

THE IMPLICATIONS FOR AUSTRALIAN COMPANIES NAVIGATING THE NEW SECTION 46 MISUSE OF MARKET POWER TEST AFTER THE EUROPEAN COURT OF JUSTICE DECISION IN INTEL

INTRODUCTION

General Counsel and boards of large Australian companies may have been considering the practical implications of the new section 46 "effects test" in the *Competition & Consumer Act 2010 (Cth)* (**CCA**).

Under the European abuse of dominance test, a dominant undertaking has a "special responsibility" not to allow its behaviour to impair genuine competition. Arguably the new section 46 effects test could create a similar responsibility for companies which have a substantial degree of power in a market in Australia. However, the recent decision of 6 September 2017 of the Court of Justice of the European Union (**CJEU**) in *Intel Corporation v. European Commission* (C-413/14P) (**Intel Decision**), has made it clear that when a corporation has reasonable commercial explanations for its conduct, the Court (and Commission), must assess the competition impact of the conduct. This outcome should provide large Australian companies with some comfort that, notwithstanding some comments in the Explanatory Memorandum to the section 46 amending legislation, an Australian Court will not consider the matter based on inferring purpose alone, or in European competition language, by "object".

In this briefing we consider the implications of the amendments to section 46 in light of the Intel Decision and consider how large Australian companies and their boards should closely analyse their conduct and document their decision making process so as to ensure that both the Australian Competition and Consumer Commission (**ACCC**) and the Australian Courts, as with the Intel Decision, will need to closely examine the actual effect of their conduct in the market. Even if large Australian companies may, when the new section 46 takes effect, practically be argued to be under a "special responsibility" as in Europe because of their market position, they can still be well positioned to successfully implement, and if required, defend their legitimate business conduct.

Key issues

- On 23 August 2017 legislation to replace section 46 of the CCA received Royal Assent, though the new section will not take effect until other Harper Review related reforms are enacted. Replacing section 46 was one of the more controversial recommendations of the Harper Review.
- In recommending section 46 should be replaced, the Harper Review pointed to the benefits of ensuring that Australia's competition laws are consistent with that in other jurisdictions.
- The European law on abuse of dominance, the equivalent of Australia's section 46, creates a "special responsibility" on large corporations to consider the impact of their conduct. Arguably, as a practical matter, the new section 46 may create an equivalent responsibility in Australia as corporations with a substantial degree of market power will have to be mindful of the effect of their unilateral (own) conduct.
- This briefing provides guidance on practical steps to be undertaken by companies subject to the new section 46 test to seek to ensure regulatory compliance.

BACKGROUND

A wide ranging review of Australia's competition laws, the Competition Policy Review, known as the Harper Review, was completed in 2015. The Government is now in the process of implementing the recommendations from that Review which it has accepted. In this regard, the *Competition and Consumer Amendment (Misuse of Market Power) Act 2017 (Amendment Act)* received Royal Assent on 23 August 2017, though will not take effect until other amendments to the CCA, recommended by the Harper Review, become law.

The Amendment Act will replace the existing prohibition on the misuse of market power contained in section 46 of the CCA. Under the new section, a contravention will occur if a corporation that has a substantial degree of power in a market engages in conduct that has the purpose, or has or is likely to have the effect, of substantially lessening competition in that market or a related market. Significantly, and some would say controversially, the new test removes a number of elements from the existing section 46. There is no need – as exists under the existing section 46 – to show that the corporation took advantage of its market position or (if the anticompetitive effect is able to be demonstrated), that the relevant corporation *intended* the anticompetitive outcome. The Explanatory Memorandum for the Amendment Act also hints that the Australian Parliament may have intended to create a per se contravention for "inherently anticompetitive" conduct.

SECTION 46 AMENDMENTS

Australia's "misuse of market power" prohibition in section 46 of the CCA has historically been considered to have a narrower scope than Europe's equivalent "abuse of dominance" prohibition in Article 102 of the *Treaty on the Functioning of the European Union (TFEU)*. After much criticism by the small business community in Australia as to the ineffectiveness of the current section 46, the Harper Review recommended the replacement of the current test with what is commonly referred to as the "effects test" or the "SLC test" (see our briefing [here](#)). The Government agreed that section 46 should be replaced and the new section 46 regime, as provided for in the Amendment Act, is expected to become operative within the next six months (see our briefing [here](#)).

The scope of the abuse of dominance prohibition has also been in the spotlight in Europe. The European test requires the conduct to have an effect on competition. In the past, the relevant European authorities have taken the approach that certain conduct is so inherently anticompetitive that it should be considered to be prohibited under Article 102 of the TFEU, without needing proof or analysis of the actual economic effects in each case. This approach has now been overruled in the Intel Decision handed down on 6 September 2017 (see briefing [here](#) for an analysis of this decision).

The Intel Decision raises an interesting question – how would Australian courts decide a misuse of market power case based on equivalent facts under the new section 46? Would an Australian court be inclined to adopt the approach of the CJEU or could it adopt the approach suggested by the Explanatory Memorandum for the Amendment Act?

SECTION 46 OF THE CCA

The current section 46

The current section 46 test requires 3 elements to be satisfied:

- the relevant corporation has a substantial degree of market power;
- it has taken advantage of that market power to engage in conduct of the type described in the next dot point; and
- it has engaged in conduct for the purpose of a listed anticompetitive purpose, that is, eliminating/substantially damaging a competitor, preventing market entry or deterring or preventing competitive conduct, in any case, in any market.

The ACCC has had difficulty in succeeding in a number of section 46 cases. For example, in *Cement Australia*¹, while the ACCC was able to establish that Cement Australia had the relevant purpose, the Court held that Cement Australia had not taken advantage of its market power, as it would have engaged in that conduct even if it had not had market power. In other cases, the ACCC has satisfied the 'taking advantage' limb but has not been able to satisfy the 'purpose' limb, for example, in *Pfizer*²

The new section 46

Under the new section 46 test the ACCC will only need to establish:

- the relevant corporation has a substantial degree of power in a market; and
- it has engaged in conduct:
 - with the purpose of substantially lessening competition; or
 - which has the effect, or likely effect, of substantially lessening competition,

in either case, in that market or any other market in which the company supplies or acquires goods or services.

Purpose will remain a subjective test, but one that may be informed by objective factors. Purpose may be inferred from conduct. Paragraph 1.36 of the Explanatory Memorandum for the Amendment Act suggests that some forms of conduct, such as predatory pricing, should be considered "so inherently anticompetitive" that the ACCC and courts should conclude that the conduct could only possibly be engaged in for an anticompetitive purpose.³ The Explanatory Memorandum therefore suggests that it would be open to the Courts to interpret section 46 as creating a per se contravention for particular types of conduct, reflecting the approach that was rejected by the CJEU in the Intel Decision.

Under the alternative "effect or likely effect" limb, the Courts will look at the actual effect of the conduct and also will consider whether there is a "real chance" that the conduct in question will have a relevant anticompetitive effect. Economic evidence is likely to be used in determining the likely effect of conduct, requiring an objective analysis of the particular circumstances of the case.

¹ *ACCC v Cement Australia Pty Ltd* [2014] FCA 148.

² *ACCC v Pfizer* [2015] FCA 113 (appealed, judgment reserved as at 12 September 2017)); see also *Seven Networks Ltd v News Ltd* [2009] FCAFC 166.

³ Competition and Consumer Amendment (Misuse of Market Power) Bill 2016, Explanatory Memorandum, paragraph 1.36.

EUROPE'S TEST

Article 102

Europe's abuse of dominance test in Article 102 of the TFEU prohibits any conduct which amounts to an abuse by any undertaking of a dominant position in a market if it impacts trade between member states of the European Union (EU). Examples of abuse are given, such as the imposition of unfair purchase or selling prices or other unfair trading conditions, but what constitutes an abuse of a dominant position is not prescriptively defined. Case law has, over time, established the particular elements that must be satisfied to prove a breach of Article 102.

In the past, concern has been expressed that European regulatory authorities have taken a "form-based" approach, rather than requiring that evidence produced that the relevant conduct in fact breaches Article 102 (despite guidance from the European Commission on this issue⁴).

The Intel Experience

European Commission and First Instance Decision

In May 2009 the European Commission imposed a record fine of €1.06 billion on Intel for abusing its dominant position in the market for the supply of processing units. Intel had offered its customers conditional rebates. The Commission alleged those rebates incentivised equipment manufacturers to buy all, or almost all, of their inputs from Intel. This, in the Commission's view, had the effect of restricting trade in the EU. The Commission, and the General Court of the EU on appeal, found that the rebates were exclusivity rebates which, when granted by a dominant company (as was the case here), by their nature, made it difficult for other businesses to compete. Therefore this type of action, without an objective justification, breached Article 102. There was no need for evidence of actual impact on competition to be considered.

Intel appealed the decision to the CJEU.

Intel v European Commission – CJEU decision

In language similar to that used by the High Court of Australia in *Queensland Wire Industries v BHP* (1989) 167 CLR 177 (where Justice Deane said "the objective [of section 46] is the protection and advancement of a competitive environment") the CJEU noted that not every exclusionary effect is necessarily detrimental to competition. In particular, competition "may by definition, lead to the departure from the market or the marginalisation of competitors that are less efficient and so less attractive to consumers from the point of view of, among other things, price, choice, quality or innovation".

The CJEU then went on to state that: "However, a dominant undertaking has a special responsibility not to allow its behavior to impair genuine, undistorted competition on the internal market (see, inter alia, judgments of 9 November 1983, *Nederlandsche Banden – Industrie – Michelin v. Commission*, 322/81, EU: C:1983:313, paragraph 57, and of 27 March 2012, *Post Danmark*, C-209/10, EU C:2012:172, paragraph 23 and the case law cited).

The CJEU held that the General Court erred in not analysing the evidence put forward by Intel as the Commission had considered Intel's arguments and

⁴ European Commission, *Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings*, (2009/C 45/02)

therefore the General Court had wrongly failed to take into consideration Intel's line of argument as to alleged errors by the Commission in its assessment. Where the relevant company submits, during the investigation, on the basis of supporting evidence, that its conduct was not capable of restricting competition, the Commission was required to assess the entity's market position, the structure, duration and market coverage of the challenged practice, as well as whether there existed a "strategy to foreclose equally efficient competitors". While the precise scope of this assessment is somewhat ambiguous, the ruling is clear that the Commission cannot in those circumstances treat the particular conduct as a per se breach of Article 102. The CJEU sent the case back to the General Court for reconsideration.

The CJEU's reference to the relevance of a "strategy to foreclose equally efficient competitors" might be useful in guiding the application of the purpose test in the new Australian section. While the ruling is open to different interpretations, it is likely that the CJEU intended to bring the law on exclusivity rebates in line with the existing test for predatory pricing under EU competition law. Under that test, it will normally be the case that pricing is only considered abusive if it is below the dominant company's "average avoidable cost" (broadly comparable to the average incremental costs incurred by the dominant company in providing the relevant volumes). However, if there is evidence of an anticompetitive intent – a "strategy to foreclose" – then the dominant company is held to a stricter standard and may be held to have committed an infringement if its pricing is above its average avoidable costs but below its "long run average incremental costs" (broadly equivalent to its average total costs, that is, taking into account fixed costs as well as incremental costs). Applying that concept to section 46 would mean that, even where there is some evidence of an anticompetitive purpose (for example, from internal documents of the relevant company), there must still be an assessment of the effects of the company's conduct. But, as a practical matter, in assessing those effects the company will be held to a higher standard than if there was no evidence of an anticompetitive purpose.

HOW WOULD AN EQUIVALENT CASE BE CONSIDERED IN AUSTRALIA?

Even though the Intel Decision limits the ability of the European Commission (and other relevant European regulators and Courts) to treat certain conduct as breaching Article 102 without analysing the impact of that conduct, it is worth considering how the conduct will be assessed in Australia under the new section 46.

It has always been the case that, if a party cannot provide evidence of its purpose for particular conduct, the Courts may infer an anti-competitive purpose. As mentioned previously, the Explanatory Memorandum for the Amendment Act emphasises that it would be open to the ACCC and the Courts to interpret section 46 as creating a per se contravention for particular types of "inherently anticompetitive" conduct, by inferring the relevant purpose. The ACCC has issued a draft framework for misuse of market power guidelines, which suggests it will not adopt the approach suggested in the Explanatory Memorandum for the Amendment Act. Nonetheless, it may prove tempting in difficult investigations to assert that an anticompetitive purpose is made out by the very nature of the conduct itself rather than by requiring evidence of purpose (or effect). In this context, it is hoped that the Intel Decision will see the ACCC always examine the

competitive impact of the relevant conduct where the company provides a legitimate business justification for its conduct.

CONCLUSION

How the ACCC and the Australian Courts apply the new section 46 to conduct seen as "inherently anticompetitive" remains to be seen. To protect against unfavourable regulatory actions, companies that could be viewed as having a substantial degree of market power should carefully document the legitimate commercial reasons for, and pro-competitive benefits arising from, engaging in any conduct which could be considered to be anticompetitive, such as long term exclusivity agreements, rebate arrangements, differential pricing or declining to supply (including on certain terms and conditions). The effects of such conduct on the competitive process will also need to be considered.

Where there is any doubt as to whether conduct could substantially lessen competition, such companies should tread carefully and seek advice from their competition lawyers.

CONTACTS

Dave Poddar
Partner

T +61 2 8922 8033
E dave.poddar
@cliffordchance.com

Alice Bradshaw
Associate

T +61 2 8922 8507
E alice.bradshaw
@cliffordchance.com

Elizabeth Hersey
Senior Associate

T +61 2 8922 8025
E elizabeth.hersey
@cliffordchance.com

Holly Cao
Associate

T +61 2 8922 8098
E holly.cao
@cliffordchance.com

Mark Grime
Senior Associate

T +61 2 8922 8072
E mark.grime
@cliffordchance.com

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www.cliffordchance.com

Clifford Chance, Level 16, No. 1 O'Connell Street,

Sydney, NSW 2000, Australia

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