IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV-2008-404-8347

	BETWEEN	COMMERCE COMMISSION Plaintiff
	AND	BRITISH AIRWAYS PLC Defendant

Hearing: 18 March 2011

Counsel: J Dixon and F Cuncannon for Plaintiff
M Dunning for Defendant

Judgment: 5 April 2011

JUDGMENT OF POTTER J

In accordance with r 11.5 High Court Rules
I direct the Registrar to endorse this judgment
with a delivery time of 2.30 p.m. on 5 April 2011.

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Introduction

[1] The defendant, British Airways PLC (BA), has admitted breaching Part 2 of the Commerce Act 1986 (the Act), in that it entered into and gave effect to price fixing arrangements contrary to s 27 (via s 30) of the Act. The Court is asked to impose on BA an agreed pecuniary penalty of $1.6 million, and to approve a proposed payment of $100,000 by BA towards the Commission's costs.

Agreed facts

[2] BA has filed admissions to the agreed statement of facts dated 10 March 2011 on the fifth and sixth causes of action pursuant to r 15.16 of the High Court Rules.

[3] BA carries on business as an airline providing international air services for both passengers and cargo. It is registered as an overseas company in New Zealand under the Companies Act 1993. Through its business unit, British Airways World Cargo (BAWC), BA provides a number of air cargo services, including the physical transport of air cargo from origin to destination. At all times material to this proceeding, BA did not fly aircraft to or from New Zealand; nor did it have employees in New Zealand. Instead, it offered air cargo services in New Zealand through a Joint Services Agreement with Qantas Airways Ltd (Qantas). It is estimated that BA carried substantially less than one per cent of all air cargo to and from New Zealand during the relevant period.

[4] The international air freight industry involves all facets of the movement of goods by air from origin to destination. Air cargo is transported in passenger aircraft using available belly space capacity, and on dedicated air freighters using both belly space and main deck capacity. Many airlines, like BA, have agreements with other airlines to carry cargo on their behalf, which enable them to offer air cargo services to or from airports that their own aircraft do not serve directly, where they do not have offices, or otherwise have capacity constraints. Air cargo carriers typically contract with freight forwarders to provide international cargo services; freight forwarders then organise the integrated transport of goods on behalf of a range of

shippers. The cost of air cargo services is thus generally passed on to shippers by freight forwarders.

[5] At all times material to this proceeding, the Commission considers, and BA accepts (for the purpose of these proceedings only), that there were markets in New Zealand for the provision of both in-bound and out-bound air cargo services between New Zealand and individual regions throughout the world. During that time, BA participated in a number of those markets in providing air cargo services in competition with other international air carriers, including Deutsche Lufthansa AG (Lufthansa). It is accepted, however, that BA and Lufthansa were neither principal competitors nor close competitors in the relevant New Zealand markets.

[6] The Commission's case is that BA entered into a cartel arrangement with other airlines through an understanding with Lufthansa, relating to the imposition of fuel surcharges. These were ostensibly to cover increased costs from escalating aviation fuel prices.

[7] The Commission alleges that in March 2002, through senior BAWC employees, BA arrived at an understanding with Lufthansa that it would exchange information in relation to the application of fuel surcharges. The amounts and timing of BA's fuel surcharges would be substantially the same as Lufthansa's, even though BA's index and methodology were designed to look different. BA and Lufthansa would also exchange information relating to their proposed application of fuel surcharges in accordance with the relevant level of their own indexes, except where local conditions prevented their application, or full application.

[8] Between March 2002 and February 2006, BA gave effect to the fuel surcharge understanding by exchanging information with Lufthansa as to the proposed application of fuel surcharges in accordance with their respective methodologies, and applying the fuel surcharges at the stipulated level by inclusion in its air waybills on the carriage of air cargo. BA employees were directed that, to the extent possible, fuel surcharges were to be charged globally in accordance with its surcharge methodology.

[9] BA however only admits that it gave effect to the fuel surcharge understanding where it applied the full fuel surcharge, and not where local conditions prevented their application, or full application. The full fuel surcharge was imposed from March 2002 to February 2006 for in-bound cargo that BA transported to New Zealand. For out-bound cargo, BA admits to imposing the full fuel surcharge only between March 2002 and June 2004. From June 2004, the fuel surcharge imposed for out-bound cargo shipments was instead determined in consultation with Qantas pursuant to its Joint Services Agreement.

[10] The commercial gain arising from BA's conduct cannot be readily ascertained. BA contends that there was no commercial gain because the fuel surcharges were offset by increased fuel costs, and competition in the total prices charged to customers, as reflected by the base freight rate, continued. The Commission's view is that there was commercial gain because, without the understanding, BA may not have been able to impose the surcharges to cover increased fuel costs. The Commission also does not accept that the total price BA charged would have remained the same, and the fuel surcharge understanding is likely to have led to some softening of the competition dynamic.

Legislation

[11] BA admits that it acted in breach of s 27 by arriving at an understanding with Lufthansa in relation to the imposition of fuel surcharges. Section 27 relevantly provides:

> **27 Contracts, arrangements, or understandings substantially lessening competition prohibited**
>
> (1) No person shall enter into a contract or arrangement, or arrive at an understanding, containing a provision that has the purpose, or has or is likely to have the effect, of substantially lessening competition in a market.
>
> (2) No person shall give effect to a provision of a contract, arrangement, or understanding that has the purpose, or has or is likely to have the effect, of substantially lessening competition in a market.
>
> ...

[12] Pecuniary penalties for breaches of Part 2 of the Act are provided for by s 80. This provides:

> **80 Pecuniary penalties**
>
> (1) If the Court is satisfied on the application of the Commission that a person—
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> (a) Has contravened any of the provisions of Part 2 of this Act; or
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> ...
>
> the Court may order the person to pay to the Crown such pecuniary penalty as the Court determines to be appropriate ....
>
> (2) The Court must order an individual who has engaged in any conduct referred to in subsection (1) to pay a pecuniary penalty, unless the Court considers that there is good reason for not making that order.
>
> (2A) In determining an appropriate penalty under this section, the Court must have regard to all relevant matters, in particular,—
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> (a) any exemplary damages awarded under section 82A; and
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> (b) in the case of a body corporate, the nature and extent of any commercial gain.
>
> (2B) The amount of any pecuniary penalty must not, in respect of each act or omission, exceed,—
>
> (a) in the case of an individual, $500,000; or
>
> (b) in the case of a body corporate, the greater of—
>
> (i) $10,000,000; or
>
> (ii) either—
>
> (A) if it can be readily ascertained and if the Court is satisfied that the contravention occurred in the course of producing a commercial gain, 3 times the value of any commercial gain resulting from the contravention; or
>
> (B) if the commercial gain cannot be readily ascertained, 10% of the turnover of the body corporate and all of its interconnected bodies corporate (if any).
>
> ...

> (6) Where conduct by any person constitutes a contravention of 2 or more provisions of Part 2 of this Act, proceedings may be instituted under this Act against that person in relation to the contravention of any one or more of the provisions; but no person shall be liable to more than one pecuniary penalty under this section in respect of the same conduct.

[13] Section 80(2A) requires the Court, in determining an appropriate penalty, to have regard to all relevant matters and specifically identifies, in the case of a body corporate, the nature and extent of any commercial gain. If it can be readily ascertained, the commercial gain arising will also determine the maximum penalty: see s 80(2B)(b)(ii)(A).

[14] The parties agree that the precise amount of commercial gain arising here is not readily ascertainable. BA disputes that there was any commercial gain, while the Commission says that there was some commercial gain, albeit one that is not readily ascertainable. In any event, the figure of $297,455 put forward as the revenue BA generated from the fuel surcharge during the relevant period would not have produced a maximum penalty in excess of $10 million. Neither will the turnover limb apply: s 80(2B)(b)(ii)(B). Ten per cent of BA's turnover measured over any of the potentially relevant periods is less than $10 million. Consequently, the parties are agreed that the maximum penalty for each breach is $10 million.

[15] Pursuant to s 80(6) of the Act, no person shall be liable to more than one pecuniary penalty in respect of the same conduct. Here it is accepted that there are two relevant breaches — that is, entering into and giving effect to the fuel surcharge understanding, which are distinct offences pursuant to s 27(1) and (2) of the Act. This suggests a maximum penalty of $20 million. The Commission however accepts that it is appropriate to proceed from a single starting point for the purpose of fixing a penalty for BA's overall conduct. I agree with that approach.

Approach to imposition of penalty

[16] In *Commerce Commission v Alstom Holdings SA*,[1] Rodney Hansen J confirmed that criminal sentencing principles provide an appropriate framework for the determination of a pecuniary penalty under s 80. His Honour said:[2]

> The parties invite me to consider the proposed penalty, broadly by reference to orthodox sentencing principles. That requires assessing the seriousness of the offending, identifying relevant aggravating and mitigating factors to determine an appropriate starting point and, finally, having regard to any factors specific to the defendant that may warrant an uplift in, or reduction from, the starting point. I accept that approach is appropriate. It is consistent with the statute and is endorsed by practice in New Zealand and other jurisdictions.

[17] That approach has been confirmed in a number of cases.[3] In *Commerce Commission v EGL Inc*, however, Rodney Hansen J noted that while the analogy with sentencing in the ordinary criminal jurisdiction provides a broad framework, the analogy must be viewed with caution as the two jurisdictions serve markedly different ends.[4] The primary purpose of pecuniary penalties for anti-competitive conduct is deterrence, whereas deterrence is only one of the many competing considerations involved in criminal sentencing.

[18] The importance of deterrence in this area is well established.[5] The aim of imposing pecuniary penalties for anti-competitive conduct is to send the message to persons in the commercial community contemplating engaging in such activity that they will be penalised. This is reflected in the Select Committee Report on the Commerce Amendment Bill 2001, where it was stated:[6]

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1 *Commerce Commission v Alstom Holdings SA* [2009] NZCCLR 22 (HC).

2 At [14].

3 *Commerce Commission v EGL Inc* HC Auckland CIV-2010-404-5474, 16 December 2010 at [12]; *Commerce Commission v Geologistics International (Bermuda) Ltd* HC Auckland CIV-2010-404-5490, 22 December 2010 at [18]; see also *Commerce Commission v New Zealand Diagnostic Group Ltd* HC Auckland CIV-2008-404-4321, 19 July 2010 at [15].

4 At [13]–[14]. See also *Commerce Commission v Geologistics International (Bermuda) Ltd* HC Auckland CIV-2010-404-5490, 22 December 2010 at [19].

5 *New Zealand Bus Ltd v Commerce Commission* [2008] 3 NZLR 433 (CA) at [197]; *Commerce Commission v Koppers Arch Wood Protection (NZ) Ltd* (2006) 11 TCLR 581 at [30]; *Commerce Commission v New Zealand Diagnostic Group Ltd* HC Auckland CIV-2008-404-4321, 19 July 2010 at [15].

6 Commerce Amendment Bill (No 2) 2001 (1-32) (Select Committee Report) at 30.

> The dominant reason for penalties under competition law is the forward looking aim of promoting general deterrence. To promote deterrence, illegal conduct must be profitless, which means that the expected penalty should be linked to the expected illegal gain. The courts should severely penalize today's offender to discourage others from committing similar acts.

[19] As Rodney Hansen J observed in *EGL Inc*, the factors that are considered in fixing pecuniary penalties and the weight they are given must be informed by the unique character and consequences of anti-competitive conduct and the overarching objectives of the pecuniary penalty regime.

Starting point

[20] The Commission has identified the following matters being relevant to the determination of an appropriate penalty under s 80(2A):

a) the nature and seriousness of the contravening conduct;

b) whether the conduct was deliberate;

c) the seniority of the employees or officers involved;

d) the duration of the contravening conduct;

e) the extent of any loss or damage caused by the contravening conduct; and

f) the extent of any benefit derived from the contravening conduct (that is, the nature and extent of any commercial gain).

[21] I accept the submission of Mr Dixon for the Commission, that the nature and scale of the operation was at the serious end of the spectrum. It involved, albeit somewhat indirectly, an arrangement between numerous key market competitors to implement a standardised fuel surcharge across the participating airlines' global networks, to eliminate competition between cartel members on specific components of the prices charged. It is true that the surcharge was only part of the total charges to customers for air cargo services, and in some cases was not imposed when

prevented by market conditions. In this sense the conduct was less egregious than in cases such as *Koppers* and *Alstom* which involved overarching agreements to maintain market share and control prices. Price-fixing conduct can be assumed to affect both price competition and the competitive dynamics, with a corresponding reduction in efficiency incentives for members of the cartel, although Mr Dunning for BA was not inclined to accept this.

[22] Factors further aggravating the conduct are that it was a sustained course of conduct, operating for a significant period of time, and that it involved covert communications between senior members of BAWC and Lufthansa employees. BA was aware that the United States Department of Transportation had rejected the conduct as being anti-competitive, and had been warned by the International Air Transport Association to refrain from such conduct, but acted deliberately in contravention of such advice.

[23] The Court is required to pay particular attention to the commercial gain resulting from the conduct. Here, the actual commercial gain cannot be readily ascertained. As mentioned above, BA accepts that it generated fuel surcharge revenue of about $297,455 on cargo sent to and from New Zealand during the relevant period, but contends there was no commercial gain.

[24] The Commission disputes this. Mr Dixon emphasised that "commercial gain" has a wider meaning than pecuniary gain, and that BA benefitted in various ways from the understanding. He submitted that BA may not have been able to impose the fuel surcharges at all without the understanding, and that the surcharges were unlikely to have accurately reflected BA's increased fuel costs. He disputed that BA's total price charged to customers would have remained the same, and asserted that, at the very least, the understanding allowed BA to impose the surcharge without the need to consider Lufthansa's likely commercial response.

[25] Mr Dixon referred by way of comparison to the *Alstom*, *EGL Inc*, and *Geologistics* cases. In *Alstom*, the Court approved a penalty of $1.05 million (together with costs of $50,000), even though there was no commercial gain. The maximum penalty there was $5 million, because the conduct occurred prior to the

amendment to s 80 increasing the maximum to $10 million. The lack of commercial gain was because there had not been tenders for the product at the relevant time.

[26] That case involved a cartel agreement for the provision of a system of circuit-breakers known as gas-insulated switchgear, where budget enquiries were determined in accordance with a price list. This was at the most serious end of the spectrum, being a price-fixing and market sharing arrangement involving all participants in the market, operating worldwide. The defendant's role was, however, limited, and the impact on the New Zealand market was negligible. A starting point of $1.25 to $1.75 million was selected. This was then reduced for the defendant's admission of liability, full cooperation with the Commission, and the implementation of a competition law compliance programme. The deterrent effect of a penalty imposed by the European commission and the impact of adverse international publicity was also taken into account.

[27] In *EGL Inc*, a starting range of $2.3 to 2.8 million was accepted for an agreement between six market competitors to charge a fee for all freight forwarding services for cargo shipped to and from New Zealand via the United Kingdom over about five years. As in this case, it was difficult to ascertain accurately the extent of any commercial gain, although it was estimated to be a low six-figure sum. The starting point was reduced by 50 per cent to recognise mitigating factors as the defendant had admitted liability at the first opportunity, cooperated in full with the Commission, submitted to the jurisdiction of New Zealand courts, and upgraded its compliance regime.

[28] In *Geologistics*, another case involving the freight forwarding industry, Allan J considered the recommended starting point range of $3.75 to $4.25 million appropriate in all the circumstances. There, a number of freight forwarders had colluded to charge a fee for cargo shipped to and from New Zealand via the United States of America for a period of approximately four years. The extent of commercial gain could not be quantified with precision, but it was acknowledged to be substantial. After discounting for the defendant's admission of liability at the earliest opportunity and a degree of cooperation with the Commission, a final penalty of $2.5 million was reached and approved.

[29] Mr Dixon submitted that a starting point slightly above that adopted in *EGL Inc* was required in this case because:

a) The market affected by BA's conduct was larger and more significant than in the *Alstom*, *EGL Inc* and *Geologistics* cases, such that the potential for gain and harm was greater than in those cases; and

b) BA obtained a benefit from its contravening conduct, more akin to the low commercial gain figure accepted in *EGL Inc* than in *Alstom*, where there was no commercial gain.

[30] Mr Dixon also noted that the starting point had to be much lower than the $8.5 to $14.5 million range in *Commerce Commission v Cargolux Airlines International SA*, heard on the same day as this case. There, the conduct involved an additional understanding, relating to the imposition of security surcharges; the conduct in relation to outbound air cargo services was of much longer duration; and the revenue generated from the fuel and security surcharges there was much higher than BA's.

[31] Based on these factors, a starting point in the range of $2.5 to $3 million was proposed for BA's conduct in relation to the fuel surcharge understanding.

[32] I accept Mr Dixon's submission that *EGL Inc* is the most analogous authority. The price-fixing arrangements in both cases related only to a component of the price of the service provided, the relevant markets were similar (being essentially different service aspects of the air freight industry), and the commercial gain could not be ascertained, but was accepted to be relatively low. I also accept that the bigger market here, compared to that in *EGL Inc*, requires a starting point slightly higher than that adopted in that case.

[33] No finding is required on the issue of whether there was commercial gain because the parties accept that their different positions are accommodated within the proposed starting point.

[34] Having regard to all aspects of BA's conduct, and the principal object of deterring like behaviour, I accept the proposed starting point of $2.5 to $3 million. I consider it to be consistent with previous authority and within the properly available range.

Mitigating factors

[35] The parties accept that BA admitted liability at the first opportunity, having always envisaged that an agreement as to penalty could be reached. BA has also cooperated with the Commission throughout the investigation and the proceedings. Moreover, BA has entered into a cooperation agreement with the Commission pursuant to which it will continue to provide cooperation in related proceedings.

[36] I am informed that BA has provided a high level of assistance to the Commission. This has involved BA proactively providing information over and above that required under s 98 of the Act, and making available for interview its officers and employees who could not have been compelled under s 98. The Commission acknowledges that a substantial discount is appropriate for BA's past and ongoing cooperation.

[37] A degree of remorse can be inferred from BA's ready acceptance of responsibility and extensive cooperation, to the extent that remorse or contrition can be attributed to a corporation.

[38] BA has not previously contravened the Act; neither has it been warned in respect of conduct likely to breach the Act. It has also upgraded its competition law compliance programme, which has now implemented globally, and is entitled to appropriate credit for that. Some allowance should also be given for the deterrent effect of significant penalties that have been imposed on BA in other jurisdictions in respect of related conduct and harm.[7] However, I accept Mr Dixon's submission that any such discount must be limited, as the penalty currently sought is for deterrence in New Zealand.

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[7] See *Commerce Commission v Alstom Holdings SA* [2009] NZCCLR 22 (HC) at [31], where this was a mitigating factor.

[39] The Commission submits that a total discount of 40 per cent is appropriate. This is higher than the one-third discount allowed in *Alstom* and *Geologistics*, but lower than the 50 per cent allowance in *EGL Inc*, where substantial and very helpful assistance was provided to the Commission.

[40] In *Commerce Commission v New Zealand Diagnostic Group Ltd*,[8] Allan J had regard to the discounts available for liability admissions in the criminal context, while cautioning that a strict application of the *R v Hessell*[9] tariff may not be appropriate in Commerce Act cases. *R v Hessell* has subsequently been reviewed in the Supreme Court in *Hessell v R*.[10] The Supreme Court has indicated that a more flexible and less prescriptive approach is preferable when determining discounts for admissions of guilt and cooperation in criminal sentencing, and has indicated that the reduction for a guilty plea component should not exceed 25 per cent.

[41] In *EGL Inc*, Rodney Hansen J observed that the Supreme Court's approach in *Hessell* was, arguably, more readily applicable to pecuniary penalties under the Act,[11] but again warned that the analogy with criminal sentencing could not be taken too far. His Honour noted that, on one hand, there was little room to attribute remorse to a corporation, but on the other hand, the public benefits derived from cooperation by a defendant in an investigation into anti-competitive conduct are of a scale and nature seldom encountered in the criminal jurisdiction.[12]

[42] The Judge then noted that it is in the public interest that substantial discounts be made for a high level of cooperation, for the purpose of recognising the savings achieved and providing appropriate incentives to those who have engaged in anti-competitive conduct to provide assistance to the Commission.[13]

[43] I consider that BA's substantial cooperation with the Commission is appropriately reflected within the total discount of 40 per cent. This would reduce

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8 *Commerce Commission v New Zealand Diagnostic Group Ltd* HC Auckland CIV-2008-404-4321, 19 July 2010 at [28].
9 *R v Hessell* [2010] 2 NZLR 298 (CA).
10 *Hessell v R* [2010] NZSC 135.
11 *Commerce Commission v EGL Inc* HC Auckland CIV-2010-404-5474, 16 December 2010 at [24].
12 *Commerce Commission v EGL Inc* HC Auckland CIV-2010-404-5474, 16 December 2010 at [24].
13 At [25].

the appropriate penalty to a final range of $1.5 to $1.8 million. The agreed penalty of $1.6 million is within this range.

Conclusion

[44] Ultimately, it is the final figure that the Court is asked to approve. The general approach of the Court is to accept and impose the penalty that the parties have agreed on, as long as it is within the permissible range.[14] As Rodney Hansen J said in the *Alstom* case:[15]

> ... there is a significant public benefit when corporations acknowledge wrongdoing, thereby avoiding time-consuming and costly investigation and litigation. The Court should play its part in promoting such resolutions by accepting a penalty within the proposed range. A defendant should not be deterred from a negotiated resolution by fears that a settlement will be rejected on insubstantial grounds or because the proposed penalty does not precisely coincide with the penalty the Court might have imposed.

[45] Having considered all of the relevant factors, I am satisfied that the proposed penalty is within the available range. Mr Dunning advises that BA considers the penalty appropriate in all the circumstances, and is in a position to pay it. Both parties have attempted to achieve an outcome that appropriately accommodates all the interests involved, and I am satisfied that the Commission is entitled to the orders sought.

Result

[46] I approve the pecuniary penalty agreed to between BA and the Commission, and order BA to pay a pecuniary penalty of $1.6 million to the Commission, along with costs of $100,000.

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[14] See *Australian Competition & Consumer Commission v ABB Power Transmission Pty Ltd* (2004) ATPR 48,848 at 48,855 (FCA); *NW Frozen Foods v Australian Competition & Consumer Commission* (1996) 71 FCR 285 (FCA); *Commerce Commission v New Zealand Diagnostic Group Ltd* HC Auckland CIV-2008-404-4321, 19 July 2010 at [45]; *Commerce Commission v EGL Inc* HC Auckland CIV-2010-404-5474, 16 December 2010 at [27]; *Commerce Commission v Geologistics International (Bermuda) Ltd* HC Auckland CIV-2010-404-5490, 22 December 2010 at [37]–[38].

[15] At [18].

Position of defending airlines

[47] The Commerce Commission has also filed proceedings against several other international airlines that it alleges are involved in the cartel. These proceedings are ongoing.

[48] The facts that will ultimately be determined at trial against other defendants can be expected to differ to greater or lesser degree to those appearing in the agreed statement. Any admissions as to facts are binding only for the purpose of the particular case in which they are made.[16]

[49] For the avoidance of doubt, I record that assertions in the agreed statement of facts involving any or all of the defending airlines have been considered as part of the narrative against BA only and involve no findings of liability against the defending airlines.

Judith Potter, J.

[16] *Commerce Commission v Koppers Arch Wood Protection* (2006) 11 TCLR 581 (HC). See also *Australian Competition & Consumer Commission v ABB Transmission and Distribution Ltd (No 2)* (2002) ATPR 41-872 (FCA) at 44-953.