a high entry cost in that the establishment of a manufacturing plant in Australia would cost in excess of $20 million.

287 Mr Baker who was employed by Abbott said that the cost of commencing supply of LVP fluids in Australia would be substantial, costing millions of dollars to build a plant. Importation of LVP fluids was difficult because of transport costs.

288 The evidence from Baxter's major competitors, namely B. Braun, Gambro and Fresenius, concerned both the effect that Baxter's conduct has had upon them, and the reasons for their asserted

inability to enter certain sterile fluid or dialysis fluid markets in Australia. Not only did this evidence seek to reinforce the view that Baxter has a sustainable monopoly in sterile fluids, it also sought to suggest that the State contracts have deterred Gambro from continuing local manufacture of PD, and prevented Fresenius from establishing a local manufacturing facility for PD.

B. Braun

289 The applicant adduced evidence from a Mr David Crawford, who was the managing director of B. Braun in relation to B. Braun's business. He gave his evidence in a straightforward and open fashion, and he attempted to answer the questions put to him without prevarication. I found him to be of assistance and I accept his evidence.

290 As to the LVP fluids market, Mr Crawford confirmed in cross-examination that B. Braun has registered with the TGA 80 per cent of the LVP fluids that were sought in the 1997 NSW tender request. However, if B. Braun were to supply generic LVP fluids in Australia, they would have to be imported from Germany or Penang, because, in Mr Crawford's view, the Australian market was not large enough to justify a $20 million to $30 million investment in a local manufacturing facility.

291 In cross-examination, Mr Crawford agreed that B. Braun's cheaper overseas method of production meant that it could land generic LVP products into Australia at competitive prices. Accordingly, although he agreed that sea transportation was a cost, he said that it was not, in fact, prohibitive.

292 The tender that was submitted by B. Braun for the supply of LVP and PD fluids in NSW in 1997 was subject to TGA approvals for a number of its products and was conditional upon it being able to import fluids from Penang. As it turned out, the TGA decided not to register the Penang plant after inspecting it, and, as a result, PD and IV solutions could not be imported into Australia by B. Braun from that plant.

293 Mr Crawford believed that B. Braun would require 20 per cent of the IV fluids market to make it viable to sell IV fluids in Australia, and he would only consider entering the LVP fluids market if there was no bundling in place. Furthermore, he also said that NSW's unwillingness to change suppliers from Baxter is another difficulty that B. Braun faces, although this is because Baxter provides good service and the States are satisfied with Baxter.

294 Despite being pessimistic in relation to the LVP market, B. Braun does currently have a plan to enter the IS market with a pour bottle. The bottle would be manufactured in France and the solution would be manufactured in Australia, since it would be uneconomical to produce the solution overseas (due to high transportation costs). Mr Crawford confirmed that this plan to enter into an Australian manufacturing contract for IS remains serious, despite the results of the 2003 NSW tender.

295 As to producing PN fluids, Mr Crawford was sceptical because he said that B. Braun would need to set up a compounding plant in Australia if it were successfully to compete with Baxter. This, however, was qualified in cross-examination, because he agreed that either hospitals sometimes do their own compounding, or that compounding can be performed by a local subcontractor. Nonetheless, it does not appear that B. Braun can easily enter this market.

296 As to HD systems, B. Braun commenced importing HD products to Australia in 1995, but found that its landed cost was the same as the local price. As a consequence, B. Braun had to shut down this initiative in 1997, because it was unable to compete with companies such as Gambro and Fresenius.

297 As to PD products, Mr Crawford said that B. Braun could supply them to Australia from its Penang plant, assuming that $3 million to $5 million was to be spent to raise the plant to an acceptable TGA standard. He also said that in the interim, B. Braun could supply PD fluids at competitive prices utilising its German or Swiss plants. However, in both his affidavit and in cross-

examination, Mr Crawford acknowledged that the main reason for B. Braun not being in the Australian PD market is that its PD systems are of lesser quality to Baxter, Fresenius and Gambro in that they do not have a connection system that conforms with Australian standards. Furthermore, although he stated that the bundled supply agreements made B. Braun's entry very unlikely, he also agreed that any decision to undertake the necessary research and development to improve the connection system would have to be considered in a worldwide sense, and not just in respect of Australia.

Gambro

298 Mr Jamie Stokoe gave uncontested affidavit evidence in relation to Gambro and the effect that the various State contracts had upon its business.

299 As to PD products, Gambro commenced selling its PD fluids to NSW Health in 1990. In July 1991, it won a twelve month tender to supply the Sydney Dialysis Centre but then, in 1992, lost the NSW tender to supply PD products and IS. The result was that existing Gambro patients were transferred one-by-one on to the Baxter system. Mr Stokoe said that Gambro was not able to match Baxter's PD prices because Baxter's PD products were, in his words, subsidised by goods that it sold in a monopoly market that is LVP fluids. However, he believed that a company like Gambro would require in excess of 500 patients before it could commit the necessary capital for building a sterile fluids plant. Thus, competing with Baxter is very difficult.

300 In the wake of losing the 1992 NSW tender, Gambro began lobbying the Federal and State governments and the then Trade Practices Commission concerning the prospect of an entrenched Baxter monopoly in sterile fluids and PD fluids.

301 By June 2000, Gambro had ceased producing PD solutions in Australia, and had contracted with Baxter to produce the solutions on its behalf. The option of importing dialysis fluids from within the group of Gambro companies worldwide was open to Gambro, but Mr Stokoe said that freight costs would make it very expensive. Although Mr Stokoe believed that the Dandenong plant remained capable of producing PD solutions, a market share of at least 500 patients would be required before Gambro could recommence manufacturing PD fluids locally. If it did, Gambro would then consider producing TRIO in Australia (a particular PD fluid).

302 It is clear from the evidence that Gambro has nowhere near 500 PD patients in Australia. As at 31 May 2003, there were 37 patients on Gambro systems in Australia, and this represented 2.04 per cent of the market. Thirty of these patients were in NSW, and this constitutes 4.34 per cent of all NSW patients. Not surprisingly, Mr Stokoe said that this number of patients is "not viable as it is very expensive to run". He also said that Gambro has only remained in the market for "long term strategic" reasons, particularly in light of the "prevailing view in hospitals".

303 In relation to patients receiving PD at home, each patient has to be trained, and their monthly stock requirements continually assessed by a Gambro customer service representative. Gambro employs two people to liaise with patients at home. As to patients receiving PD in hospitals, Gambro employs a Product Manager to liaise with and market the products to doctors and nurses at the hospitals. These costs are necessary, though Mr Stokoe said that Gambro needed 100 to 150 patients on Gambro systems to justify the provision of each specialist who is required to provide services to these patients. In addition to this Gambro incurs storage costs for the fluids that it provides, because patients require approximately 3000 litres of PD fluids per year. As at February 2002, Gambro estimates that its total costs for the provision of PD services was around $520,000.

304 Under the 2003 NSW/Victorian contract, Gambro has seen a gradual increase in the patients that are using its PD products

Fresenius

305 Three witnesses swore affidavits relating to Fresenius in the proceedings for the applicant. The first was a Mr Shaun Hand, who was formerly a Sales Manager and then General Manager Products at Fresenius between 1997 and December 2002. Mr Hand reported directly to Mr Mechtersheimer, the Managing Director of Fresenius, and was responsible for Fresenius' responses to invitations to tender from NSW (1997), QLD (2000), SA (2000), WA (2000) and ACT (2000).

306 It should be noted however that Mr Hand became an employee of Baxter on 1 March 2003, whereas he had formerly been an employee of Fresenius. His affidavit also included [123] and [142] which discussed the reasons why Fresenius did not believe its presence in the PD market was economically viable. In examination-in-chief, Mr Rushton, Senior Counsel retained by the ACCC, asked Mr Hand whether there was anything in his affidavit that he would like to change. Mr Hand said that there was not, although he did note that Mr Mechtersheimer had removed some parts of the affidavit prior to his swearing it.

307 In cross-examination, Mr Yates, Senior Counsel retained by Mr Hand's employer, Baxter, tested Mr Hand's evidence in [123] and [142] of his affidavit. In [123] which related to the Queensland tender in 2001, Mr Hand had said that:

> *This 5 per cent allowance was no real benefit to FMC* [Fresenius Medical Care] *as it was too small to make entry into the PD market economically viable for FMC.*

In cross-examination though, Mr Hand sought to qualify the term "economically viable" by stating that he meant that if Fresenius had *only* sold PD, it would not have been viable to enter the Australian market. Mr Hand then agreed that there were *other* circumstances that made PD viable, namely the fact that PD was part of Fresenius' dialysis portfolio.

308 Paragraph 142 was similar in that Mr Hand had originally said that:

> *The Queensland PD market is not viable for FMC, with only 11 patients, and it is currently running at a loss in this State.*

309 Then in cross-examination, although Mr Hand said that this meant that the return on PD in Queensland was not high enough, he qualified this by agreeing that because it was part of Fresenius' dialysis portfolio, this fact provided a circumstance to make it viable. Mr Hand said that PD was not viable on the basis that it was the only market in which Fresenius entered.

310 In re-examination, and without opposition from Mr Yates, I allowed Mr Rushton under s 38 of the *Evidence Act 1995* (Cth) to treat Mr Hand as unfavourable, and to then cross-examine him. Mr Hand then agreed with Mr Rushton that there was no reference in his affidavit to PD not being viable only on the basis that it was a separate business for Fresenius (i.e. if that was the only market that Fresenius entered).

311 Similarly, as to making a loss on PD in Queensland, and despite his assertion of it as a fact in his affidavit at [142], he agreed that there was no documentary evidence to support it. Rather, it was an assumption. Mr Hand agreed that [142] is misleading, but in response to Mr Rushton's question that he sought to mislead the court, he said that he did not have this intention. As to an explanation as to why this was put in the affidavit, Mr Hand said they were trying to paint the picture that PD was not viable, and in his opinion, PD was being sold at a loss in Queensland.

312 Ultimately, I found Mr Hand's evidence to be most unsatisfactory, notwithstanding his swearing to [123] and [142] of his affidavit under oath. In reality he gave no explanation for the qualifications made, and when regard is had to the correspondence he had with NSW Supply when he was employed by Fresenius, it is with reluctance that I am bound to say that I place little reliance upon the qualifications made by Mr Hand while under cross-examination.

313 Mr Hand also gave evidence in relation to Exhibit C on the basis that he was familiar with the underlying records of Fresenius from which the document was prepared. He said that various costs, including cost centre MED AU", a warehouse in Canberra and various trucks, all related to both HD and PD products. In re-examination, it emerged that he had had a brief conference on the morning he gave evidence with Mr Yates and that he had not seen the document before that time. Accordingly, I place little reliance upon his evidence in this regard, and his explanation of Exhibit C is highly qualified.

314 Other issues that were raised in cross-examination concerned whether Mr Trevor Garland was the Peritoneal Dialysis Therapy Manager at Fresenius. Mr Hand said that he was and confirmed that he reported to him. He also agreed that Fresenius did not run its PD and HD businesses separately, and that common administrative staff were utilised. Only Mr Garland was allocated specifically to PD products.

315 The second witness for the applicant in relation to Fresenius was Mr Thomas Mechtersheimer, Vice President, South Asia Pacific of Fresenius Medical Care.

316 In his affidavit, Mr Mechtersheimer said that, in 1995, it was Fresenius' aim to enter the HD and PD markets in each State of Australia. In 1996, Fresenius began offering HD and PD products and services to hospitals Australia-wide, and also acquired Ajax Chemicals, along with its production plant at Smithfield, Sydney. Although that plant was suitable for producing HD products, it was not suitable for producing PD Fluids without first being converted to a sterile plant.

317 Mr Mechtersheimer said that the minimum investment required for the creation of a PD products manufacturing plant was $10 million. Prior to entry, Fresenius reviewed available data and came to the view that the Australian market was a good size market and that there was room for another competitor in both markets. To be successful, Fresenius predicted that its break-even point required a 25 per cent market share for PD and HD. It was thought that this would take four to five years to achieve. Soon after entering the Australian market, Mr Mechtersheimer became aware of the restrictive agreements in place between Baxter and the various SPAs. According to Mr Mechtersheimer these agreements (that is, including the bundling of sterile fluids and PD products) were the reason why Fresenius did not ultimately construct a PD manufacturing facility in Australia.

318 By 2000, although Fresenius had become the market leader in the HD market (it had more than 50 per cent market share), it had still only managed to capture less than 5 per cent of the PD market from Baxter. As at January 2003, Fresenius had 219 PD patients Australia-wide (12 per cent of the total); although a substantial number of these, namely 124, resided in Victoria (this represents 28 per cent of the Victorian market).

319 Mr Mechtersheimer then said in his affidavit that it was his belief that the contracts between Baxter and the respective SPAs prevented Fresenius from capturing an acceptable amount of PD market share. The losses that Fresenius incurred were unacceptable to him in the long term, and he said that if the contractual restrictions remain, Fresenius will be forced to exit the WA, SA and QLD markets. Indeed Mr Mechtersheimer held this view so strongly that he explained to Fresenius Kabi's executives that Australia is not an open competitive market and that entry into the IV market is not advisable.

320 The evidential substantiation of the losses said to have been made on Fresenius' PD operations in 2001 was less than entirely satisfactory. Mr Mechtersheimer said that his Finance Director had done the calculations, although he had checked them. The figure for the loss was said to be a minimum figure, and Mr Mechtersheimer explained that this was because a number of the figures were calculated simply on a pro rata basis. Affidavit evidence that had been previously rejected was then admitted into evidence, showing a loss on PD business in Australia of $400,000 in 2001.

321 Mr Mechtersheimer gave further evidence in his affidavit in reply concerning the consideration Fresenius gave to entering the PD Products market in Australia. He said PD manufacturing facilities have been built by Fresenius in Thailand and Japan rather than Darwin, which had been contemplated, and that Fresenius imports PD products from there to Australia.

322 During the decision-making process relating to the construction of a PD plant in Australia, Mr Mechtersheimer was the Finance Director. He said that a PD plant in Darwin would have catered both for the South East Asian market and the Australian market (there being no plant at that time in Asia).

323 In cross-examination, Mr Mechtersheimer agreed that Fresenius had an interest in the outcome of this proceeding, and that to a limited extent, an interest in an outcome that is favourable to the ACCC. This is not surprising given that Baxter is one of Fresenius' largest competitors.

324 Mr Mechtersheimer denied that his awareness of the exclusive contracts between the States and Baxter arose in 1995 before Fresenius entered the market. Rather, at that time, he said that he only knew patient numbers and that Baxter had most of the market. He maintained that it was in 1996 that he acquired a knowledge of the restrictive contracts. However, Mr Mechtersheimer did concede that the feasibility of a Darwin plant was not further investigated once the knowledge of the restrictive contracts surfaced. In fact, he agreed that no *formal* feasibility study in this regard was ever conducted. His only qualification was that he did his own calculations, which could not be located.

325 Mr Mechtersheimer was questioned in relation to the Fresenius' expansion in Australia. He confirmed that the Smithfield plant produces HD Products, and that since 1996, Fresenius has supplied HD and PD products in Australia. Furthermore, Fresenius opened offices in QLD, Victoria, WA, and SA in 1998, and employed a clinical representative at each of these offices. In the ACT, there was a technician but no offices. Dialysis clinics are also run in Perth, Freemantle, Adelaide, Melbourne, the Gold Coast and north of Brisbane.

326 It was also clear from cross-examination that Fresenius sees itself as a dialysis company. It is ready and willing to supply its complete PD product range in Australia although it sees its strength in the HD market (a treatment which 85 per cent of renal failure patients must or will use). Mr Mechtersheimer did not however agree that PD and HD were part of the same business, because in his view, the two products are very different, and are therefore sold and marketed differently. This meant that dedicated staff arerequired for each, and that separate performance statements are generated for each business. Common sales and administrative staff are utilised.

327 He was cross-examined generally in relation to the part he played in drafting the affidavit of Mr Hand, and this evidence revealed that Mr Mechtershimer had checked Mr Hand's affidavit for accuracy, and had had discussions with Mr Hand concerning business issues and costs. Although Mr Mechtersheimer did display a degree of embarrassment over this, it could not be taken from this that he had done anything inappropriate. It appears that he simply examined the affidavits of various people at his solicitor's direction. In reality, there was not sufficient detail in this evidence upon which to base a criticism of him, and indeed Mr Yates did not put matters of particularity to him.

328 As to the proposed Darwin plant, I not prepared to accept at face value Mr Mechtershimer's evidence that the bundled long term supply contracts in the 1990s were the cause of a decision to build in Thailand and Japan, rather than Australia. His evidence in this regard was less than compelling. The long term tied contracts may have been a factor tending against construction in Australia of a PD plant, but I am not prepared to accept that it was a determinative factor.

329 The third witness called by the applicant in relation to Fresenius was a Mr Bhargava, who was the Executive Vice President of the South East Asia Pacific Region of Fresenius Kabi, which includes Australia. He gave uncontested evidence in relation to Fresenius Kabi operations which is a wholly owned subsidiary of Fresenius AB. It operates in the fields of infusion therapy, parenteral nutrition,

enteral nutrition, infusion technology, transfusion technology, ambulatory care and medical devices but has no employees in Australia.

330 Mr Bhargava said that Fresenius Kabi produces PN and EN fluids and also manufactures a comprehensive range of LVP fluids. Fresenius Kabi has local manufacturing plants in almost all of the countries to which it supplies products. Mr Bhargava also noted in his affidavit that producers of LVP products usually hold significant stockpiles so as to meet demand when large volumes are required by hospitals at short notice.

331 Fresenius Kabi does not, and nor has it ever, supplied LVP fluids or EN products to Australia. Fresenius Kabi does however supply some PN products in Australia indirectly through Baxter. These products are imported from Austria, Sweden and China. In 2000, Fresenius Kabi's PN fluids constituted 18 per cent of the Australian PN market.

332 Mr Bhargava said that although Fresenius Kabi has considered entering the Australian PN, LVP and EN fluids markets, it had chosen not to do so for three main reasons. First, the requirement of TGA registration for each product it sells is both costly (up to $200,000) and time consuming (up to two to three years). Secondly, the existence of long term supply agreements made it impossible for Fresenius Kabi to profitably enter the market because demand from non-government health organisations is not high. Thirdly, freight and storage costs were sufficiently high to provide a disincentive to Fresenius Kabi's entry. Mr Bhargava said that Fresenius Kabi would not enter the market whist the long term supply agreements with Baxter remain in place. Furthermore, it would require a 50 per cent market share to justify the construction of a manufacturing plant in Australia.

Regulatory barriers to entry: TGA Approval

333 Detailed uncontested affidavit evidence was given by various officers and employees of the TGA as to the registration processes and costs involved in registering and maintaining registration of products of the kind here. Ms Hunt, the Assistant Secretary of the Drug Safety & Evaluation Branch of the TGA, gave uncontested affidavit evidence in respect of the TGA registration process for medicines. Ms Tang, who is the Section Head in the Medical Devices Assessment Section of the Office of Devices, Blood and Tissues of the TGA, gave uncontested affidavit evidence in relation to the TGA registration process for therapeutic and medical devices. Mr Tribe, the head of the Manufacturer Assessment Section, Office of Devices, Blood and Tissues, a Branch of the TGA, gave uncontested affidavit evidence in relation to the TGA's audits and standards for manufacturing processes.

334 It is unnecessary to deal with this evidence in detail. It is sufficient to say that there is a body of procedures, which require detailed careful attention and the investment of time and money that must be undertaken to distribute products of the kind under consideration. This is a cost of doing business. It is not, however, a barrier to entry of any real magnitude. The time taken to achieve registration of products and manufacturing plants may be a number of months. This means, to a degree, that rapid entry into the market is not possible.

335 Mr Stokoe of Gambro said that it usually takes two years for a product to be registered with the TGA, and the application process costs around $20,000-$30,000. There is also an annual audit and fee of $10,000 associated with manufacturing facilities.

336 Mr Hand of Fresenius noted that TGA requirements in Australia mean that typical new drug registrations for PD Solutions cost around $39,000. Fresenius also paid $25,000 and $10,000 to the TGA in 2002 to maintain its HD and PD product ranges respectively.

Evidence of Clinicians

337 Evidence was led from clinicians on issues concerning product quality, technological innovation,

servicing and clinical choice. These facts were said to go to assist in the assessment of the amount of market power that Baxter had. If the States genuinely sacrificed quality against their wishes, this might be evidence of Baxter's market power. Similarly, if it can be said that Baxter had not brought product innovations on to the Australian market, this might also suggest a negative effect upon competition or that Baxter is unconstrained in the market.

338 Ultimately, this evidence was inconclusive. A number of clinicians were strongly of the view that the Baxter products were inferior and that Baxter had failed to bring new technology on to the Australian market in a timely fashion. This was said to be a consequence of the market power of Baxter and a tangible clinical effect of the impairment of the competitive process. Other clinicians gave evidence that leads one to conclude that the above is an overstatement of the position.

339 I am left with a body of evidence which does not enable a conclusion to be drawn one way or another in these reports.

340 Lest I have misunderstood the significance of this body of evidence, I set out below its nature and relevant findings concerning it and the people who gave it.

Dr Chapman: Negative as to Baxter

341 Dr Jeremy Chapman, who was the Director of the Renal Unit at Westmead Hospital, a position which he has held for approximately eight years, gave uncontested affidavit evidence. Dr Chapman noted that selection in a tender of a product does not guarantee long-term superiority because products are likely to reverse in superiority over time. In 1993, when Baxter became the almost sole supplier of PD fluids and products in NSW, Dr Chapman said that he was concerned that this might adversely affect the provision of product and patient support, as well as product development and technological innovation.

342 In 1996, Dr Chapman became a member of the Contract Monitoring Committee. In February 1997, Dr Chapman was also appointed to the Contract Management Committee for the 1998 NSW agreement. Dr Chapman noted that he, as well as others, were concerned that during the long exclusive contract with Baxter since 1993, there had been little technological innovation and the new Freeline Solo system (one of Baxter's PD products) was very expensive.

Dr Falk: Negative as to Baxter

343 Amongst other evidence he gave, Dr Falk who was chief of renal medicine at Canberra Hospital, gave some evidence that there were some clinical advantages in using Gambro and Fresenius products because Baxter dialysis fluids were stored in PVC bags that released a particular compound. There was some real doubt thrown on the evidence of Dr Falk in this regard (although I do not impugn in any way Dr Falk's credit) bearing in mind the material upon which he founded it being not published until 2002. There was a wider debate which it is not possible to answer on the present state of the evidence as to whether there was any particular greater element of danger to patients in Baxter products than in Gambro and Fresenius products by reason of the use of PVC in bags. I am not able on the evidence to draw any conclusions contrary to Baxter in this regard.

Mr Garland: Negative as to Baxter

344 Mr Garland was a consultant with Fresenius and had held this position since February 2003. Between July 2001 and February 2003, he was employed by Fresenius as the National Peritoneal Dialysis Therapy Manager, and prior to this, from 1980 to February 2001, he was employed by St Vincent's Hospital in Sydney as a Clinical Nurse Consultant. Mr Garland has 23 years' experience as a clinician in the area of dialysis. Mr Garland was not cross-examined.

345 Mr Garland gave evidence about the St Vincent's PD Clinic. In the early 1980s, when St Vincent's opened its PD Clinic, Baxter was the only supplier of PD Fluids and Products in Australia. This continued until Gambro entered the market as an alternative supplier in 1990. In 1991 and 1992, the SDS awarded Gambro and Baxter a dual tender for the supply of PD fluids and products. Between 1991 and 1993, 70 to 80 per cent of St Vincent's patients were using Gambro products, namely because both the Gambro CAPD machine and APD machine were easy to handle and were cheaper than the Baxter equivalents.

346 In 1993, after the award of the NSW contract and after discussion amongst renal nurses, Mr Garland wrote to Dr Amos of NSW Health on 22 April 1993 to advise him that the renal nurses at St Vincent's had unanimously decided that further discussion was required. On 5 May 1993, a further meeting of renal nurses was held and Mr Hawkins of the NSW Health attended and explained the circumstances behind the agreement with Baxter. On 10 May 1993, Mr Garland wrote to Mr Hawkins to request that PD fluids be exempt from Contract 904.

347 Shortly after the commencement of the Contract 904, Mr Garland received numerous complaints about the contract from Gambro. Mr Garland also became aware of Abbott's concerns.

348 Despite the commencement of Contract 904, clinicians at St Vincent's continued to place new patients on Gambro systems. Mr Garland also came to understand that Baxter representatives were sent to hospitals to check compliance with the contract.

349 Mr Garland gave evidence about the Contract Monitoring Committee meetings that he attended, which considered compliance and servicing issues, as well as the price of Baxter's products. Mr Garland was particularly annoyed by Baxter's refusal to lower the price of "Freeline Solo", because in his view, Baxter was holding clinicians to ransom by dictating the type of treatment that could be provided to patients (i.e. older Baxter products).

350 Mr Garland was disappointed with the 1998 NSW Agreement, because in his view it prevented patients from having access to superior technologies. St Vincent's continued to place new patients on non-Baxter PD products. Baxter continued to complain. Though it did not take any action against St Vincent's for refusing to comply. Mr Garland said that at the time he left St Vincent's in early 2001 around 50 per cent of patients at St Vincent's were using non-Baxter PD products.

351 In Mr Garland's opinion, the NSW agreements reduced the ability of clinicians to treat their patients with what they thought were appropriate products. He also believed that Gambro and Fresenius had superior products and that Baxter only released new PD products into the market when it was convenient for Baxter to do so, as opposed to in response to user need.

Ms Sugar: Negative as to Baxter

352 Ms Sugar was a retired renal nurse and clinician. She was employed at the Sydney Dialysis Centre for 20 years from 17 October 1982 to 20 December 2002. She gave affidavit evidence and was not cross-examined.

353 Prior to 1993, the SDC was responsible for calling for tenders for fluids and machines used in home-based PD and HD. The Sydney Dialysis Centre used to call for tenders on an annual basis, and Ms Sugar noted that when Gambro entered the PD market, Baxter's commitment to service improved.

354 The Sydney Dialysis Centre switched a number of patients in 1991 to Gambro PD systems, and Ms Sugar says that there were a number of advantages in the Gambro product. She says that Gambro PD systems were easier for patients to use, and this was particularly the result of their locking system.

355 At meetings prior to entering into the 1993 NSW Agreement, Ms Sugar said that she raised some

of her concerns with Alan Kinkade, which included the concern that the contract effectively restricted the access that patients had to technological advances, better systems or alternative systems. It was Ms Sugar's view that the contract was entered into without proper consultation. During 1993, Ms Sugar received correspondence both from Baxter's competitors and clinicians expressing their views with respect to the contract. She also sets out disquiet amongst renal nurses and dialysis patients concerning the forced changeover to Baxter products.

356 Ms Sugar expressed her concerns at meetings of the Contract Monitoring Committee.

357 Ms Sugar was a member of the 1998 Purchasing Committee which met over a six month period prior to the signing of the 1998 NSW contract. In Ms Sugar's view, the 1998 NSW Agreement compromised the ability of renal clinicians to treat patients with products that they considered to be the most appropriate. This was particularly problematic for patients who were on Gambro products for specific reasons. Ms Sugar also believed that the bundled contract reduced patient access to the most technologically advanced treatment, because it prevented patients from utilising non-Baxter products, and the bundling itself did not provide any incentive to Baxter to innovate. Furthermore, she said that Baxter PD systems utilised the "spike" system, which according to her, is antiquated and is more susceptible to contamination.

Ms Evans: Positive as to Baxter

358 Ms Evans had been a Regional Manager, Renal Therapy Services in Brunswick, Victoria for Baxter since February 2000. Her duties entailed promoting Baxter dialysis products to private hospitals and other places. Between 1968 and 2000, Ms Evans worked for the Austin Hospital in Melbourne. From 1968 and 1988 she was a clinician, and from 1988 to 2000 she was in a management position.

359 Between 1968 and 2000, both as a dialysis technician and later as a manager, Ms Evans was heavily involved in advising on, and the negotiation of, purchasing arrangements between Austin Hospital and suppliers of HD and PD products.

360 From about 1990, the Austin Hospital Renal Unit began to acquire Gambro PD products almost exclusively, although this was in the absence of formal contracts. Due to patient complaints and some home servicing difficulties, the hospital decided in about 1993 to commence purchasing PD products from Baxter. In her experience, Baxter's service was superior to that of Gambro.

361 In 1995, Baxter offered to supply Austin Hospital for three years with its new Freeline Solo PD range with significant volume discounts if exclusive supply was agreed. After a 5 per cent allowance was negotiated for the trialling of other PD products, the offer was accepted. In Ms Evans view, the three year contractual period did not lock the Austin Hospital out of significant developments in PD technology, particularly as Gambro and Fresenius offered very few PD products for trial. In 1998 or 1999, this contract with Baxter was extended for a further two years.

362 For the duration of the contractual period for the 1995 contract, Ms Evans considered the quality of Baxter's products, service and performance to be very good. Ms Evans also disagreed with the evidence of Ms Sugar, Mr Garland and Dr Chapman, all of whom criticised Baxter for withholding technological innovation. In her experience, she said that it is not uncommon for Australia to be the final "cascade" of commercial releases of technology. Ms Evans was also impressed by Baxter's home delivery service, and in her experience, Baxter never refused to deliver products. She also said that Baxter never failed to honour its goods return policy, although she qualified this by noting that it is often difficult to re-issue home-delivered fluids, because they have often not been correctly stored. Also, Ms Evans could not recall any other renal clinicians, apart from Ms Sugar and Mr Garland, who felt that the 1993 NSW contract compromised clinical choice.

363 Ms Evans confirmed that Baxter did monitor PD patient numbers for the purpose of planning

production runs. She also said that at no time did Baxter place adverse pressure on the Hospital to utilise its products.

364 In cross-examination, in response to questions as to whether Baxter had delayed in bringing locking technology to Australia, Ms Evans said that she was not aware of this. She was unable to recall that there was a delay in releasing Freeline Solo in Australia that time. Ms Evans said she became aware of Mr Garland's and Ms Sugar's views and concerns at conferences. Ms Evans was straightforward and open. I have no reason to doubt her evidence.

Dr Irish: Positive as to Baxter

365 Dr Irish was a nephrologist and since July 1999 had been the Director of the Renal Unit at the Royal Perth Hospital.

366 In respect of the supply agreement between Baxter and WA, Dr Irish said that it was logical for WA to enter the agreement, given that Baxter's delivery network was first-rate, and its products were safe and reliable. He also suggested that the delivery of IVs and PDs was similar. Dr Irish said that the 10 per cent allowance for non-Baxter products was sufficient for trialling new products of other manufacturers and also said that he preferred to have one predominant supplier so as to save on inventory costs.

367 Dr Irish said that although each company's PD product had its advantages and disadvantages, in his opinion, Baxter had a superior overall range and service when compared with Gambro and Fresenius. Dr Irish also said that Baxter had been involved in innovation.

368 In cross-examination, Dr Irish agreed that there is a difference between delivery of IV and PD fluids, whereas in his affidavit he said that it was similar.

369 Dr Irish agreed there were 200 PD patients in WA, which means that 20 patients equates to 10 per cent. Although the 10 per cent limit applies to each hospital, Dr Irish noted that, given there are only three dialysis units that offer PD in Western Australia, this on average works out to be three to four patients per hospital.

370 Dr Irish agreed, in relation to the 10 per cent allowance, that Fresenius may be reluctant to embark upon a large distribution program for a minimal financial reward. Also, although Dr Irish said that patients on HD or PD in remote areas are equally likely to require more complex and extensive delivery systems, he did agree that in metropolitan areas, a more extensive distribution system is necessary for PD because there are more PD patients who receive their treatment at home.

371 Dr Irish confirmed that the Luer lock system is seen as a significant advance on the spike system, which has a greater risk of infection. He agreed that Baxter used the spike system until the late 1990s.

372 Dr Irish denied that PVC bags are of great clinical concern. In relation to an article that was annexed to his affidavit, Dr Irish said that no significant difference in peritonitis rates between the Baxter and Fresenius PD systems was found. Furthermore, in his view, the ultimate findings of the article are that there are no significant differences between the two systems. This was despite a number of negative conclusions in the article relating to Baxter's product.

373 In relation to paragraph 19 of his affidavit, where Dr Irish said that the Baxter product had overall superiority, he said that this conclusion takes into account service and delivery capabilities.

374 Dr Irish was straightforward and open. I have no reason to doubt his evidence.

Mr Kinkade: Positive as to Baxter

375 Mr Kinkade had been the CEO of Greenslopes Private Hospital since 2002. Between 1988 and 1994, Mr Kinkade was employed by the Northern Sydney Area Health Service, first as its Director of Financial Services and subsequently as its Deputy Chief Executive Officer – Management Services. It was during this time that he became familiar with the Sydney Dialysis Centre.

376 Mr Kinkade gave evidence concerning the Contract Monitoring Committee meetings, where Mr Garland expressed his concerns in relation to the 1993 NSW Agreement. Mr Kinkade was of the view that Mr Garland's criticisms as to lack of consultation and the lack of clinical choice were not valid, given that clinicians had been invited to participate by the negotiating committee (and indeed Dr John Mahoney and Mark Tudehope, both from Royal North Shore Hospital, participated). Moreover, Mr Kinkade was of the view that Mr Garland's opinions were not representative of the broader community of clinicians. His arguments and comments appeared to Mr Kinkade to be irrational and lacking in logical foundation. Indeed, Mr Kinkade recalled that he received positive feedback in relation to the contract from clinicians.

377 In 1993, Mr Kinkade considered Baxter products to be of equal quality to those of its competitors. Since then, his experience with Baxter has been that its reputation for quality remains and that it has continued to improve its products. Mr Kinkade also said that Baxter's quality of service delivery is excellent.

378 At the Greenslopes Private Hospital, there was dissatisfaction with Gambro in relation to its supply of PD and HD between 1998 and 2002. Some of the problems included irregular servicing of machines, missing orders and a lack of commitment to staff education. In March 2002, after a tender process, a new contract was awarded to Baxter to provide HD and PD on an exclusive basis. As a far as Mr Kinkade is concerned, Baxter's service is very satisfactory.

379 Mr Kinkade noted that he has not heard of any servicing complaints in relation to Fresenius.

380 Mr Kinkade said that it was not uncommon, in his experience, for the products of one company to be compatible only with other products from that same company.

381 In cross-examination, it emerged that he has been involved in procurement throughout his career, but his experience with the NSW sterile fluids contract is limited to the early 1990s.

382 Mr Kinkade refused to resile from his opinion that the way in which clinicians like Mr Garland had expressed their views was irrational and unjustified. He said that these clinical concerns were evaluated by the Contract Monitoring Committee which decided that overall, they did not "hold water per se".

383 Mr Kinkade gave his evidence in a straightforward fashion. He did experience some lack of recollection at times, but I accept his evidence. In my view, the Baxter clinic at the hospital where he was the CEO was not a sufficiently direct interest to impeach his credibility.

Evidence of Baxter's Employees

384 Evidence was given on a number of topics by employees by Baxter. Some of the evidence concerns the issues of the purpose of Baxter's conduct for both ss 46 and 47 of the Act.

Evidence relating to cost saving if Baxter ceased supply of PD to NSW

385 Uncontested evidence was given by Mr Craig Smith, who had been the Director of Finance at Baxter since 1997, in relation to the cost savings that Baxter would generate if it were to cease supplying PD products to NSW. This evidence was directed to the issue of whether or not Baxter would have to significantly raise prices if it lost the NSW PD contract. That is, if the cost savings

were small, Baxter would be justified in raising prices to cover the lost revenue.

386 Mr Smith set out Baxter's main "cost centres": "General Management" which covers expenses such as salaries for Baxter's managing director and assistant, and fees for legal, professional and consulting services; "Information Services/Technology" which captures the administration costs of Baxter's computer systems; "Finance" which relates to financial operations and invoices; "Personnel" which relates to the cost of the Human Resources department; "Office Services" which relates to the cost of the reception and mail room; and "Health and Safety" which relates to employee training. In Mr Smith's opinion, none of these costs would be reduced if Baxter ceased to supply PD fluids to NSW, and none is attributable to the production or sale of PD.

387 As to the costs that would be reduced, Mr Smith produced a spreadsheet which set out the savings that were calculated by various Baxter employees at his direction. Mr Ian Williams, who is the National Distribution Manager, calculated the savings in freight, home delivery and warehouse and distribution. In his uncontested affidavit, he said that there would be an overall annual logistical saving of $916,760. Mr John Warburton, who was the National Manager, Customer Service and Homecare, calculated the cost savings estimate for the Customer Service and Homecare cost centres. In his uncontested affidavit, he said that although there would be no saving in Customer Service, there would be an annual $162,000 saving in Homecare. Mr Charbel Hatem, who is the National Technical Services Manager, calculated the cost savings estimate for the "Service Department" cost centre. In his uncontested affidavit, he said that it would amount to $392,691 per year.

388 Ms Marie Coy, who is the General Manager Healthcare Solutions, provided an estimate of the savings in Sales and Marketing. In her view, there would be no reduction in the cost of Renal Marketing, because the same promotional activities would have to be undertaken given that PD would continue to be supplied in other states. She also said that no reduction in general NSW or national sales costs would occur because the employees in these departments would still have to sell Baxter's other products in NSW. Similarly, Healthcare Solutions General Management, Business Development, Marketing Management, Business Services and Corporate Affairs would also not experience cost savings. Only NSW Renal Sales costs, in Ms Coy's view, would be reduced, and this would be by a magnitude of 75 per cent (or $200,000), because less staff would be required. Accordingly, the total savings would be $200,000.

389 In cross-examination, Mr Rushton tested Ms Coy in relation to whether the marketing department would only save $200,000 if Baxter ceased its PD supply in NSW. She answered Mr Ruston's questions upon the assumption that this loss of supply only lasted three years and was not permanent. She denied that there could be any greater savings and said that Baxter would still require a significant marketing presence, with staff being used to consider re-entry. She also denied that marketing bonuses would be reduced, because staff would then have other projects and programs for which bonuses could be granted. Mr Rushton then put it to her that Baxter was an inefficient company to which she said that Baxter "is a company that is focussed on different therapies that need resourcing".

390 I formed the view that Ms Coy was honest and intelligent. I accept her evidence. With respect to some of the cross-examination, it appeared to lack a commercial focus. On the hypothesis upon which Ms Coy was working I can well understand how (unless the loss of PD was recognised to be permanent – which was not her hypothesis) the loss of the PD sales would not reduce costs in sales and marketing.

391 In the light of these calculations, Mr Smith said that the total of all cost centres in the 2004 Baxter budget was $40,892,423, and that the estimated cost savings if Baxter were to cease supplying PD in NSW would be $1,671,920.

392 These calculations were relevant to some of the modelling prepared by Mr Ergas and Professor Nalebuff. They do not explain nor were they put forward as explaining any significant part of the

large difference between the "cherry pick" prices and the bundled offer prices. Indeed no attempt was made by Baxter to analyse the "cherry pick" prices by reference to the cost base or the increased marginal cost of production positing any given reduction in volume throughput of the Toongabbie factory.

Evidence relating to Baxter's manufacturing and feasibility of another local PD plant: Mr Bragg

393 Mr Bragg, who was Baxter's General Manager Operations, gave evidence in relation to Baxter's manufacturing process (to which reference has been made) and the feasibility of a manufacturing plant dedicated in Australia to PD products in Australia.

394 Mr Bragg gave evidence about the capacity of the Toongabbie Plant and that it manufactures not only for Australia, but also New Zealand and the Pacific Islands.

395 Mr Bragg noted in his affidavit that Baxter had undertaken a substantial amount of capital expenditure in relation to the Toongabbie plant, particularly between 1990 and 2002. This included investment in automation, clean rooms, sterilisation vessels, extrusion equipment and other structural modifications of the building layout.

396 Mr Bragg expressed the view that the market in Australia was not large enough to justify Baxter having a dedicated PD plant. Accordingly, he also said that he believed that it was not possible for any company to set up a viable PD plant in Australia for the production only of PD. In doing so he calculated capital expenditure and manufacturing costs on a number of assumptions.

397 In cross-examination, Mr Bragg agreed that the point he made in his affidavit was that a supplier could not compete against Baxter for PD if it set up a PD manufacturing plant in Australia. He also agreed with Mr Rushton, after being shown Exhibit JAB6, that the unit volumes of PD put through the Toongabbie plant were relatively low, and usually did not constitute more than 10 per cent of the total volume produced there.

398 He agreed that the unit cost of PD bags fell if volume of IV and PN rose and that the hypothetical circumstances that he was positing only compared a PD plant with a plant that produced a full range of sterile fluids. Mr Bragg did not consider the possibility of a company building a PD plant and then moving into other sterile fluids (or visa versa). Mr Bragg also agreed that model was limited to producing 413,000 units of PD only and that no competitor had threatened to enter in this limited manner. He also accepted that his model did not take account of production for export.

399 On the assumptions made by him, I accept his evidence. Given the limited assumptions on which his evidence was based the use of his evidence is limited.

Evidence relating to Baxter's purpose and the calculation of its prices

Mr Gerard Wallace

400 Mr Gerard Wallace, who was at the time of giving evidence the President of Baxter Healthcare (Asia), was from 1992 until 1997 responsible for all of Baxter's New Zealand operations, and between 1998 and 2001, was Baxter's General Manager Sales and Marketing. In cross-examination, he confirmed that his responsibilities as General Manager Sales and Marketing included creating marketing strategies and plans. Some of these plans were shown to Baxter International, and he confirmed that regard was had to Global Business Practice Plans issued by Baxter International when developing these strategies.

401 In his affidavit, Mr Wallace said that although he was involved in the tenders for the supply of

sterile fluids to SPAs in NSW in 1998 and in Queensland, Western Australia and South Australia in 2000 and 2001, he was not responsible for determining prices or strategy. He did not recall the specifics of the NSW 1998 tender, but did recall being concerned to preserve the viability of Baxter's local manufacturing plant. He said that Mr Lee took the leading role in those negotiations.

402 Mr Wallace was not aware of any discussions amongst Baxter employees that canvassed the linking of PD pricing to IV pricing with a view to excluding competitors or deterring them from competing with Baxter.

403 As to the tenders in Queensland, Western Australia and South Australia, Mr Wallace said in his affidavit that he had no recollection of the detailed pricing in those tenders. He did however believe that he reviewed their final form. The tender process was left to Mr Browne to run, and as to prices, it was Mr Wallace's understanding that these reflected differing levels of anticipated volume of production through the Toongabbie plant. He also recalled that discussions relating to those tenders did not focus upon Baxter's competitors.

404 In cross-examination, Mr Wallace was asked some general questions about tying and bundling. He said that his understanding of "tying" did not mean that two products are sold together. He also said that "bundling" meant selling a broad range of products together, and he denied that Baxter International discouraged its practice due to competition concerns. Mr Wallace was then shown Baxter's *International Global Business Practice Standards* (Exhibit AA) and was taken to page 37 where it said that there should be no anti-competitive practices, including "tie-ins".

405 The cross-examination then turned to Baxter's strategies and purpose, and after confirming that he saw and reviewed budgets, Mr Wallace was asked some questions about Baxter's 1999 Australian Marketing Strategy (Exhibit K), which is a document that he had approved. The document contained the words, "Fresenius - potential to bundle renal and IV products" [page 1], and Mr Wallace explained that Fresenius did have the potential to put together such a bundle in a global sense. He also agreed that Baxter had sought to meet this threat by maintaining long-term fluid contracts, and that Baxter's bundling would maintain its position, although this was at its customers' request.

406 In relation to the words, "bundling of pumps with needle-less systems to leverage and protect needle-less business" (page 1-00319), Mr Wallace said that it could have meant that Baxter was seeking to protect its needle-less business by bundling pumps with needle-less systems. The only alternative explanation that he could offer was that these documents were prone to embellishment, being marketing presentations to its US parent. Importantly, he denied that "protect" referred to protection from needle-stick injuries, that being a suggestion which was made by Mr Lee.

407 As to the "Action Plan" (page 1-00328) within Exhibit K, which said "continue to tie up State contracts leveraged with other sterile fluid products", Mr Wallace said that he did not develop that plan and that he did not know who did. Nonetheless, he agreed that an interpretation of these words was that Baxter was aiming to meet the competitive threat posed by Fresenius by tying up PD with LVP, IS and PN fluids in State contracts. Moreover, he conceded that there was no other reasonable interpretation. In contrast to some of the evidence of other witnesses, in particular Mr Lee, Mr Wallace appeared willing to confront and deal with the internal documents of Baxter.

408 Mr Wallace was then shown the Baxter Australia Budget 2001 (Exhibit L) and he confirmed that he had not seen this document until the day before his evidence. He denied that there was pressure in the market place to have Baxter unbundle or shorten its contracts (page 2-00138), but agreed that it was Baxter's strategy to maintain its contracts, and that since many contracts called for bundling, Baxter responded in that way.

409 Later, Mr Wallace was taken to page 100371 of Baxter's 2000 Budget (Exhibit CC) and was asked some questions about the stated strategy within it of "bundling". He said that it was simply the continuation of bundled contracts in response to customers' wishes. He denied that Baxter developed

the strategy, or that it was in response to competitive threats. However, he agreed that its effect upon competition was a happy side effect.

410 In the context of how the "cherry pick" prices were determined, Mr Wallace agreed that Baxter wanted the bundled offers to be accepted, even though he qualified this by saying that this was what the customer wanted. He also said that Baxter aimed at both customer satisfaction and the maintenance of volume through the Toongabbie plant. He denied that the "cherry pick" prices were designed to compel the States to take bundled offers. Rather, he said, they were designed to protect Baxter if they lost volume, although obviously they could not completely compensate for such a loss.

411 Mr Wallace also denied that he thought there were no other viable competitors in the sterile fluids market at that time, and put forward B. Braun and Fresenius as examples. He also said that he was unaware that B. Braun's manufacturing facility had been rejected by the TGA. He appreciated that there was a risk that the States would reject the bundled offer, but said that it was not overly significant given the States' history of preferring long-term contractual arrangements. He said the "cherry pick" prices were "not punitive".

412 Later, in re-examination, Mr Wallace said that the "cherry pick" prices were at or below Baxter's published list price. These list prices were prices in the market place for clinics or vets or small hospitals that chose to buy from Baxter in very small quantities.

413 Mr Wallace was also questioned in cross-examination in relation to the specific circumstances in the South Australian and Queensland markets. In respect of South Australia, he was shown Annexure P to Mr Battersby's Affidavit, which was Baxter's tender in SA. He agreed that he signed and approved it. He was then shown SA's request for an Offer 1A and Baxter's response (Exhibit S and Exhibit T), which he did not recall. As to whether this indicated that Baxter would give no discount unless SA took both IV and PD from Baxter, Mr Wallace said that this was a reasonable interpretation, and that he could not think of any other explanation

414 Mr Wallace was also shown the email in which Mr Battersby raised his concerns under the Act with Baxter (Exhibit U), but he denied having seen the document, and denied being informed of the issue at the time by Mr Browne. Mr Wallace said that it was very unlikely that Baxter was giving its PD away and that you would have to consider the cost of the bundle and the product mix. In response to a question as to how Gambro or Fresenius could compete with Baxter's offer, Mr Wallace said that they would have to have a better product. He then denied that it was Baxter's intent to ensure that they could not compete, and instead said that Baxter's offers are made on the basis of best value for customer and volume through the plant.

415 In relation to QLD, Mr Wallace was unable to recall whether "cherry pick" prices were put forward or not in tendering for PN products. He was shown some documents produced by QLD Health under subpoena (Exhibit BB) and agreed that they contained a supply proposal for PN products into QLD in 1998. He was asked to explain why the NSW "cherry pick" price was higher than the item-by-item prices offered to QLD. He suggested that this was because NSW had moved onto a differently compounded product, which meant that the volume for that code was higher in QLD (as less of the former product sold in NSW), and hence the NSW price was higher. He did not accept that QLD was offered lowered prices because there was no ability to bundle PN with other sterile fluids. Later, Mr Wallace was shown some correspondence (Exhibit DD) that contained the Annexure to the 1998 NSW Agreement. It demonstrated that the units of PN supplied to NSW for the codes supplied in Queensland was substantially higher even after doubling the QLD figures to take account of the fact that they were for a half year. He agreed that NSW had higher volumes, and then conceded that this shows that different volumes are unlikely to explain the price differential in Queensland.

416 Finally, the topic of technological innovation was addressed, and Mr Wallace was shown a Leur Lock Conversion Launch Package March 2000 (Exhibit EE). He agreed that management in 1998 had

delayed the pursuit of the Leur lock.

417 Although at times Mr Wallace's evidence was self-serving, he did not resort to wordy non-responsive answers. He generally conceded points where he had no alternative. I look upon his evidence with some reservation, in particular, in relation to the purpose of the item-by-item prices. I have later expressed my views about Baxter's purpose in the structure of the tender bids. Mr Wallace's evidence was, by and large consistent with what I consider to have been the purposes of Baxter and the role of the item-by-item prices. To the extent that it can be seen as inconsistent with that I reject it.

Mr Christopher Browne

418 Mr Christopher Browne, who was at the time of his evidence the CEO of the Leukaemia Foundation of Victoria, was from 2002 the Director - Northern Region of Baxter and, before that, was Baxter's Executive Director – Sales. Mr Browne reported directly to Mr Wallace at Baxter. One of his responsibilities was to prepare tenders called by various SPAs. It was his experience between 1985 and 2002 that Baxter generally prepared various alternative tender bids to SPAs, each differing in levels of exclusivity, volume commitment and pricing. The "stand alone" or item-by-item prices were, he said, generally based upon Baxter's hospital list prices for "off contract" purchases. Mr Browne also said that costs and historical pricing were taken into account in any given tender, and that he always attempted to ensure that prices were set to ensure gross profit across the range.

419 Specifically, Mr Browne said in his affidavit that he determined prices by taking account of the period, customer, freight, warehousing and other costs. In calculating Baxter's best price, he worked on the assumption that Baxter would supply 100 per cent of the client's IV fluids needs and at least 90 per cent of its PD fluids requirements. In calculating the item-by-item "cherry pick" prices, he worked on the assumption that Baxter would lose its largest contract at the time, namely the NSW sterile fluids contract, which he believed represented approximately 35 per cent of its total sterile fluids business. Mr Browne claimed to believe that there was always a possibility that Baxter might lose a tender, particularly as it lost the NSW contract to Abbott in the 1980s. Furthermore, Mr Browne said that although he did not expect the SPAs to accept the "cherry pick" offers, he did regard the "cherry pick" prices as genuine, and did believe that there was a real possibility that the SPAs would choose to opt for flexibility, and therefore the "cherry pick" offer.

420 As to competition, Mr Browne said that he regarded Fresenius and Gambro and B. Braun as the main competitors in HD and PD fluids. He also perceived that B. Braun was a potential competitor in the IV fluids market because he knew that it had registered IV products with the TGA. Indeed, even in 2000, Mr Browne said that he believed that Baxter's IV fluids volume was not secure and that B. Braun would enter the IV fluid market.

421 Throughout the late 1990s and 2000-2001, it was Mr Browne's perception that Fresenius, Gambro and Baxter shared the renal markets equally. He said that Baxter never had a strategy of seeking to exclude either company. Mr Browne said that he was aware of Baxter's obligations under the Act, particularly as Baxter had become the only substantial supplier of IV products. He also believed that the SPAs had the contracts vetted by their lawyers, and as a result, was of the view that there were no competition concerns.

422 Mr Browne also gave affidavit evidence in relation to the transactions that occurred in particular States. As to WA, Mr Browne noted that he was largely responsible for the pricing and structure of Baxter's 2000 tender. Since the tender request was in relation to the full range of IV, PD, IS and PN products, it was Mr Browne's objective to put together the most attractive package on all the products that Baxter wanted to supply. He said that he did not set the "cherry pick" price at a prohibitive level, but rather, set the price having regard to the possibility of losing volume in other states while still being bound by its contract in WA to supply products on a discounted basis. The discount offered in return for longer terms and exclusivity was based upon volume and the ability it gave to Baxter to

confidently invest for the long term. Moreover, Mr Browne said that he did not turn his mind to the extent of the discount on PD that the bundle created. Rather, he said that the offer structure simply made it clear to the government that without a predictable long term high volume supply agreement, the prices would have to be higher. Also, Mr Browne said that the discounting of PD products was lower, because under the item-by-item offers competitive PD prices still had to be offered, due to competition in the market. Mr Browne did not believe that WA was forced by the bid structure to accept the bundled offer.

423 As to the QLD tender in 2000, Mr Browne said that he was not aware of the apparent difference between the discounts offered for IV and PD. Rather, at the time, he was concerned with presenting the best overall offer to Queensland on all products. Furthermore, he had also expected B. Braun to enter the market with a bid, given that it had TGA registrations that covered 80 per cent of the volume of IV products. As to the exclusivity terms in the contract, it was Mr Browne's understanding that this did not preclude the purchase of new technology from non-Baxter suppliers, or the use of non-Baxter products if clinical choice required this. In his view, the 7.5 per cent allowance for non-Baxter products made this possible.

424 As to the SA tender in 2000, Mr Browne said that he was primarily responsible for preparing both the bid and the pricing. He confirmed that he read the email from Mr Battersby dated 5 December 2000 in which Baxter was requested to provide an Offer 1A for the supply of all sterile fluids except renal products for a period of five years (as opposed to 2 years). Mr Browne also recalled communications with Mr Battersby in which he expressed his concerns that Baxter was giving its PD away when Offers 1, 1A and 2 were compared. In relation to this, Mr Browne said that because the number of PD patients in South Australia was very small, the total cost of providing PD was less than the difference between Baxter's best long term volume discount offer on all products (Offer 2) and Baxter's "cherry pick" offer (Offers 1 and 1A).

425 As to why Offer 1A pricing was identical to Offer 1 pricing, Mr Browne explained in his affidavit that a loss of PD products would reduce Baxter's revenue in SA by 30 to 40 per cent. Since Baxter currently had 100 per cent market share, Mr Browne said that this was something Baxter did not want to lose. He also said that he had anticipated some negotiation of this offer. SA did not attempt to negotiate.

426 Mr Browne also said in his affidavit that he did not intend Mr Battersby or anybody else in South Australia to analyse the offers in the way that Mr Battersby did. He said that at no time did it occur to him that it would be cheaper for SA to purchase four products (i.e. LVP, IS, PN and PD) as opposed to three products from Baxter. As to the trade practices issue that was raised, Mr Browne recalled speaking to Mr Bycroft in WA, who told him that they had checked out the offer to WA legally, and were comfortable from a trade practices perspective. As a result, Mr Browne said that he did not perceive there to be a trade practices problem in SA.

427 In the 1998 contract with NSW, there was a "most favoured customer" clause. Mr Browne suggested that setting prices in SA in line with larger States, given the low number of PD patients, also contributed to the difference between Offers 1 and 1A and Offer 2.

428 In cross-examination, Mr Browne said that although he had total responsibility for the tenders in SA and WA, he was not the first person to initiate or develop Baxter's typical structure of tender offers. Mr Browne was asked some questions concerning the purpose of Baxter's tender structure, and he agreed that Baxter had two aims, namely to win the business and to maintain the market by tendering in a way the State wanted. Not surprisingly, he did concede, though, that the offers were structured in such a way as to give Baxter the greatest chance of winning the tender and a competitor the least chance of winning the tender. However, he denied that Baxter wanted to stop other competitors competing, or having the opportunity to compete, for the business.

429 As to Mr Browne's expectations of what the SPA's would do, he agreed that if no other company

entered the market he expected the item-by-item offers to be rejected, given that the "cherry pick" prices were substantially higher than the States were then paying. He then denied that the item-by-item offers were made simply to make the bundle look more attractive. Rather, he said, it was to give the states a choice just in case another company put in a bid.

430 Mr Browne asserted that rival bids in the IV market were possible because other companies had TGA product registrations. This, however, contradicted what he had said to the ACCC in the s 155 proceeding where he had agreed that Baxter had the IV fluids market at that time and that there were no other competitors. Accordingly, Mr Browne tried to qualify these statements by denying that he thought there was no competition for IV fluids, and was forced to concede that his answers before the ACCC could have been misleading, although not intentionally so.

431 As to the effect of Baxter's offer structure, it was put to Mr Browne that it made it impossible for Fresenius and Gambro to compete in the PD market. At this point he attempted to avoid the question, but the substance of his response was that competitors had to have a product of similar quality and reputation. He then conceded that they would probably have to have a better product, and ultimately suggested that nephrologists would have to specifically want the Gambro or Fresenius product. Despite this, Mr Browne denied that the offers were intended to have the effect that competitors could not compete, although he did concede that in WA, competitors would not have been able to compete.

432 In relation to the calculation of the "cherry pick" prices, Mr Browne suggested that they were calculated with regard to history and price lists even though he agreed that he had not seen any document at Baxter explaining how the prices were reached. Before the ACCC in the s 155 proceeding, Mr Browne had said that Baxter could have charged what it liked for IV, but did not because it was a good and moral corporate citizen.

433 As to the 2000 tender in WA, Mr Browne was shown Annexure F to the affidavit of Mr Bycroft, which was the WA tender request. As to whether the tender request envisaged a long term exclusive offer, Mr Browne suggested that it did, based upon clauses 1.2.1 and 2.6. In particular, the words in clause 1.2.1 "sterile fluids for 5 year period" suggested to him that this included PD, and hence the invitation for a bundled offer. It was then put to Mr Browne that bundling was not really a response to tender requests, but that it was developed to meet competitive threats. He denied that Baxter had a marketing strategy of bundling IV and PD, and said that it was more historical in the sense that that was how Baxter responded to tenders over many years.

434 Mr Browne was then shown the Australian Marketing Strategy 1999 (Exhibit K), and he said that he did not participate in preparing that document. When asked about the words, "potential for Fresenius to bundle IV, renal and nutrition products", Mr Browne said his understanding was that Fresenius would ultimately have these products in Australia. Nevertheless, he said that maintenance of long-term fluids contracts was Baxter's aim regardless of competitive threats. However, as to the words "tie up state contracts leveraged with other sterile fluids" and whether they related to competitive threats in the PD market, Mr Browne was dismissive of the proposition and said that this document "contained a lot of fluff", being a presentation to the US parent. However, given that Mr Wallace conceded that this document did suggest that Baxter had the stated strategies and with the application of some common sense, it would seem that Mr Browne was being less than frank with these responses.

435 Mr Browne agreed that Baxter "loosely" monitored the compliance, by using Baxter's clinical nurses. He was shown a summary sheet of patient numbers (Exhibit KK) and agreed that the clinical nurses would have looked at what Baxter's competitors were doing as well as reviewing Baxter patient numbers. He also agreed that Baxter had records that demonstrated patient numbers for competitors at any time (Exhibit M). On the evidence there was nothing "loose" about Baxter's monitoring of the various contracts.

436 Mr Browne was taken to Mr Battersby's email requesting an Offer 1A (Exhibit S) and he agreed

that pricing and discounting information was not provided because he did not want to disclose it. He was then shown Baxter's Offer 1A (Exhibit T) and he agreed that if South Australia took all its sterile fluids (excluding PD) from Baxter, it was still going to have to pay the "cherry pick" price.
Mr Browne then denied that it was intended to compel South Australia to take the bundled offer, despite the fact that South Australia had to take its IV from Baxter.

437 Nevertheless, he did make this concession:

> *"Q. Wasn't the reason why Offer 1A was put in terms of a cherry pick offer to drive them into accepting the bundled bid?*
> *A. I would have hoped that they would have from that, but I would have also expected a negotiation from South Australia from that 1A bid.*
>
> *Q. Oh, yes, but that was its purpose, was it not?*
> *A. The purpose – well, the purpose was to tell them that I wasn't happy with losing, you know, 40 per cent of my revenues, and you can – if you're going to take 40 per cent of my revenue away, no, I'm not going to give you some good pricing"* [T894]

Given that this was despite the fact that there were only 78 PD patients in South Australia, it is clear that Mr Browne did not want to lose the PD business. This suggests that the real purpose of Offer 1A was to achieve a guaranteed PD market share for Baxter.

438 He agreed that the volume discount was the difference between the "cherry pick" price and the bundled price, and that this could also be looked at as an increase in price from the SA's point of view.

439 Mr Browne was then shown Mr Battersby's calculations which demonstrated that it was cheaper to take four as opposed to three products (Exhibit U), and he said that these numbers surprised him. He agreed that on these numbers, it would be very difficult for a PD competitor to compete. But he denied that that effect was the intention of the offer structure. Rather he said that it just worked out that way due to application of the same formula as used elsewhere and the fact that there were a low number of PD patients in SA. Baxter satisfied itself that the offer did not breach the Act with in-house counsel. I do not accept that Mr Browne was unaware at the time of the results of these pricing matters. He would have known full well the reality reflected by Mr Battersby's calculations.

440 Mr Browne was defensive and at times refused to make admissions. I have real reservations about important parts of his evidence, in particular in relation to the 2001 SA tender and as to his understanding of the purpose of the structure of Baxter's offers. His purpose was, I find, as I have set out later in describing Baxter's purpose.

Ms Marie Coy: Baxter's General Manager Healthcare Solutions

441 Although Ms Coy did not give any affidavit evidence concerning her involvement in tenders, Mr Rushton, after establishing that she had responsibility for the administration of the tenders between 1991 and 1997, cross-examined her in relation to Baxter's purpose and strategies.

442 In relation to Baxter's practice of using "cherry pick" offers, Ms Coy denied that their purpose was to compel States to take the bundled offer. Rather, she said, the purpose was to demonstrate to a State the "value" that the bundled offer represented, and to comply with the tender. She agreed that the "cherry pick" prices made the bundled offers more attractive. This notion that the "cherry pick" prices were there to "demonstrate value" was a more straightforward answer than that given by other witnesses called on behalf of Baxter that the "cherry pick" prices were set to compensate in some fashion for the loss of market share. Mr Lee denied that the "cherry pick" prices were designed and intended to make the bundled offer look more attractive. I reject this evidence. The denials of Mr Wallace in this regard were not convincing and I reject them. Mr Browne's evidence on this regard,

as a whole, should be seen as conformable with Ms Coy's evidence.

443 As to the position of Gambro and Fresenius, Ms Coy denied it was a purpose of the alternative offer strategy to prevent them from competing and moreover, she did not think that the offers had this effect. When asked to consider how this could be true, she responded by saying that Gambro and Fresenius could and did put in tender offers themselves. This answer threw up one aspect of the cross-examination of a number of witnesses and of the case to which I will refer in more detail in due course: the relevant notions of "competition" and "compete" in this context.

444 Whilst I accept that Ms Coy was honest, I gained the impression she was keen to defend the interests of her employer.

Mr Brian Lee

445 Mr Brian Lee, the former Managing Director of Baxter, gave evidence for Baxter. He was the Director of Sales and Marketing between 1987 and 1995, and during that period was primarily responsible for the coordination of sterile fluid tenders to SPAs. In 1995, Mr Lee was appointed Managing Director, and although he continued to have an active role in most decisions affecting sterile fluids tenders, the principal control was delegated to Mr Gerard Wallace and Mr Chris Browne. Also, Mr Lee denied having a high-level involvement in the tenders in SA, WA and QLD in 2000. In relation to the negotiation of the 1998 NSW Agreement, Mr Lee did not have day-to-day responsibility for its preparation. He was, however, involved in the negotiating process.

446 In his affidavit, Mr Lee suggested that his two main objectives for tenders were to maintain percentage gross margins and to maintain volumes. As a result, he claimed that he generally did not seek increases in percentage gross margins that would price Baxter out of the market in the long-term, and said that he had never approved pricing a product or class of products below the average cost of manufacture. This was regardless of whether "cherry pick" or "sole supply prices" were offered.

447 In relation to "cherry pick" prices, Mr Lee's affidavit evidence was that he gave prices that were similar to Baxter's hospital list prices, which were lower than "list" prices for individuals. He said that these prices were also formulated taking into account the possibility of a significant loss of volume across all States. His experience of losing the sterile fluids contract in NSW in the mid 1980s made him wary of this prospect. Indeed, he was conscious that the Toongabbie plant might be closed if production of sterile fluids became uneconomical.

448 As to his intentions, Mr Lee said:

> *"my concern has been to compete for business against all other tenderers (whoever they might be) with a view to winning as much business for Baxter as is possible. I have never intended or expected that any tender Baxter, or subsequent offer by Baxter in the course of negotiations with respect to a tender would exclude another tenderer from being a competitor of Baxter".*

449 Once again this answer threw up this notion of "competition" or "compete". Plainly Mr Lee was directing this evidence to preventing any other tenderer putting in a bid.

450 Mr Lee also pointed to growth in demand for IV fluids, PN fluids and PD products throughout the 1990s, which meant that he offered low prices so as to discourage overseas entry. He said that the Australian market is probably incapable of supporting more than one local manufacturer of IV fluids, irrigating solutions, PD fluids and PN fluids, on account of Australia's high manufacturing cost, low patient population and demand for world parity pricing.

451 Mr Lee in his affidavit evidence also outlined his intentions, expectations and purpose in

submitting the kind of bid made to NSW in 1998. See [214] above. The thrust of these expectations was said to be as follows. He expected Gambro and Fresenius to bid on PD products and B. Braun to bid on eight codes of IV fluids (which constituted 80 per cent of Baxter's volume). He expected that NSW would reject Baxter's offers and seek to further negotiate, with the result that ultimately, Baxter would win an exclusive contract for IV fluids and irrigating solutions and about 80 per cent of the PD business through post-tender negotiations. As a worst case scenario, Mr Lee considered that B. Braun might win 40-60 per cent of the IV market, but not 100 per cent because it did not have such capacity. Accordingly, he asserted that the "cherry pick" price was calculated having regard to a loss of 40 to 60 per cent of IV volume and a loss of 40 per cent of PD volume. He also said that he believed that Baxter could not push prices too high as it would stimulate interest from overseas manufacturers.

452 Mr Lee said that during negotiations with NSW he told NSW representatives that there was always pressure from head office in the US to close the Toongabbie plant, and that the construction of such a plant with its supporting distribution network would cost in the order of $80 million. As to the revised Offers 5a and 5b, Mr Lee said that although he reviewed the prices he did not formulate them.

453 Mr Lee confirmed that the ACT was given the same prices for sterile fluids as NSW from 1993. After the 1998 agreement had been made with NSW, Mr Lee delegated to Ms Spink the task of organising arrangements with the ACT. He was aware of the correspondence between Ms Spink and Mr Bonato and the acceptance signed by Mr Bonato on 17 March 1999.

454 After being informed by a Baxter employee that Canberra Hospital had issued a request for proposals for the provision of dialysis services (including both HD and PD), Mr Lee instructed Mr Wallace to write to the ACT protesting about this. Despite also submitting a proposal for HD products, it later turned out that the contract was awarded to Fresenius. Accordingly, Mr Lee thought that ACT was in default of its agreement, and although he believed that prices should increase (due to the loss of a commitment to volume), he did not think that Baxter should withhold supply.

455 Mr Lee recalled a conversation with Mr Keith Barton of Queensland Purchasing and Sales in the mid 1980s, where Mr Barton had said "Give us a bid for the lot".

456 The preparation of Baxter's 2000 tender in QLD was undertaken by Mr Chris Browne and Mr Gerard Wallace. Mr Lee said that he gave instructions suggesting that Baxter ought to make a complying bid and an overall three year bid, and that these be on the assumption that B. Braun would bid for IV solutions and that Fresenius and Gambro would bid for PD. At this time, he also said that he thought that Fresenius was likely to enter the IV market shortly. Mr Lee approved the final version of Baxter's offer, although he was not involved in its formulation or the calculation of item-by-item prices. He believed that the pricing was prepared on the same basis as it had been in NSW.

457 Mr Lee said that he was aware that in mid-2000, the WA Government had issued a request for sterile fluids. Baxter's tender was prepared by Mr Browne and Mr Wallace and Mr Lee did not see the final version. Mr Lee said that he believed that the pricing was prepared on the same basis as it had been in NSW. He had no contact with representatives from WA in respect of the 2000 tender process. He did remember that the WA Government wanted the ability to obtain 10 per cent of PD products from other suppliers, which he said he thought was reasonable.

458 Since Baxter's 2000 tender in SA was prepared by Mr Browne, Mr Lee did not "sign-off" on the document. He was kept informed about the tender process in SA, and said that he believed that the pricing was prepared on the same basis as it had been in NSW.

459 In cross-examination Mr Lee was questioned at length in relation to his and Baxter's expectations and subjective purpose behind the structure of the tender offers to each of the States. As to expectations, he agreed that Baxter expected to win a sole supply contract with NSW in response to the 1998 tender request. He also agreed that a similar expectation had been held in 1993, because there was virtually no risk of Baxter being excluded from the supply of IV products and IS through

the NSW tender in that year. However, when asked whether Baxter expected to win exclusive supply contracts for IV and IS fluids in all States during the 1990s, Mr Lee denied that this was true after 1996.

460 Mr Lee was asked about "product leveraging" and he agreed that it is where a company bundles a product in respect of which it has substantial power with a product in respect of which it does not have market power, or where a company uses one product to sell another product. Furthermore, he understood how leveraging or bundling could secure, maintain or expand a company's market share. Despite this understanding, however, he denied that Baxter's bundling of IV products with PD products was product leveraging, because he said that the products had different usages and that this bundle was directed toward securing throughput and volume for the Toongabbie plant as opposed to expanding or preserving PD market share. This explanation was inconsistent with the understanding of "leveraging" that Mr Lee claimed to have. I do not accept Mr Lee's evidence in this regard. I find that he viewed the package of PD fluids in contracts with sterile fluids as bundling or leveraging and that it was directed to preserving or expanding Baxter's PD market share, and thereby maintaining plant throughput.

461 Mr Lee also denied that Baxter's bundling was for the purpose of keeping Fresenius and Gambro out of PD market. When asked to explain how Gambro and Fresenius could possibly compete with bundled bids, he said that he simply did not know, which was how he answered the question before the ACCC in the s 155hearing. When further pressed, he suggested that they could have put in a better tender. I reject this evidence. I find that the arrangement of the offers was understood by Mr Lee to have the consequence that it would be difficult, if not impossible, for Gambro or Fresenius to put in more attractive bids on price for PD fluids without their, in some fashion, combining with another supplier of sterile fluids to match Baxter's scope of supply. Indeed Mr Lee ultimately conceded that if it were true that Baxter was giving away its PD in SA then it would have been impossible for Gambro and Fresenius to compete. This reflected the reality of which Mr Lee was aware. The purpose of the bundling in the exclusive supply contract was not to prevent others such as Gambro and Fresenius putting in a tender, but it was to prevent such tenders as they put in being realistically competitive.

462 Later, Mr Lee also denied that bundling was in response to threat of competition in PD and denied that it was part of an action plan to meet the entry of Fresenius by tying up State contracts with bundles. I reject this evidence. Whilst it was not a strategy which was forced on the States by Baxter, it was part of Baxter's intended method of defeating Fresenius and Gambro in the PD market.

463 After the situation in SA was raised with Mr Lee in the s 155 proceeding before the ACCC, he said that he then checked whether Baxter was within the Act. This entailed instructing Mr Wallace to speak to Baxter's lawyers. Also, although he read Mr Battersby's email about the tender in SA and understood on his view that he was concerned that Baxter was giving its PD away, he did not check whether it was true that PD was being given away in South Australia. I reject this evidence. I have no doubt that Mr Lee made himself aware of the pricing structure in SA and of its straightforward consequences if analysed even at a basic level.

464 As to whether Baxter had the same strategy in all its tenders, Mr Lee denied that Baxter engaged in identical conduct in its dealings with NSW, WA, SA and QLD throughout the 1990s and early 2000s. It was put to him that he had said the opposite in a letter written to ACCC on 7 April 2004 (Exhibit E). In response to this, Mr Lee said that he was discussing Baxter's ethics in that letter. He then clarified what he meant by "not identical" and although he agreed that in each tender there was at least one bundled and one item-by-item offer, he said that each contract was ultimately formulated in post-tender negotiations, which in his view, were different in each State. I found this body of evidence from Mr Lee to be most unsatisfactory. Plainly he was aware that Baxter had the same structure in all the tenders in question. In this body of evidence Mr Lee was attempting to be deliberately argumentative and to avoid a plain and straightforward answer.

465 Mr Lee denied that Baxter was the only company that could bid for all products across the range required by each State. He was then reminded of the evidence he had given about WA in the s 155 hearing where he agreed that Baxter was the only company who could supply all IV products. Accordingly, he clarified his answer by stating that there were competitors for each category, but not every code of product. It was far from clear, however, that during the 1990s Mr Lee and others at Baxter did not have legitimate grounds to consider that B. Braun, at least, may at any time have the capacity to import sterile fluids.

466 Mr Lee agreed that Baxter regarded the long term bundled offer as being in its best interest and that this offer was made as attractive as possible. He denied, however, trying to make the "cherry pick" offer as unattractive as possible. Baxter had to comply with the tender request, which was to give prices for each item and then alternative bids.

467 After being cross-examined at length in relation to Baxter's purpose in general, Mr Lee was taken to specific marketing strategy and company documents. Ultimately, it is my view that those documents speak for themselves, and Mr Lee's explanations for very telling phrases within them are largely questionable, and at times unreasonable and not to be relied upon.

468 The first of these documents was a Capital Project Approval dated 1 April 1993 for a new steriliser (Exhibit G). It contained a statement that patient growth in dialysis solutions for 1992 and 1993 would be 16.6 per cent, and further stated that:

> *This growth in patients is for two reasons: 1. the recovery of competitor patients by the strategy of bundling dialysis solutions with long term I.V. solutions contracts in the various states.*

Quite clearly this refers to a strategy. It reflects a strategy on Baxter's part which the evidence otherwise supports.

469 Whilst Mr Lee at first suggested that this document did not have any input from the marketing department, he ultimately conceded that predictions concerning sales volume could only have come from there. Accordingly, although Mr Lee maintained that Baxter never had such a bundling strategy, he conceded that someone in the marketing department must have held the mistaken belief that it did. He explained that "bundling" must have been that person's terminology for describing the fact that IV and PD were on the same contract in NSW. I reject this evidence of Mr Lee.

470 In another Capital Project Approval for a steriliser dated 30 April 1998, under the heading "Key strategies to maintaining market position and growth" were the words: "Move from price to cost", "Build competitive barriers", "Leverage products" and "Incentivise customer loyalty" (page 1-00188). Mr Lee approved this document (Exhibit H). Mr Lee denied that "Build competitive barriers" and "Leverage products" referred to bundling IV and PD, and denied that "Incentivise customer loyalty" referred to providing APD machines to hospitals free of charge. Instead, he explained that "building competitive barriers" referred to Baxter's "100 per cent service level, our homecare division", and that "incentivise" referred to the programs that Baxter has developed in the industry. As to "leveraging products", Mr Lee said that it referred to the introduction of new products, and the provision of the IV giving sets that go with the IV fluids. It is at this point that I can note that a pattern was emerging in Mr Lee's evidence whereby he would explain away clear words of Baxter documents, even where he had no plausible explanation to offer. These explanations I find to be unsatisfactory and not to be relied upon.

471 In Baxter's "Australia 1999 Budget", which Mr Lee approved and sent to the US parent company (Confidential Exhibit J), were the words "contracts" and "bundling" in a "Baxter strategies" box on page 12 of the document (1-00204). In Mr Lee's view, "contracts" referred to all of Baxter's contracts, and that bundling, although usually meaning, "if you don't buy this, you're not going to get that", referred to Baxter's total product portfolio, and not bundling IV with PD. As to "lock up PD

prices and volume" (1-00213), Mr Lee agreed that this was Baxter's strategy, but said that volume discounts were utilised to achieve this as opposed to bundling. He did, however, concede that Baxter's renal business, particularly its high market share and profit in the PD market was under threat, this was reinforced when he agreed, by reference to Baxter's 1999 marketing plan (Exhibit K), that Baxter did consider Fresenius Medical Care's potential to bundle IV, renal and nutrition production as a competitive threat. Despite the concessions, it was Mr Lee's explanation of "bundling of pumps with needle-less systems to leverage and protect needle-less business" in Exhibit K that revealed most how unreliable his evidence in this area really was. In relation to those words, he suggested that since hospitals wanted to switch to needle-less systems to prevent needle-stick injury, but found the price of pumps unaffordable, Baxter built the cost of the pumps into the cost of the ancillaries. He then said that the word "protect" was a reference to protecting users from needle-stick injuries. The subsequent exchange between Mr Rushton and Mr Lee was as follows:

> *Q. Do you think the word "protect" might be a reference to protection from needle-stick injury, do you?*
> *A. Yeah, protect the needle-less system. One of the real issues that the government has is ---*
>
> *Q. No, please, are you suggesting the word "protect" is a reference to protecting users of these products from needle-stick injuries?*
> *A. Yes.*
>
> *Q. Is that a serious answer?*
> *A. Well, it's a very small part of the market.*
>
> *Q. Is that a serious answer?*
> *A. Yes.*

I am driven to say that this response verges on the ridiculous, and this is demonstrated by the explanations given by other witnesses. At this point, Mr Lee was simply attempting to offer explanations that did not prejudice Baxter's position, even if they were not true. Unfortunately, I am compelled to say that it appeared to me that Mr Lee appreciated this at the time of giving his evidence. Mr Lee had a different explanation for the word "protect" in relation to needle-less systems shortly after the above evidence.

472 Another document (1-00328) suggested that the phrase used "continue to tie up State contracts leveraged with other sterile fluid products", was an action plan in response to the emergence of Fresenius as a threat in the PD market. Mr Lee denied that Baxter had such a strategy, and suggested that it was directed towards maintaining volume. Ultimately though, he did concede that the person who wrote the document was purporting to suggest that Baxter had this strategy. His explanation as to how this came about when Baxter, he says, did not have such a strategy, was inadequate and unconvincing.

473 The word "bundling" under the heading "strategy in the Baxter Australia Budget 2001 (Confidential Exhibit L) (see pages 4-5), was not a reference to a strategy of bundling IV with PD according to Mr Lee. On the second last page of the document where "monitor Fresenius trials to ensure they remain within State contracts" was listed as an initiative. He denied that the purpose of this was to ensure that Fresenius did not become a competitive threat by supplying above the 5 to 10 per cent threshold. Rather, he said that it was because Baxter had also invested $3 million into the program. As to the question of monitoring, Mr Lee said that Baxter employees did monitor patients to see which system was better and to resolve clinical issues, but he said that he did not think that Baxter employees monitored patients to ensure compliance with the State contracts (apart from the monitoring conducted through the CMC). When shown a field compliance form, which he denied ever seeing such a document (Exhibit M), he agreed that Baxter had a system of monitoring gains and losses in patients, but denied that this had anything to do with monitoring market shares in PD and

ensuring that Gambro and Fresenius did not breach the 10 per cent limit. I reject this evidence. The balance of the evidence on this issue reveals that Baxter was monitoring hospitals, carefully.

474 In the Baxter Budget 2002, which Mr Lee approved, (Confidential Exhibit N), there appears to be a change in strategy, with the words, "attempt to unbundle contracts" (2-00231). Mr Lee said that this referred to the ACCC's attempts to have Baxter unbundle its contracts and that the word "bundling" was a reference to contracts with private hospitals, and not to the bundling of IV with PD in State contracts. The difficulty with this evidence was apparent when Mr Lee was forced to admit that there were no IV products sold to private hospitals as a bundle. He also again denied that Baxter monitored patients to ensure that Gambro and Fresenius products were not used on more than 10 per cent of patients. I reject this evidence.

475 In a quarterly sales and marketing meeting document (Exhibit O) the phrase "Monitor compliance to NSW Fluid Contract" was said by Mr Lee not to mean that Baxter monitored compliance by NSW with the 1998 Agreement; rather it referred to the CMC. As to the words "Improve accuracy of patient monitoring" under the heading "Strategy", Mr Lee he said that this was about seeing which patients were on which Baxter PD product to assist the manufacturing division, as opposed to checking who was on a non-Baxter product. I reject this evidence.

476 Mr Lee was also shown the 2004 Budget Presentation Australia (Confidential Exhibit Q), and he agreed with a statement within it that suggested that increasing market pressure in the PD market had forced Baxter to sacrifice part of its margin to protect market share (p2-00450). Mr Lee was also shown Baxter's 2004 Strategic Plan (Confidential Exhibit R), and he agreed that in both documents there was no reference to the strategy of bundling. It was then put to Mr Lee a number of times that this indicated that Baxter had changed its strategy between 2002 and 2004 so that it no longer bundled products. Mr Lee, however, disagreed and said that "nothing's changed in the market place" and that Baxter still had bundled contracts. He was however forced to concede that the 2003 NSW and Victoria contract was on an unbundled non-exclusive basis and that the reason for shying away from bundling was the "ACCC issue".

477 Mr Lee was also cross-examined in relation to the methodology utilised by Baxter for determining its "cherry pick" prices. From the outset, although Mr Lee agreed that the "cherry pick" prices exceeded what the States were currently paying, he continued to affirm that Baxter calculated those prices with regard to the risk of losing volume in other states when those contracts came up for renewal. He was then challenged with the proposition that Baxter had no such fear in NSW, because there was no risk of losing volume after the closure of Abbott's plant in 1993. At first, Mr Lee maintained (unsatisfactorily) that the prices were calculated in the same way that they had been under the previous contract and that in reality, the 1998 NSW tender was not serious, because Baxter was engaging in private negotiations with NSW. Ultimately, however, Mr Lee was forced to make a number of concessions. He conceded that the item-by-item prices were calculated using the hospital list prices (prices which they gave to private hospitals), that the States had never purchased at list prices, and that as a result it was not the offer Baxter intended to be taken up. Nevertheless, he denied that the item-by-item prices were utilised to drive NSW to accept the bundled offer, and said that rather, the offer was made to comply with the tender. At this point, Ms Coy's evidence that the purpose of the "cherry pick" prices was to "demonstrate value" to a State that the bundled offer represented should be recalled.

478 There was no satisfactory evidence (beyond assertion) as to how the "cherry pick" prices were set. No doubt, to a degree, such higher prices would lessen the blow of a loss of volume. But I reject the evidence of Mr Lee and others that that is how they were set. There was no documentary support for that. They were set at a level to be taken seriously as a credible alternative and to maximise the apparent benefit for the State in taking the bundle: to demonstrate the value of the bundle.

479 In the light of the fact that the volume discount represented the difference between the "cherry pick" prices which, as Mr Lee said at one point, "weren't really a serious offer", and the bundled

price, Mr Lee denied that there really was no discount and that Baxter gave nothing away. He remained adamant that the "cherry pick" price accounted for the risk of not obtaining the whole volume.

480 Whilst much of Mr Lee's oral evidence was less than satisfactory, one aspect must, in fairness to him, be noted. There was a lack of material upon which to found a conclusion that Mr Lee, or others at Baxter, knew in 1998 that B. Braun would not obtain TGA approval for its Malaysian factory.

481 Mr Lee agreed that if any of the States had chosen the "cherry pick" prices, other companies would have had an incentive to enter the sterile fluids market during or at the end of the five years.

482 The evidence concerning the SA transaction illuminates considerably Baxter's conduct. After being shown the email from Mr Battersby to Mr Browne dated 5 December 2000 (Exhibit S), Mr Lee agreed that in his experience, Baxter would have still offered volume discounts to a State, such as SA, that agreed to take all its IV fluids, but not its PD fluids, exclusively from Baxter. Then, after being shown an email from Mr Wallace to the Strategic Procurement Unit of South Australia dated 8 December 2000 (Exhibit T), he agreed that it appeared that Baxter was threatening SA with "cherry pick" prices unless it took its PD as well as its IV from Baxter. However, he tried to deny that this offer left SA with no alternative. Finally, after being shown an email from Mr Battersby to Mr Browne dated 5 February 2001 (Exhibit U), that referred to concerns under the Act, Mr Lee accepted that if Baxter was effectively giving away its PD fluids, then it was impossible for Gambro and Fresenius to compete. Ultimately when driven to this in cross examination Mr Lee recognised that the bundling and the place of the "cherry pick" alternative as credible made the bids of Gambro and Fresenius for PD unacceptable to the States behaving rationally. I have no doubt that Mr Lee was aware of this contemporaneously and that it was his and Baxter's purpose in the structure of the offers made during the period 1998 to 2001.

483 Mr Lee was shown a letter from himself to Health Services Purchasing and Logistics Group in QLD dated 26 August 1997 (Exhibit W), and he agreed that Baxter was undertaking monitoring in QLD. Nevertheless, he denied that the monitoring in QLD (or other States for that matter) was for the purpose of checking compliance with the contract. Rather, he said it was undertaken for the Renal Society. This is highly improbable, given the evidence of other witnesses. I do not accept this evidence.

484 Mr Lee agreed with Mr Rushton that Baxter could not import products from overseas facilities and sell them at prices competitive with the products produced in the Toongabbie facility. (This evidence, however, should be examined with some care. That Baxter could not import such products does not mean that others could not do so. The effectiveness of import competition depends upon the economic factors attending the posited importation. This would include (but not be limited to) the location and cost structure of the foreign factory, the distance, methods and cost of transport and available distribution networks. Mr Crawford's evidence made clear that a degree of potential import competition existed in relation to sterile fluids.)

485 Mr Lee was not an unintelligent man. He did his best on many occasions to not answer questions that were contrary to the interests of Baxter. In some circumstances he had, and knew he had, no answer to the questions, and this provoked non-responsive wordy assertions. I approach his evidence with great caution. Some of his answers in relation to strategy were more than difficult to accept. I also do not accept his evidence as truthful in a number of respects.

Mr Peter Leyland

486 Mr Leyland who was the Vice President, Global Therapeutic Marketing, Competitive Intelligence in the Renal Division of Baxter International Inc ("BI Inc") gave evidence. He had held various positions within the Baxter group of companies since 1988, largely in the UK. His current role involves strategic business analysis, which involves four areas, namely: sales activities and

product support, life cycle management, competitors' behaviour and activities in the future, and Baxter's long-term corporate strategy formulation.

487 In his affidavit, Mr Leyland noted that Baxter manufactures both PD and HD products, and that Baxter pioneered PD treatment in the 1970s. The Renal Division of BI Inc operates in all major regions worldwide and in 2002 had sales of USD1.7 billion The Medication Delivery business, which includes IV and PN solutions achieved sales of USD 3.3 billion in 2002. The BioScience business generated sales of USD 3.1 billion in 2002.

488 In the early 1990s, Mr Leyland said that he observed a trend towards bundled supply of IV and PD at the request of customers. The reasons behind this were attempts by hospital administrators to improve prices and achieve efficiencies. By 1994 and 1995, however, pressure exerted by clinicians for greater clinical choice resulted in a winding back to unbundled supply. Over the period 1998-2003, Mr Leyland says that he noticed a new phenomenon whereby customers band together to purchase one line of products, meaning that suppliers bid for an "all or nothing" contract.

489 Mr Leyland stated that he understood that the ACCC was alleging that Baxter engaged in a strategy of linking IV pricing to PD pricing and offered very deep discounts on IV prices to force customers to purchase Baxter's PD products and thereby exclude Baxter's competitors. In response to this, Mr Leyland said that such a strategy was not one that had occurred to him and that he had not encountered such a strategy in the course of his employment with BI Inc.

490 In cross-examination, Mr Leyland agreed that paragraph [49] of his affidavit was the sum total of the knowledge he had been given about this case. He obtained his understanding from Baxter's lawyers. Mr Rushton handed up a document (Exhibit FF) and asked him to confirm that it was a summary of the case put by the ACCC. He agreed that it was consistent with his understanding of the case.

491 Mr Leyland agreed that he understood competition principles and bundling. He then said that this was not a case of bundling because the premise upon which it is based, namely that Baxter has a monopoly in IV is not true. He suggested that other companies like B. Braun are capable of entering the market, and that there was a requirement upon Baxter to ensure that the capacity of the Toongabbie plant was utilised.

492 Mr Leyland said that on the assumption that no other company could supply the IV market, and that Baxter was a monopolist, Mr Leyland then agreed that this might mean logically that the "cherry pick" offer was directed towards driving the state to the bundled offer. As to how a PD company could compete, Mr Leyland suggested that a "cherry pick" price at 161 per cent would provide sufficient incentive for entry.

493 Mr Leyland's evidence was ultimately of little assistance.

Mr Stephen Garchow

494 Mr Garchow was the Vice President of Global Marketing Infusion Systems for Baxter and had held that position since 2000. Between 1994 and 2000, however, Mr Garchow was the renal business unit manager in Australia. Mr Garchow was not available for cross-examination. The applicant had no objection to such parts of paragraphs [1] to [20] of his affidavit being read without cross-examination, subject to the weight that should be attached to his affidavit on the basis that it had not been tested.

495 Mr Garchow's evidence was directed primarily to his role in the setting of prices for PD products. He gave evidence that it was a primary concern of his to maintain PD market share and revenue growth by offering the most attractive pricing for PD products. He recalled that when he arrived in Australia in 1994 PD pricing was in his view relatively high compared to other international markets. Mr Garchow had little to do with the formulation of pricing of other products.

He did not take into account the pricing of other products in setting the price for PD products. He had no recollection of any discussion in which he or others discussed any strategy of linking IV and PD products. One matter of particular relevance in his affidavit was that Mr Garchow recalled a general concern expressed by Baxter employees, which he shared, that B. Braun would bid on major IV codes which it then had registered, in or about 1998.

Mr Thomas Russell

496 Mr Russell was the Chief Executive Officer of Baxter Health Care Limited in New Zealand. He reported to the Managing Director of Baxter. His evidence concerned the importation and distribution of products in New Zealand. It is unnecessary for that reason to deal with his evidence beyond the recognition that the market for PD fluids in New Zealand is competitive and that Baxter's ability to import from Australia gave it a competitive edge both due to shipping costs and shipping speed from Australia.

The Expert Economic Evidence

497 The ACCC led expert economic evidence from Professor Barry Nalebuff, who was the Milton Steinbach Professor of Management at Yale University, and Ms Rhonda Smith, who was a senior lecturer in the Economics Department at the University of Melbourne. Professor Nalebuff's academic focus and area of expertise concerns the practice of bundling, and Mrs Smith, who is a former Commissioner of the ACCC, has extensive experience with market definition and determining market power. The ACCC also led evidence in relation to costs and revenues from Ms Tamara Lindsay, who was an accountant. Baxter led expert economic evidence from Mr Henry Ergas, who was the principal of Network Economics Consulting Group. Mr Ergas has extensive experience in advising on the economics of competition law issues in Australia.

Market definition

498 Both Mrs Smith and Mr Ergas addressed the definition of the relevant markets. Both employed a purposive approach to market definition. Mrs Smith said that:

> *The market definition must facilitate analysis of the competitive process. It is necessary to define a market in relation to the particular issue to be examined so that it provides the best possible representation of the competition issues.*

Whilst Mr Ergas fully agreed with this particular framework, he disagreed with significant aspects of its application in Mrs Smith's report. In particular, he analysed Mrs Smith's views as to geographic factors and supply-side substitutability and disputed her conclusion under the purposive approach.

499 Mrs Smith's methodology took account of four dimensions: product, geography, the functional, and the temporal. The first two were defined by demand-side and supply-side substitutability, being the extent to which when prices increase, consumers will switch to another product and producers will alter their production mix to produce more of that product. Using this definition, and given the significant functional differences between PD fluids and HD, LVP, IS and PN fluids, Mrs Smith expressed the view that the demand or supply substitutability between PD fluids and those other fluids was very low. She also suggested that demand substitutability between LVP, IS and PN fluids was low, and that supply-side substitutability was small, assuming low technological flexibility.

500 Bearing in mind this low product substitutability, Mrs Smith considered the geographic dimension, which was integral to her argument that there were Australia-wide markets for LVP, IS and PN fluids, and only State-based markets for PD fluids. The thrust of her argument vis-à-vis PD products was that given the large number of patients who receive PD treatment at home, buyers only purchase from firms that have the requisite State-based distribution network within their State. Thus, the PD market is defined by State-based geography. By contrast, the sterile fluids markets are defined

by national geography, because each utilises a centralised, as opposed to State-based distribution network.

501 Mr Ergas, who was informed by a similar methodology, was of the view that the relevant markets should be wider than those proposed by Mrs Smith. Instead of separate national LVP, IS and PN fluids markets, Mr Ergas suggested that there should be one national sterile fluids market (which combines LVP, IS and PN). His argument was based upon the views of Mr Lee and Mr Crawford (of B. Braun), who said that there is scope for supply-side substitution between LVP and IS, and LVP and PN production. (See the affidavit of Mr Lee at paragraph [6.33] and the affidavit of Mr Crawford at paragraphs [73] to [74].) Similarly, instead of state-based PD markets, Mr Ergas argued that there is a national PD market, because PD suppliers appear to operate on a national basis with centralised manufacturing facilities. This assessment of PD production gave less weight to distribution.

502 Mr Ergas also proposed a more extreme application of the "purposive" approach to market definition by suggesting that the relevant market for analysing the conduct at issue is the *joint* supply of sterile fluids: that is, LVP and PN fluids and IS and PD fluids. His argument in this respect was that since the ACCC's experts had claimed that Baxter's conduct was directed in part at least towards protecting its position in sterile fluids, Professor Nalebuff must have had in mind a long-run equilibrium with competitors competing in both sterile fluids and PD (Professor Nalebuff certainly did not disagree in cross-examination with the proposition that Baxter wanted to stop a competitor setting up a local PD manufacture and then moving into LVP, IS and PNs. Accordingly, the truly relevant market was said to be a joint market of PD and sterile fluids, because "such a wider approach best captures the true field of rivalry between firms in market equilibrium". Although Mrs Smith disagreed with this view in reply, she did note that precise market definition does not seem to be critical in analysing the alleged conduct in this case.

Market Power

503 In relation to whether Baxter had a substantial degree of market power in the sterile fluid(s) market(s), the debate between the experts centred upon the extent of the SPAs' countervailing power and Baxter's ability to recoup its profit sacrifices (if indeed, that was even necessary or, if indeed, there were any). Mr Ergas propounded the view that the strength of SPAs' bargaining power negated any market power that Baxter would have otherwise had, whereas Mrs Smith and Professor Nalebuff were sceptical of this view. What might be said to be the usual indicia of market power market concentration, lack of import substitution, product differentiation, barriers to entry/exit and long term agreements – were largely not contested by Mr Ergas.

504 In that respect, Mrs Smith noted that these indicia all pointed to the existence of market power. Baxter's share of the LVP, IS and PN market was high, and import competition posed little (at least short term) competitive constraint due to high transport costs. Structural barriers to entry were high and took the form of regulatory controls and standards, high capital costs and the scale of business require so that effective competition with the incumbent would be facilitated. Mrs Smith did concede in cross-examination that "all or nothing" tenders soften the impact of high incumbent market share, and allow entrants the opportunity to quickly gain market share.

505 Mr Ergas' main argument against a finding that Baxter had a substantial degree of market power was his belief that "Smith under-estimates the power of major buyers, most notably State Governments". In particular he noted that SPAs have:

(a) the ability to define the nature and mechanics of the competitive process;
(b) the ability to sponsor or more generally facilitate competing entry; and
(c) the consequent ability to impose major losses on Baxter.

Support for his view is said to be found in the economic literature relating to auctions and bargaining

theory: see Steuer, R (2000) "Customer-Instigated Exclusive Dealing" 68 *Antitrust Law Journal* 239-257. (At this point the negotiations in 1992 in New South Wales should be recalled.) I have already commented earlier about the real role for States in these respects.

506 In Mr Ergas' view, the ability to define the competitive process is not insignificant, because when a First Price Sealed Auction (Tender) is chosen the prices faced by a buyer are reduced for three reasons. First, if there are multiple bidders, and sellers are risk averse (which arguably they will be in the presence of high fixed costs) lower bids are more likely to win. As a result, lower prices are obtained than under price leader oligopoly. Secondly, sellers are unlikely to collude because cheating is very costly (i.e. it is tempting for a seller to bid just below the collusive bid so as to capture all, instead of a share, of the same profit). Thirdly, assuming asymmetric costs, more bidders are encouraged to enter the tender because incumbents are not expected to bid too low.

507 Furthermore, Mr Ergas argued that in procurement auctions, bundling makes supplier bids more likely to reflect economies of scope, because suppliers need to be sure of a commitment to a certain volume before such a bid can be put in. Indeed, he also noted that even Professor Nalebuff has said that "bundle against bundle is ferocious competition". (See Nalebuff, B (2000) "Competing against bundles" in *Incentives, Organisation, and Public Economics*; Peter Hammond & Gareth Myles, eds., Oxford University Press.) In examination-in-chief Mr Ergas noted that SPAs had the ability to inflict significant losses upon Baxter due to Baxter's high sunk investment in production facilities. Thus, in this light, a finding that Baxter had substantial market power requires a demonstration that the SPAs' options "are not sufficient to prevent Baxter from retaining the unilateral ability to persistently set price above long run costs". In Mr Ergas' view, their options were sufficient.

508 On the other hand, Mrs Smith argued that the SPAs' inability to negotiate more than a 10 per cent allowance for non-Baxter PD and no less than a three to five year contract was indicative of their low countervailing power. Furthermore, she noted that in the auction context, multiple bidders are required for low prices (with Baxter's monopoly, this is probably not the case here) and that the SPAs are limited by financial constraints and information asymmetries. Professor Nalebuff, drawing upon his experience of auctions and bargaining in both the United States and New Zealand, also made the point that a successful auction requires bidders to turn up (and he gave examples of unsuccessful government auctions where this failed to occur). He then argued that since there is effectively only one bidder for sterile fluids in Australia, the auction and bargaining literature therefore does not apply.

509 Undoubtedly this issue of countervailing power is very important to the issue of market power here. Clearly there are strong arguments either way. Ultimately, the resolution of this issue relies upon the evidence in the case. The extent to which the SPAs can create a process that prevents Baxter from setting prohibitive prices when it is unable to sell in the way that it prefers will be important. On the evidence, particularly that in respect of NSW and QLD the reality of the power of the States was present in bargaining. There was, to a degree, a constraining power present: the threat of foreign sponsorship to local sunk capital cost. Further, the State had control of the bidding mechanism. They could have prohibited the bundling of PD with sterile fluids. This would have then placed Baxter in the position of forcing a bundle upon the States, against their wishes. This did not happen in any State.

510 There was also a disagreement over profit sacrifice recoupment. Mr Ergas argued that exclusionary conduct requires market power so that any profits sacrificed for the exclusionary motive can be recouped. Furthermore, he said that if the conduct is exclusionary, the incremental price of a bundle is below the avoidable cost of the marginal product, which means there must be a profit sacrifice. However, since neither Professor Nalebuff nor Mrs Smith had provided any evidence that Baxter could recoup any profit sacrifices that it allegedly made, Mr Ergas argued that any claim that Baxter had substantial market power had not been made out.

511 Professor Nalebuff responded to this argument by asserting that market power was not necessary

for exclusionary conduct, because it can be used to gain market power. However, he did concede that "without market power, exclusionary bundling has no teeth". He also said that recoupment was not a requirement of market power, because there is not necessarily a profit sacrifice exclusionary bundling. Rather, exclusionary bundling relies upon a threat to overcharge a single good A if bundle A+B is not purchased. If this threat is believed, the conduct is costless (and there is nothing to recoup). Naturally, if the threat is not believed, there will be a profit sacrifice, because the seller essentially threatened to sacrifice profit to compel the buyer to choose the bundle. At the very least, therefore, there is a risk of profit sacrifice.

Testing taking advantage and the effect of the conduct

512 A large part of the economic expert evidence of Professor Nalebuff and Mr Ergas concerned the development of the theories and tests which sought to establish whether Baxter's conduct amounted to taking advantage of market power, or had the effect of lessening competition. It was in relation to this that the more substantial disagreements emerged. These differences were in the main debated between Professor Nalebuff and Mr Ergas, and not only did they disagree upon the appropriate model that should be used to test Baxter's conduct, they also disagreed over the data and costs that should be included in the model that was eventually tested. Ultimately, whilst I find the theories put forward helpful in parts, this debate eventually highlighted some important features and limitations that are inherent in both economic theory and modelling applied in a case such as this.

513 It may be said that relatively simple economic theories which rest upon simple assumptions conforming broadly to commonly observable human conduct often have the most explanatory power, because they are readily comprehensible (at least at an intuitive level). However, to rely confidently upon the models generated by these theories, in court, as an *accurate* representation of reality, requires the underlying assumptions and theory to be truly representative of the market described. Unfortunately, accuracy usually necessitates complexity both within the underlying assumptions and the variables comprising the model, which may mean that the results are either incalculable or incomprehensible.

514 The models that have been presented in this case exhibit features that I have just described. As I will go on to explain, the model put forward by Professor Nalebuff of exclusionary bundling (which is similar to the horizontal "price squeeze" test of Mr Ergas) is one that is comprehensible and intuitive because it is relatively simple. However, although it does provide useful insights, I cannot rely upon it confidently as an accurate representation of Baxter's conduct within the relevant markets, because, as Mr Ergas correctly pointed out, it fails to take into account a key element of an auction process, namely uncertainty and because of the limitations on the accuracy of the base data. As a result, whilst I can use the model as an indicator (where the correct data is used and the model's result is correctly computed), it cannot ultimately provide the mathematical answer to the question as to whether Baxter did take advantage of its market power. Further, as a model it cannot take the place of the application of the words of the statute in both the notion of "taking advantage of" and the relevant purpose, and of the necessary fact finding process based on evidence (human and documentary) placed before the Court.

515 The model put forward by Professor Nalebuff centred upon the notion of bundling, which he defined as the "practice of selling two (or more) products together; the products may be available only as a bundle or, if available separately, are offered at a discount relative to their individual prices". On this view the practice is not always anti-competitive, because sometimes, bundling can generate efficiencies through production or distribution cost savings, double marginalisation or increased quality. However, when these motives are absent, the bundling is probably for an exclusionary purpose.

516 Professor Nalebuff defined *exclusionary* bundling as follows:

> *exclusionary bundling arises when a firm has market power in product A and faces*

> *competition in product B. It engages in exclusionary bundling when the incremental price for an A-B bundle over A alone is less than the avoidable costs of B. ([43] of Exhibit BN1)*

517 He then explained that there are at least three kinds of exclusionary bundling; namely, foreclosure, tied sales and predation. Foreclosure, in the form of bundling, is summarised by the *Eli Lilly Case* 427 FSupp 1089; and on appeal 575 F2d 1056, where Eli Lilly bundled products in which it had market power and goods in which it did not by giving rebates if a certain quantity of products were bought. By reason of the effective prices of the products in question the rebates created an effective discount of 20 per cent for the product in respect of which there was otherwise real competition, this being a discount with which no other supplier could compete. This foreclosed the market for this product. Exclusionary bundling results in a "de facto tie" where a firm only offers A at a low price when B is also purchased – otherwise, a high price for A is charged. Where the price of the bundle is less than the price of A, or the incremental price of the bundle is less than the avoidable cost of B, all rational buyers will opt for the bundle, which will exclude other equally efficient sellers from the market. Finally, exclusionary bundling can also take the form of predatory pricing where in a bundle of A and B, the monopoly profit of A is used to subsidise the price of B for the purpose of eliminating competitors.

518 As a caveat, Professor Nalebuff did note that where bundling allows the generation of scale efficiency and scope efficiency, the cost savings may justify some level of cost saving, although probably not at the level offered by Baxter. Moreover, if producing an A+B bundle costs less than producing A and B separately, a firm would be justified in granting an incremental price for the bundle that is less the *individual* avoidable cost of B (so long as it is not below the *incremental* avoidable cost of B). Similarly, Mrs Smith noted that pricing below avoidable cost in a bundled situation can be rational under competitive conditions if the firm is clearing stock, failed to realise its price was below cost or where the cost of exit and re-entry is higher than staying in the market. However, outside of these purposes, exclusionary bundling is only rational if it has an exclusionary purpose.

519 Professor Nalebuff then made 4 assumptions:

1. Baxter has a substantial degree of power in LVP, IS and PN markets;
2. PD is a competitive market;
3. LVP, IS, PN and PD are not substitutes;
4. Demand is inelastic to a point (until import substitution becomes feasible).

520 In this light, he argued that "in essence the State purchasing authorities had but one choice to make: whether or not to buy PD products from Baxter", given that from the SPAs' point of view, Baxter was the only supplier of LVP, IS and PN fluids. Accordingly, Professor Nalebuff said that Baxter's conduct potentially fell within the category of exclusionary bundling, because while it was offering its monopoly products at high item-by-item prices, it was offering them bundled with PD for a significantly lower price. To test whether this was the case, he suggested that all that is required is an analysis of whether the effective PD price (i.e. the price for PD less the bundle discount on all products) is less than the avoidable cost of producing PD.

521 Mrs Smith did a similar analysis, if I may say so without the slightest intended disrespect, in a less theoretical way.

522 Mr Ergas, in his first report, agreed that a price squeeze test would be relevant to the conduct of an incumbent who controlled an essential input A to final good B, where that incumbent was selling A to other producers and B to final consumers, because the sales of A are a "sure thing". That test is essentially identical to Professor Nalebuff's test, because it says that there is a price squeeze when the additional revenue from selling B (not just A) is less than the avoidable cost of B. This would mean that if Baxter's sales of LVP, PN and IS fluids were assured, the "horizontal price squeeze" test would

be relevant to a finding of taking advantage under s 46 and exclusionary conduct under s 47, since firms cannot act in an exclusionary fashion under competitive conditions.

523 By contrast, if the sales of A (the monopoly good) were not 100 per cent sure, Mr Ergas said that the price squeeze test would be inappropriate if unadjusted for uncertainty. His argument to this end was that if the sales of A are treated as sure when they are not, the test will overstate the "unbundled" revenues from A and therefore overstate any implied discount upon B, which would very likely lead to a finding of a price squeeze when there is none. Since Baxter was faced with a tender, it could not have been sure of the tender result or the prices and quantities that would ultimately prevail. Hence Mr Ergas argued that the sale quantity of LVP, IS and PN fluids was not assured, and from Baxter's point of view, it did not give up the unbundled revenue discounted for the probability of each offer being accepted. Accordingly, Mr Ergas proposed that an appropriate price squeeze test would be one that compared expected incremental bundled revenue with expected avoidable cost of PD, because this would be how a rational firm in Baxter's position would make its decision as to how to structure its tender.

524 Unfortunately, as Mr Ergas said, "given the complexity of the computation involved, such a model (incorporating uncertainty in auctions) currently does not exist in the literature". Nevertheless, Mr Ergas did provide a worked example to illustrate his point. What he did was to define the probabilities for each of Baxter's bundled and unbundled offers being accepted, and to then calculate the expected revenue from that bid. He then sought to extract the incremental revenue of the bundle from this result. Professor Nalebuff said that " [Mr Ergas] cannot provide a logical explanation for this calculation". With respect, I tend to agree. It might be thought that one would compare the expected revenue from an offer structure containing a bundled bid to that which does not offer a bundled bid. Then it might be determined whether Baxter was engaging in a profit sacrifice by offering the bundle.

525 Professor Nalebuff, in reply, presented his own version of a model that, he said, properly considered uncertainty. He performed a cost-benefit analysis in relation to offering the bundle by looking at what those persons (who would purchase the bundle) would do if they could not purchase the bundle.

526 Professor Nalebuff's main critique of Mr Ergas' position that there was no need to consider uncertainty and to this end he said the following:

> *As there have been no qualified bids for sterile fluids over the last decade in any SPA tender, I believe that the probability Baxter would have won the sterile fluids contract should be near one ([131] of Exhibit BN2).*

527 That is, Professor Nalebuff believed that Baxter would have been assured of 100 per cent volume for sterile fluids (excluding PD) at its "cherry pick" prices if the bundled bid had been rejected. Moreover, in examination-in-chief, he suggested that if the bundle leads to an exclusionary result, there is no chance the buyer will not take the bundled offer.

528 The difficulty with this approach is that if this is what Baxter expected the need for putting in an unbundled bid is unclear. From Baxter's perspective, any number of tender results were possible. It is difficult to see why, from Baxter's perspective, an SPA may not have valued clinical choice highly and refused the bundle, whereupon it might have forced Baxter to face the reality of requiring its "cherry pick" prices and possibly lowering them, perhaps concerned by the possibility of encouraging another supplier to set up in Australia (the item-by-item contract was only 12 months), or even purchasing some of its sterile fluids from B. Braun. Furthermore, it is even possible that a rival could have undercut Baxter's bid, which is a point Professor Nalebuff conceded. Indeed Mr Ergas in his reply said:

> *As Baxter does not know its opponents' costs or its opponents' bids, it does not seem*

plausible that it would assign probability zero to the event described above. ([157] of Exhibit HE2)

529 Accordingly, any model that seeks to properly represent the relevant market accurately, in my view, would have to account for some uncertainty of the tender process.

530 This discussion, of course, raises another important point of contention between the experts, namely, expectations. Quite clearly, the above analysis relies upon the *seller's* expectations being relevant, which is a state of affairs for which Mr Ergas contended. Professor Nalebuff however vehemently disagreed, and argued that it is the buyer's expectations that matter, because "it's the buyer who decides which bid will win". If this is true, then building uncertainty into the model is not required (since the buyer knows what it will decide when confronted with bids), and Professor Nalebuff's test would then be an appropriate indicator of whether Baxter's conduct was exclusionary for the purpose of s 46 or s 47.

531 Professor Nalebuff's view seemed to rest on two grounds. First, he said that since there is no reason to believe the item-by-item bid is optimal, the right comparison from the seller's perspective could not be with that bid. Secondly, if the seller has correct expectations of volume, but the buyer does not, the seller can propose a discount that looks exclusionary to the buyer, although it is not to the seller. In that situation, it is what the buyer expects that determines whether the conduct is exclusionary, or if it has that effect. However, in cross-examination, Professor Nalebuff did concede that where the seller's purpose is relevant to making out anti-competitive conduct, one needs to look at the seller's expectations, because while it is possible the conduct has exclusionary effect, it might not be intended to be anti-competitive because the seller did not expect this.

532 Mr Ergas, under cross-examination, confirmed that if the conduct at issue is Baxter's then Baxter's expectations are relevant, because economists are interested in what the rational purpose for a firm's conduct was. Furthermore, and this goes to what Professor Nalebuff said, Mr Ergas contended that even if the buyer had erroneous expectations (which Baxter knew) and rivals are as well informed as Baxter, they will still be able to put in a matching bid, so that what ends up mattering is not the buyer's expectation, but the seller's. In this respect, given that "take advantage" in s 46 is directed toward whether a firm could engage in the conduct under competitive conditions, the firm's "rational" purpose (which is imputed) is important. Accordingly, I agree that the seller's expectations are relevant here (and hence uncertainty should be included in the model). However, in relation to s 47, and whether there has been the effect of substantially lessening competition, I am inclined to think that the buyer's expectations are relevant, because since it is the buyer's decision that excludes competitors, the effect that a tender has on a buyer will affect competition.

533 Nevertheless, despite the critical view of Professor Nalebuff's model that Mr Ergas held, he did himself perform a horizontal price squeeze test for each of Baxter's tenders in NSW, QLD, WA and SA, so as to ascertain whether Professor Nalebuff carried out his analysis correctly. Mr Ergas' calculations mostly differed from Professor Nalebuff's. The explanation for the discrepancies largely sprang from their difference of opinion over expectations (which affected what product usage figures should be used) and as to how avoidable PD costs should be calculated.

534 Professor Nalebuff's analysis relied upon calculations performed by Ms Tamara Lindsay of Horwath Accountants. Ms Lindsay calculated the effective price of PD ("price" here is used as the total cost to the buyer) as a percentage of the unbundled price of PD for each State, utilising, the usage figures that were annexed to the contracts or proposals. In cross-examination she agreed that she had assigned a "0" usage to a number of product codes, either because the usage was unknown, or the product was new. These figures were relied upon because they represented "the expectations of the parties as to future usage at the time the offer was made".

535 As to avoidable PD costs, although Ms Lindsay used them in her calculations, Professor Nalebuff set out sources and justification for those costs in his first report. He utilised Baxter's "1997 Bills of

Material" to estimate its avoidable PD labour, material, fixed overhead and variable overhead costs, and argued that since plant cost, over the long-run, should be avoidable, depreciation should be included and set at 20 per cent of Baxter's fixed costs from its anti-dumping application. Then, using Baxter's anti-dumping application, Professor Nalebuff estimated an average cost for selling, distribution and administration equal to 57.5 per cent of production costs, and an average cost for warehousing and delivery equal to 18.5 per cent of production costs. He also estimated that receivables costs amounted to 2.3 per cent of production costs, but since this was a provisional estimate, he did not include it. Finally, Professor Nalebuff noted that in Baxter's Annual Report (2001/2002) there was a variable cost of 82.5 per cent of sales, which left a profit margin of 17.5 per cent.

536 Later, in examination-in-chief, Professor Nalebuff suggested that his approach to costs was conservative. Various debates took place in relation to costs, including the avoidable costs of marketing if PD was lost in NSW, the supply fee, research and transport, royalties paid and the costs related to the twin-Bag machine. It is unnecessary to resolve such disputes.

537 Using Ms Lindsay's results, Professor Nalebuff noted that the tender in SA had a negative incremental price for PD (namely, $385,731),which could never be above avoidable PD cost. As to NSW (Tables 4 & 5 in Exhibit BN1), the effective PD price of $2,180,528 equated to an 81 per cent discount on the unbundled PD price. Since the avoidable cost of PD in NSW amounted to 42 per cent of the unbundled price, the incremental price for PD was below avoidable cost. As to WA (Tables 6 & 7 in Exhibit BN1), the buyer faced an effective PD price of $729,981, which represented a discount of 72.8 per cent off the unbundled price. Since the avoidable cost of PD in WA amounted to 49.1 per cent of the unbundled price, the incremental price for PD was below avoidable cost. As to QLD (Tables 8 & 9 in Exhibit BN1), the buyer faced an effective PD price of $2,980,382, which represented a discount of 50.5 per cent off the unbundled price. Since avoidable cost for years one, two and three was 47.8 per cent, 54.5 per cent and 58.4 per cent respectively of the unbundled price the incremental price for PD was below avoidable cost in years two and three. Accordingly, Professor Nalebuff concluded that Baxter had engaged in exclusionary bundling in each of the states.

538 Mr Ergas, in his reply, criticised Professor Nalebuff's findings on a number of grounds. First, he argued that Professor Nalebuff had utilised usage figures which corresponded to the buyer's expectation, not the sellers. Secondly, Mr Ergas disputed Professor Nalebuff's treatment of 20 per cent of fixed cost as avoidable and criticised his reliance upon the anti-dumping application, because it only provided average total cost benchmarks. Then thirdly, he disputed the assumption of significant cost savings if the PD contract (in NSW, for example) was lost, primarily because of Baxter's evidence on this point. Accordingly, Mr Ergas performed his calculations with lower avoidable cost figures for PD. He also utilised Baxter's budgeted sales figures from 1998 and 1999 so that the sellers expectations on an *ex ante* basis could be properly taken into account although he continued to use Ms Lindsay's discount figures and prices. The end result was that Mr Ergas found a price squeeze occurring only in SA for the entire alleged period of contravention and for only two years in NSW.

539 A series of replies were then made by both Professor Nalebuff and Mr Ergas, which set off a series of amended calculations. Professor Nalebuff criticised Mr Ergas' original calculations on a number of grounds. First, he maintained that buyer expectations are more relevant, and that budget figures are therefore inappropriate. Secondly, he argued that Mr Ergas' failure to use budget figures for sterile fluids risked underestimating sterile fluids volume and that the budget figures, in any case, appeared to overestimate PD sales. There were also a number of other criticisms that Professor Nalebuff made, not to mention his assertion that when he utilised budget or actual PD sales figures, he still found a case of exclusionary bundling in all states, although this presumably relied upon his cost calculations.

540 As to costs, Professor Nalebuff said that over a five year period, fixed costs should become more avoidable, and he gave the example of Baxter's purchase of the twin-bag PD machine in 1998, which

in his view would have been avoidable if Baxter had lost the NSW PD contract. Moreover, he noted that there was still exclusionary bundling in NSW and WA when fixed costs were excluded.

541 In his second report, Mr Ergas confirmed that it is *ex ante* PD quantities that are relevant to Baxter's expectations, and that an *ex ante* approach is the only relevant one, if the test is relevant at all. However, Mr Ergas conceded, in the light of Ms Bailey's third affidavit, that the budget figures were inaccurate (because they omitted ranges of IS and PN fluids) and did not reflect Baxter's expectations (with the exception of year one). He also conceded that although he utilised Ms Lindsay's sterile fluids to minimise points of difference, there was an inconsistency in his analysis if budget figures were not also applied to sterile fluids. These same concessions were affirmed in cross-examination and indeed Mr Ergas further conceded that he does not have the requisite data for performing a proper *ex ante* test. (It is to be noted that no explanation was given as to why Baxter had apparently not sought to provide these figures to him, based, as they were, on the seller's expectations.)

542 In light of these developments, Mr Ergas was instructed to perform an *ex post* analysis utilising actual sales figures, which he said are indicative of Baxter's expectations as long as Baxter had a reasonable prior perception as to outcomes. In relation to QLD and WA, Mr Ergas found that there was no price squeeze when actual sales volumes were utilised. As to NSW, Mr Ergas found that in two years, incremental PD revenue fell below avoidable cost by $1,504,817 and $505,219 respectively, and by $191,984 over the life of the contract. He dismissed this as being unexpected by Baxter.

543 In a third statement, Mr Ergas made some corrections. The result was that in NSW, incremental revenue fell below avoidable cost over the life of the contract by $480,000, although the revenue outweighed avoidable cost by $53,116 when CPI was taken into account (as it should have been). Also, when CPI was taken into account in QLD and WA, a price squeeze was found in WA for years two and three of the contract, and it amounted to -$116,304 and -$6,268 respectively. Then in a letter to his instructing solicitors (Exhibit 10), Mr Ergas made a final correction, which resulted in an overall price squeeze in NSW using actual sales volumes (incremental revenue fell below avoidable cost by $72,454).

544 As a final point in relation to figures, Professor Nalebuff pointed out in examination-in-chief that Mr Ergas had included deflation in the NSW figures from year three in his third report. He then provided a table in Exhibit YY that corrected this error and found a case of exclusionary bundling in NSW. Mr Ergas' response to this in cross-examination was simply that he had relied upon Ms Lindsay's figures.

545 Ultimately, I have to decide what to do with all of these calculations. In light of my views in relation to whose expectations are more relevant and the accuracy of Professor Nalebuff's model, I am inclined to disregard these results in relation to my decision on "take advantage" for the purpose of s 46. First because these tests do not take into account uncertainty, secondly, because there has been no properly specified reliable *ex ante* test performed (which to my mind is the relevant test for this purpose) and thirdly because of a need to examine the whole of the evidence before me. However, given the relevance of buyer expectations for the *effect* that the conduct had for the purpose of s 47, and to the extent that Professor Nalebuff's test represents how the buyer perceived each auction, I am inclined to use Professor Nalebuff's figures for this purpose, at least as a guide or framework within which to assess the whole of the evidence.

546 Ultimately, I am wary of using the tests of either Professor Nalebuff or Mr Ergas definitively. The evidence of Ms Bailey (including her cross-examination) as to the extraction of figures left me with the view that significant parts of the underlying material were less than precise. Further, it was also clear that Baxter did not provide Mr Ergas with data for his seller expectation based calculation. Thus, if I rely on these figures at all, I rely upon them only as a guide and against which to test or confirm what the balance of the evidence tells me.

The case under s 46 of the Act

The law

547 There was no dispute as to the principles applicable under s 46 deriving from the decision of the High Court and of the Full Court of this Court: see in particular *Boral Besser Masonry Ltd v ACC*C; *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd* (2001) 205 CLR 1; and *Queensland Wire Industries Pty Ltd v Broken Hill Proprietary Co Ltd* (1989) 167 CLR 177.

548 The provisions of Part IV of the Act are to be interpreted in accordance with the subject, scope and purpose of the legislation, in particular, the object stated in s 2 of the Act of enhancing the welfare of Australians though the promotion of competition. In this respect, the position of consumers through the competitive process is central; though, the position of competitors may well assist and be relevant in that respect.

549 The elements of s 46 must be considered, sequentially, in the following order: market definition; whether the respondent has a substantial degree of power in a relevant market or markets, whether it has taken advantage of that power, and whether it had a proscribed purpose: *Boral,* per Gleeson CJ and Callinan J at [120], Gaudron, Gummow and Hayne JJ at [168] and [172] and McHugh J at [262]. These elements must co-exist and there must be a connection between them, such that the firm whose conduct is in question can be said to have taken advantage of its power: *Boral* per Gleeson CJ and Callinan J at [120]; *Melway* at [44]; *Rural Press Ltd v ACCC* (2003) 216 CLR 53at [51].

Market Definition

550 Both sides urged a "purposive approach" to the assessment of the markets, as did the expert evidence. The evaluative selection of the limits of the market is affected by the appreciation of the conduct said to be anti-competitive – the offering of PD together with or tied to sterile fluids at a particular price. Thus, the complaint (whether under s 46 or s 47) is of that conduct which links two groups of products. The real issue is whether PD fluids form a different market from, or, as urged by Baxter, form part of an agglomerated market with, sterile fluids.

551 Having considered and been greatly assisted by the helpful expert discussion on the market, I have come to the view that the appropriate market definition in which to apply the Act in the circumstances of this case is that there is an Australia-wide PD market separate from an overall Australian sterile fluids market (using that term as used by the ACCC in these proceedings). It is unnecessary to come to a view as to whether that sterile fluids market encompasses PN fluids, or whether the national sterile fluids market is a number of product markets: LVP, IS and PN.

552 I come to this view significantly persuaded by the analysis carried out by Mrs Smith. The only departure from her conclusions, if it can be seen to be a departure, is the view that I have come to that, notwithstanding the State based buying systems and distribution network to consumers, the analysis of the relevant PD market is more accurately undertaken by the identification and recognition of an Australia-wide approach.

553 Because I have reached my view substantially persuaded by the discussion of Mrs Smith I can be brief in my reasons for concluding that there are two relevant markets.

554 Whilst there is the need for locally-based staff and warehousing as well as distribution facilities, the conduct complained of is to be analysed by reference to its effect in preventing competition in a one non-substitutable product market (for PD), which would be supplied by importation or local manufacture. The essential question for the operation of the competitive process for the putative competition and, through it, the interests of consumers, is the ability of a competitor to obtain a sufficient share of PD sales nationally to make it worthwhile to sustain the costs of economic activity in, or into, Australia in relation to PD. Baxter supplies all States of Australia, New Zealand and the

Pacific Islands from its Toongabbie plant. A competitor would either import PD (as Fresenius does) or produce locally (as Gambro has done).

555 Whilst there is a clear relationship between the two markets (sterile fluids and PD) – a foothold in PD may enable a foothold to be taken in, and undermine a rival's market share in, the sterile fluids market, in particular because of the supply side substitutability of production – that is not a reason for rejecting the analysis of Mrs Smith.

556 Renal products are not only not substitutable with LVPs ,IS or PN fluids, but the structure of the industry with specialist renal companies, such as Gambro, assists in recognising the important difference in function between the products and the markets.

557 Baxter urged strongly that the supply side substitutability represented by Baxter's ability flexibly to adapt production to perceived need, the capacity to sub-contract distribution, the centralised State-based buyers and the fact that it would be uneconomic to have a PD-only plant in Australia, all pointed to one sterile fluids market in Australia including PD fluids and products. PD fluids can be, and are at Toongabbie, produced in the same factory and using the same equipment as is used to produce sterile fluids. That is not an unimportant factor. Also, because of the size of the Australian market, I accept Mr Bragg's evidence that a factory manufacturing PD alone, but only for domestic use, would not be economical.

558 I do not think that these factors are determinative. The products (sterile fluids and PD fluids) are functionally quite separate. They are non-substitutable. They involve a separate clinical area of analysis. They involve separate and distinct patient bases. They can be made by one business, (see Baxter and B. Braun (and also Fresenius, if one includes Fresenius Kabi), but PD also forms the product foundation for specialist renal companies. Thus, although Gambro has the capacity to produce PD at Dandenong, it does so or can do so in conjunction with the production of HD products, not sterile fluids. It does this because of the renal nature of its business. The economies of the PD-only factory must be considered in the light of the fact that importing PD is entirely viable. So that the need in the Australian market (assuming that one is not manufacturing for export) to manufacture PD together with other products does not mandate the conclusion that PD and those other products are one market.

559 In particular, in the light of the conduct involved, its purposes and consequences, the evidence reveals that PD fluids and products are a sufficiently segregated and distinct group of products to be viewed separately from sterile fluids. To a degree this is illustrated by Mr Browne's refusal to give any discount in SA for sterile fluids on a sole supply basis. PD fluids by volume were insignificant, but their revenue made up 30 to 40 per cent, he said, of the bid. Leaving aside questions of demand and supply side substitutability and functionality, this revealed the clear separate importance of the high value PD product to Baxter.

560 The examination and resolution of the question of market definition in the purposive way may, perhaps, be seen to have a degree of circularity. However its legitimacy can be seen by the different answers one would get to the question as to whether PD fluids were part of the wider sterile fluid market if the context of the question was a discussion of industry markets at the level of generality of coal, iron ore, bauxite, hotel and hospitality and sterile fluids for medical uses, compared to a context, as here, of assessing the conduct of Baxter in connection with sterile fluids for medical uses.

561 It is not irrelevant, it seems to me, that the plain and evident purpose of the structure of all impugned (and preceding) bids since the early 1990s was to tie the sale of PD as closely as possible to sterile fluids. It is in the context of that behaviour one asks whether PD is in a separate market to LVP, IS and PN. In my view it is.

Market Power

562 It is necessary to consider whether Baxter had "a substantial degree of market power" in the Australia-wide sterile fluids market: cf ss 46(1) and (4)(a).

563 The essence of power is the absence or degree of absence of constraint: *Boral* at [121]. Constraint may arise from competitors or customers: see 46(3). The notion of giving less and taking more (not limited to questions of price) is involved: *Queensland Co-operative Milling Association* (1976) ATPR 40-012 at p 17,246; *Queensland Wire* at 188.

564 A large market share may or may not give or reflect the existence of market power: *Boral* at [137].

565 The adjective "substantial" requires a "considerable or large degree of such power": *Eastern Express Ltd v General Newspapers* (1992) 35 FCR 43 at 63; *Universal Music Australia Pty Ltd v ACCC* (2003) 131 FCR 529 at [151]-[152].

566 Here, the market shares of Baxter in the sterile fluids market after the exit of Abbott, together with the position of being the only local manufacturer assist, though do not determine, the consideration of the power and its substantiality.

567 A number of matters need to be considered in the assessment of the market power held by Baxter from 1998 to 2001. First, it was the only local manufacturer of the broad range of sterile fluids. Care must be taken not to translate that into a conclusion of a monopoly position. As the evidence of Mr Crawford made clear, there was clearly a capacity to compete if an importer such as B. Braun could obtain registration of its products and approval of its manufacturing facilities from the Australian authorities. That potential competition was qualified in the way discussed by Mr Crawford, but it is a consideration which would lead me to conclude that there was a degree of constraint on Baxter in how it behaved by reason of this potential for competition. The nature of this constraint was not immediate, but it was real. A competitor using imports would face transport costs, the likely need for greater local inventory and foreign exchange risks. Nevertheless, the potential for import competition was real. The evidence demonstrates that Baxter understood itself in the period 1998 to 2001 to have a dominant market share in sterile fluids and that in the absence of demonstrated opposition it was likely to retain that share. Mr Lee did recognise, however, that if SPAs were required to pay prices such as the "cherry pick" prices there would be a significant stimulus to entry of participants. Mr Lee also recognised the potentiality for import competition. There was, however, recognition by both Mr Lee and Mr Browne in their evidence that Baxter was likely to win the sterile fluid tenders and that, to a degree, Baxter could charge what it liked for sterile fluids.

568 The barriers to entry to competitors in the sterile fluid market were not insignificant though not overwhelming. Local production would require considerable investment of funds in a production plant, being a significant risk of costs sunk in a market which had already "seen off" other local manufacturers who complained of low margins. TGA and other regulatory approval were detailed and strict. There was a tender loading in favour of local manufacturers in some States.

569 The evidence of Mr Crawford as to the capacity to import both sterile fluids and PD fluids is to be borne in mind. This evidence makes it clear (and it was recognised by Baxter) that at least where sterile fluids are produced close by in the region the threat of import competition for sterile fluids and PD was real, if not immediate at any particular time.

570 Mrs Smith concluded in her report that the structural barriers to entry were high reflecting the high sunk costs associated with entry and the significant economies of scale and scope that Baxter had from its high market share and extensive product range. These factors were compounded by long-term contractual arrangements in the 1990s which minimised the timing of entry into the market and heightened the risk of failure at identified points of time.

571 There was a body of countervailing power. Baxter was dealing with governmental agencies. That

power was said by ACCC not to have "kicked in". I am not sure that the Baxter negotiators in NSW in late 1992 would have agreed with that. In any event, it is not a matter of its exercise; it is a matter of the constraining effect of its availability, potential and present existence. If Baxter had sufficiently energised one or more States to exercise governmental or semi-governmental power, Baxter stood to lose large parts of its market share by a small number of decisions by buying SPAs. Competitors could be sponsored. Therefore, Baxter could not act as if unconstrained entirely. It was required not to act in such a fashion as would lead to governments taking steps to avoid dealing commercially with Baxter. Given the unusual nature of such a course of action by governments, one can conclude that short of behaving in a fashion to provoke that backlash, this countervailing power of reprisal still left some considerable room to behave as a sole supplier in the market. This is particularly so because it was no doubt recognised that such conduct by the SPAs would also come at a cost to governments. Other countervailing constraints can be posited upon the States' ability to act governmentally (and not in the course of business) and so unconstrained by the Act. For example, the power in the States to combine and to set the terms of the governmental tender process.

572 However, the demand for the sterile fluids was substantially inelastic and large volumes simply had to be acquired. Short of the kind of behaviour to cause an SPA revolt (of which, except with the 1992 threat in NSW, there was no evidence) Baxter had a real degree of flexibility in how much it charged. Its own witnesses accepted that real degree of discretionary freedom.

573 The reality of the countervailing power was said by Baxter to be demonstrated by the events in NSW and VIC in 2003 and the refusal by the ACT to pay the prices demanded by Baxter. There is force in this proposition. Where a centralised broad tender is not used and circumstances are such as to deny the opportunity to tie products there have been greater inroads by Gambro and Fresenius into Baxter PD market share. This does reveal that there is a real capacity in the buyers to control the shape and operation of the relevant markets.

574 Equally important in this respect were the views of Mr Kelly and Mr Kinkade (of QLD and NSW, respectively) that they did not consider there to be an imbalance in bargaining power between them and Baxter. They were experienced negotiators in fields with which they were familiar. Mr Bycroft gave evidence, however, that he considered WA had a lack of bargaining power. Further, although Mr Browne said that he thought SA would negotiate on Offer 1A, the absence of such and Mr Battersby's evidence is reflective of a degree of lack of bargaining power of SA.

575 Nevertheless, the States had available to them a free flow of information amongst themselves.

576 There was a body of evidence from which it can be concluded that the margins on sterile fluids were not large. Certainly that was the view of Abbott in 1992. Mr Bhargava of Fresenius Kabi said that margins on standard solutions were low. Mr Crawford of B. Braun said that there were very low margins on IV generic solutions.

577 Neither Mrs Smith nor Professor Nalebuff sought to analyse the sterile fluid margins. In submissions some examples were put to me to support the proposition that sterile fluid margins were commercially healthy. Without, however, some more rigorous analysis I am not prepared to draw any conclusions as to the margins for sterile fluids and what that tells me about market power.

578 As Mr Ergas said in some of his evidence, the existence of margins, which are not unreasonably large, tends to reveal a degree of constraint on the firms setting prices.

579 There is, however, a temporal aspect to consider. At the relevant times of the impugned transactions Baxter had been the sole domestic manufacturer and dominant (nearly exclusive) supplier for between six and nine years. The last local competitor had left in 1992, unable, it said, to justify the maintenance of its plant in Australia, without a guaranteed share and a price increase. No competitor since then had sought to challenge Baxter in relation to sterile fluids. The products were price inelastic. They were essential. There were constraints, but not such as to deny to the Baxter

executives the confident expectation that Baxter would be successful in its sterile fluids tenders.

580 Not without some hesitation, I agree with Mrs Smith and Professor Nalebuff that during the relevant period Baxter had what could be said to be considerable market power in the Australian sterile fluids market. I am not persuaded by Mr Ergas' criticisms of their evidence that I should conclude that Baxter did not have significant market power (a conclusion which Mr Ergas himself did not reach).

Taking advantage of market power

581 The separate operation of the element of taking advantage of the substantial degree of market power has been stressed by the High Court.

582 The words connote a body of human behaviour which would not or could not be done in other circumstances where the substantial power did not exist. It also requires the answer to the factual question whether the impugned conduct was the taking advantage of the power. That latter factual question is important here. When one examines the history of the market, from the 1980s through to the exit of Abbott and the tendering processes, with the exception of Offer 1A to SA in 2000, one does not see any of the relevant offers being made over the opposition of the SPAs or the exclusive contracts somehow forcibly extracted from them. The relevant offers were not made in circumstances in which it can be seen that advantage was being extracted from the position of power by obtaining something from the SPAs which was resisted. Other than SA in Offer 1A, no SPA asked for a volume discount for sterile fluids on an exclusive basis, detached from PD.

583 The history of the tenders recounted earlier reveals that the SPAs were willing parties to the acceptance of these bundled contracts. This willing participation and indeed in some respects the calling for this kind of structured bid, is an essential background to the assertion that Baxter took advantage of its substantial degree of market power.

584 The ACCC made reference to a number of cases in the US dealing with bundling. None is, of course, decisive of the operation of ss 46 or 47 of the Act. They are, however, of assistance as analogies for the purpose of analysis, just as are the models of Professor Nalebuff and Mr Ergas. Through the understanding of the facts in such cases as *SmithKline Corp v Eli Lilly & Co* 1978 – 1 Trade Cases 62,007; *Le Page's Inc v 3M* 324 F 3d 141 (2003); and *Northern Pacific Railway Co v US* 356 US 545, 550, and the economic evidence here, one is assisted to understand how by linking a product in a competitive market with products in a less competitive or non-competitive market one can impede the success of competitors or potential competitors in the former market.

585 The case made against Baxter in paragraph 45 of the Statement of Claim and as propounded at the trial was that Baxter had a strategy (the alternative offer strategy) which was designed to give the SPAs no real alternative but to enter into exclusive contracts for a substantial period for the purchase of PD fluids as well as sterile fluids.

586 I have no doubt that what Baxter sought to do in the impugned bids was to win as much of the available business as possible. That was the logic of the structure of the bids. It was the stated purpose of the Baxter witnesses. In doing so, it linked its PD products to its sterile fluids, in the only bids which offered a price below what were hospital item-by-item list prices. No attempt was made to offer a discount for all sterile fluids without including PD products.

587 The ACCC's case was that this was part of a strategy to drive the SPAs to the bundled exclusive bid. It was said that this could not have been done had Baxter not had a substantial degree of market power.

588 The conduct in the various tenders in the 1990s, including during the relevant period, bore a consistent pattern from which I infer an intended similarity. As long as the item-by-item offer was

taken by the buyers as a real alternative, it made a choice of PD products other than from Baxter an expensive alternative, and one unlikely to be taken, otherwise than based on considerations of quality or other non-cost considerations. The contemporaneous analysis of the tenders and the work of both Professor Nalebuff and Mr Ergas reveal that, subject to the quality of Baxter's products being radically inferior (which, the evidence revealed, was not the case), the alternatives to the Baxter bundled offer were significantly more expensive.

589 The purpose of Baxter plainly was to structure a bid so as to maximise the likelihood of winning all business including PD products by ensuring that, through a credible alternative higher price, there was a very high cost disincentive to purchase competitive PD products. The internal documents of Baxter make that plain. I reject such of the oral evidence as there is to the contrary.

590 However, it is to be recalled that the bids were structured in a way that conformed with what was requested by the controllers of the tender (save for Offer 1A in SA).

591 The item-by-item prices were not intended to be accepted. But they were intended to be taken seriously by the SPAs. Baxter wished to obtain exclusive contracts. Baxter knew that as long as its bundled bid prices did not create offence with the SPAs and as long as the item-by-item prices were taken seriously, there was no incentive on the SPAs to change supplier. Baxter knew that this did not run counter to any real desire of the SPAs; the bid structures were permitted and indeed encouraged by the SPAs.

592 There are two major evidential hurdles in concluding that Baxter would not or could not have structured bids in the way impugned in the absence of its market power. The first concerns the circumstances surrounding the 1998 NSW contract. The second is the absence of analysis of the item-by-item prices as monopoly prices, not being ones capable of being charged in a market in which Baxter did not have a substantial degree of market power. The two points are related.

593 In relation to the tendering for the 1998 NSW contract, there is no basis for concluding that Baxter was aware that B. Braun would not obtain or did not have approval for its Penang factory. B. Braun had products registered for 80 per cent of the sterile fluids range of products in the request for tender. There was evidence that Baxter was aware of that. Mr Crawford's evidence was that import competition for sterile fluids was possible. In those circumstances, it cannot be concluded that Baxter would not rationally behave, or could not have behaved, as it did in a market in which it was not able to take advantage of its market power.

594 Set in the context of the history of the various tenders, I cannot conclude that in respect of any of the bids (leaving aside Offer 1A in SA) there was a relevant taking advantage. The tender structures either permitted, or in some cases expressly encouraged, exclusive supply tenders over all products.

595 When one appreciates that there was no attempt to analyse the item-by-item prices by reference to costs (by either Baxter or the ACCC), or by reference to what might be a monopoly pricing or otherwise, beyond the difference between the bundled prices and the item-by-item prices, it is difficult to draw specific and particular conclusions about the item-by-item costs. Against a background of some evidence of the low margins for sterile fluids, it is therefore difficult to conclude that those prices could not have been offered as an alternative in circumstances where Baxter did not have a substantial degree of power in the sterile fluid market prices.

596 Offer 1A in the SA bid is more problematic. It was an isolated event in dealing with one buyer in the national PD market. If Mr Browne had had any real concern about there being workable competition in the sterile fluids market at that time in SA I do not think that he would have displayed what was a fairly high-handed approach. He said that he expected some negotiation and that his Offer 1A was not expected by him to be taken at face value. That may be; and that may go to purpose, but he would not have so acted if he had not had the confidence that he undoubtedly did have in Baxter's position in the sterile fluids market at that time in SA.

597 I am prepared to conclude that that point blank refusal to give a discount for volume in Offer 1A on sterile fluids was a taking advantage by Baxter of its substantial degree of market power.

598 The relevant occasions of passing (or it may be preferable to use the word 'failing') Professor Nalebuff's exclusionary bundling test and Mr Ergas' price squeeze test do not persuade me to conclude, in all the circumstances of the history of this bidding, that there was "taking advantage" for the purposes of s 46, other than in respect of putting forward Offer 1A in the SA bid.

Proscribed Purpose

599 The relevant purposes for s 46 are:

> *s 46(1)(a)*: eliminating or substantially damaging a competitor in the sterile fluids market or the PD market;
> *s 46(1)(c)*: deterring or preventing a person engaging in competitive conduct in the sterile fluids market or the PD market.

600 From the pleadings (see paragraphs 57(a) and (b), 68(a) and (b), 76(a) and (b) and 84(a) and (b)), the s 46(1)(a) competitors were Fresenius and Gambro in the PD market and the s 46(1)(c) competitors were Fresenius and Gambro and the other potential suppliers in the PD market.

601 The purpose is the subjective purpose viewed in the context of all the surrounding circumstances. It is thus necessary to have regard to the evidence of Baxter employees, documents and the relevant surrounding circumstances.

602 A number of matters stressed by Baxter are of importance. First, the conduct took place in a bidding system under the control of the buyer. Secondly, notwithstanding the criticism of the ACCC that its expression was used as a mantra, it was vital to Baxter to ensure the maximum throughput of product at the Toongabbie plant. Abbott had expressed the same proposition in 1992. The commercial exigencies attending this proposition are plain. They were given added illumination in the context of this case and the Australian market by what Mr Bragg said in paragraph [66] of his affidavit:

> *In my opinion, the size of the Australian market relative to other markets has dictated the nature of Baxter's operations and, in particular, the mix of products manufactured at the Toongabbie Plant. In Europe and the United States of America, for example, some plants are solely dedicated to the production of one specific type of sterile fluid because volumes of production can justify such a dedicated investment. In Australia, however, the reality of the market size necessitates combining the production of varying types of complementary sterile fluids to maintain a viable production facility (in the sense of producing products in Australia at a reasonable cost as against importing such products). In this context, it is my view that the Toongabbie Plant could not remain viable by producing PD's only.*

603 Thus, I accept that there was a clear and defensible reason for the otherwise commercially understandable desire to obtain as much business as possible and to maintain maximum throughput through the plant.

604 Whilst more than a little of Mr Lee's evidence was difficult to accept and unsatisfactory, in light of the history of Abbott and other manufacturers leaving the market and of Mr Bragg's evidence, I am prepared to accept Mr Lee's evidence that the level of Baxter's capital investment and the fixed costs component of its production are such as to make local manufacture viable only if it maximises the volume of fluids manufactured at Toongabbie. Mr Lee said the following in paragraph11.5(w) of his affidavit:

> *With respect to each tender, my concern has been to compete for that business against all other tenderers (whoever they might be) with a view to winning as much business for Baxter as is possible. I have never intended or expected that any tender by Baxter, or subsequent offer by Baxter in the course of negotiations with respect to a tender, would exclude another tenderer from being a competitor of Baxter. Furthermore, it has not been my intention, or expectation, that, by making offers and winning business under a tender, Baxter would, or could, stop or discourage another tenderer from offering competitive products on other occasions.*

I accept that evidence. It is, however, necessary to examine its limitations; and that is best done by reference to the internal documents of Baxter to which I have already made reference, in particular in discussing the evidence of Mr Lee. It is also necessary to bear in mind the limits of this evidence in terms of not intending to exclude another tenderer from being a competitor. This is not to be understood as not intending to affect competition.

605 It should be recognised that one could have the benign aim of maximising throughput, by having a purpose (by way of a substantial purpose as one of the purposes: s 4F(1)(b) of the Act) found in s 46 (1)(a) and (c). That is, there may be a finding that a party had a proscribed s 46(1) purpose as the means of ensuring the "legitimate" commercial aim of having a vulnerable factory maximise its throughput and lower its marginal costs.

606 The Baxter documents (see in particular Exhibits G, H, K, L andN) reflected a recognition at the senior corporate level in Baxter, including by Mr Lee, that Baxter was employing a technique or strategy of "bundling" or "leveraging" of dialysis products with sterile fluids, in part because it was being permitted, or tacitly encouraged, to do so. It seems to me tolerably plain that Mr Lee and others at Baxter, including Mr Browne, recognised that by tying or bundling PD to sterile fluids in the context of a credibly framed item-by-item alternative the consequence would be to make the bids of competitors in respect of PD, such as Gambro and Fresenius, unlikely to be acceptable. One does not need the sophistication of the analysis of Professor Nalebuff or Mr Ergas to appreciate the significant additional cost of the item-by-item approach as the price of taking a competitor's PD products. (Though their respective calculations give it theoretical foundation.) There were a number of contemporaneous tender analyses in evidence. That consequence was plainly appreciated by the SPAs and intended by Baxter.

607 Whilst some of the Baxter witnesses gave evidence that the item-by-item prices were set at a level to recompense Baxter should it lose volume, there was no evidence put forward by Baxter to relate the item-by-item prices to the increased marginal cost of production should any particular volume be lost. The reality was, as was demonstrated in the cross-examination of Mr Lee and Mr Browne, that though Baxter believed that there were competitive pressures from B. Braun, Baxter believed that likelihood was that it would maintain its position in the supply of sterile fluids and it could ensure that the real and present reality of competition in the PD market could be practically eliminated as long as the credible alternative to sole supply from Baxter in respect of all products was very costly. There was no evidence to support any proposition (and Baxter did not seek to say this) that the item-by-item prices reflected the increase in marginal costs of sterile fluids, should PD be lost to competitors.

608 Thus, it seems to me clear that the purpose involved, as a substantial purpose, was to frame a bid structure involving a credible item-by-item alternative to maximise the chances of bringing about circumstances in which the bids of competitors with substantially equivalent products could only be accepted at a significant cost penalty.

609 This was not a purpose within s 46(1)(a).

610 Whether or not this is a purpose within s 46(1)(c) is more problematic. If s 46(1)(c) is directed to deterring or preventing Fresenius or Gambro or anyone else from engaging in conduct at any time in

the PD market, I do not think Mr Lee or anyone else at Baxter had such a purpose. Fresenius and Gambro (as well as B. Braun and Abbott) were large worldwide concerns. Just as Baxter did not have a purpose to damage or eliminate them, it did not have a purpose to deter or prevent them from trying to gain sales in Australia by undertaking conduct in Australia, such as by submitting competing tenders. Baxter's purpose was to bid in such a way as would prevent rival bids in the PD market being "competitive", that is likely to succeed over Baxter's bid. The purpose in so constructing the bids in question was, it seems to me, plainly to meet the developing competition for PD fluids in Australia from Fresenius and Gambro. That the approach was encouraged or tacitly or expressly approved by the SPAs is not to the point. Baxter could have structured its bids otherwise. It did not. It offered a tie or bundle at, largely, historical prices, and a credible threat of an alternative with much higher prices. The purpose was to make rival PD bids uncompetitive in the sense of unacceptable, because of the credible cost alternative of Baxter's item-by-item offer.

611 I have no doubt that that was the purpose (in the sense of a substantial purpose) of Baxter. The question is whether that satisfies s 46(1)(c).

612 The notion of "competitive conduct" should be understood in a practical business sense conformable with the subject, scope and purpose of the legislation, including the objects stated in s 2 of the Act: *Boral* at [159] and [261]. This involves the welfare and protection of consumers through the preservation of the competitive process: *Queensland Wire* at 191.

613 The proposition put forward by Baxter is that the purpose of Baxter was not directed to the competitive process in that Baxter's purpose was not to deter or prevent Fresenius or Gambro from engaging in conduct in Australia, whether bidding at tenders or otherwise offering bids for their products or their products for sale. Expressed at that level of generality, I agree. However, the competitive process involves not merely the existence of an ability to put forward a rival offer, it involves the existence of circumstances which make it likely or, at the very least, feasible, that the rival offer might be successful and so might compete in a real and practical sense. The phrase "competitive conduct" can be taken to mean conduct that is competitive in a real and not nominal sense: here, not just the ability to submit paper that can be seen to be a bid of a rival, but that bid having some prospect of success, of being "competitive". Looked at in that way I have no doubt that Mr Lee, Mr Browne and the other senior executives concerned at Baxter, and thus Baxter, had a substantial purpose in structuring the bids in a way to prevent rival bidders (Fresenius and Gambro) for PD products from being able to put forward bids that were realistically competitive by the existence of credible alternative high item-by-item pricing. In the tender bidding system prevailing, albeit structured and dictated by the buyers (the SPAs), the purpose was to create circumstances in which Fresenius and Gambro could not put forward realistically competitive bids and so prevent them engaging in conduct that was, in a real sense, competitive. True the act of Baxter did not impinge directly on Gambro or Fresenius doing anything. Rather, it was directed to affecting the environment in which their actions (their bids) would be judged. Bearing in mind the aim and purpose of the legislation that, it seems to me, is to prevent Fresenius and Gambro from engaging in relevant conduct, because of the controlling or focal role for the adjective "competitive".

614 Of course, many traders will attempt to make their rivals' bids uncompetitive. They may do so by cost reduction, quality, service or other attribute of their product or service. Here, however, the posited circumstance is that a trader has taken advantage of a substantial degree of market power with the purpose in question.

615 The importance of the difference between simply preventing Fresenius or Gambro doing anything, and the preventing what they might do having a competitive quality, can be seen in Mr Wallace's evidence. Mr Wallace had some involvement with the NSW tender. He was not aware of any discussions about linking PD products to IV products with a view to excluding the competitors or to targeting the competitors in any way. So much can be accepted. Mr Garchow said something similar. The evidence of Mr Lee set out at [604] above was to similar effect. None of this evidence answers, or is even directed to, the question as to whether the structure was intended to make the rival

bids "uncompetitive". That was the core, however, of the purpose of the bundle or tie. The essence of the purpose can be expressed as it was in the particulars to paragraph 57 of the Statement of Claim (taken from an exchange between Mr Browne and an ACCC questioner):

> *Questioner If you were confident you could compete with Gambro and Fresenius by reference to service quality and price on PD, why would you need competitively to put a tender in which bundled IV and PD products?*
> *Mr Browne Well, there's also a – I suppose you don't give any – you try to eliminate any opportunity for your competitors if you can.*
>
> *Questioner And you appreciated that Gambro and Fresenius just couldn't compete with you in the IV market when you submitted the tender?*
> *Mr Browne Yes.*
>
> *Questioner And you understood that they couldn't, in effect, match the discounts which you were offering in the bundled offers for IV products?*
> *Mr Browne They couldn't.*

616 This reflects the essence of what I otherwise take from an examination and assessment, I hope on a common sense basis, of the evidence before me. The purpose of the bid and its structure was to foreclose the likelihood or restrict the possibility of a competitor's bid having any realistic prospect of success. The stubbornness of Mr Browne's attitude to the request for Offer 1A in SA in 2001 reflects the reality of the purpose of the structure of the bids. To give a genuine discount for volume would be to make Fresenius' and Gambro's PD bids ones that had realistic prospects of success. It was that that was to be prevented, thereby protecting the PD revenue stream.

617 The finding of purpose in this context and that to which I will come to with regard to a s 47 purpose below does not necessarily infer the taking of advantage of market power to achieve this purpose. As I indicated at [581] above, s 46 does not merely require the coexistence of market power, conduct and proscribed purpose to infer a "taking advantage". It requires the separate and distinct operation of the element of the taking advantage of market power. There must be a necessary connection between the limbs in order to infer that Baxter can be said to be taking advantage of its substantial market power: *Melway* at [44]. My findings as to a proscribed purpose therefore should be seen as distinct from and in no way negating my findings as to whether Baxter took advantage of its market power.

The s 47 claim

618 There was no substantive issue but that the pleaded impugned conduct amounted to conduct that fell within s 47(2) of the Act and so within s 47(1) of the Act, if s 47(10) was satisfied.

619 Thus, whether or not the impugned conduct was a contravention of s 47(1) depended upon whether the impugned conduct of Baxter:

- had the purpose of substantially lessening competition, or,
- had or was likely to have had the effect of substantially lessening competition

within the meaning of either s 47(10)(a) or (b). Of course "lessening competition" includes "preventing or hindering competition": s 4G of the Act.

620 In order that the conduct of Baxter be assessed by reference to s 47 a number of matters need to be borne in mind. The preventing or hindering of competition must be of the competitive process: *Stirling Harbour Services Pty Ltd v Bunbury Port Authority* (2000) ATPR 41-752 at 40,732, [2000] FCA 38 at [114]; *ASX Operations Pty Ltd v Pont Data Australia Pty Ltd (No 1)* (1990) 27 FCR 460 at

478; and *Universal Music Australia Pty Ltd v ACCC* , at [242] and [266]. Competition or the competitive process is the means of protecting the interests of consumers: *Queensland Wire* at 191.

621 The identification of the competitive process and thus competition which may be affected requires a temporal reference point. The relevant time period in which to judge or assess the competitive process will depend on all the circumstances of the case, including the structure of the industry and the asserted anti-competitive conduct.

622 Here, one can examine Baxter's conduct and purpose at a relatively high level of generality and long range time period: Was the purpose to affect the viability of entry of competitors into the Australian market? Was the effect to prevent same? Was Fresenius dissuaded from building a competitive factory in Australia? Were Fresenius and Gambro so affected by the loss of the tenders in 1998-2001 as not to be able to bid competitively in later years, for example because of the development of incumbency advantages in Baxter?

623 At another level, focussing more on the tender process as the chosen competitive process, different questions arise. They do not involve directly any examination of long term effects on entry, incumbency advantages and the like, though these matters may flow from the discussion. Rather, they involve an examination of the purpose and effect of the conduct on the operation of the tender process as the mechanism that had been chosen by the SPAs as buyers for them to buy goods in the market.

624 Each of the SPAs and the State governments which put in place a tender process intended that the operation of that process would produce real competition for the products the subject of the tender process. The purpose of Baxter was, as I have said, to structure the bids made by it in a way to prevent rival bidders for PD products from being able to put forward bids that were realistically competitive, by the existence of credible alternative high item-by-item pricing. The purpose was to ensure, as far as possible, that the competitive process of the tender process would not bring about realistically competitive bids for PD products by tying or bundling PD products to sterile fluids, and by providing a credible alternative which would make a choice of any likely rival PD product financially damaging to the State.

625 Is that a purpose of "lessening competition"? In my view it is. The competitive process here was the tender system used by the States. Suppliers in the relevant field were asked to bid on an hypothesis that each would be competing in a process that would be conducted in such a way as would enable each, subject to price and quality considerations, to have a realistic prospect of success. That is the nature of a tender process. Of course, if the quality of a rival's product is inferior, or its price too high, its prospects of success will be low. However, if there are rivals with equivalent products and there is no reason to think that they are any less efficient than each other, conduct, which enables one rival to ensure that the others' bids cannot be realistically competitive in the process, requires examination. If this effect on the prospects of success by rivals is a result of some competitive edge (a new process, a new invention, a radically reduced cost base) one can conclude that the other rivals' bids are not competitive by reason only of the success of the competitive process. Here, however, one may conclude that the rivals' bids are not competitive by reason of the realistic consequences that will occur to the buyer if the condition imposed by one rival on its offer to supply is not complied with. In those circumstances, it is the perceived consequences of not accepting the offer of bundled supply, that is, of not accepting the offer amounting to exclusive dealing within s 47(2), which hinders the effective operation of the tender process in relation to PD products. That plainly was the purpose of the bundled bids. That purpose, in my view, is one directed to hindering the competitive process of the tender bids and so hindering competition.

626 This approach to the conduct and the purpose of Baxter concentrates upon that part of the conduct which was an offer to supply on the stated conditions up to the entry into each contract. The entry into each agreement and the supply of products under each agreement cannot be said to have been for the purpose of hindering the competitive process in the form of the tender process since that process was complete. This conduct must be examined for Baxter's purpose and its effect at a higher

level of generality and in a wider temporal framework.

627 Before coming to this wider framework, it is necessary to consider the question of the word "substantially" in the operation of s 47(10) in connection with the offer to supply.

628 The word "substantial" has the sense of being meaningful or relevant to the "competitive process": *Rural Press v ACCC* at 229, 220 and 249 ,[41], [2] and [108]; citing French J in *Stirling* at 40,732. See also *Rural Press v ACCC* at [41] and ftnt 26 for the proposition that it is not sufficient for liability merely because the relevant effect was quantitatively more than insignificant or not insubstantial.

629 Viewed from the perspective of the effect on the tender process, the purpose was substantially to hinder the competitive process and so substantially to affect competition. Viewed from the same perspective, the likely effect on the competitive process was as was intended by Baxter. Assisted by the exclusionary bundling test of Professor Nalebuff, the price squeeze test of Mr Ergas, the examples of contemporaneous analysis by the SPAs and by common sense, the likely effect at the time of the offering to supply (see *Universal Music* at [247]) was to hinder substantially the tender process of PD products in the way that I have identified in dealing with purpose. Whilesoever the States found it useful or proper to organise their purchasing by State-wide tenders for all sterile fluid products and PD products, the bundling of PD with sterile fluids with the credible high priced item-by-item alternative hindered the operation of that process. Looking at the matter in that way imbues the purpose and effect of the conduct with an indefinite duration, though one, to a significant extent, within the control of the States.

630 If the appropriate framework and timeframe are broader than the operation of the tender process, my conclusions are different. Undoubtedly one of the main aims of Baxter was to deny their competitors market share in the PD market. That is only another way of saying that Baxter wanted to win all the business. Its purpose was to do that by making the bid process such that its competitors could not realistically succeed, and in that sense compete. I have dealt with that. It did not, it seems to me have a purpose beyond that, in some wider manner, to impede or hinder the competitive process. By and large Baxter had no control over how the competitive process would operate – whether by centrally run State-wide tenders, or by individual hospital purchasing. It could not prevent B. Braun, Gambro, Fresenius, or Abbott (all large multinationals) from taking any step in relation to the Australian market.

631 Thus, if I am wrong about the legitimacy of viewing each tender as the competitive process I do not think that it has been shown that Baxter had a relevant purpose for s 47(10).

632 With this wider framework and timeframe the question of effect and likely effect must be considered.

633 The word "likely" has been the subject of considerable discussion in the cases. As a single Judge it seems to me that the balance of authority favours construing "likely" to mean "real chance or possibility": *Tillmanns Butcheries Pty Limited v Australasian Meat Industry Employee's Union* (1979) 42 FLR 331 at 346-48; *Monroe Topple & Associates Pty Ltd v Institute of Chartered Accountants in Australia* (2002) 122 FCR 110 at [111], 140; *Australian Gas Light Company v ACCC* [2003] ATPR 41-966 at [341]-[358]. That does not encompass a mere possibility: *Dowling v Dalgety Australia Limited* (1992) 34 FCR 109 at 136. It is to be recalled what is important is the text of the statute not the linguistic synonyms employed to explicate meaning. I agree with Lockhart J in *Dowling* that the word indicates propensity or tendency; and in accordance with Deane J in *Tillmanns* that it theorises the sense of a real chance. I also agree with what was said by French J in *AGL* at [348].

634 Baxter put forward a number of legal submissions in relation to the effect or likely effect on competition. Most were non-contentious. Some need comment.

(a) The Court must apply a "with and without test" to the impugned conduct.

(b) The effect is on the competitive process, not individual competitors.

(c) The effect or likely effect on competition is to be judged by reference to the effect or likely effect on "market structure". This was said to flow from what was said in *Pont Data* at 478, that the test is concerned with the state or condition constituting the market or markets in question, actually or potentially. That is not to import some broad framework of "structure". Here the "structure" of the market was in significant respects able to be shaped or controlled by the SPAs in their choice of behaviour and how they wanted purchasing to be organised. That is not to say, however, that conduct may affect and be likely to affect the competitive process within the chosen organisation of purchasing and so within that "structure". *Pont Data* is not authority for any proposition preventing the assessment of the affect on competition by reference to the operation of the processes of the market such as the tender process here.

(d) The effect or likely effect involves considering whether there was any material enhancement of any pricing discretion, relative to that which it would have had. In a sense, this is just one aspect of the "with or without" approach.

(e) The effect or likely effect must be durable, not transient. Baxter referred to what the Full Court said in *Universal Music* at [242] which, with respect, bears repetition:

> *Competition is a process and the effect upon competition is not to be equated with the effect upon competitors, although the latter may be relevant to the former. Competition is a means to the end of protecting the interests of consumers rather than competitors in the market (*Queensland Wire *per Mason CJ and Wilson J at 191). Competition is defined to include competition from imported goods (s 4). The Court has to make a qualitative judgment about the impact of the impugned conduct on the competitive process. For example, a short term effect readily corrected by market processes is unlikely to be substantial. The lessening of competition must be adjudged to be of such seriousness as to adversely affect competition in the market place, particularly with consumers in mind. It must be 'meaningful or relevant to the competitive process':* Stirling Harbour Services Pty Ltd v Bunbury Port Authority *[2000] FCA 38; (2000) ATPR 41-752 at para [114].*

What is unlikely to be substantial is a short term effect readily corrected by market processes. That is not to say however that the only substantial effects are long term, or that one cannot look to the effect on the competitive process, here the tender process, so long as that process is in place, and even if the choice of whether to use that process is in the hands of another. The hindering of the chosen competitive process of open tenders, assessed looking forward, may, conceivably, be only for the life of the tender in question. It may be for a longer period, if further like tenders are to be called. That is not, however, short term. It prevents real competition for supply for a number of years or for the length of time of operation of the chosen competitive process. Also, looking forward, it prevents the market processes working efficiently in an important way – by open tender.

(f) The comparative assessment is not speculative or merely theoretical.

635 Looking at the likely effect on competition using a broader framework and timeframe than the operation of the individual tenders, it might be said that what was at stake was competition for the market, and as long as rivals were able to compete on the next occasion and as long as there had been no impairment of the ability of the States to choose the competitive process that they desired, then no harm had been done to the competitive process. If one accepts the premise of the proper framework for analysis, there is, I think, significant force in this argument. I am not prepared to accept on the basis of Mr Mechtersheimer's evidence that the conduct of Baxter was a determinative factor on whether or not a plant was built in Darwin by Fresenius. The evidence led from him was far from compelling and I tend to think that it was coloured by the interest of his firm. In any event, even if I

am wrong about the influence of the tied contracts on any decision as to where to build a PD plant, the evidence discloses that competition in PD is well able to be undertaken by imported product. Thus, the tied contracts may have had an effect on industry policy and employment, they did not, in this respect, have, nor were likely to have, any substantial effect on competition.

636 I accept that Gambro has been unwilling since the mid-1990s to produce PD products at its Dandenong plant while it cannot gain a relevant share of the market. Nevertheless, it is able to produce such products at the plant and no impediment to its producing has been created by Baxter, should the market process of open tendering no longer be the market "structure" chosen by the States. Further, the evidence is clear that it can compete with imported product. This reveals, it seems to me, the legitimacy of examining the competitive process by reference to the operation of the tender bids. So long as there is a lack of likelihood of there being a realistic prospect of rival PD firms supplying any part of the PD market, any such firm, such as Gambro is unlikely to invest in establishing and maintaining any production facilities.

637 There was some evidence of Mr Bhargava of Fresenius Kabi that there was a possibility of that firm establishing a plant in Australia to manufacture IV and PN fluids. This was largely speculative. There is no reason why Fresenius Kabi cannot build such a plant. No conduct of Baxter has made it more difficult to do so. It can challenge Baxter in the sterile fluids market. The tying or bundling prevents PD competitors putting forward realistically acceptable bids in the way I have described. It does not place any impediment in Fresenius Kabi or B. Braun or Abbott in fighting for the sterile fluid market.

638 The evidence likewise does not disclose any effect of Baxter's conduct of bundling upon Fresenius Kabi's ability to supply PN fluids. Indeed, Baxter has supplied Fresenius Kabi PN fluids (produced pursuant to a distribution agreement) within its own responses to tender.

639 On the evidence of Mr Crawford, there is the capacity of B. Braun to compete by importing sterile fluids. One issue which has been influential in persuading B. Braun not to enter was the long term contracts enjoyed by Baxter. The long term nature of supply contracts made expenditure in Australia whether of a production plant or supply chain infrastructure riskier in terms of sunk costs, since loss of a major contract for a significant length of time exposed such capital expenditure to under utilisation or non-utilisation. The bundling of sterile fluids with PD products did not, however, make it more difficult for B. Braun to compete for the sterile fluid market, except to the extent that it made an exclusive bid (sterile fluids and PD) by Baxter more likely to be successful. In any event B. Braun stands ready to compete by import competition in sterile fluids and PD products should it be prepared to invest in its overseas plant to obtain TGA approval and to invest in inventory and a supply chain in Australia. It should also be noted that Mr Crawford recognised that the B. Braun PD systems were unlikely to be competitive on quality with Baxter, Gambro and Fresenius. Thus for the suppliers of sterile fluids the impediments are caused by the size of the market, the flexibility enjoyed by Baxter in local production, the risk of large sunk costs and the existence of long term centralised contracts (even assuming no bundling) which sees large portions of the market bid for and won or lost at long term intervals.

640 I do not think that the existence of the bundled contracts, other than by shutting out PD competitors for the contract period, raised barriers to entry in any substantial way. It merely delayed to another time in the future the opportunity for market entry for that State. Though to the extent, as they did, that Gambro and Fresenius had on-going costs in their business in Australia, those costs were being denied revenue and so, in one sense, increased.

641 If the correct analysis is that the competition is for the market there is force in Baxter's submission that each rival remains a viable, robust and substantial force in the supply of sterile fluids and PD products in Australia. That can be accepted. Whilst there are some incumbency advantages such as entrenched supply capacity and patient inertia there are no long term impediments to Gambro and Fresenius effectively competing for PD – if one ignores any future bundling of sterile fluids with

PD or to B. Braun, Fresenius Kabi, Abbott or others competing for the sterile fluids market.

642 A submission was put that even absent bundling, Baxter would have structured its prices in a way which best enhanced its prospects of maintaining volumes in respect of each product group. Thus, it was said, it was likely to have discounted its PD products and won the business in any event. Aspects of the behaviour of the Victorian market were pointed to. However, since 2003 (with the end of the 1998 NSW Agreement) the PD market shares of Fresenius and Gambro have increased. I am not prepared to accept that absent the impugned conduct that the market would have behaved the same.

Summary of my views as to the operation of the Act (subject to the "Crown immunity" point)

643 Thus, for the reason that I have expressed, leaving out of account the next question to be discussed: the proper scope of operation of the Act in respect of State and Territory polities, I would dismiss the Application insofar as it asserts and relies on contraventions of s 46 of the Act with the exception of Offer 1A in South Australia; and I would, subject to settling the precise terms of the relief, make declarations and injunctions, and consider the imposition of penalties, in relation to the conduct of Baxter in responding to requests for tenders and in negotiating the contracts in question with NSW, SA, WA and QLD as amounting to contravention of s 47 of the Act and in relation to the making of Offer 1A to SA as amounting to a contravention of s 46 of the Act.

644 The way I have approached the impact on the competitive process was one way in which the affectation of competition and purpose was put throughout the case by the ACCC. It is true that a significant body of the ACCC's case was directed to the wider structural effects to which I have referred in dealing with the competitive process at the more general and wider level. However, the thrust of the cross examination and the aspect of the case which concentrated upon the denial to Gambro and Fresenius of likely success in the PD market make clear that the way I have put the matter was well within the ACCC's case. Indeed, it was the part of the ACCC's case which led the cross examination of Baxter's witnesses on many occasions to become, if I may say so without disrespect to Mr Rushton, an unproductive engagement of assertion and counter assertion. Many of the propositions being put by Mr Rushton were to the effect that the conduct had the purpose and effect of ensuring that the conduct of Grambro and Fresenius could not be competitive in the way I have described. Many of the counter-assertions and answers from the witnesses can be seen as directed to purpose or effect in stopping Fresenius or Gambro doing anything, that is, taking any steps.

Crown Immunity

645 There was no issue but that all the impugned conduct of Baxter was undertaken in the context of dealing with the executive governments of the various States and the ACT. There was also no issue (the matter being conceded) that the States and the ACT were not carrying on business, whether directly or indirectly for the purposes of s 2B of the Act.

646 To appreciate the arguments and the issues for decision it is necessary to call to mind the precise nature of the impugned conduct and the precise terms of the relief sought.

647 The conduct of Baxter alleged to amount to a contravention of s 46(1)(a) and (c) in respect of NSW was by:

(a) submitting a response to the invitation to tender issued by NSW which response contained the impugned "alternative offer strategy" in various offers to contract;
(b) revising the terms of the response by submitting amended offers to contract; and
(c) entering into an agreement with NSW substantially in terms of one of the offers.

(See paragraphs 47, 48, 49, 51 and 85 of the Statement of Claim.)

648 This conduct of Baxter was in the context of the pleaded conduct of NSW in issuing an invitation to tender (paragraph 46 of the Statement of Claim) and in accepting the relevant offer which formed the basis of the contract (paragraph 50 of the Statement of Claim). Similarly framed conduct was pleaded in respect of SA, WA and QLD.

649 The conduct of Baxter said to amount to a contravention of ss 46 and 47 has been set out earlier.

650 No relief is sought against any State or the ACT. All relief sought is, in terms, directed to Baxter. Paragraphs 1 to 8 of the Application seek declarations that Baxter, "by its conduct in negotiating and entering into" the pleaded agreements, relevantly contravened s 46 of the Act.

651 Paragraphs 9 to 20 of the Application seek declarations that Baxter, "by its conduct in negotiating, entering into and supplying pursuant to" relevant agreements contravened s 47 of the Act.

652 Paragraphs 21 and 22 of the Application seek injunctive relief restraining Baxter for up to five years from making any offer to enter into or entering into or giving effect to any contract, agreement, arrangement or understanding with a State or Territory containing provisions that in substance provide for exclusive bundled supply of LVP, PN, IS and PD fluids.

653 The effect of orders in accordance with paragraphs 21 and 22 would include a requirement that Baxter not give effect to the impugned contracts that in fact have been entered into and that are on foot as at the date of the commencement of the proceedings, as well as restraining future conduct. In recognition of this affectation of existing contracts, paragraph 22A of the Application seeks a mandatory injunction requiring Baxter to supply LVP, PN (except for QLD), IS and PD at prices set out in the relevant impugned agreements, but without any bundling requirement.

654 Paragraph 23 of the application seeks penalties against Baxter for all the above conduct: negotiation of, entry into and supplying pursuant to the impugned agreements.

655 WA, SA and NSW intervened in the proceedings. They were made parties (the second, third and fourth respondents, respectively). Notwithstanding the absent of QLD and the ACT, the submissions put by the State parties were reiterated by Baxter in relation to its position generally. No issue was taken that QLD and the ACT were in any different position.

656 The position propounded by the respondents is that irrespective of the merits of the proceedings, the Act does not reach or apply to any conduct of Baxter. This is so, it was said, because were it to be otherwise the interests of the States and the ACT would be so affected as to amount to an application of the Act to the Crown otherwise than as provided by s 2B of the Act.

657 The starting point of the analysis is s 2B of the Act which is in the following terms:

> *SECT 2B* ***Application of Act to States and Territories***
> *(1) The following provisions of this Act bind the Crown in right of each of the States, of the Northern Territory and of the Australian Capital Territory, so far as the Crown carries on a business, either directly or by an authority of the State or Territory:*
> *(a) Part IV;*
> *(aa) Part VB;*
> *(b) Part XIB;*
> *(c) the other provisions of this Act so far as they relate to the above provisions.*
> *(2) Nothing in this Act renders the Crown in right of a State or Territory liable to a pecuniary penalty or to be prosecuted for an offence.*
> *(3) The protection in subsection (2) does not apply to an authority of a State or Territory.*

658 This provision was introduced into the Act by Act No 88 of 1995 (the *Competition Policy Reform*

Act 1995 (Cth)) that came into effect on 20 July 1996. Its introduction was an implementation of one of the recommendations of the Report by the Independent Committee of Enquiry into National Competition Policy (the "Hilmer Report"). The context of this provision was, of course, the clear proposition (leaving to one side the limits of its application) that the Act did not apply to the Crown in the right of the States, including entities, instrumentalities, emanations or agents of the Crown that were entitled to the immunity of the Crown: *Bradken Consolidated Ltd v BHP* (1979) 145 CLR 107; or to the Crown in the right of the Northern Territory: *Burgundy Royale Investments Pty Ltd v Westpac Banking Corporation* (1987) 18 FCR 212. (No suggestion was made that the ACT was in any different position to the Northern Territory in this regard.)

659 *Bradken* was decided by reference to the principle of construction that no statute binds the Crown unless the Crown is expressly named therein or unless there is a necessary implication that it was intended to be bound: *Province of Bombay v Municipal Corporation of Bombay* [1947] AC 58 at 61. The inflexibility and stringency of that principle was ameliorated or relaxed in *Bropho v Western Australia* (1990) 171 CLR 1; but the "settled construction of particular existing legislation" was expressly said not to be overturned: *Bropho* at 22.

660 In any event, from the clear terms of s 2B it can be taken that the Commonwealth Parliament intended that the terms of that provision were to mark out the limits of the application of the Act to States and Territories. Outside s 2B the Act should be taken not to bind and not to be intended to apply to the States or Territories. In this respect see *Bass v Permanent Trustee Co Ltd (*1999) 198 CLR 334 at 348-9.

661 In this case, the issue is the application of the principle to the facts here. It is common ground that the States and the ACT cannot be taken to have contravened any law of the Parliament. No relevant laws (ss 46 and 47) applied to them. Thus, no relief is sought against them. That, however, the ACCC submitted, is the limit of the application of the principle. The other party to the contract (a) can be restrained from enforcing its terms (in conjunction with a mandatory order against that party ensuring the State or the ACT gets the benefit, otherwise, of the contract), (b) is liable to a penalty for negotiating, entering into and supplying pursuant to the contract and (c) can be restrained in the future from negotiating or entering with a State or Territory or giving effect to any contract, agreement, arrangement or understanding with a State or Territory that would contain like impugned terms.

662 The respondents submitted that all such relief impermissibly applied the Act to the Crown by denying it the right, power and capacity that it had and has to enter a contract of such kind as it wishes. This was said to be an interference directly with its rights and not a mere adjectival interference with its commercial interests.

663 The content and extent of application of the relevant principle has been discussed in a number of High Court cases, as well as in appellate decisions in England. The parties disagreed as to the effect of these cases. In order to distil the relevant applicable principle and its proper application here, it is appropriate to work back through the authorities beginning with the most recent discussion of the principles in *NT Power Generation Pty Ltd v Power and Water Authority* (2004) 210 ALR 312.

664 In *NT Power* the issues of Crown immunity concerned two entities: the Power and Water Authority ("PAWA"), a body corporate constituted under the *Power and Water Authority Act* (NT) and an emanation of the Northern Territory Government, and Gasgo Pty Ltd ("Gasgo"), a corporation in which PAWA held all the shares. The issue concerning PAWA was whether it was carrying on business for s 2B of the Act. The High Court, in upholding the appeal, found that it was. In this respect, the case is irrelevant for present purposes. There were two issues concerning Gasgo, only one of which is presently relevant. The first (irrelevant) issue was whether Gasgo was an emanation of the Government. The High Court, in upholding the appeal, held that it was not. The second (relevant) issue was whether, on the premise that Gasgo was not such an emanation, the principle of Crown immunity extended to it. The High Court held that it did not. An understanding of the resolution of that (relevant) issue requires an appreciation of the relevant facts of the case.

665 NT Power generated electrical power at its own facility. In order to sell power to consumers in the Territory, if it were not to build its own infrastructure, NT Power required access to the existing electricity and distribution infrastructure owned and controlled by the PAWA. PAWA generated electricity from its own facilities, as well as buying it from NT Power. PAWA refused to make its infrastructure available to NT Power. Gas is the cheapest fuel available in the Territory for the generation of electricity. Gasgo had long term purchase agreements with gas suppliers which contained provisions giving Gasgo pre-emptive rights to buy the gas that the suppliers were prepared to sell to others (such as NT Power) at the prices those others were prepared to pay. Gasgo refused to give undertakings to NT Power not to rely on these pre-emptive rights. NT Power accused PAWA and Gasgo of contravening s 46 of the Act.

666 The rejection of any Crown immunity in favour of Gasgo involved the rejection of the proposition that a non-government party enjoyed Crown immunity in its dealings with other non-government parties if to apply the statute (in that case, s 46 of the Act) to the first party would adversely effect the interests of the Crown, such interests being adversely affected being only financial and not any legally enforceable interest. The reasoning involved in that rejection illuminates the core of the principle and its application here.

667 The majority judgment at [170] first posited the issue in terms expressed by Kitto J in *Wynyard Investments Pty Ltd v Commissioner of Railways* (NSW) (1955) 93 CLR 376, 393, as follows:

> *...This is to ask whether s 46, in preventing enforcement of a clause in a contract between two parties, neither of whom is the government, caused "some impairment of the existing legal situation of" the Northern Territory Government in this case. ...*

668 The majority at [170] then referred to what had been said by the majority in *Bass v Permanent Trustee Co Ltd* (1999) 198 CLR 334, 354 at [42] that *Bradken* illustrated the common law rule of construction:

> *[t]hat a statute is not to be construed as divesting the Crown of its property, rights, interests or prerogatives in the absence of express words or necessary implication to that effect. ...*

669 The majority in *NT Power* at [170] expressly reformulated this *obiter* expression in *Bass* which used language of "divesting" of "property, rights interests or prerogatives" as follows:

> *...The better view is that the principle applies to proprietary, contractual and other legal rights and interests and not otherwise, notwithstanding that it has been said to extend to "arrangements or understandings". That phrase was used by Mason and Jacobs JJ in* Bradken Consolidated Ltd v Broken Hill Pty Co Ltd*http://www.butterworthsonline.com/lpBin20/lpext.dll?f=FifLink&t=document-frame.htm&l=jump&iid=fba79c6.77b6821c.0.0&nid=1371a7 - JD_210-ALR-312fntxt186 but, as appears below, requires further consideration. ...*

670 The explication of "arrangements and understandings" was then dealt with by the analysis of Gasgo's arguments. The first of those arguments was that Gasgo's participation was at the behest of the government, and so, it was said, must be seen to be part of an arrangement or understanding involving the government. It was said that the reasons of Mason J and Jacobs J in *Bradken* supported this argument. This argument was rejected by the majority in *NT Power* by reference to the fact that in *Bradken* the arrangement or understanding was one to which the Commissioner of Railways was a party.

671 The second argument was by reference to the affectation of PAWA's financial interests, otherwise than by the affectation of contractual or property rights. It was argued that there was no logic to limiting the relevant interference to categories based on direct legal rights. This argument was

rejected as too wide and as without legitimate support: at [173]. The majority then analysed and rejected the matters said to have supported this argument. The first asserted support was the wider expression of the principle by Gibbs ACJ in *Bradken* who (at 124) used the phrases "prejudicial to the interests of the Crown" and "affect prejudicially the interests of the Crown" as the expression of the relevant principle to dispose of the matter before him. In pointing out that these expressions should not be taken beyond the problem that was there before the Court, the majority pointed out (at 174) that the Commissioner had entered into a contract, arrangement or understanding with BHP contrary, it was said, to ss 45 and 47 and where the actual decision was:

> *[W]here the Commissioner was not bound by ss 45 or 47, the Act could not apply to BHP either. That was because application of the Act would affect the government's enjoyment of a direct consensual relationship between itself and a non-governmental party ...*

672 The majority at [175] recognised that if PAWA had had the agreement with the suppliers "it would have fallen within the four corners of the decision in *Bradken"* (subject, of course, to s 2B). (Stopping at this point of the analysis of *NT Power*, there is nothing thusfar in the reasons of the majority to throw doubt upon the decision of *Bradken* insofar as it extends to protecting the non-governmental party to a contract with the Crown. Thus, here, unless the balance of *NT Power* demands the contrary *Bradken* would appear to require that Baxter be protected from any allegation that the entry into and supply pursuant to the impugned contracts contravened ss 46 and 47 on the basis that it fits four square within *Bradken.*)

673 The majority then dealt (from [176]) with an argument put forward by the Solicitor-General for South Australia that the immunity principle extended to protecting a non-government party to a contract with another non-government party if the interference with that contract affected the ability of one of those non-government parties to fulfil its contractual obligation either with the government or with another non-governmental entity which affected a governmental interest. In either case, the interest of the government was removed from the direct legal relationship affected. Reliance was placed on *Re Telephone Apparatus Manufacturers' Application* [1963] 1 WLR 463. The analysis by the majority of *Re Telephone Apparatus* illuminates the content of the principle expressed in *NT Power*.

674 In *Re Telephone Apparatus,* there were two agreements. The first was between eight manufacturers of telephones and the Postmaster-General and provided for the terms of supply by the former to the latter. The second was between the manufacturers and dealt with the allocation of orders made under the first agreement. It was held that there was no need to register the second agreement under the *Restrictive Trade Practices Act 1956* (UK) because that legislation did not apply to the second agreement. This was so by reason of the application of the Crown immunity principle.

675 The majority in *NT Power* identified two ways of analysing *Re Telephone Apparatus* – one in accordance with the principle as expressed by them, one not. The narrow basis of the decision in *Re Telephone Apparatus* which "should be treated by Australian courts as the true ground of the decision" (at [183]) was that the two agreements were in truth one composite agreement to which the government (through the Postmaster-General) was a party. Viewed thus, the case was similar to *Bradken.*

676 The wider basis of the decision in *Re Telephone Apparatus* treated the two agreements as distinct. On this basis, the second agreement between the telephone companies was not within the reach of the legislation because the Postmaster-General's "interest" or "rights and interest" would be prejudicially affected. These interests were only commercial because its legal position was unimpaired. In a passage important to the resolution of the this matter the majority said the following at [181]:

> *...Willmer LJ said that the Postmaster-General's "interests" would be prejudicially affected by the invalidity of the TAM agreement, and Upjohn LJ said that the Crown's "rights and interests" would be prejudiced. But the interests were only commercial*

> *interests: the* legal *position of the Postmaster-General was unimpaired. Harman LJ said that to interfere with the TAM agreement was "to frustrate in whole or in part the Crown agreement, and thus to interfere with the freedom of contract of the Crown". That "freedom" was not a legal right: the Crown and the manufacturers could have included within the Crown agreement any term of the TAM agreement they wished, but they chose not to.*

677 The above passage, and in particular the last sentence, must be read in its context. It is not authority for the proposition that was asserted by the ACCC that the freedom of the Crown to contract in such terms as it wishes is not a legal right or part of the "legal situation" of the Crown (see Kitto J in *Wynyard Investments,* referred to by the majority at [170]). Rather, it was a statement that what truly was being interfered with was the commercial consequences of another legal right (the second contract between manufacturers) and not the legal right of the Postmaster-General. That legal right was unimpaired and free since any term the parties desired could have been placed in the first contract. Thus, I do not see this passage to stand for the proposition asserted by the ACCC that all conduct prior to the formation of a legal right, relevantly here a contract with a State, can only affect the commercial interests of the State, as opposed to the legal rights, or legal situation, of the State.

678 The majority in *NT Power* then noted that in *Bradken* only Stephen J could be taken to have expressed himself in terms wide enough to be seen to give approval to the wider basis in *Re Telephone Apparatus.* That statement of Stephen J was *obiter* and also to be seen in the context of the argument put forward in *Bradken,* where *Re Telephone Apparatus* was only relied upon for the proposition underlying the narrow basis of the case, that the immunity of the Crown "extends to contracts arrangements or understandings made by the Crown with others": see *Bradken* at 109 and the majority in *NT Power* at [185].

679 Finally, the majority (at [188]) referred to some New Zealand cases (*Doyle v Edwards* (1898) 16 NZLR 572; *Lower Hutt City v Attorney-General* [1965] NZLR 65 at 75, 77-8 and 81; and *Wellington City Corporation v Victoria University of Wellington* [1975] 2 NZLR 301 at 305) referred to without disapproval in *Bradken* that might be seen to be broader than the interference with the legal rights of the Crown. Two were analysed as capable of falling within *Bradken;* the third was not central to the reasoning in *Bradken* and its place in *Bradken* should not be seen to widen the principle there found.

680 Thus, the following can be taken from the reasons of the majority in *NT Power*, in particular from its dealings with *Bradken* and *Wynyard Investments:*

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

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

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

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

681 The last proposition ((4) above) is clear from *Bradken* and *NT Power*. The principle is not so much an immunity of the Crown as the application of a principle of the construction of a statute. By that principle, if the statute when construed is found not bind the Crown, that means that the statute will be taken not to have application to, or an operation to extend to, the Crown, or to circumstances or parties where to do so would interfere with proprietary, contractual and other legal rights and interests of the Crown: *Wynyard Investments* at 393; *Commonwealth v Rhind* (1960) 119 CLR 584 at

598-9; *China Ocean Shipping Co v South Australia* (1979) 145 CLR 172 at 187-8, 199, 221 and 240; *Bradken* at 121, 127 and 135.

682 The principle is not one whose operation depends upon the fashioning of terms of relief. It is one concerning the reach or the extent of operation of the statute. Plainly, no remedy can be given against the relevant States or the ACT here. That is not merely because the States and the ACT are immune from the remedy. It is because the Act's operation does not extend to their legal rights found in the impugned contracts. It follows from that limitation on the operation of the Act (a limitation intended by the Commonwealth Parliament) that the other party to the contract is not affected by the operation of the Act. Thus, at least to enter into and give effect to (here by supplying pursuant to) the contract is not touched by the Act. To do so would be to make unlawful the performance of obligations or the taking advantages of rights bargained for or granted by the State or Territory in its contract. The legal rights of the Crown would be directly affected. Thus, in *Bradken*, the Act did not operate to entitle injunctive relief to restrain performance of the agreement.

683 The ACCC here seeks to avoid this consequence by including mandatory order 22A. By this, it was said, there was no *prejudicial* interference with the performance of the impugned contracts, because, although orders 21 and 22 restrain the giving effect to any of the impugned contracts still on foot, order 22A gives an equivalent benefit of the contract without the bundling restrictions.

684 The relief sought, however, has the following effect:

(a) making it unlawful to enter and give effect to the contract with the Crown;
(b) restraining the performance of the terms of the contract to do that which the Crown agreed;
(c) substituting another bundle of rights said by the ACCC and adjudged by the Court (on this hypothesis) to be non-prejudicial to the Crown; and
(d) subjecting a party who has entered into a contract with the Crown, for their perceived mutual interests, to penal sanctions.

685 These are affectations of the contractual and legal rights and interests of the Crown. To substitute the views of a litigant (here the executive authority of another polity) and or court (here a court exercising the judicial power of another polity) for those of the State and Territory as to what contractual rights and obligations it should enjoy or be prepared to bear in exchange for bargained rights and advantages is not an interference with commercial interests, but with legal interests. If the Crown is prepared to bargain for an arrangement with an exclusive supply or bundling condition, that may be because it perceives its financial, administrative and governmental interests to accord with that course. To deny the State and Territory the operation of the contract for which it bargained in favour of an alternative, perceived by others to be non-prejudicial, would be to deny it the contractual and legal embodiment of its self-perceived economic or political interests. That is to interfere with its legal rights.

686 Thus, even if all other matters had been made out by the ACCC, I would not make the declarations in paragraphs 1 to 20, or the injunctions in paragraphs 21 and 22 or order any penalty as sought in paragraphs 23 of the Application insofar as they concern the entering into or giving effect to (by supplying pursuant to) contracts made between Baxter and any State or the ACT.

687 This leaves the issue of whether the principle only prevents the application or operation of the Act to the entry into or giving effect to the impugned contracts once formed, as crystallised legal rights, or whether it extends to prevent the application or operation of the Act to the commercial negotiations leading up to the formation of the impugned contracts. If the former, then Baxter will have contravened s 46 of the Act by making Offer 1A in SA and and s 47 of the Act by negotiating, and making the offers it made leading up to the formation of, the impugned agreements. Not only will this have the consequences that declarations to that effect will be made and that Baxter will be liable

to the imposition of penalties, but also, Baxter can be restrained from the repetition of such conduct in the future. This would thereby prevent or foreclose the State or the ACT from making a contract with Baxter by preventing its negotiation, notwithstanding that if such a contract were to be formed the Act would not extend to either Baxter or the State or the ACT as to its formation and performance.

688 The ACCC says that the interests of the State or the ACT thus affected would be commercial or financial or administrative only. The respondents say that legal rights and interests, including the Crown's prerogative are directly affected.

689 *Bradken* was concerned with an existing agreement. *NT Power* was concerned with existing agreements. The majority in *NT Power* recognised and accepted that the relevant issue was to be expressed in terms used by Kitto J in *Wynyard Investments* at 393:

> *whether the operation of the provision upon the subject would mean some impairment of the existing legal situation of the sovereign*

690 Once the impugned contracts were entered into, their existence and terms formed part of the legal situation of the States and the ACT. They obtained vested legal rights and obligations by reference to an accepted juridical source of private and public obligation and privilege justiciable and enforceable in the courts: the respective contracts.

691 Antecedent to the creation of this form of recognised juridical vessel of rights and obligations, the States and the ACT had legal situations which included the lawful capacity or authority to negotiate and enter into such contracts as were entered into. If no particular statute or delegated legislation touches the matter, the entitlement or lawful freedom or capacity of the executive government of the relevant polity to negotiate and enter into such a contract can be characterised as an aspect of the prerogative or as a mere capacity: *Davis v Commonwealth* (1980) 166 CLR 79 and Seddon *Government Contracts: Federal State and Local* (3rd Edn), chapter 2. Each of the executive governments concerned had the lawful capacity and entitlement to ask Baxter, whether by request for tender or otherwise, to provide it with offers for the supply of goods. Each was unconstrained by the Act in that regard. Each could ask for an offer which, in terms, and in the context of the relevant markets, offended s 47. It was unnecessary for there to be a statute or piece of delegated legislation that in terms proclaimed a "right" to do this. The right, or lawful capacity, was an attribute of each polity as a juristic person and the absence of binding contrary law. That was the "legal situation" of each government prior to its respective agreement.

692 Some of the respondents helpfully set out the particular legislative and regulatory regimes governing the tendering for the relevant contracts. It is unnecessary to descend to this level of detail. It is sufficient to identify the entitlement or capacity of the States and the ACT to call for tenders and negotiate offers leading up to the relevant impugned contracts as aspects of the legal situation of the States and ACT as legal (as opposed to financial or commercial) rights, interests or prerogatives of the kind recognised by the principle as enunciated in *NT Power, Bradken, Bass* and *Wynyard Investments.*

693 Does, then, the Act operate to make it unlawful for non-government parties to respond to such tenders or invitations or to participate in negotiation if a specified norm of conduct is contravened? If the answer to that were yes, it would follow (at least insofar as the response was such as to be within the contemplation of the request or invitation) that the legal rights, interests or prerogatives of the polity in question were qualified or impaired. Thus, the answer must be, no.

694 In some factual circumstances it may not be easy to discern whether a party is really responding to what a government has called for. For example, if a non-government party made an unsolicited offer to a government or made a response to an invitation which was so discordant with that invitation as to be characterised as an unsolicited offer, it may be more difficult to see how the operation of the

Act to cover such offers and any conduct leading up to that point affects the legal situation of the Crown.

695 Thus, it is necessary to examine the circumstances here, as pleaded and as found, for the purpose of assessing whether the offers and negotiations fell within that called for by the States and ACT.

696 As to the 1998 NSW Agreement contract the pleaded case (paragraph 46 *et seq* of the Statement of Claim) was that the offers and revised offers were in response to the relevant invitation to tender. The history of the preceding tendering was such as to allow the comfortable conclusion that the form of the impugned offers and revised offers was reasonably within that which was called for by the invitation. None of the history of negotiations between Baxter and NSW grounds a proposition that the offers, insofar as the ACCC asserts a relevant contravention, were outside the responses being called for. Indeed clause 4.32 of the Request for Tender (see [209] above) specifically contemplated sole supplier bids over a range of, or all, products.

697 No negotiations were pleaded in relation to the ACT agreement (see paragraphs 52 to 55 of the Statement of Claim).

698 As to the 2001 SA Agreement, the pleaded case (paras 58 *et seq* of the Statement of Claim) was that the offers were responses to the invitation to tender. The history of preceding tendering and supply and of the negotiations makes clear that the sole exclusive supply offers were clearly within what was called for. The refusal, in Offer 1A, to give a discount for volume for sterile fluids, other than PD does not alter this conclusion. A bid was called for. One was given. It may have disappointed SA. But it was a response to the request.

699 As to the 2001 WA and QLD Agreements, once again, the pleaded cases (paragraphs 69 *et seq* and 77 *et seq* of the Statement of Claim) were that the offers were responses to the invitation to tender. The history of tendering and supply and the terms of the invitations make clear that the offers were within that which was called for.

700 Therefore, the Act does not apply to or operate upon the conduct of Baxter said to contravene ss 46 and 47 up to the entry into the impugned contracts. Thus, no declarations as to past conduct or penalties as to past conduct can be made. On this basis, it would also be inappropriate and without foundation to grant orders restraining any future conduct with the States or the ACT.

701 Some of the submissions of the ACCC were to the effect that to accept the submissions of the respondents and to conclude that the principle of Crown immunity has the result which, in my view, it does, would be to emaciate the operation of the Act and in some fashion undermine the operation of competition law in this country. Neither of these things are a result of the views that I have expressed.

702 The operation of the principle is one of statutory construction. It involves an issue that is, subject to any constitutional restraints, one for the Parliament. If the Parliament wishes to ensure that the Act is to be construed such that persons dealing with the governments of States or Territories are fully liable to the operation of the Act no matter what impact that may have on the legal situation of the States and Territories, it can say so. It has not.

703 Further, if States and Territories wish to subject parties dealing with them to an equivalent regime they may, again subject to any constitutional restraints.

704 For the above reasons the Act does not extend to Baxter's conduct here. Therefore, the Application should be dismissed. I will hear the parties on the questions of costs.

705 I would like to express my gratitude for the careful assistance given to me by solicitors and counsel for all parties.

I certify that the preceding seven hundred and five (705) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justice Allsop.

Associate:

Dated: 16 May 2005

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