

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

Working Party No. 3 on Co-operation and Enforcement

ROUNDTABLE ON CARTELS INVOLVING INTERMEDIATE GOODS

-- Australia --

27 October 2015

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*More documents related to this discussion can be found at:
www.oecd.org/daf/competition/cartels-involving-intermediate-goods.htm*

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HYPOTHETICAL SCENARIO AND SUGGESTED QUESTIONS

-- Australia --

Introduction

1. The Roundtable uses the hypothetical example of a cartel relating to the sale of Component X (made in Country A) when incorporated into a consumer good (in Country B), which is sold to end consumers (in Country C). The Roundtable seeks to examine how the enforcement response of members' competition authorities would depend on whether they are located in Country A, Country B or Country C.
2. Australia's cartel provisions under the *Competition and Consumer Act 2010* (CCA) give rise to criminal or civil penalty liability for '*making*' a cartel, and separately for '*giving effect*' to a cartel, in Australia. The CCA extends jurisdiction to conduct engaged in outside Australia by those incorporated or carrying on business in Australia, and by Australian citizens or residents.
3. Even if cartel conduct is susceptible to the provisions of the CCA, there are circumstances in which the Australian Competition and Consumer Commission (ACCC) would exercise its discretion not to take enforcement action, even though cartels are an enduring priority of the ACCC. The ACCC exercises this enforcement discretion in accordance with its *Competition and Enforcement Policy*. Factors relevant to the ACCC's discretion include the level of harm in Australia, the educative or deterrent effect of ACCC action and the significance of the market.
4. Australia's submission is provided in the form of the attached table.

Application of CCA principles to the scenario when Australia is Country A, Country B or Country C

	Country A (where Alpha and Beta are organised, and where they manufacture, and agree to fix the price of, Component X)	Country B (where integrators have factories and incorporate Component X into finished electronic products)	Country C (where integrators sell finished products)
Liability (See Note 1)	<p>Alpha and Beta would be liable for 'making' the cartel agreement in Country A.</p> <p>Alpha and Beta would be liable if they did anything in Country A to give effect to the cartel e.g. they generated price lists there, which they sent to integrators in Country B.</p> <p>There would be no need to rely on extended jurisdiction under s.5 as the relevant conduct occurred in Country A (i.e. Australia).</p>	<p>There would be no liability for 'making' the cartel, if the cartel was made in Country A, unless:</p> <p>Alpha/Beta 'carry on business' in Country B (which would enliven extended liability under s.5)</p> <p>(under the alternative scenario) Alpha and Beta attended price-fixing meetings in Country B.</p> <p>Alpha and Beta would be liable if they did anything in Country B to give effect to the cartel e.g. they <i>addressed</i> communications to integrators to effect sales of Component X.</p>	<p>There would be no liability for 'making' the cartel, if the cartel was made in Country A, unless:</p> <p>Alpha/Beta 'carry on business' in Country C (which would enliven extended liability under s.5)</p> <p>(under the alternative scenario) Alpha and Beta attended price-fixing meetings in Country C.</p> <p>Alpha and Beta would be liable if they did anything in Country C to give effect to the cartel. Alpha and Beta may be taken to give effect to the cartel by discussing market conditions and tracking sales of finished products in Country C or (under the alternative scenario) by contacting finished product purchasers in Country C about Component X pricing.</p>
Factors relevant to the decision whether to bring enforcement action (See Note 2)	<p>The following are relevant to the decision to take enforcement action in Country A, when the harm of the cartel is mainly felt in Country B or C:</p> <p>The limited harm of the cartel in Country A is relevant, but not determinative, in the exercise of enforcement discretion.</p>	<p>The following are relevant to the decision to take enforcement action in Country B:</p> <p>The impact of the cartel in Country B. This will depend on the extent to which integrators absorb the overcharge (the scenario does not provide detail about product sales in Country B) and/or lose sales.</p>	<p>The following are relevant to the decision to take enforcement action in Country C:</p> <p>The impact of the cartel in Country C. This will depend on the extent to which:</p> <ul style="list-style-type: none"> -the integrators pass on the overcharge and it results in harm to purchasers of finished products in Country C, and -(under the alternative scenario) the extent to which the parent companies of the integrators (established in Country C)

Even if there is limited harm in Country A, deterring the making of cartel agreements will be important in Country A.

Whether enforcement action or private damages action has been taken in Country B or C for the same conduct.

Jurisdiction could readily be asserted over Alpha and Beta in Country A, where they are incorporated, for:

- serving originating process
- for exercising investigative powers, and
- the enforcement of penalties (they have assets in the form of factories).

Establishing the extent of this impact may be difficult – see Note 3.

Whether enforcement action or private damages action has been taken in Country A or C for the same conduct.

Logistical difficulties in asserting jurisdiction or investigating the conduct will influence the enforcement discretion, including the following.

-It will be necessary to serve originating process on Alpha and Beta overseas (leave of the court would be required for service outside the jurisdiction, which requires proof of a *prima facie* case); the Hague Convention on service abroad may assist the formalities. For criminal matters extradition is a possibility.

-Any investigative notice requiring documents/information would need to be served on Alpha and Beta (enforcement of such notices may not be practicable if the addressees are not amenable to Australian jurisdiction.)

-How readily relevant evidence will be available from other countries, including through international cooperation (e.g. gateways), or from a cooperating party. (For criminal matters mutual assistance arrangements would provide for use of compulsion when evidence gathering overseas; equivalent civil arrangements are less widespread.)

Whether any penalty awarded in Country B will be recognised and enforced against Alpha and Beta overseas.

suffer loss (their loss could relate to sales worldwide and potentially be the subject of regulatory action in other countries).

Establishing the extent of this impact may be difficult – see Note 3.

Whether enforcement action or private damages action has been taken in Country A or B for the same conduct.

Logistical difficulties in asserting jurisdiction or investigating the conduct will influence the enforcement discretion (the same as for Country B).

Whether any penalty awarded in Country C will be recognised and enforced against Alpha and Beta overseas (the same as for Country B).

(Competition penalties are not generally the subject of mutual recognition and enforcement although special arrangements exist for this between Australia and New Zealand.)

Factors relevant to penalty

In its public enforcement function the ACCC does not have the power to decide whether there has been a CCA contravention, nor the power to impose penalties or remedies. Instead, it investigates and brings appropriate matters before the Federal Court of Australia for determination, and if successful the Court assesses the penalty.¹ In addition to penalties it is common for Australian courts to order injunctive relief in the case of cartel conduct. Injunctions may extend beyond the geographical confines of Australia.²

The maximum penalties that may be imposed on a corporation for each separate contravention is the greater of \$10million, three times the benefit obtained directly or indirectly that is “reasonably attributable to the act or omission” or 10% of the annual turnover during the 12 months ending in which the act or omission occurred. In the case of criminal offences individuals may be imprisoned for up to 10 years.

In assessing the appropriate penalty, the Court has regard to the maximum penalty that may be imposed and then determines the penalty after taking account of the circumstances of the case and specifically a range of factors, including the nature and extent of the contravening conduct, the size of the contravener, the deliberateness of the conduct, the period over which it extended, whether it involved senior management, whether it has a corporate culture conducive to CCA compliance, whether the contravener has cooperated with the authorities, whether it has engaged in similar conduct in the past, the effect on the functioning of the market and other economic effects of the conduct, and whether the conduct was systematic, deliberate or covert.³ In criminal matters a court must impose a sentence that is of a severity appropriate in all the circumstances of the offence, and takes account of such of the following matters as are relevant: the nature and circumstances of the offence; other offences (if any) taken into account; any course of conduct of which the offence forms part; the personal circumstances of any victim; any resulting injury, loss or damage; the degree of contrition shown (e.g. by making reparation); the extent of any failure to comply with pre-trial or ongoing disclosure in the proceedings; whether a guilty plea was entered; the degree of cooperation with law enforcement agencies in the investigation of the offence or of other offences; the deterrent effect that any sentence may have on the person; the need to ensure that the person is adequately punished for the offence; the character, antecedents, age, means and physical or mental condition of the person; the prospect of rehabilitation; and the probable effect that any sentence would have on any of the person’s family or dependants.⁴

¹ A recent case ruled that the practice of prosecutors providing submissions on the bounds of available sentences should cease (*Barbaro v The Queen* [2014] HCA 2). This is because a judge can only act upon the law and the evidence – submissions about the appropriate penalty are statements of opinion, and submissions cannot be used to supplement evidence by opinion. In *FWBII v CFMEU* [2015] FCAFC 59 the Full Federal Court concluded that the same principle applies to all civil penalty matters. In light of this development, it may not be appropriate to speculate about the practice of the Federal Court in relation to penalty assessment unaided by parties’ submissions.

² See for example *ACCC v Chen* [2003] FCA 897 [2003] FCA 897.

³ These factors were developed in *Trade Practices Commission v CSR Ltd* (1991) ATPR 41-076 (TPC v CSR) at 52,152-52,153, *NW Frozen Foods Pty Ltd v ACCC* (1996) 71 FCR 285 and *J McPhee & Son (Aust) Pty Ltd v ACCC* (2000) 172 ALR 532.

⁴ *Crimes Act 1914*, Part IB, Division 2.

Significance of sanctions in other jurisdictions (See Note 4)

The main connections with Country A are that it is where the cartel was made, and it is where the participants are based. Since there is no apparent harm in Country A, if a deterrent sanction is imposed in another jurisdiction there may be less need for deterrence in Country A.

This may justify a decision to take no enforcement action.

Such a decision would be assisted by an injunction granted in Country C, which extended to Country A, to prevent further cartel activity.

If enforcement action is taken in Country C on the basis that this is where cartel harm primarily occurred, it would be appropriate to determine whether the same harm has been the subject of penalties in another jurisdiction.

In principle the question of overlap should not arise where:

sanctions in Country B are based on harm occurring there to integrators on their worldwide sales of finished product incorporating Component X, to the extent that the integrators absorbed the cartel overcharge and/or lost sales, and

sanctions in Country C are based on harm occurring there on the sale of finished products to end users, to the extent that the cartel overcharge was not absorbed but passed on.

However, if sanctions in Country C address the loss incurred by the integrators' parent companies in Country C (through their interest in the integrators) then there is likely to be overlap with sanctions in Country B, to the extent that both relate to the absorption of overcharge by the integrators and/or lost sales. The loss incurred by integrators and their respective parents would not be coterminous but the sanctions in both countries would still relate to the same absorption of cartel overcharge and/or lost sales.

There would arguably be no need for sanctions to be imposed in Country B, in respect of the integrators' loss in absorbing the cartel overcharge and/or lost sales, if sanctions in Country C took account of this when addressing the harm to the parent companies in Country C.

See Note 4.

*Notes***1. Primary and extended liability under the CCA**

5. The CCA prohibits the ‘making’⁵ or ‘giving effect’⁶ to a cartel in Australia. Any act or thing done in accordance with a cartel agreement will be ‘giving effect to’ the cartel agreement. For example, if a cartel agreement is made in Country A in relation to the manufacture or sale of Component X, and that component is then sold into Australia by a cartel member, the courts would regard the cartel as having been given effect to in Australia.

6. Section 5 of the CCA extends the territorial coverage of the CCA’s competition law provisions to conduct engaged in outside Australia by those incorporated or carrying on business within Australia, Australian citizens, or individuals ordinarily resident within Australia.⁷

7. Whether a corporation is carrying on business in Australia is a question of fact.⁸ It is not necessary for it to have a place of business in Australia. However it must be engaged in business activities on a continuous and repetitive basis within Australia.⁹ Relevant activities may include product sales in Australia,¹⁰ and may include invoicing or receiving payment directly from Australian customers, but more decisive would be physical activity in Australia.¹¹ Negotiations in Australia for the sale of products, or advertising in Australia may also suffice. The relevant time for carrying on business in Australia is the date of the contravention.¹²

2. Factors relevant to deciding whether to bring enforcement action

8. Of primary relevance to the decision to bring enforcement action is the extent of any harm from the cartel in Australia. The rationale is provided by section 2 of the CCA, which states that the object of the CCA is to enhance the welfare of Australians through the promotion of competition and fair trading and provisions for consumer protection.

⁵ CCA s. 44ZZRF (criminal offence); s. 44ZZRJ (civil penalty liability). Note there is an exemption for export cartels. CCA s.51(2)(g) exempts contracts relating solely to the export of goods or supply services outside Australia, provided particulars are submitted to the ACCC within 14 days. The register is not open to the public.

⁶ CCA s. 44ZZRG (criminal offence); s. 44ZZRK (civil penalty liability).

⁷ Future reforms in the area of extended jurisdiction were recommended in the recent Competition Policy Review, chaired by Prof. Ian Harper. The Final Report was released on 31 March 2015. It recommended that s.5 be amended to replace the existing requirement with one that applies competition law to overseas conduct insofar as it relates to trade or commerce within Australia or between Australia and places outside Australia. The Government is still considering its response to the Report.

⁸ See e.g. *Norcast S.ár.L v Bradken Limited (No 2)* [2013] FCA 235 at paras. 254-255 per Justice Gordon: ‘carrying on a business generally involves conducting some form of commercial enterprise, systematically and regularly with a view to profit ... a company may be found to carry on business in Australia even though the bulk of its activities are conducted elsewhere’.

⁹ *Bray v Hoffman La Roche* [2002] FCA 243 (*Bray*) at paras. 62-63. See also *Paper Products Pty Ltd v Tomlinsons* (1993) ATPR 41-272 at 41 where French J found that the making of representations from the UK by telephone and facsimile to Australia constituted conduct in Australia.

¹⁰ *Bray* at para. 81.

¹¹ *Campbell v Gebo Investments Ltd* (2005) 190 FLR 209, para 31.

¹² *Bray* at para. 57.

9. The ACCC's *Compliance and Enforcement Policy* describes how the ACCC prioritises matters and exercises its discretion. The ACCC regards cartel conduct as so detrimental to consumer welfare and the competitive process that cartels will always be a priority. When dealing with international cartels, the ACCC will focus on pursuing cartels that have a connection to, or cause detriment in, Australia. ¹³

10. However, the fact that there is jurisdiction to take enforcement action against a cartel does not mean that the ACCC will always do so. For example, if the only connection to Australia is that cartel participants at the relevant time were incorporated there, or were Australian citizens/residents, but the conduct occurred and its effects were felt entirely outside Australia, it will generally be more appropriate to leave enforcement to other jurisdictions most directly affected. For example, the ACCC did not take enforcement action in relation to the price-fixing of dynamic random access memory (DRAM) products, which was the subject of action in other jurisdictions, and it did not pursue allegations of price fixing on fuel surcharges on transatlantic passenger services owing to the minimal effect in Australia. Nevertheless, the ACCC does give enforcement priority to matters that demonstrate conduct of significant public interest or concern to Australia, conduct resulting in substantial consumer detriment, and conduct demonstrating a blatant disregard for the law.

11. Furthermore, the ACCC is more likely to refer a criminal matter to the Commonwealth Director of Public Prosecutions (CDPP) for consideration for prosecution where: the conduct was covert; the conduct could or did cause large scale or serious economic harm; the conduct was longstanding or could have a significant impact on the market; the conduct could or did cause significant detriment to the public, or significant loss or damage to customers of the participants; the participants were involved in previous cartel conduct; senior representatives within the relevant corporation(s) were involved in authorising or participating in the conduct; the Government, and thus taxpayers, were victims (even where the value of affected commerce is relatively low); or the conduct involved the obstruction of justice or other collateral crimes. ¹⁴

3. Establishing the impact of a cartel overcharge

12. In the case of an intermediate good cartel, establishing where the impact of the cartel overcharge falls (producers of goods that incorporate the cartelised component, known as integrators, in Country B and/or end consumers in Country C) and how (lower margins, lost sales, higher prices, sub-optimal consumption patterns) will depend on a number of factors.

13. First, consider a scenario where the integrators in Country B are able to turn to an alternative source of supply (Country D) for the components. If this alternative source were no more costly than the pre-cartel components from Country A, then there would be no, or only temporary, pass through of the cartel prices. Furthermore, the cartel would seem futile and would likely quickly collapse.

14. If the alternative source of the components was more expensive or otherwise inferior compared to the pre-cartel components from A, but cheaper than the cartelised price, the integrators in Country B would have higher costs (whether from the new source or from the cartelists rationally adjusting their cartel price in light of the price and quality of supplies from Country D).

¹³ 2015 ACCC *Competition and Enforcement Policy*, p.3.

¹⁴ *Memorandum of Understanding between the Commonwealth Director of Public Prosecutions and the Australian Competition and Consumer Commission regarding Serious Cartel Conduct*, signed 15 August 2014. See also *Prosecution Policy of the Commonwealth: Guidelines for the Making of Decisions in the Prosecution Process*.

15. The extent to which the integrators in Country B would be able to pass this through to consumers in Country C would depend on the price elasticity of demand for their final product in Country C - that in turn would depend on both the extent of competition in Country C from other sources of the final product (e.g. integrators in Country E), which have access to a cheaper source of components and the extent to which consumers would switch to substitute products.

16. The end result in all these cases would likely be some reduction in sales of the final good produced by integrators in Country B to consumers in Country C, unless final demand for the integrators' product is completely price inelastic (which is rare). End consumers in Country C are likely to face higher prices unless final demand for the integrators' product is completely price elastic (which, again, is rare). Consumer welfare will also be harmed to the extent that substitution in response to cartel prices results in second best choices and reduced consumer surplus (either by the integrators using inferior components or by consumers substituting to cheaper but less valued products).

17. Now consider a scenario where the integrators in Country B are not able to turn to an alternative source of supply for the component. The same downstream variables influence where the impact of the cartel overcharge falls and how. That is, it would depend on the price elasticity of demand in Country C for products supplied by Country B, i.e. whether there are competing cheaper sources of the final product from integrators in Country E and the extent to which consumers would switch to substitute products.

18. As in the first scenario, the impact of the cartel will then be felt in some combination of lower sales and margins of integrators in Country B and higher prices and sub-optimal consumption choices for end consumers in Country C.

4. The significance of sanctions imposed by other jurisdictions in bringing enforcement action

19. The significance of sanctions imposed across different jurisdictions arose in the *Air Cargo* case, which concerned allegations of price fixing on the fuel surcharge element of the cost of air cargo transport services. The parties to the contraventions were multinational airlines operating throughout the world, for which Australia was not the focus of the contravening arrangements but merely one of many places directly affected by the conduct. The Court in the Qantas settlement accepted that the degree of connection to Australia was relevant to the quantum of penalty, and that it was appropriate to focus primarily upon the effects of a contravention in Australia. Surcharges imposed on flights to and from Australia were taken to have the most direct connection with loss or damage suffered by businesses or consumers in Australia. The fines imposed on Qantas in the US addressed flights to the US from all parts of the world, and from the US to all parts of the world. They therefore encompassed flights from the US to Australia and from Australia to the US. Having regard to the global nature of the market, the Court took into account the sanctions already imposed, or yet to be imposed on Qantas elsewhere, without putting a precise figure on how those sanctions were taken into account.¹⁵

20. In the *Animal Vitamins* cartel, where the same conduct was the subject of penalties in more than one jurisdiction, the Federal Court referred to a penalty imposed by the Federal Court of Canada as an indication that the level of penalty proposed by it was appropriate (based on the percentage which the penalty represented of the total affected sales).¹⁶ In the case of the *Marine Hose* cartel the Court was not able to use European Commission fines as a basis of comparison owing to the significant differences in the two regimes.¹⁷

¹⁵ *ACCC v Qantas Airways Ltd* [2008] FCA 1976 at paras. 39-42. The same approach was followed in *ACCC v British Airways PLC* [2008] FCA 1977 at 20.

¹⁶ *ACCC v Roche Vitamins Australia* [2001] FCA 150, para 44.

¹⁷ *ACCC v Bridgestone Corporation* [2010] FCA 584, at para. 48.