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ARE THERE EXTRATERRITORIAL LIMITS TO THE OPERATION OF AUSTRALIAN COMPETITION LAW?

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The Air Cargo Cartel Proceeding

International airlines typically carry cargo from airport to airport. The customers for that service are freight forwarders at the origin airport.

For a range of commercial, regulatory and operational reasons air cargo services are sold for one way carriage only from the airport of origin to the destination airport.

Freight forwarders on-sell the airline service as part of their carriage from door to door.

From 2001 to 2006 airlines generally imposed fuel and insurance surcharges as part of their price for the carriage of cargo.

Throughout that period decisions on whether surcharges would be imposed, and on the amount to be imposed were made at some airports through collective decision making by airlines.

That circumstance resulted in numerous competition regulators, including Australia's, taking enforcement proceedings against airlines.

In Australia, the regulator commenced proceedings against fifteen airlines. Within a week of the trial commencing thirteen of those fifteen had admitted to one or more contraventions and had agreed on remedies, including penalties, with the regulator. Two airlines, the flag carriers of two of Australia's closest neighbours, Garuda Indonesia and Air New Zealand, contested the ACCC's claims.

Following a six month trial, Perram J in the Federal Court of Australia found the conduct alleged by the regulator had occurred but found that that was not conduct

[1] Tom Brennan has been junior counsel for Garuda in each hearing of the Air Cargo Cartel Case.

which had occurred in a "market in Australia" and therefore was not conduct regulated by the Australian law.

By a majority the Full Court of the Federal Court reversed that decision. It is unnecessary to refer to the majority's reasons which were, in any event, difficult to understand.

The airlines appealed by special leave to the High Court of Australia. On 14 June 2017 the High Court dismissed that appeal unanimously[2].

Territorial Limits in Australian Competition Law

Since its enactment in 1974 the Australian competition law has operated with two territorial limitations.

First, it applies to bodies corporate which carry on business in Australia, Australian citizens and persons ordinarily resident in Australia.

Secondly, many, but not all of its competition provisions are limited to operate by reference to a "market in Australia".

Self-evidently airlines flying to and from Australia carry on business in Australia. Consequently, the air cargo cartel proceedings turned on the second question, did the conduct alleged occur in a "market in Australia".

To determine whether conduct occurs in a "market in Australia" requires firstly that the market be identified or defined and then there be a determination whether that market was "in Australia".

Market definition

The principles for market identification or definition in Australia had appeared well settled. The seminal statement of the Trade Practices Tribunal in *Re Queensland Cooperative Milling Association Limited*[3] had been repeatedly cited with approval and applied:

> "We take the concept of a market to be basically a very simple idea. A market is the area of close competition between firms, or, putting it a little differently, the field of rivalry between them … within the bounds of a market there is substitution – substitution between one product and another, and between one

[2] *Air New Zealand v ACCC* [2017] HCA 21
[3] (1976) 8 ALR 481 at 517.

> source of supply and another, in response to changing prices. So a market is the field of actual and potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given a sufficient price incentive."

The High Court had considered market definition in *Queensland Wire Industries Pty Limited v Broken Hill Pty Co Limited.*[4] Mason CJ and Wilson J referred to and applied that passage from the Trade Practices Tribunal, together with reasoning of the Court of Justice of the European Communities[5] to explain that the defining feature of a market is substitution.

In the same case Dawson J cautioned that elasticities of supply and demand and the notion of substitution provide no complete solution to the definition of a market. Rather a question of degree is involved – at what point do different goods become closely enough linked in supply or demand to be included in the one market. That caution was in the context of reasoning by his Honour that:

> "A market is an area in which the exchange of goods or services between buyer and seller is negotiated. It is sometimes referred to as the sphere within which price is determined and that serves to focus attention upon the way in which the market facilitates exchange by employing price as the mechanism to reconcile competing demands for resources."

The Air Cargo Case

In the Air Cargo Cartel Case the plurality relied upon that reasoning of Dawson J to conclude that:

(a) substitution cannot be the defining feature of a market;[6]

(b) substitutability may be an important and sometimes a decisive factor;[7]

(c) a market, at least for transport services, may be located in all of the places where the interplay of forces of supply and demand for that service take place.[8]

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[4] (1988 – 1989) 167 CLR 177.
[5] *F. Hoffman La Roche v Commission* [1979] 1 ECR 461; and *United Brands v Commission* [1978] 1 ECR 207.
[6] At [25] and [26].
[7] At [26].
[8] At [30].

The trial judge had found that the place of substitution of air cargo services was the airport of origin. The plurality accepted that conclusion.

However, the plurality reasoned that the places where the interplay of forces of supply and demand occurred resulting in substitution at the airport of origin extended to all those places where as a matter of commercial reality airlines competed to secure custom. While the immediate customers of airlines were freight forwarders at the airport of origin, switching decisions by those freight forwarders could be influenced by dealings between the airlines and consignees who might engage the freight forwarders.

Consequently, the interplay of forces of supply and demand could occur in places in which the airlines marketed to consignees: meaning the market was in each of those places.

By that reasoning the geographic location of a market for Australian competition law purposes (at least in the case of transport markets) extends to those places where conduct occurs which influences price negotiations between buyers and sellers.

That reasoning involved a significant shift in principle. Freight forwarders were the only buyers of air cargo services and there was only one place where the exchange of air cargo services was negotiated between those freight forwarders and airlines: the origin airport. Dawson J's reasoning in *Queensland Wire*, along with that of Mason CJ and Wilson J, supported the trial judge's conclusion.

The plurality's approach to market definition was not supported by any of the extensive evidence of economic experts in the case.[9]

That approach also departs from the approach to the same question adopted in other jurisdictions. In the United States, markets are geographically defined as the area in which the seller operates and to which the purchaser can practically turn for supplies.[10] Europe and Canada define the geographic limits of a market by reference to substitution of sources of supply.[11]

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[9] The ACCC called Professor Jeffrey Church, a Canadian and Dr Phillip Williams, an Australian. Air New Zealand called Professor Richard Gilbert, an American.

[10] *United States v Phillipsburg National Bank and Trust Co* 399 US at 357 to 358; *United States v Philadelphia National Bank* 374 US at 359; *Tampa Electric Co v Nashville Coal Co* 365 US 320 at 327; *Hherwagen v Clear Channel Communications* 435 F. 3D 219.

[11] *Kish Glass v Commission* [2000] ECR II – 1885 at [81] to [82]; *Atlantic Container Line AB v Commission* (2005) 4 CMLR 20 at [853] to [856]; *Commissioner of Competition v Superior Propane Inc* [2000] CACT 15 at [84].

Air Cargo – the facts

Garuda, as the flag carrier of Indonesia, had chaired the Indonesian committee of airlines which set the surcharges. That all occurred in Indonesia. The immediate effect of that conduct was on dealings with freight forwarders in Indonesia.

Nevertheless, Garuda's conduct in Indonesia in agreeing with other airlines on the imposition of fuel surcharges from Jakarta and Denpasar to various international destinations, including Australia was found to be in a market in Australia and therefore a contravention of the Australian legislation.

What constituted that conduct by Garuda a contravention of the Australian legislation, was the fact that it occurred in a market in Australia, because:

(a) airlines engaged in rivalrous behaviour in Australia seeking to match the supply of their services with the demand of shippers in Australia that were a substantial source of demand for the airline's services;
(b) airlines appreciated that the large shippers who required air cargo services to ports in Australia were the economic foundation of the market;
(c) airlines tusselled to obtain the custom of shippers in Australia who were substantial importers; and
(d) airlines pursued sales and marketing strategies in Australia promoting their services to shippers in competition for orders to provide freight for their cargo.[12]

There was no evidence and no finding that Garuda engaged in any of the conduct engaged in by airlines in Australia.

The findings upon which the plurality relied were based on evidence of conduct by Singapore Airlines, Air New Zealand, Cathay Pacific, Qantas, Emirates and possibly Korean Air.[13]

There was no evidence that Garuda knew of any of the conduct of any of those other airlines in Australia.

It was not an element of Garuda's contravention that the offshore conduct had an effect in Australia. Perram J found that the ACCC had failed to establish that Garuda's conduct had the effect, or likely effect, of substantially lessening

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[12] At [31] - [33].
[13] *ACCC v Air New Zealand* (2014) 319 ALR 388 at [272] – [308].

competition in a market in Australia because there was no evidence as to the effect of that conduct, if any, on the ultimate price of air cargo services into Australia.

A supplier of services is very likely to know of the location or locations where services in close competition are offered. It follows that when markets are defined by reference to substitution, it would be an extraordinary case where a supplier was ignorant of questions of market structure which lead to the supplier's inculpation.

The facts in the Air Cargo Cartel Case show that there are cases where a supplier may not know of conduct of its competitors antecedent to the offering of substitutable services; yet on the approach taken in the Air Cargo Cartel Case that conduct of competitors may lead to the inculpation of that supplier for contravention of Australian competition law.

Learnings

The reasoning in the Air Cargo Cartel Case leaves open a conclusion that conduct affecting any field of international commerce might occur in a "market in Australia" for the purposes of Australian law.

Six weeks after the High Court's decision in the Air Cargo Cartel Case the Federal Court entered the first conviction under Australia's criminal cartel provisions against Nippon Yusen Kabushiki Kaisha (NYK) and imposed a fine of $25 million for the giving effect to a cartel affecting the price of importation of vehicles to Australia.

In imposing the fine Wigney J commented that the cartel conduct:

> "Is ultimately detrimental to, or at least likely to be detrimental to, Australian businesses and consumers. The penalty imposed on NYK should send a powerful message to multinational corporations that conduct business in Australia that anti-competitive conduct will not be tolerated and will be dealt with harshly."

That is so, whether the conduct occurs in or outside Australia and whether or not it can be shown to have an economic effect within Australia.

Corporations engaged in international commerce need to consider whether they might manage those risks by not themselves carrying on business in Australia and instead having any business in Australia conducted by a subsidiary or affiliate.[14]

Alternatively, compliance with Australian competition law needs to be considered by reference to Australian legal norms which now appear to depart from both economic orthodoxy and the approach of other legal systems.

[14] Whether an international parent carries on a business by, through or in conjunction with a local subsidiary was considered in *Bray v F Hoffman La Roche Ltd* (2002) 118 FCR 1; *ACCC v Yazaki Corp (No 2)* [2015] FCA 1304.