ACCC CASE THEORY TERMINAL

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Legal Briefings – By **Annalisa Heger**

***Update:** On 27 June 2019, the ACCC announced that it has lodged an appeal to the Full Federal Court against the Federal Court's decision. The ACCC stated that its appeal will focus on the ability of courts to accept undertakings given the ACCC's concerns about the ability of access undertakings to resolve competition issues arising from a merger.*

In July 2017, Aurizon and Pacific National entered into a number of agreements for the sale and purchase (or subcontract) of Aurizon's Acacia Ridge Terminal, its interstate intermodal business and its Queensland intermodal business. The ACCC alleged that in doing so Aurizon and Pacific National reached an understanding that had (or Pacific National's proposed acquisition of the Acacia Ridge Terminal would have) the effect or likely effect of substantially lessening competition.

Justice Beach of the Federal Court found that the ACCC failed in its case in relation to the subcontract as:

1. it was unlikely that Pacific National would have the ability to discriminate against a new entrant or that barriers to entry would be raised, given Aurizon's ongoing presence under the terms of the agreements; and
2. the ACCC's alternative argument that the sales process would have continued with another participant acquiring the assets (and therefore that barriers to entry would not be raised) did not properly assess the likely impact on competition and involved an 'impermissible causation analysis'.

Justice Beach found that the proposed acquisition would have the effect of substantially lessening competition if Pacific National had not offered an unconditional undertaking on the last day of the hearing.

BACKGROUND

Aurizon and Pacific National (**PN**) are national freight companies that (at the relevant time) were the only two suppliers of intermodal freight and bulk steel rail linehaul services (**Services**) within Queensland and two of only three suppliers into/out of Queensland.

'Intermodal' refers to the movement of containers or pallets using multiple 'modes' of transport (such as using rail to move containers long-distances, then trucking the containers the remaining distance to the end customer). The Services relate to the rail leg of the intermodal movement, and similar services supplied in relation to steel products. Containers are transferred between modes of transport at an intermodal terminal such as the Aurizon-owned Acacia Ridge Terminal (**ART**). ART is significant for both Queensland and interstate Services, as it also facilitates the change between narrow gauge trains used in Queensland and the standard gauge trains used in other states.

In April 2017, Aurizon commenced a sale process for the ART, its interstate intermodal business (**IIB**) and its Queensland intermodal business (**QIB**). It received six non-binding offers for all or parts of the businesses in May 2017, and invited PN, Qube and three other bidders to make binding bids by 4 August 2017. PN made a pre-emptive binding bid for the ART on 20 July 2017. On 28 July 2017, PN entered into a suite of agreements with Aurizon including:

- a $170 million Business Sale Agreement for the ART (**ART BSA**);
- a Terminal Services Subcontract (**TSS**) by which PN was appointed operator of the Brisbane Multi User Terminal (**BMUT**) from 1 December 2018 (replacing the previous operator Qube) – BMUT is the narrow-gauge terminal at ART which facilitates interstate Services;
- a Commitment Deed by which PN would pay Aurizon $10 million for granting PN exclusive preferred bidder status for the possible sale of the QIB; and
- an Agreement for Ongoing Commercial Arrangements between PN and Aurizon by which PN would pay $30 million, which the ACCC characterised as being a non-refundable 'break fee' in relation to the acquisition of ART.

On 11 August 2017, Aurizon agreed to sell the QIB to PN for $20 million. On the same day, Aurizon resolved to close the IIB, and this closure was carried out in December 2017. On 12 February 2018 and 15 March 2018, Aurizon announced that the QIB would be closed if the ACCC did not approve the acquisition.

INTERLOCUTORY PROCEEDINGS

On 18 July 2018, the ACCC sought an injunction requiring Aurizon to continue operating the QIB 'in the ordinary course of business' (ie not to shut down the QIB) until the substantive case was resolved. The Court acknowledged that a mandatory injunction of this kind was 'exceptional' and would cause significant prejudice to Aurizon, but it was granted on 13 August 2018, on the basis of the relatively short period in which it would apply and the fact that it was necessary to preserve the competitive *status quo*. A separate injunction sought by the ACCC to restrict PN from soliciting employees or customers of Aurizon was rejected, including on the basis that it could discourage normal competitive behaviour.

On 12 October 2018, between the grant of the injunction and the commencement of the main hearing, Aurizon agreed to sell the QIB to Linfox (which did not have existing rail assets in Queensland) and to supply Linfox with certain rail services for a period of 10 years. The ACCC stated that it would not oppose the transaction on 12 October 2018.

MAIN HEARING

On 19 July 2018, the ACCC commenced proceedings in the Federal Court alleging that Aurizon and PN had arrived at an understanding that had the purpose, and/or had or would have the likely effect, of substantially lessening competition (**SLC**) for the Services in each of the Queensland and interstate markets. In November 2018 (just prior to the commencement of the main hearing), the ACCC dropped the 'purpose' element of its case and only pursued the 'effect'/'likely effect' case.

THE ACCC'S CASE

The ACCC alleged that PN, as proposed owner of the ART or operator of the BMUT, would be the dominant supplier of rail linehaul services on the interstate routes and one of two suppliers in Queensland.

If PN acquired the ART, PN would be able to limit or deny access to the ART by competing rail operators as it would own the ART: without access to the ART a rail operator cannot sustainably commence operating rail linehaul services on interstate routes.

If PN did not acquire the ART, PN would have substantial operational control of the BMUT via the TSS. A new entrant would have a substantial competitive disadvantage to PN, as according to the ACCC:

- **Primary TSS case:** entry into the TSS created a barrier to entry, whereby PN (as operator of BMUT) would have, or be perceived to have, the ability and incentive to deter new entry. The ACCC submitted that potential entrants would therefore be deterred from commencing the supply of rail linehail services on the relevant routes. The ACCC primarily relied on Qube's evidence that it would not enter the market if PN owns the ART. In the ACCC's view, if a well-resourced, experienced operator like Qube would not enter, it is highly unlikely new entrants would either.

- **Alternative TSS case:** entry into the TSS brought Aurizon's sale process to an end, preventing potential purchasers from acquiring the QIB and IIB. The QIB was likely to be shut down if not sold to PN and the IIB was likely to be shut down in any event. The ACCC therefore submitted that without entry into the TSS, the sale process would have continued and there was a real chance another participant would have acquired the ART, the IIB and/or the QIB. The ACCC further submitted that even if a new entrant did not commence supplying services, barriers to entry would have been reduced as an owner other than PN would have a strong incentive to provide open access to the ART to earn revenue.

The ACCC submitted that, whether or not PN acquired ART, PN would have, and be perceived by potential competitors to have, the ability and incentive to discriminate against a new entrant. As such, the ACCC submitted that barriers to entry would be raised and potential entrants would be deterred. Without the ART acquisition or TSS, Aurizon, Qube or another potential entrant which was not the dominant supplier of rail linehaul services (as PN is) would have owned the ART and new entrants would have had the opportunity to enter the interstate markets if it were profitable for them to do so, in competition with PN.

TSS AND POTENTIAL BREACH OF SECTION 45 OF THE COMPETITION AND CONSUMER ACT

Justice Beach found, based on an analysis of the relevant provisions of the TSS, that the ACCC had 'overstated' and did not make out its primary case. In particular, Beach J found that with the existence and discipline of Aurizon's presence, it was unlikely that PN 'could engage in a meaningful and concerted campaign to substantially discriminate against a new entrant, particularly where there are downsides and disincentives to PN in doing so'.

The alternative case failed because of what Beach J described as ‘an impermissible causation analysis that is not justified by the proper approach’. The ACCC attempted to characterise the entry into the TSS as ‘intrinsically linked’ to the sale process and therefore the likely commercial outcome if the TSS was not entered into was the continuation of the sale process for the entire intermodal business. The ACCC’s approach to the counterfactual failed as it was limited to a causative analysis of PN and Aurizon’s commercial relationship but not – as is required – consideration of the likely effect on competition but for the contested arrangement. On the facts, Beach J found that the relevant counterfactual involved the parties entering into the ART BSA and the QIB sale agreement in any event. Further, Beach J found that even if the rejected causation analysis was permissible, the alternative case failed as the ACCC’s alleged counterfactual was not supported by the evidence.

ART ACQUISITION AND POTENTIAL BREACH OF SECTION 50 OF THE COMPETITION AND CONSUMER ACT

The ACCC argued that heightened barriers to entry would leave relevant users with only two potential suppliers of rail linehaul services on interstate routes: PN and SCT Logistics. The ACCC relied on Qube’s evidence that it would not enter the market if PN owns the ART.

Justice Beach found that, but for PN’s undertaking given to the Court unconditionally on the last day of the trial, the ACCC would have succeeded. Justice Beach noted that in the absence of the undertaking, barriers to entry, real or reasonably perceived, would be heightened. However, despite the ACCC’s criticisms that the undertaking does not satisfactorily prevent discrimination against third parties, and contains compliance deficiencies that make it unworkable, Beach J found that the undertaking removes any significant ability of PN to discriminate. Therefore the ACCC’s case that the ART acquisition amounted to a breach of section 50 of the Competition and Consumer Act failed.

Interestingly, Beach J (at the urging of the ACCC) rejected PN’s attempts to offer the undertaking on a conditional basis. PN unsuccessfully argued that the undertaking should only be implemented in circumstances where the Court would otherwise find the acquisition to SLC. The ACCC argued (and the Court accepted) that doing so would involve the Court offering an impermissible ‘advisory opinion’ regarding potential hypothetical scenarios. The Court also rejected the ACCC’s attempts to have the Court grant it ‘monitoring powers’ over the proposed undertaking, as doing so would go beyond the ACCC’s statutory powers.

KEY TAKEAWAYS

1. The Court has reaffirmed that a clear counterfactual analysis requires considering the future likely effect on competition with and without the contested arrangement.

2. If a party wishes to offer an undertaking as a potential remedy to mitigate an SLC, it will likely need to be unconditional.

3. The ACCC’s view that undertakings are an ineffective remedy has again been rejected by

the Court (as it did in AGL's acquisition of Loy Yang A).

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

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