

Competition Law

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This review discusses developments arising from three recent decisions in the field of competition law.

The first is the High Court of Australia's decision in *NT Power Generation Pty Ltd v Power & Water Authority* [2004] HCA 48 ("NT Power"). That decision relates to the application of monopolisation laws in circumstances where there is a denial of access to a so-called "essential facility". The focus of the discussion of this case here is upon the "taking advantage" limb of the monopolisation test under s 36 of the Commerce Act 1986. This inquiry is of particular importance because it establishes whether there is a causal connection between the existence and relevant use of monopoly power.

The second topic is the Court of Appeal's discussion of the "purpose test", under Part II of the Commerce Act, in *ANZCO Foods Waitara Ltd v AFFCO NZ Ltd* (CA 181/04, 23 June 2005).

This review concludes with a discussion of the principles applying to the variation and revocation of authorisations, as enunciated in the Commerce Commission's most recent *OMV/Shell/Todd* ("Pohokura") decision (Decision 581, 2 June 2006).

Access to Essential Facilities

There has been a recent traffic in Australia of monopolisation cases that are of particular relevance to the New Zealand setting because the wording of s 46 of the Trade Practices Act 1974 (Cth) is identical to s 36 of our Commerce Act. Therefore, the Australian case law on s 46 is likely to be highly influential on the interpretation of s 36 of our Act. Indeed, in this context, the influence of the Australian case law on predatory pricing was discussed in the last "Competition Law" review; see [2005] NZ Law Review 267.

It will be recalled from that review that the central inquiry in determining whether there has been a "taking advantage" of market power for the

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purposes of s 36 is as follows: “[I]f a dominant firm is acting as a non-dominant firm otherwise in the same position would have acted in a market which was competitive it cannot be said to be using its dominance to achieve the purpose that is prohibited” (*Carter Holt Harvey Group Ltd v Commerce Commission* (2004) 11 TCLR 200, para 52). This inquiry has become known as the “counterfactual test”.

The most recent decision of significance on the subject of what constitutes “taking advantage” of market power is *NT Power*. The facts of that case were as follows. The Power and Water Authority (“PAWA”) in the Northern Territory is a vertically integrated enterprise. It has electricity generation facilities that it either owns or controls through contracts. PAWA also owns transmission facilities (which carry power of 33 kV and above) and distribution facilities (comprising low voltage electricity lines and related assets eventually leading into the meter box of each individual customer). Finally, PAWA is also a retailer of electricity.

In early 1998, NT Power acquired the gas-fired power station located at the Mt Todd Mine. NT Power decided to generate electricity from its surplus power at this station, and to sell that electricity to the general public and commercial users in Darwin and Katherine, in competition with PAWA. However, in order to be able to do this NT Power required access to PAWA’s transmission and distribution facilities. PAWA declined to deal with NT Power pending the anticipated imposition of an access regime that was expected to be introduced no sooner than April 2000.

This case therefore involved a denial of access to what has become commonly known as an “essential facility”. The “essential facilities doctrine” has its origins under United States antitrust law. It has been embraced internationally, with varying degrees of enthusiasm.

The following analysis of *NT Power* is in three parts, as follows. First, it is informative to provide an introductory overview of the United States essential facilities doctrine to inform upon the issues to be addressed. Next follows a review of the judgments in *NT Power*. Finally, consideration is given to the implications of that decision for New Zealand in relation to access to essential facility situations.

A *The essential facilities doctrine*

All firms, including monopolists, have a fundamental right to decide with whom they will deal. However, the right is not unqualified. Regulation has for the most part been introduced internationally to mandate access in key sectors, such as telecommunications and energy markets. Further, a specific monopolisation rule formulation has emerged under United States antitrust law to meet circumstances where a monopolist controls a facility or resource

that is “essential” in the sense that competitors must have access to it in order to compete with the defendant. It is an act of monopolisation for a monopolist in such a situation unjustifiably to deny competitors access upon fair terms and conditions to the facility or resource, where granting access is reasonably feasible and denying access is without countervailing competitive justification. The doctrine was first applied to railroad lines and has since extended to various facilities (often termed “bottleneck facilities”) ranging from electricity transmission lines and gas pipelines, to football and basketball stadiums.

The doctrine, and its formulation in the United States, is not free from controversy. Significant debate surrounds the origins of the doctrine; see, eg, Areeda, “Essential Facilities: An Epithet in Need of Limiting Principles” (1990) 58 Antitrust LJ 841. There is significant scholarship in the United States to the effect that the doctrine is both harmful and unnecessary and should be abandoned; see, eg, Areeda & Hovenkamp, *Antitrust Law* (2nd ed, 2002) 771c. But there is also the contrary view that the doctrine has a long and respected history as part of United States antitrust law, reflected by the fact that the courts have consistently recognised that the doctrine should be applied in appropriate, though limited, circumstances; see, eg, Pitofsky, Patterson & Hooks, “The Essential Facilities Doctrine Under US Antitrust Law” (2002) 70 Antitrust LJ 443. This debate will, no doubt, be reignited by the United States Supreme Court’s recent adverse comment on the doctrine in *Verizon Communications Inc v Law Offices of Curtis V Trinko LLP*, 134 S Ct 872, 881 (2004).

Notwithstanding this uncertainty surrounding access to essential facilities under United States antitrust law, it is nonetheless informative to review the previously recognised elements of the doctrine. It is generally acknowledged that the leading formulation of the essential facilities doctrine was articulated by the Seventh Circuit in *MCI Communications Corp v AT & T Co*, 708 F 2d 1081 (1983), cert denied, 464 US 891 (1983). The Seventh Circuit set out the following four matters that must be proved (p 1132):

- (a) control by a monopolist of an essential facility or resource serving the monopolist’s market;
- (b) a competitor’s inability practically or reasonably to duplicate the essential facility;
- (c) the unjustified denial of the use of the facility to a competitor; and
- (d) the feasibility of providing access to the facility.

A review of the elements of the *MCI* formulation provides some insights into matters that ought to be taken into account in the essential facility setting. The first two elements of the *MCI* formulation are of relevance to the market power threshold under s 36 and are, accordingly, beyond the scope

of the current discussion. The third and fourth elements, however, relate to matters that are the domain of the “taking advantage” inquiry, and therefore warrant some further comment. In particular:

- (a) It appears that denial of access may be justified. Alternatively, access may be denied on grounds of feasibility. Interestingly, a parallel rule of objective justification has also emerged under European Community law; see *Sealink/B & I Holyhead: Interim Measures* [1992] 5 CMLR 255, para 41.
- (b) There is little judicial guidance on when such justifications might apply. Notwithstanding conflicting authority on the point, it appears that it is no excuse to argue that competition will be unaffected by the defendant’s denial of access; see *Fishman v Estate of Wirtz*, 807 F 2d 520 (7th Cir, 1986). However, most courts have accepted that, even if there might be anti-competitive effects, the controller of an essential facility need not impair or compromise its own business to accommodate others. For example, the absence of spare capacity has been found as a ground to justify denial of access; see *City of Chanute v Williams Natural Gas Co*, 955 F 2d 641 (10th Cir, 1992), cert denied, 506 US 831 (1992).
- (c) It follows that access may be denied where there is no spare capacity. A contrary view would serve to deter investment. Presumably, the owner of a facility also cannot be compelled to increase capacity to enable the grant of access.
- (d) Other possible grounds for denial of access may include: (i) technical questions about the ability of the third party to properly access the facility; (ii) safety issues; and (iii) the financial status of the party seeking access.

B NT Power

Two of the judgments in *NT Power* warrant particular scrutiny. They are the minority decision of Finkelstein J in the Full Federal Court and the majority decision of the High Court of Australia, which followed the approach taken by Finkelstein J.

Finkelstein J first concluded that PAWA satisfied the market power threshold for s 46 to apply because it held a substantial degree of power in the transmission and distribution markets; see *NT Power Generation v Power & Water Authority* [2002] FCAFC 302, paras 142–156. He then proceeded, most significantly for present purposes, to explore whether PAWA had by its conduct of denying NT Power access to these facilities taken advantage of this power. He outlined two approaches. The first, which he described

as “unexceptional”, was the counterfactual approach as it has come to be known (paras 174–179). The second was the “different path” approach (para 180), which he traced back to the purpose test observations made by Deane J in *Queensland Wire Industries Pty Ltd v Broken Hill Pty Co Ltd* (1988) 167 CLR 177, 197–198. His approach to these two paths warrants some coverage.

Finkelstein J noted that the origins of the counterfactual test lay in the need to establish a nexus between the existence and relevant use of market power. This nexus was said to be determined by considering how the firm in question would have acted in a competitive market. There is nothing controversial in this approach. Indeed, it is consistent with the counterfactual approach endorsed by the Privy Council in relation to s 36 of our Act; see *Carter Holt Harvey*, para 52. What is of particular interest here, however, is Finkelstein J’s articulation of how the counterfactual test may apply to natural monopoly circumstances, such as those at issue in this case (electricity transmission and distribution), where the hypothetically competitive market will only ever be a fiction.

Finkelstein J made the following assumptions and predictions:

- (a) PAWA had the capacity to allow its infrastructure to be used by third persons;
- (b) there was (hypothetically) at least one other firm with a similar infrastructure that was located in substantially the same geographic region as PAWA’s infrastructure, and that other firm also had spare capacity available to third parties;
- (c) the hypothetically competitive market was also based on the assumption that both PAWA and the other firm would make their infrastructure available to third parties on reasonable terms and conditions; and
- (d) it was also assumed that, downstream, PAWA would lose retail business to an effective competitor for the supply of electricity.

Against this background, Finkelstein J concluded that PAWA would in a competitive market have provided NT Power with access to its infrastructure. There were two central reasons for this conclusion. The first was that a profit-maximising firm in a competitive market would not stand by and allow a competitor to provide transmission and distribution services. It would at the least contest the business. Second, PAWA would not be deterred from bidding for this business because such access would introduce competition downstream in the retail electricity supply market. The reason for this was that such retail competition would be faced whether or not PAWA granted access, because of the ability of the competitor to access the other firm’s hypothetical infrastructure. Accordingly, this counterfactual analysis

established that PAWA had taken advantage of its market power, because it would not have been rational for PAWA to deny access in a competitive transmission/distribution market situation.

Turning to the “different path” (which for convenience can be referred to as the “purpose exception”), Finkelstein J noted the alternative approach advocated by Deane J in *Queensland Wire*, which was based upon drawing an inference of use of market power from purpose. There Deane J found that Broken Hill Pty Co Ltd’s (“BHP’s”) refusal to supply Y-bar to Queensland Wire Industries (“QWI”) was for the purpose of preventing QWI from manufacturing fences in competition with a wholly-owned subsidiary of BHP. Deane J said: “In refusing supply in order to achieve that purpose, BHP has clearly taken advantage of that substantial power in the market” (p 198). Finkelstein J also noted that the High Court of Australia in *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd* [2001] HCA 13 appeared to endorse this approach, although it was emphasised that the Court in *Melway* saw the nature of the purpose and the particular circumstances in *Queensland Wire* to be important to any inferences that might be drawn from purpose. Indeed, it will be recalled from *Melway* that the Court pointed to the dangers of proceeding too quickly from a finding about purpose to a conclusion about taking advantage (para 31). Reliance for this proposition was, in fact, placed upon the decision of the Privy Council in *Telecom Corporation of NZ Ltd v Clear Communications Ltd* [1995] 1 NZLR 385, 402.

Finkelstein J saw this alternative approach as being of relevance to the present case because (para 180):

Just as BHP had the capacity to prevent QWI from becoming a manufacturer of star pickets in *Queensland Wire*, so here PAWA had the capacity to keep NT Power out of the electricity supply market. It had that power because it was the monopolist in the transmission and distribution markets. I regard the conclusion that PAWA used its market power in those markets to keep NT Power out of the electricity supply market as self-evident.

The reference here to the “self-evident” nature of these conclusions reflects that cases like *Queensland Wire* and *NT Power* are at one end of the factual spectrum. Obviously, QWI and PAWA had the ability to frustrate altogether downstream competition by reason only of their ability to refuse to supply an essential raw material (in *Queensland Wire*), and to deny access to infrastructure (in *NT Power*).

The majority of the High Court of Australia endorsed the approach taken by Finkelstein J. The key points made by the majority were as follows (paras 143–150):

(a) The hypothetical counterfactual approach outlined above was

favourably endorsed. PAWA had argued that this approach was flawed because it was based upon assumptions beyond the realms of reality. The High Court explained that earlier decisions that had cast some doubt on the use of hypothetical counterfactuals, such as *Melway*, did not say that unrealistic assumptions could not be made. Rather, the cautionary words previously sounded urged only the need for cogent analysis.

- (b) The High Court appeared to accept the cogency of the counterfactual analysis in an infrastructure case such as the present because, if such an approach were not open, it would be difficult ever to demonstrate that a firm whose monopoly power depended on infrastructure had taken advantage of its market power.
- (c) Finally, the alternative purpose approach derived from *Queensland Wire* was endorsed on the facts and in the circumstances of this case. PAWA's decision to deny access was made in the appreciation of its market power. PAWA's purpose to exclude NT Power from the retail electricity supply market could not have been achieved had it not been for the power vested in PAWA's infrastructure. The decision does not explore this issue in any detail because PAWA did not, apparently, direct any argument against this finding of Finkelstein J.

Interestingly, and for the sake of completeness, it can be noted that no reference was made in *NT Power* to the material facilitation test as a basis for finding the taking of an advantage. This test emerged from dicta in *Melway* (para 51) and is to the effect that it may be proper to conclude that a firm has taken advantage of market power where it does something that is materially facilitated by the existence of market power. The potential impact of this test is unclear. To the extent that case law has touched upon this issue since *Melway*, this serves to demonstrate that the material facilitation test is likely, in practice, to be subservient to, or absorbed as part of, counterfactual analysis; see, eg, *ACCC v Australian Safeway Stores Pty Ltd* [2003] FCAFC 149, paras 325–333.

C *Implications of NT Power*

A number of essential facilities cases have come before our courts. It will come as no surprise that the American essential facilities doctrine has been advanced in argument in these cases. The approach of the courts has been to say that it is helpful to have regard to the elements of the United States doctrine. However, not surprisingly, this United States doctrine has not been imported into our jurisprudence as a specific monopolisation rule formulation; see, in particular, *Union Shipping NZ Ltd v Port Nelson Ltd*

[1990] 2 NZLR 662, 704. (For further discussion of earlier New Zealand cases on this subject matter, see *Gault on Commercial Law* (looseleaf, c1994–) CA36.22–25.)

Prior to *NT Power*, it was difficult to express confidence in the use of the general counterfactual test as a cogent basis for assessing essential facility fact situations. The requirement of the test, to assume a parallel competitive network alongside a natural monopoly, is hypothetical to the point of creating an inherent unease in the use of such counterfactual analysis. However, *NT Power* does much to answer this concern. What precedent is *NT Power* likely to set in relation to the two rule formulations it addresses in relation to the “taking advantage” limb, namely (1) the counterfactual test, and (2) the purpose exception?

NT Power demonstrates that the counterfactual test can be applied to essential facility situations where straightforward factual assumptions may be made. Where, as here, it could be assumed that (1) the competitor’s network had spare capacity (because the incumbent had spare capacity), (2) access would be granted on reasonable terms and conditions, and (3) competition at retail was inevitable in the counterfactual setting, it logically followed that in this case it would not be rational for PAWA to deny access. The utility of the counterfactual approach could, however, become more problematic if these assumptions about spare capacity and the grant of access on reasonable terms and conditions could not be made. Will it always be the case that these assumptions can be made?

Presumably some guidance on capacity assumptions under the counterfactual can be taken from the justification considerations discussed above in relation to the *MCI* formulation. As it happens, justification or business rationale has been accepted as a relevant consideration in assessing the “taking advantage” limb of s 36 (*Carter Holt Harvey*, para 54). On this basis, it follows that where there is no spare capacity, it would be illogical to assume that it exists in the counterfactual. A contrary approach would potentially expose the controller of an essential facility to relief that will require the surrender of part of its business in circumstances where it had no spare capacity. Apart from the invasion of such relief upon private property rights, this outcome would also presumably require the controller of the essential facility to break existing contractual commitments. Surely, such an outcome cannot be considered appropriate.

Presumably, related assumptions arising from the *MCI* discussion above, such as concerns about the technical compatibility of access seekers, should also be taken into account in formulating counterfactuals. For example, the counterfactual should be fashioned to assume that an access seeker’s claim would be dependent on technical compatibility, compliance with proper safety standards, and the like. If an access seeker is not technically compatible with the incumbent’s network, it would make no sense to assume that such

concerns may be overcome because of assumed technical compatibility with a hypothetical alternative network.

Assumptions about the terms and conditions upon which access may be granted are also potentially problematic. The complexity of this issue is well illustrated by reference to those cases where the courts have been required to formulate an order where monopolisation has been found to occur. For example, in *Queensland Wire*, the High Court of Australia did not appear to hesitate in referring back to the Federal Court the issue of the price at which Y-bar should be set; see *Queensland Wire*, p 217.

Does counterfactual analysis allow for easy assumptions to be made that a hypothetical competitor to a monopolist (like PAWA) would grant access to its network on the same terms and conditions as the monopolist might apply to its vertically integrated operations (or others who may have been granted access)? Or is more detailed analysis required into what may be an appropriate assessment of the terms of access that may be expected in a hypothetically competitive market? It is difficult to answer this question in the abstract. Instinctively, where the facts permit, there is an attraction to the pragmatism of the former approach. If such an approach serves to establish liability, additional inquiries into terms and conditions in a hypothetically competitive market would appear to be superfluous. Where such easy assumptions cannot be made, more detailed analysis will be required into likely prices in a hypothetically competitive market. This task is achievable; see, eg, *Telecom v Clear*, pp 395–397.

It therefore follows that *NT Power* reflects that counterfactual analysis can provide the core framework for the assessment of the taking advantage limb under s 36 in an essential facility fact situation. Some cases may be more difficult to analyse than others. However, there should be a solution to most problem cases.

Much less reliance can be placed on the purpose exception. There are three main reasons for this:

- (a) The purpose exception is, in practice, likely to stand subservient to counterfactual analysis. For the moment our case law reflects that counterfactual analysis must necessarily be undertaken in all cases; see *Carter Holt Harvey*, para 60. Even if this requirement is relaxed and the test is applied only in circumstances where the analysis is cogent (as suggested by the High Court of Australia in *Melway*, para 52), the fact remains, and the case law to date reflects, that counterfactual analysis will apply in most, if not all, cases. Counterfactual analysis therefore forms the primary rule. Accordingly, the purpose exception will only provide an alternate rule. Findings under the counterfactual approach will presumably prevail over any contrary views that may be raised under the purpose exception.

- (b) The decisions to date reflect that the purpose exception will only apply in obvious cases where the findings are “self-evident”. The earlier discussion of *Queensland Wire* and *NT Power* reflects that the findings as to purpose were self-evident on the facts of those cases. The approach taken in other cases stands in contrast. For example, in *Melway* the High Court of Australia found that the purpose exception did not apply because it was not inevitable that Melway’s conduct would exclude the complainant from engaging in at least some form of competition (para 30).
- (c) The purpose exception must always, in any event, be applied with real caution because of the dangers of inferring the use of market power from findings as to purpose; see *Telecom v Clear*, p 402, and *Melway*, para 31.

Purpose

A purpose test appears as an element in each of the key restrictive trade practices provisions contained in Part II of the Commerce Act 1986. Contracts, arrangements, or understandings and covenants are prohibited if they have the purpose of substantially lessening competition in any market (ss 27 and 28). This purpose element is combined in both of these provisions with alternative tests of effect and likely effect. Other specific forms of coordination, namely exclusionary provisions and price fixing (ss 29 and 30), are likewise prohibited on the basis of a purpose test. In the case of monopolisation (s 36), the test of purpose stands alone: Has the relevant market power been taken advantage of for a prohibited purpose? The additional element of effect does not arise in the monopolisation context, because such a test would inherently run the risk of rendering unlawful legitimate competitive rivalry.

Accordingly, in the case of each of these provisions, the approach to the purpose test may be pivotal. It alone is a basis for determining liability. The approach to be taken in relation to purpose in each of these instances under Part II should be in parallel. No reason exists to suppose that the purpose inquiry should vary in any of these different contexts. Indeed, a contrary approach would do much to introduce unnecessary uncertainty; see *Commerce Commission v Port Nelson Ltd* (1995) 5 NZBLC 99-352, 103,774.

The purpose inquiry is typically problematic. Where, as is so often the case, the conduct in question is ambiguous, there is the obvious temptation to explore the defendant’s intent. The problems that attach to a subjective assessment of purpose are notorious. “Win at all costs” language is commonplace and suspect for liability purposes, particularly when it

will often be made by those not truly responsible for formulating strategy. On the other hand, a subjective approach to purpose may be helpful where there is clear evidence of non-sanitised strategic planning. An objective approach to purpose, on the other hand, which seeks to draw inferences from the defendant's conduct and surrounding circumstances, potentially involves problems of parallel magnitude, and also runs the risk of becoming a surrogate for competition analysis. For example, if a firm has power in a concentrated market, to which entry is difficult, intent may be too readily inferred where steps are taken to exploit advantages. (For further discussion of this issue, see Areeda, "Monopolization, Mergers and Markets: A Century Past and the Future" (1987) 75 Cal L Rev 959, 963–965.)

Against this background, it is hardly surprising that the courts have struggled with the approach to, and the reliance to be placed upon, purpose inquiries. The recent decision of the Court of Appeal in *ANZCO Foods Waitara Ltd v AFFCO NZ Ltd* (CA 181/04, 23 June 2005) is the latest pronouncement on this issue. The contrasting approaches of Glazebrook and William Young JJ on the question of purpose serve to provide the most thought-provoking exploration of the topic to date.

The relevant facts in relation to the Commerce Act issue in *ANZCO Foods* can be briefly stated. AFFCO, like other companies in the meat processing industry, has had significant excess capacity. Throughout the 1990s, this problem was addressed by way of industry rationalisation with plant closures. Where the sale of such plant occurred, encumbrances were typically registered to prevent the continued use of plant for meat processing purposes. In the present case, ANZCO bought land and plant from AFFCO situated at Waitara with a 20-year encumbrance. The land and plant was sold at a discount in recognition of this encumbrance. ANZCO's plans to use this facility for cooling, freezing, and storing meat, and for the production of small goods, resulted in AFFCO commencing proceedings to enforce the encumbrance.

The Commerce Act issue was whether enforcement of the encumbrance was precluded under s 28, which prohibits covenants having the purpose, effect, or likely effect of substantially lessening competition in any market. It was common ground that the Waitara encumbrance did not raise issues under the effect element of this s 28 prohibition. The Waitara plant accounted for around two per cent only of the North Island market for the procurement of livestock. Further, it was accepted that there were low entry barriers, and that competition in the market with or without the Waitara encumbrance would, after the short term, be unaffected (para 269). Accordingly, the potential application of s 28 was based solely upon the purpose element of that section.

There are two key discussion points in this case pertaining to the purpose test under s 28. The first relates to the well-trodden debate on whether

purpose is to be assessed objectively or subjectively. The second relates to the argument raised by William Young J in his dissenting judgment that there is no need to establish an actual or likely substantial anti-competitive effect for the purpose test to apply. For convenience, this approach is referred to below as the “per se purpose approach”.

A *Objective and/or subjective?*

There have been fluctuating views on whether the purpose test is objective or subjective. There is conflicting Australian authority in relation to parallel legislation, the Trade Practices Act 1974 (Cth). Some early cases took the approach that the test is objective. But more recent, and now the bulk of, Australian authority takes the approach that a subjective approach should be taken to the purpose test; see *Gault on Commercial Law* (looseleaf, c1994–) CA27.11.

A different emphasis has emerged under New Zealand case law. The Court of Appeal in *ANZCO Foods* reaffirmed the approach taken by Cooke P in *Tui Foods Ltd v New Zealand Milk Corporation* (1993) 5 TCLR 406, 409, namely, that an objective test is to be preferred, but that subjective evidence may also be taken into account. Glazebrook J understood Cooke P to be saying that evidence of subjective intent may be relevant in borderline cases where the assessment of objective purpose is inconclusive. Accordingly, Glazebrook J concluded that the test of purpose is “an objective one but evidence of subjective purpose can be adduced and taken into account in assessing objective purpose” (para 255). The other judgments did not address this point in any further detail, although it would appear that the Judges were at one on this issue. William Young J referred to the subjective assessment of purpose as having a “supplementary role” to play to the objective assessment of purpose (para 146).

So, in contrast to the position taken in Australia, an objective approach holds centre stage in New Zealand, with subjective purpose coming to the rescue where necessary. However, ultimately, this technical distinction may not be all that important. That has been the view of the Court of Appeal. Gault J observed in *Commerce Commission v Port Nelson Ltd* [1996] 3 NZLR 554 that the distinction is unimportant in practice because “there will be very little difference in most cases between ascertaining subjective purpose by inference from what is said and done and ascribing objectively a purpose from evidence of what was said and done” (p 564). Parallel observations have been made in several recent decisions of the High Court of Australia; see *News Ltd v South Sydney District Rugby League Football Club Ltd* [2003] HCA 45 at para 44 per McHugh J, and *Rural Press Ltd v ACCC* [2003] HCA 75 at para 111 per Kirby J.

B *The per se purpose approach*

The conflicting approaches of William Young and Glazebrook JJ regarding the per se characteristic of the purpose test are based upon two valid points of view, which can be described as follows:

- (a) If the establishment of the substantial lessening of competition limb of s 28 is insisted upon in all cases, this will effectively render the purpose element of the section redundant.
- (b) A per se approach to s 28 will effectively result in the substantial lessening of competition element being read out of the section.

William Young J advocated a per se approach to purpose under s 28. He reached the conclusion that he was “satisfied that there is no logical inconsistency between concluding that a covenant which has not been established to have had an actual or likely substantial anti-competitive effect may nonetheless be held to have had the purpose of substantially lessening competition” (para 153). Further, he thought that while the question of competitive effect is “necessarily relevant”, that matter did not necessarily control the application of the purpose test (para 154). William Young J’s reasoning for this approach appears to be based on three main threads, as follows:

- (a) An unduly rigorous application of an objective test of purpose would simply be to equate the test of “purpose” with “effect” or “likely effect” (paras 145 and 147).
- (b) The need to prove substantial anti-competitive effect or likely effect should be relaxed because of the uncertainties, expense, and imperfections in trying to assess this very issue (para 152).
- (c) It was more likely than not that the covenant had the proscribed purpose, as otherwise there was no point in accepting the shortfall on sale, which was the correlative of the covenant (para 154).

The contrasting approach taken by Glazebrook J (with which Anderson P concurred) was (para 257):

[T]he purpose that must be proved for ss 27 and 28 is one that has, as an end in view, the substantial lessening of competition in a market. Where it is obvious that that could not be achieved if the provision or the covenant were implemented then, assessed objectively, the provision or the covenant cannot have that purpose.

Glazebrook J responded to the three matters above that were raised by William Young J as follows:

- (a) The weight of authority supports an objective approach to purpose, with subjective analysis playing only a secondary role, as noted above. Further, anything other than an objective approach to purpose would subvert the application of per se provisions, such as ss 29 and 30 (para 260). Glazebrook J's views on the appropriateness of the application of an objective approach in this case were also presumably coloured by her various references to the fact that "it is difficult to see how AFFCO could rationally have thought it could lessen competition in the whole North Island (let alone to do so substantially) by not allowing a competitor to use a site that accounted for such a small proportion of the market" (para 279).
- (b) Glazebrook J considered that William Young J's concerns over the litigation risks were misguided (para 262). Such an approach could inappropriately prohibit conduct simply because of difficulties of evaluation or proof. This case, involving as it did no substantial lessening of competition in the market, would be such a case in point. Glazebrook J observed that it would be wrong to regulate wishful thinking that could in fact objectively have no anti-competitive effect.
- (c) Finally, rather than merely assuming purpose because the shortfall on the sale price was a correlative of the covenant, Glazebrook J undertook detailed competition analysis (paras 266–294) and arrived at the conclusion that competition was unaffected by the encumbrance. Glazebrook J accepted that AFFCO must have been aware that this encumbrance would have minimal, if any, effect on the market. It was therefore not possible to attribute a purpose to AFFCO (either objectively or subjectively) that this encumbrance could result in any substantial lessening of competition. Therefore, Glazebrook J concluded, it would in these circumstances be wrong to impose the kind of per se rule that would logically flow out of the approach suggested by William Young J (para 278).

Which approach is to be preferred? On balance, the approach of Glazebrook J is to be preferred for the following reasons.

- (a) The structure of s 28 does not entitle a severance to be drawn between the purpose and substantial lessening of competition limbs of the provision.
- (b) It follows that the Act does not seek to impose liability in the s 28 setting without the establishment of the substantial lessening of competition threshold.
- (c) Section 28 is not structured in the manner of the other so-called per se provisions, such as s 30, where competition effects are deemed

to occur by virtue only of the establishment of certain conduct. Provisions such as s 30 do not beg competition analysis, whereas provisions such as s 28 (and s 27) clearly do. Accordingly, a per se approach to the purpose element of s 28 is unintended within the scheme of the legislation.

- (d) While it is true that the competition threshold inquiry under s 28 may in one sense render redundant the purpose test in favour of the effects test, this concern is outweighed by the uncertain nature and application of a per se purpose test, and the risk of false positives. As already noted, the scheme of the legislation is not to contemplate the imposition of liability if no substantial lessening of competition is likely to occur (or can be deemed to occur by virtue of per se provisions such as s 30).

Variation and Revocation of Authorisations

Applications for the authorisation of restrictive trade practices have been few and far between. Consequentially, the powers of variation and revocation of authorisations under s 65 have seldom been at issue. For this reason, the recent *Pohokura* decision assumes particular significance. This decision is the first occasion on which detailed consideration has been given to the operation of s 65. The Commission's earlier consideration of s 65 in *NZ Kiwifruit Exporters Association (Inc)/NZ Kiwifruit Coolstores Association (Inc)* (1989) 2 NZBLC (Com) 104,513 provided little in the way of guidance.

A Background

In September 2003, the Pohokura joint venture parties (OMV, Shell, and Todd) obtained authorisation to jointly market and sell all natural gas produced from the Pohokura field; see Commerce Commission, Decision 505, 1 September 2003. The Commission found that the practice of joint marketing was likely to result in a substantial lessening of competition when compared with separate marketing (paras 424–450). The practice was nonetheless authorised on the basis of countervailing public benefits (paras 451–516). The primary benefit was that of early production from the field. It was argued that there would be delays in negotiating all necessary arrangements to support separate marketing. The applicants used a three-year time delay for the purpose of assessing benefits in the application. They argued that this was a conservative likely time delay because, on more detailed analysis, the potential delay could be up to six years (para 328). In undertaking this assessment of the time delay, the applicants submitted

that a final investment decision for development of the field could only be made in mid-2004 if there was joint marketing of all gas from the field. The Pohokura joint venture predicted that, under separate marketing, the likely date for the final investment decision would not be until mid-2010. A matter of particular uncertainty surrounding separate marketing was the need, under this scenario, for the Pohokura joint venture parties to negotiate and conclude a gas-balancing agreement. No such agreement had been previously negotiated in New Zealand and, in the absence of a spot market for gas, it was anticipated that gas-balancing arrangements would not be straightforward.

The Commission rejected the three-to-six-year time delay assessment and instead concluded that joint marketing was likely to bring the field into production just one year sooner than would be the case under a separate marketing scenario (para 338).

The Commission accepted that, even on the basis of a one-year time delay, the benefits of early production were substantial in circumstances of limited and diminishing gas supplies. In particular, it was accepted that early gas production was important to ensure that new electricity generation projects could proceed in a timely manner in order to meet growing economic demand for electricity (paras 452–495). The Commission also accepted other likely benefits of earlier joint production. These included lower production and transaction costs, the more efficient depletion of the field, and an increase in exploration incentives (para 514).

Events took a different turn in 2004. In April 2004, each of the Pohokura joint venture parties announced that they proposed to enter into contracts to separately market the tranche 1 gas from the Pohokura field. Further, the final investment decision to develop the field was made in June 2004, and the anticipated date for first production of gas under this separate selling scenario was the same as the previously anticipated start date under joint marketing.

It was against this background that the Commission proceeded to consider whether it should revoke the authorisation, pursuant to the powers contained in s 65. The particular concern raised by the Commission was that the nexus between joint marketing and early production no longer appeared to exist.

There are two key inquiries under s 65. The first is whether the Commission has jurisdiction to invoke the powers under s 65. The second relates to the exercise of the discretionary powers under s 65. The remaining parts of this review trace the principles and analysis that emerge from the *Pohokura* decision in relation to these inquiries.

B Jurisdiction

There are various grounds upon which the Commission may invoke the powers of variation or revocation under s 65(1). The two at issue in *Pohokura* were whether:

- (a) the authorisation was granted on information that was false or misleading in a material particular (s 65(1)(a)); and
- (b) there had been a material change in circumstances since the authorisation was granted (s 65(1)(b)).

The Commission placed primary reliance upon the material change of circumstances limb of s 65(1) and, accordingly, this is an appropriate place to begin the discussion on jurisdiction.

The analysis of the change in circumstances in this case was not straightforward, because the authorisation related to a gas field that had not yet been brought into production. Further, the tranche 1 gas (the subject of the separate contracts) had yet to be delivered, and the prospect remained that the joint marketing of the remaining gas may still provide the most efficient and optimum way in which to develop the balance of the field. Therefore, the authorisation was not “dead letter”, even if the proposed separate marketing of tranche 1 gas did eventuate.

The subject matter of s 65(1)(b) relates most obviously to changes in market circumstances. This is demonstrated by the Australian cases that the Pohokura joint venture parties and the Commission endeavoured to rely upon. For example, in *Re Media Council of Australia* (1996) ATPR 41-497, the Australian Competition Tribunal relied upon changes in market structure and conduct between 1978 and 1996 as the basis for finding a change in circumstances (pp 42,268–42,271).

The Commission’s approach in *Pohokura* was to rely entirely upon *Media Council* for the finding of a material change of circumstances, without discussion as to the different context of this authority (paras 42–43). The Commission was non-responsive to the arguments advanced that the reference to a change in circumstances in s 65 was intended to apply only to factors that are exogenous of the authorised contractual arrangement. The Commission’s ultimate finding was that the material change of circumstances in the present case related to “the need for joint marketing and sale of gas, which was proposed as crucial to achieving the benefits of early production” (para 43). Accordingly, the Commission’s approach to material changes of circumstances is expansive and extended in this case to changes in the proposed contracting arrangements of the applicants. There is some authority in *Media Council* to the effect that “circumstances is a word of wide import which includes all facts, matters and conduct relevant to an authorisation and

to a revocation” (p 42,240). However, the Commission did not endeavour to explain in *Pohokura* how the contracting arrangements of the joint venture parties themselves came within the import of this formulation.

The Commission’s approach to the second ground for jurisdiction is more problematic. The *Pohokura* decision records that the Commission alleged in the Draft Determination that the applicants provided false or misleading information so far as they indicated that the final investment decision could only be achieved by 2004 with joint marketing (para 32). The Draft Determination made no reference to relevant case-law principles regarding what may be false or misleading in circumstances where, as here, the parties were merely making predictions as to the future. Further, the allegation was surprising given that two independent experts, including the Commission’s own independent expert, had made predictions in line with those of the applicant (paras 50 and 58).

The *Pohokura* joint venture parties argued that the reference to “false or misleading” information contained in s 65 could be informed by reference to case law under the Fair Trading Act 1986. This was hardly surprising given the legislative origins, and the supplementary nature, of the Commerce Act and Fair Trading Act; see Pengilly, “The New Zealand Fair Trading Act: The Likely Impact of the Law and Commercial Conduct in Light of Australian Experience” [1987] NZLJ 59, 60. Further, it is apparent from the case law to date that the courts are unlikely to be persuaded that there are material differences where parallel matters are at issue under these two statutes; see, eg, *Giltrap City Ltd v Commerce Commission* [2004] 1 NZLR 608, 623.

The case law in point under the Fair Trading Act is to the following effect (*Commerce Commission v Chalmers* (1990) 3 TCLR 522, 553):

- (a) the Commission should be slow to infer that because the representation as to future events has turned out to be wrong it must therefore, and for that reason alone, have been misleading; and
- (b) representations as to future events will not be false or misleading if
 - (i) there is a proper basis for them, (ii) they are based on views that are honestly held, (iii) they are made by an appropriate expert, and
 - (iv) they are based on rational grounds involving an application of the relevant expertise.

Against this background, the following problematic aspects emerge from the Commission’s analysis of s 65(1)(a) in *Pohokura* (paras 48–51):

- (a) It is asserted that the words “false or misleading” in s 65 stand in a materially different statutory context to those words as they appear in s 9 of the Fair Trading Act. No reasons are given to support this proposition. (As it happens, the term “false or misleading” does not

appear in s 9 of the Fair Trading Act, as the Commission asserts (para 48). Rather, this phrase appears in s 13.)

- (b) The Commission then proceeds to conclude that the words “false and misleading” under s 65 mean “untrue or misleading in fact and does not necessarily import any element of deliberate falsehood or intent to mislead” (para 49).
- (c) Notwithstanding the introduction of this framework, the Commission does not then proceed to find that false or misleading statements were made because these statements turned out in time to be untrue in fact. Rather, the Commission’s ultimate conclusion is (para 51):

[T]he Commission considers that in this case there existed an objective basis for the one year [delay] forecast ... The Commission considers, however, that if it is wrong, and there was not an objective foundation for the information at issue at the time, the information can be properly regarded as “false or misleading” in terms of section 65(1)(a).

The Commission’s findings therefore appear to be in accord with the approach outlined in *Chalmers*. Against this background, it is difficult to understand the Commission’s formulation of principles that are not in harmony with *Chalmers*. The Commission’s approach to this issue, therefore, leaves considerable room for uncertainty about the meaning to attach to the reference to “false or misleading” under s 65. It is submitted that s 65 does not invite an approach contrary to that suggested in *Chalmers*.

C *Exercise of the discretion*

Assuming that the Commission has jurisdiction, s 65 confers various discretionary powers upon the Commission to revoke, amend, or substitute an existing authorisation. The approach taken by the Commission to this task appears to be non-controversial. The Commission considers that the exercise of its discretionary powers under s 65 involves the potential selection of one of four possible outcomes, as follows (paras 64–65):

- (a) *Revocation of authorisation*. This is appropriate where the benefits of the conduct in question no longer outweigh their detriments (para 72).
- (b) *Amendment of the authorisation*. An amendment may be appropriate where the conduct in question and its associated benefits and detriments have only changed in a minor way, such that the benefits of the authorisation will continue to outweigh their detriments (para 71).

- (c) *Revocation and the grant of a substituted authorisation.* This approach may be appropriate where there are significant changes in respect of the authorised conduct. However, these changes may not be of such magnitude as to fundamentally change the existing authorisation (para 73). It will, presumably, in some cases be difficult to assess the dividing line between a substituted and a new authorisation set of circumstances. However, this dividing line may not be of great moment. In the borderline case where such doubt arises, there may not be much difference in the compliance costs involved in pursuing a new or a substituted authorisation.
- (d) *The status quo, leaving in place the original authorisation.* If the benefits and detriments remain essentially the same as applied under the original authorisation, it will be appropriate to leave the authorisation in place (para 74).

The Commission accepted that it should apply standard authorisation analysis in determining the exercise of its discretionary powers under s 65 (para 82). Therefore, a comparative assessment is required of the factual (that is, revocation or an amended or substituted authorisation) and the counterfactual (which will be the continuation of the authorisation in place). The essence of the Commission's analysis in *Pohokura* was that revocation was justified because it would be likely to result in a greater amount of separate marketing than would occur under the counterfactual (paras 108–143).

D *Some remaining questions*

Authorisation analysis is seldom straightforward. Predictions and assumptions must be made that are inevitably open to question, and which can ultimately be proven wrong. In this context, three questions that arise in the present case are:

- (a) A centre-point of the Commission's analysis is that the market will be more competitive under separate rather than joint marketing of gas. Presumably, the Commission remains of the view that it held in Decision 505 that joint marketing would be likely to lead to higher prices than would occur under separate marketing (paras 429 and 444). But if this assumption is correct, why has there been separate marketing of the tranche 1 gas? Market developments since Decision 505 appear to call into question the Commission's central theory of the case, namely, that prices will be higher under joint marketing. The apparent problems with this theory of the case are not explored in this revocation decision.

- (b) While separate contracts have been entered into for the tranche 1 gas, no gas-balancing agreement had been negotiated at the time of revocation of the authorisation. Therefore, there are certain risks in drawing assumptions, as the Commission has done, that these separate contracts will be performed. If there were a need to revert to joint marketing to achieve development of the field, this would most likely result in the need to duplicate compliance costs with a further authorisation application. If events were to unfold in this way, there would be delays to field commencement, and significant economic harm as a result.
- (c) It is not necessarily clear that there will be much difference in the volumes of separate sales (assuming that separate delivery does occur) under the factual and counterfactual. The Commission assumed in the counterfactual that all gas produced after 2012 would be jointly sold (para 111). This assumption is clearly open to question, given that the Commission assumes that the separate contracts for tranche 1 gas will be performed.

The answers to these questions will, no doubt, become apparent to those who will have the benefit of hindsight.

