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COMMERCE COMMISSION

Decision No. 584

Determination pursuant to the Commerce Act 1986 in the matter of an application for clearance of a business acquisition involving:

GE Fleet New Zealand

and

Custom Fleet (NZ) Limited

The Commission:	David Caygill Donal Curtin Peter JM Taylor
Summary of Application:	The acquisition by GE Fleet New Zealand of the business of Custom Fleet (NZ) Limited
Determination:	Pursuant to section 66(3) (a) of the Commerce Act 1986, the Commission determines to give clearance to the proposed acquisition.
Date of Determination:	5 July 2006

EXECUTIVE SUMMARY

1. A notice pursuant to s 66(1) of the Commerce Act 1986 (the Act) was registered on 7 June 2006. The notice sought clearance for the acquisition by GE Fleet New Zealand of the business of Custom Fleet (NZ) Limited.

2. The Commission considers the relevant markets to be the national market for the provision of fleet leasing services and the national market for the provision of fleet management services.

3. The Commission considers that the counterfactual is that Custom Fleet would be acquired by another company, either one with a significant presence in the New Zealand fleet leasing and fleet management markets, or an overseas company not already present in the New Zealand market.

4. The Commission considers that the proposed acquisition would not result, nor would be likely to result, in a substantial lessening of competition in the national market for the provision of fleet leasing services and the national market for the provision of fleet management services due to the presence and strength of existing competitors.

5. The Commission is therefore satisfied that the proposed acquisition would not have, nor be likely to have, the effect of substantially lessening competition in any market.

THE PROPOSAL

1. A notice pursuant to s 66(1) of the Commerce Act 1986 (the Act) was registered on 7 June 2006. The notice sought clearance for the acquisition by GE Fleet New Zealand of the business of Custom Fleet (NZ) Limited.

PROCEDURE

2. Section 66(3) of the Act requires the Commission either to clear or to decline to clear the acquisition referred to in a s 66(1) notice within 10 working days, unless the Commission and the person who gave notice agree to a longer period. An extension of time was agreed between the Commission and the Applicant. Accordingly, a decision on the Application was required by 12 July 2006.

3. The Applicant sought confidentiality for specific aspects of the Application. A confidentiality order was made in respect of the information for up to 20 working days from the Commission's determination notice. When that order expires, the provisions of the Official Information Act 1982 will apply.

4. The Commission's approach to analysing the proposed acquisition is based on principles set out in the Commission's Mergers and Acquisitions Guidelines.[1]

STATUTORY FRAMEWORK

5. Under s 66 of the Act, the Commission is required to consider whether the proposal is, or is likely to have the effect of substantially lessening competition in the market. If the Commission is satisfied that the proposal is not likely to substantially lessen competition then it is required to grant clearance to the application. Conversely if the Commission is not satisfied it must decline. The standard of proof that the Commission must apply in making its determination is the civil standard of the balance of probabilities.[2]

6. The substantial lessening of competition test was considered in Air New Zealand & Qant*as v Commerce Commission*, where the Court held;

> We accept that an absence of market power would suggest there had been no substantial lessening of competition in a market but do not see this as a reason to forsake an analysis of the counterfactual as well as the factual. A comparative judgement is implied by the statutory test which now focuses on a possible change along the spectrum of market power rather than on whether or not a particular position on that spectrum, i.e. dominance has been attained. We consider, therefore, that a study of likely outcomes, with and without the proposed Alliance, provides a more rigorous framework for the comparative analysis required and is likely to lead to a more informed assessment of competitive conditions than would be permitted if the inquiry were limited to the existence or otherwise of market power in the factual.[3]

7. In determining whether there is a change along the spectrum which is significant the Commission must identify a real lessening of competition that is not minimal.[4] Competition must be lessened in a considerable and sustainable way. For the purposes of its analysis the Commission is of the view that a lessening of competition and creation, enhancement or facilitation of the exercise of market power may be taken as being equivalent.

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[1] Commerce Commission, *Mergers and Acquisitions Guidelines, January 2004*.
[2] Foodstuffs (Wellington) Cooperative Society Limited v Commerce Commission (1992) 4 TCLR 713-722.
[3] *Air New Zealand & Qantas Airways Ltd v Commerce Commission,* unreported HC Auckland, CIV 2003 404 6590, Hansen J and K M Vautier, Para 42.
[4] Fisher & Paykel Limited v Commerce Commission (1996) 2 NZLR 731, 758 and also Port Nelson Limited v Commerce Commission (1996) 3 NZLR 554.

8. When the impact of market power is expected to be predominantly upon price, for the lessening, or likely lessening, of competition to be regarded as substantial, the anticipated price increase relative to what would otherwise have occurred in the market has to be both material, and ordinarily able to be sustained for a period of at least two years or such other time frame as may be appropriate in any give case.

9. Similarly, when the impact of market power is felt in terms of the non-price dimensions of competition such as reduced services, quality or innovation, for there to be a substantial lessening, or likely substantial lessening of competition, these also have to be both material and ordinarily sustainable for at least two years or such other time frame as may be appropriate.

ANALYTICAL FRAMEWORK

10. The Commission applies a consistent analytical framework to all its clearance decisions. The first step the Commission takes is to determine the relevant market or markets. As acquisitions considered under s 66 are prospective, the Commission uses a forward-looking type of analysis to access whether a lessening of competition is likely in the defined market(s). Hence, an important subsequent step is to establish the appropriate hypothetical future with and without scenarios, defined as the situations expected:

    - with the acquisition in question (the factual); and
    - in the absence of the acquisition (the counterfactual).

11. The impact of the acquisition on competition is then viewed as the prospective difference in the extent of competition in the market between those two scenarios. The Commission analyses the extent of competition in each relevant market for both the factual and the counterfactual, in terms of:

    - Existing competition;
    - Potential competition; and
    - Other competition factors, such as the countervailing market power of buyers or supplies.

THE PARTIES

Applicant

GE Fleet

12. GE Fleet New Zealand was incorporated in New Zealand in 2004 and was until recently a dormant company. It is a wholly-owned subsidiary of GE Finance and Insurance Limited, which is in turn a wholly-owned subsidiary of GE Capital and Global Financial Holdings Incorporated (United States).

13. GE Capital Fleet Services New Zealand Limited is a wholly-owned subsidiary of GE Capital Holdings Corporation (United States). GE Capital Fleet Services New Zealand Limited operates a fleet leasing and management business in New Zealand.

14. Both GE Fleet New Zealand and GE Capital Fleet Services New Zealand Limited are ultimately subsidiaries of General Electric Company (*GE*) in the United States. GE is listed on the New York Stock Exchange.

15. GE Fleet refers to either GE Capital Fleet Services New Zealand Limited or that company together with GE Fleet New Zealand.

16. GE Fleet provides operating lease services for [ ] vehicles, and management services for [ ] vehicles across New Zealand. GE Fleet's customers are primarily corporate and government entities.

Target

Custom Fleet (NZ) Limited (Custom Fleet)

17. Custom Fleet is a wholly-owned subsidiary of Bank of New Zealand (BNZ), which is in turn a wholly-owned subsidiary of National Australia Group (NZ) Limited (NAB Group).

18. Custom Fleet's main business functions are the funding and management of vehicle fleets to corporate customers. In New Zealand, Custom Fleet has approximately [ ] lease vehicles and provides management services for [ ] vehicles across New Zealand.

OTHER PARTIES

Esanda FleetPartners ("Esanda")

19. Esanda FleetPartners is the trading name for Truck Leasing Limited, a wholly-owned subsidiary of U D C Finance Limited, which is in turn a wholly-owned subsidiary of ANZ National Bank.

20. Esanda primarily provides fleet leasing services for [ ] cars and light commercial vehicles and [ ] heavy commercial vehicles throughout New Zealand, from its offices in Auckland, Wellington, Palmerston North and Christchurch.

Orix New Zealand Limited ("Orix")

21. Orix entered the New Zealand market in 1994 and currently provides fleet leasing services for [ ] vehicles, including [ ] heavy commercial vehicles, throughout New Zealand.

22. Orix is a wholly-owned subsidiary of the Orix Corporation of Japan, which is a major international finance company.

Leaseplan New Zealand Limited ("Leaseplan")

23. Leaseplan was established in New Zealand in 1993, and is a wholly-owned subsidiary of Leaseplan Corporation in Holland.

24. Leaseplan provides both fleet leasing and fleet management services for [ ] cars and light commercial vehicles across New Zealand.

Toyota Finance New Zealand Limited ("Toyota Financial Services" or "TFS")

25. TFS is a fleet leasing company that was incorporated in New Zealand in 1989, and is a subsidiary of Toyota Financial Services Corporation (Japan) and Toyota Finance Australia Limited.

26. TFS provides fleet leasing services for [ ] vehicles across New Zealand. [ ].

Transport Fleet Management Limited (“Fleetwise”)

27. Fleetwise is a fleet management company that was established in 1995 as a result of the outsourcing of non-core fleet management activities by the Manawatu/Wanganui District Health Board.

28. Since 1999, Fleetwise has expanded its customer base from approximately [ ] vehicles to [ ] passenger and commercial vehicles, and its current turnover for fleet management is $[ ] per annum.

29. Fleetwise also facilitates leasing arrangements between its customers and leasing companies (excluding Leaseplan), which generates an additional revenue stream of $[ ] per annum in brokerage services.

Fleetsmart Fleet Management Limited (“Fleetsmart”)

30. Fleetsmart is a wholly-owned subsidiary of Cardlink Systems Limited. Fleetsmart’s parent company Cardlink is a fuel card company that was established in New Zealand in 1984 and is also involved in software development of loyalty card management systems (e.g. Flybuys).

31. Fleetsmart was established as a division of Cardlink in 1999 as a result of the outsourcing of non-core fleet management activities by Telecom. Fleetsmart currently provides fleet management services for [ ] vehicles throughout New Zealand. Its annual turnover for fleet management is $[ ].

INDUSTRY BACKGROUND

Fleet Leasing

32. A fleet lease refers to an agreement entered into by a financier with a customer to fund the acquisition or use of motor vehicles. Financiers enter into this kind of arrangement with a customer to provide leases for all, or some, of the company’s vehicles.

33. There are two types of leases available to customers in New Zealand, operating leases and finance leases. Typically, customers enter into a master contract under which any number of individual leases can be provided.

34. The choice between lease types is usually dictated by the customer’s preferred accounting practices (balance sheet requirements, cash flow, and tax considerations) and willingness to accept residual value risk.

35. In addition to finance leases and operating leases, companies active in this sector may also offer a range of other finance products, such as chattel mortgages, factoring arrangements or commercial hire purchase.

Operating Lease

36. The individual vehicles provided under the master lease contract are provided to the customer for a specified lease period, for a fixed monthly rental and specified kilometre distance allowance.

37. The lease period for an operating lease is usually three years for a car, and six to ten years for heavy commercial vehicles[5].

38. In an operating lease, title to the vehicle remains with the lessor (the financier). The risk associated with any fluctuation over the residual value set at the

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[5] The length of time of an operating lease is determined by Inland Revenue’s depreciation rules, which state the maximum lease period is 75% of the vehicle’s useful life.

commencement of the vehicle lease, and the vehicle's ultimate sale price at lease end, reside with the lessor.

39. Accounting rules allow this type of lease to be 'off balance sheet' for a customer, allowing it to maintain a better debt to equity ratio, granting the customer the ability to access greater borrowings.

40. There are variations on operating leases, for example the fully maintained operating lease (FMOL), where the monthly lease payment also contains a set charge for servicing and maintaining the vehicle based on the lessor's estimate of costs to service. Under an FMOL arrangement, in addition to assuming the residual value risk for the vehicle, the lessor also assumes the "maintenance risk" shortfall (or gain) between the set amount charged to the lessee and the amount actually spent in servicing a fully maintained vehicle.

Finance Lease

41. The main point of difference between an operating lease and a finance lease is the accounting principles involved: the vehicle is 'on balance sheet' for the lessee and the lessee takes the residual value risk[6] upon sale of the vehicle at lease end. Additionally, a finance lease contract period is generally longer than that for an operating lease.

42. As with an operating lease, the lessor retains title to the vehicle and the customer has the option to buy the vehicle[7] at the end of the lease.

43. Much like the master operating leases, finance leases can also be provided with a fully maintained option.[8]

Fleet Management

44. Fleet management refers to the provision of maintenance and the monitoring of a company's vehicle fleet.

45. A customer's decision to purchase fleet management services is separate from its decision on how to fund the vehicles (i.e. fleet management services can be provided regardless of whether the customer owns the fleet itself or whether the fleet is financed externally).

46. Fleet management services include the on-road vehicle maintenance services provided by fleet leasing companies under FMOL (vehicle registration, warrant of fitness, servicing and tyre replacement), as well as supplementary value-added services, including:

- vehicle acquisitions and disposal;
- accident management and breakdown services;
- insurance options and protection plans;

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[6] Residual value is the resale value of the vehicle at the end of its lease. The residual value is estimated at the time of lease commencement, and is estimated by the leasing company. The risk associated with residual value is that the estimate will not match the sale price of the vehicle at lease-end (residual value is subject to the volatile nature of the second-hand car market).

[7] At the end of a finance lease contract, the lessee is not obliged to purchase the vehicle from the lessor. This is in contrast to a hire purchase, where the customer is required to make a balloon payment (the residual value) of the vehicle at the end of the lease period, whereby ownership is then transferred to the customer.

[8] This is not a particularly common option in New Zealand as most finance leases (as opposed to operating leases) are for a single vehicle.

- comprehensive fleet management reporting, including fleet utilization and fuel consumption reports; and
- risk assessment and practical driver training.

47. Fleet management providers may also provide purchase card services (such as cards which may be used for the purchase of fuel and oil) and other specialist services, such as vehicle salary packaging services, on-line services and the re-marketing of ex-leased vehicles.

PREVIOUS COMMISSION DECISIONS

48. The Commission has examined the fleet leasing and fleet management services markets in Decision 478: Custom Fleet and Hertz Fleetlease in October 2002.

49. In Decision 478 the market was defined as:
    - the market in New Zealand for the provision of fleet leasing services; and
    - the market in New Zealand for the provision of fleet management services.

50. The Commission granted clearance for the acquisition on the basis that the combined entity would be constrained, within both the fleet leasing and fleet management markets, by existing competition within these markets.

51. In relation to the fleet leasing market, the Commission considered that the combined entity would face additional constraints from:
    - potential competitors, given that there are no significant barriers to entry[9]; and
    - its customers, in the form of countervailing power[10], where customers have the ability to switch easily between lease providers, or even self-fund vehicles.

MARKET DEFINITION

52. The Act defines a market as:

> "… a market in New Zealand for goods or services as well as other goods or services that, as a matter of fact and commercial common sense, are substitutable for them."[11]

53. For the purpose of competition analysis, the internationally accepted approach is to assume the relevant market is the smallest space within which a hypothetical, profit maximising, sole supplier of a good or service, not constrained by the threat of entry would be able to impose at least a small yet significant and non-transitory increase in price, assuming all other terms of sale remain constant (the SSNIP test). The smallest space in which such market power may be exercised is defined in terms of the dimensions of the market discussed below. The Commission generally considers a SSNIP to involve a five to ten percent increase in price that is sustained for a period of one year.

54. The Applicant submits that the market definition should be that which was defined by the Commission in Decision 478:
    - the market in New Zealand for the provision of fleet leasing services; and
    - the market in New Zealand for the provision of fleet management services.

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[9] Decision 478, Para 121
[10] Decision 478, Paras 128 and 136
[11] S 3(1) of the Commerce Act 1986.

Product Market

55. The greater the extent to which one good or service is substitutable for another, on either the demand side or supply side, the greater the likelihood that they are bought and supplied in the same market.

56. Close substitute products on the demand side are those between which at least a significant proportion of buyers would switch when given an incentive to do so by a small change in their relative prices.

57. Close substitute products on the supply side are those between which suppliers can easily shift production, using largely unchanged production facilities and little or no additional investment in sunk costs, when they are given a profit incentive to do so by a small change to their relative prices.

58. In defining the relevant product market, the Commission assessed the degree of demand- and supply-side substitution between the following:

- fleet leasing and fleet management;
- operating leases and finance leases; and
- the provision of fleet leasing services for heavy commercial vehicles and the provision of fleet leasing services for passenger/light commercial ("passenger") vehicles.

Fleet Leasing and Fleet Management

59. The Applicant submitted in its Clearance Application that a large proportion of customers that decide to have their fleets managed seek a 'holistic solution' involving both the leasing and managed elements[12], and that the overlap between the two products can be interpreted as an indication that fleet leasing and fleet management lie within one market.

<u>Supply-Side Substitution</u>

60. Presently, there are a number of market participants that provide both fleet leasing and fleet management services.

61. Industry participants advised the Commission that there would be minimal sunk cost involved with switching from fleet leasing to fleet management; however, there would be significant sunk costs associated in switching from fleet management to fleet leasing.

62. Industry participants, such as Fleetwise and Fleetsmart, told the Commission that the sunk costs arise from the initial acquisition of vehicles, which are then leased out to the customer, and that costs associated with vehicle acquisition could not always be recovered during the lease period. For instance, [ ] said that presently, most lease companies are operating at a loss of $[ ] per vehicle, due to the fluctuation in residual values.

63. The Commission considers that supply-side switching between fleet management and fleet leasing is feasible and could occur within a reasonable timeframe. However, the Commission considers that the investment required to acquire vehicles would be largely sunk.

64. Consequently, the Commission considers that there is only a limited degree of supply-side substitutability between fleet leasing and fleet management.

[12] Clearance Application, page 25

Demand-Side Substitution

65. On the demand side, there is some small overlap between the management services contained within a FMOL, and value-added fleet management services, in terms of vehicle "on-road" maintenance[13].

66. However, in general, leasing is a lending facility through which a customer acquires a vehicle for business purposes, which is a substantially different product from the value-added services offered through fleet management.

67. The Applicant submitted that a customer's decision to purchase fleet management services is separate from its decision on how to fund its vehicles, i.e. the service can be provided regardless of whether it owns the fleet itself or whether the fleet is financed externally[14].

68. Although there may be some degree of substitutability at the supply side, the Commission considers that fleet management and fleet leasing are not substitutable on the demand side. Consequently, the Commission considers that fleet management and fleet leasing do not fall within the same market.

Operating Leases and Finance Leases

69. In Decision 478, the Commission concluded that operating leases and finance leases were substitutable on both the demand and supply side and therefore fell within the same market.[15]

70. Industry participants advised the Commission that they all offer both operating leases and finance leases, because the provision of finance is the same for both lease types. Differences between the two lease types are driven by taxation and accounting rules[16], which industry participants advised primarily affect the customer rather than the fleet leasing company itself.

71. Industry participants advised the Commission that it is the taxation and accounting rule differences that determine a customer's preference for, and ability to switch between, operating leases and finance leases. As such, the ability for demand-side substitutability will be discussed below.

72. In Decision 461, *GE Capital Finance Australasia Pty Limited/Australian Guarantee Corporation (NZ) Limited* the Commission concluded that on the demand-side, consumers have the ability to switch easily between different lending formats, in terms of leases and other finance products in general[17].

73. In Decision 478, the Commission found that ease of demand-side substitutability between lending and finance products also applied within the narrower context of lease types[18] within the fleet leasing services market[19].

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13 Market participants indicated that a majority of lease customers opt for the FMOL over non-maintained leases. Many stipulated that the service included within a FMOL tends to be comparatively basic "on-road" services (such as warrant of fitness, servicing, tyres and registration) in contrast to the value-added fleet management services discussed in paragraph 51.
14 Clearance Application, page 23
15 Decision 478, Para 44.
16 As discussed in Para 41.
17 Decision 478, Para 40.
18 Decision 478, Para 41, the Commission found that fleet leasing is a subset of motor vehicle finance. Motor vehicle finance was found to be a subset, in Decision 461, Para 29 and 30, of the greater financial products market.
19 Decision 478, Para 43.

74. Industry participants told the Commission that there have been recent changes to Fringe Benefit Tax (FBT) rules, which came into effect 1 April 2006. The change in FBT rules impacts on certain accounting rules that previously differentiated operating leases from finance leases, from the customer's point of view.

75. Previously, it was beneficial for a lessee to use a 1+1+1 operating lease (for a car) in order to minimize FBT payments. FBT was based on the value of the car at the commencement of each one year lease. Effectively, this meant that in the second and third year, FBT was paid at the depreciated value of the vehicle.

76. The change in FBT rules[20] means that the 1+1+1 operating lease is no longer advantageous to the lessee in terms of the payment of less FBT, bringing the FBT calculation for operating leases into line with the FBT calculation used for finance leases. This removes one of the reasons that customers have traditionally had a preference for one lease type over the other.

77. The Commission concludes that there is high supply- and demand-side substitutability between operating leases and finance leases and therefore both fall within the fleet leasing market.

Passenger/Light Commercial Vehicle Leasing and Heavy Commercial Vehicle Leasing

78. Industry participants commented that there are some key differences between providing fleet leasing services for passenger vehicles and heavy commercial vehicles[21]:

- The average value of a heavy commercial vehicle is up to ten times greater than that for passenger vehicles;
- The lease period for heavy commercial vehicles is 2-3 times longer than that for passenger vehicles; and
- Heavy commercial vehicles are usually built to customer specification, and require specialist maintenance services.

79. However, industry participants explained that the longer contract term and the comparatively higher level of customer service and fleet maintenance are used by fleet leasing companies to mitigate the greater financial risk associated with providing fleet leasing services for heavy commercial vehicles.

80. It follows that service or contract differences between passenger vehicle fleet leasing and heavy commercial vehicle fleet leasing are a result of asset value and the provision of financing those assets. It is therefore the provision of asset financing that will be examined from the supply and demand side.

<u>Supply-Side Substitution</u>

81. The provision of finance for a heavy commercial vehicle is considered to be the same as that for passenger vehicles, but on a larger scale. The Commission considers that a fleet leasing company able to provide fleet leasing services to a customer that requires a fleet of ten or more passenger vehicles, would have

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[20] FBT must be calculated as 20% of the original purchase price of the vehicle.
[21] Heavy commercial vehicles include truck and trailer units, forklifts, specialist machinery and plant equipment.

sufficient magnitude to likewise absorb the sunk costs associated with providing fleet leasing services for a heavy commercial vehicle.

82. The ability to substitute the provision of heavy commercial vehicles and passenger vehicles on the supply side is demonstrated by the fact that the majority of larger fleet leasing companies (e.g. Esanda, Orix and TFS) provide fleet leasing services for both heavy commercial vehicles and passenger/light commercial ("passenger") vehicles. There are also some small leasing companies, such as Driveline (which has [ ] vehicles on its books), which provide fleet leasing services for both heavy commercial vehicles and passenger vehicles.

83. Fleet leasing companies that provide leasing services for heavy commercial vehicles through a parent or sister company (e.g. Custom Fleet and GE Fleet) advised the Commission that this arrangement is driven by business strategy rather than the inability to switch between supplying heavy commercial vehicles and passenger vehicles.

84. The Commission considers that there is high supply-side substitutability between the provision of fleet leasing services for heavy commercial vehicles and the provision of fleet leasing services for passenger vehicles.

<u>Demand-Side Substitution</u>

85. From the demand side, the ability to substitute between fleet leasing for heavy commercial vehicles and passenger vehicles is very limited; it is unlikely that a business that requires a piece of specialist heavy machinery for a particular operation can instead utilise a small passenger vehicle, and vice-versa for the corporate business that requires a small passenger vehicle for its day-to-day business activities.

86. The Commission considers that the strong supply-side substitutability of the provision of fleet leasing services for heavy commercial vehicles and passenger vehicles outweighs the inability to substitute between the two on the demand-side, in this particular case. The Commission considers that both fall within the fleet leasing market.

87. In any case, the Commission considers that the acquisition of Custom Fleet by GE Fleet will not impact upon competition for the provision of fleet leasing services for heavy commercial vehicles. Most heavy commercial vehicle customers that approach Custom Fleet are referred to BNZ, and subsequently managed as part of BNZ's asset management portfolio[22]. BNZ and Custom Fleet's customer base was divided in this way in order to prevent conflict that may arise from a parent company (i.e. BNZ) competing against its subsidiary (i.e. Custom Fleet) for customers[23].

[22] The proposed transaction is for the Custom Fleet business, and does not include any customers managed by its parent, BNZ. Consequently, the asset management portfolio of BNZ is not being acquired by GE Fleet as part of the Custom Fleet acquisition.

[23] Custom Fleet does have a small number of heavy commercial vehicles on its lease book. Some of these customers are existing Custom Fleet customers that lease passenger vehicles as well as heavy commercial vehicles and prefer to deal with one lessor. The remainder are historical customers which were acquired when Custom Fleet acquired the business of Hertz Fleetlease in 2002.

Differentiated/Undifferentiated Products

88. Differentiated product markets are those in which the product offering of suppliers varies to some degree and in which buyers make their purchase decision on the basis of product characteristics as well as price. In such a market, suppliers' products are imperfect substitutes for one another and less close substitutes impose a lesser competitive constraint than others.

89. In Decision 478, the Commission found that fleet leasing services are relatively standard across the industry, to the extent that a customer's decision to lease vehicles with a particular supplier is usually driven by price. Although market participants will seek to differentiate themselves through brand reputation and customer service, leasing products are viewed as close substitutes for one another[24].

90. The Commission also found in Decision 478 that fleet management services tended to be differentiated in the same way that fleet leasing services were differentiated: by price, brand reputation and customer service[25].

91. The Commission therefore concluded in Decision 478 that the fleet leasing and fleet management markets are largely undifferentiated, and do not warrant the special analysis associated with fully differentiated products[26].

92. For the purpose of assessing the current Application, the Commission considers that the conclusions drawn in Decision 478 remain valid in this case.

Conclusion on Product Markets

93. The Commission concludes that for the purpose of assessing the competition implications of the proposed acquisition, the appropriate product markets are:

- the market for the provision of fleet leasing services; and
- the market for the provision of fleet management services.

Functional Markets

94. The production, distribution, and sale of a product typically occur through a series of functional levels, conventionally arranged vertically in descending order. Generally the Commission identifies separate relevant markets at each functional level affected by an acquisition, and assesses the impact of the acquisition on each.

95. In the market for the provision of fleet leasing services, there is some interaction between vehicle manufacturers and fleet leasing companies at the retail level, when the leasing company is in the process of acquiring vehicles. However, the proposed acquisition does not concern aggregation at the retail level. The scope of the acquisition is at the service level, where the fleet leasing and fleet management companies manage a direct relationship with customers.

96. The Commission concludes, for the purposes of the present Application, that the appropriate functional level is the provision of fleet leasing services and fleet management services.

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[24] Decision 478, Para 47
[25] Decision 478, Para 48
[26] Decision 478, Para 49

Geographic Markets

97. The Commission defines the geographic dimension of a market to include all of the relevant, spatially dispersed sources of supply to which buyers would turn should the prices of local sources of supply be raised.

98. In Decision 478, the Commission considered that the appropriate geographic market was that for New Zealand[27].

Supply-Side Substitution

99. Industry participants advised the Commission that the provision of fleet leasing services is considered to be national, because all of the financial provisioning facilities and customer management facilities are based in a centralised head office.

100. Industry participants that provide fleet leasing services told the Commission that by utilizing a network of car dealerships and local mechanics to provide many of the customer-facing business operations[28] there is no need to have fleet leasing services located regionally. Although Esanda, Custom Fleet, Orix and TFS have small offices in regional centres, these market participants advised the Commission that their regional offices are part of a business strategy aimed at providing comprehensive customer service and sales support, rather than serving mandatory operational purposes.

101. Industry participants that provide fleet management services told the Commission that again there is no need to have regional presence when provisioning fleet management services, for the reasons stated above. By example, Fleetwise told the Commission that most of its communication with its customers is by telephone or email, and it arranges local service providers for the customer-facing business operations.

102. The Commission notes that prices are co-ordinated on a national basis. The absence of regional price variation further supports industry participants' comments regarding national markets, as the competitive constraint is uniform throughout New Zealand.

Demand-Side Substitution

103. Given that a majority of the fleet leasing and fleet management companies operate on a national basis, without the need for regional presence, the Commission considers that there would be little difficulty for a customer to switch between service providers that are differentiated on a geographical basis.

Conclusion on Geographic Markets

104. The Commission concludes that for the purposes of assessing the competition implications of the proposed acquisition, the relevant geographic market is a national market.

Conclusion on Market Definition

105. The Commission concludes that for the purpose of assessing the competition implications of the proposed acquisition, the appropriate markets are:

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[27] Decision 478, Para 53

[28] E.g. A customer chooses and collects their new vehicle through a car dealership, and any vehicle maintenance will be done through a local mechanical service provider, arranged by the fleet leasing/management company.

- the market in New Zealand for the provision of fleet leasing services; and
- the market in New Zealand for the provision of fleet management services.

COUNTERFACTUAL AND FACTUAL

106. In reaching a conclusion about whether an acquisition is likely to lead to a substantial lessening of competition, the Commission makes a comparative judgement considering the likely outcomes between two hypothetical situations, one with the acquisition (the factual) and one without (counterfactual).[29] The difference in competition between these two scenarios is then able to be attributed to the impact of the acquisition.

Factual

107. In the factual scenario, GE Fleet would acquire the Custom Fleet business and [ ].

108. In the factual scenario, there would likely be a minimal change to the provision of fleet leasing services for heavy commercial vehicles. Custom Fleet has few heavy vehicle lease customers. Custom Fleet's heavy commercial vehicle customers are managed by BNZ as part of its asset management portfolio[30]. Custom Fleet's customer base was segmented and divided in this way in order to prevent conflict that may arise from a parent company competing against its subsidiary for customers[31]. The Commission understands that in the factual, BNZ would continue to operate commercial vehicle leasing arrangements. [ ].

Counterfactual

109. Custom Fleet advised the Commission that if the acquisition by GE Fleet was not to proceed, Custom Fleet would be sold to another party.

110. Custom Fleet advised the Commission that the highest bidders for Custom Fleet were:

- [ ]; and
- [ ].

111. [ ] also advised the Commission that they submitted bids for Custom Fleet.

112. The Commission considers the most likely counterfactual to be that Custom Fleet is sold to a company that is not already present in the New Zealand fleet leasing and management markets.

113. The Commission considers a less likely counterfactual to be that Custom Fleet is purchased by an industry participant such as [ ]. In this counterfactual scenario, it is likely that there would be some aggregation in the fleet leasing and fleet management markets, and this aggregation may be greater than in the factual scenario where GE Fleet purchases Custom Fleet.

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[29] Air New Zealand & Qantas Airways Ltd v Commerce Commission (No.6), unreported HC Auckland, CIV 2003 404 6590, Hansen J and KM Vautier, Para 42.

[30] Refer to footnote 22.

[31] Refer to footnote 23.

COMPETITION ANALYSIS

Existing Competition

114. Existing competition occurs between those businesses in the market that already supply the product, and those that could readily do so by adjusting their product-mix (near competitors).

115. An examination of concentration in a market can provide a useful indication of the competitive constraints that market participants may place upon each other, providing there is not significant product differentiation. Moreover, the increase in seller concentration caused by a reduction in the number of competitors in a market by an acquisition is an indicator of the extent to which competition in the market may be lessened.

116. A business acquisition is considered unlikely to substantially lessen competition in a market where, after the proposed acquisition, either of the following situations exists:

    - The three-firm concentration ratio (with individual firms' market shares including any interconnected or associated persons) in the relevant market is below 70% and the combined entity (including any interconnected persons or associated persons) has less than in order of 40% share; or
    - The three-firm concentration ratio (with individual firms' market shares including any interconnected or associated persons) in the relevant market is above 70% and the market share of the combined entity is less than in the order of 20%.

Fleet leasing market

117. The Applicant states that there is a wide range of competitors in the market for fleet leasing services, from specialist fleet lessors to those offering a more general range of products.

118. The Commission has measured market shares for fleet leasing in terms of number of vehicles leased, which industry participants stated is a common measure used within the industry. The Commission also used the value of net earning assets[32] as a measure for market share, in order to capture the difference in the sectors of the fleet leasing business within which each company operates and specialises (e.g. commercial vehicles versus passenger vehicles, luxury vehicles versus standard passenger vehicles). The market share figures in Table 1 are based on figures submitted by the Applicant and other major fleet leasing companies.

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[32] This measure was also in Decision 478, but was termed "lease book value".

Table 1: Fleet leasing Services

Operator	No. vehicles	Market Share (no. vehicles) (%)	Value of Net Earning Assets (millions)	Market Share (Net Earning Assets) (%)
Custom Fleet	[ ]	[ ]	$[ ]	[ ]
GE Fleet	[ ]	[ ]	$[ ]	[ ]
Combined Entity	*[ ]*	*[ ]*	*$[ ]*	*[ ]*
Esanda	[ ]	[ ]	$[ ]	[ ]
Orix	[ ]	[ ]	$[ ]	[ ]
TFS	[ ]	[ ]	$[ ]	[ ]
Leaseplan	[ ]	[ ]	$[ ]	[ ]
MARAC	[ ]	[ ]	$[ ]	[ ]
Honda	[ ]	[ ]	$[ ]	[ ]
Other	[ ]	[ ]	$[ ][33]	[ ]
Total	[ ]	100	**$[ ]**	100.

119. Table 1 indicates that the combined entity would have a market share of [ ] % based on fleet size and the three-firm concentration would be [ ] %. When the measures are based on Net Earning Assets, the combined entity would have a market share of [ ] % and the three-firm concentration would be [ ] %. Both of these measures are outside the Commission's safe harbour guidelines.

120. The Commission recognises that concentration is only one of a number of factors to be considered in the assessment of competition in a market. In order to understand the impact of the acquisition on competition, and having identified the level of concentration in a market, the Commission considers the behaviour of the businesses in the market.

121. Industry participants advised the Commission that the major competitors in the market were the "big four" – Custom Fleet, Esanda, Orix and Leaseplan. Industry participants did not consider GE Fleet to be a major competitor in the fleet leasing market and stated that GE Fleet does not currently have the ability to tender for lease contracts for large fleets.

122. In addition to the four large lease companies, there are a number of smaller companies that offer fleet leasing services. Financial branches of a number of the major car manufacturers offer lease arrangements. Industry participants advised the Commission that TFS was very competitive, especially on contracts for Toyota-only fleets. John Garland, Managing Director TFS, stated that TFS [

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123. The major fleet leasing companies also face limited competition from other financial institutions such as MARAC and Speirs Finance, and smaller lease

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[33] The value of net earning assets for the 'other' category is based on average vehicle value of $[ ]. (This is calculated by dividing the total value of Net Earning Assets for all companies, by the total number of vehicles for all companies).

companies such as Driveline Finance Limited and Flexilease. Industry participants advised the Commission that these smaller companies do not usually have access to funding at the same rate as the major lease companies (many of which are subsidiaries of international banks), and are therefore often not competitive on leases for large fleets of vehicles.

124. The Commission was advised by fleet leasing customers such as [ ] that it is not difficult to switch between lease providers. The Commission understands that it is quite common for customers to have a number of different lease providers for their fleet of vehicles. Each time a new lease is required, a customer will generally receive quotes from most of the major lease providers. [ ] advised the Commission that it currently uses three lease providers - Custom Fleet, Leaseplan, and Esanda.

125. In the Application, the Applicant advised the Commission that:

- Griffins Foods has a panel of four lease providers, namely GE Fleet, Custom Fleet, Orix and Esanda;
- Tyco uses a panel of three different lease providers;
- Heinz Watties has a panel of providers bidding for fleet leasing contracts via an Internet based live auction;
- Transfield has a panel of four lease companies with which it has current lease agreements in place. Each lease company provides a quote on each new order of vehicles; and
- many other large customers have fleet leasing contracts with more than one supplier.

126. Industry participants advised the Commission that customers frequently compare the lease service provided against the option of owning vehicles themselves. For example, [ ], has a procurement manager who benchmarks the lessor’s price with the estimated cost of owning the vehicles themselves.

127. GSB Supply Corp (formerly the Government Stores Board, now a privately-owned consultancy) acts as a broker and runs tenders for the lease contracts of government bodies. Jack Gordon-Crosby, General Manager, GSB Motor Vehicles, advised the Commission that GSB Supply Corp frequently models the cost of ownership versus leasing for all its clients. It has successfully converted a number of government bodies, such as [ ], from leasing back to ownership.

<u>Conclusion on Competition in the national fleet leasing market</u>

128. The Commission considers that existing competition would be likely to constrain the combined entity in the factual, such that there would be little difference between the factual and the counterfactual, due to:

- the presence of other major competitors in the fleet leasing market in New Zealand, such as Esanda, Orix, and Leaseplan; and
- limited competition from a number of other small lease companies and finance companies (e.g. MARAC, Driveline, and Speirs Finance).

Fleet management market

129. As stated above, fleet management services range from the standard maintenance and servicing of vehicles to specialised services such as fleet reporting, vehicle utilisation modelling and the acquisition and disposal of vehicles.

130. Competitors in the fleet management market include the major lease companies such as Leaseplan and Custom Fleet, as well as companies that specialise in fleet management only, such as Fleetwise and Fleetsmart.

131. The Commission has used two measures of market share. Table 2 details the market share figures in the fleet management market based on number of vehicles. The figures obtained from each company relate to vehicles that are managed by each company but not leased (i.e. the figures do not include FMOLs which are offered by most major lease companies and which encompass some management services).

Table 2: Fleet management market shares based on number of vehicles

Operator	No. vehicles	Market Share (No. vehicles) (%)
Custom Fleet	[ ]	[ ]
GE Fleet	[ ]	[ ]
Combined Entity	*[ ]*	*[ ]*
Fleetsmart (Cardlink)	[ ]	[ ]
Fleetwise	[ ]	[ ]
Leaseplan	[ ]	[ ]
Esanda	[ ]	[ ]
Other	[ ]	[ ]
Total	**[ ]**	100

132. Table 3 details the market share figures in the fleet management market based on revenue received from the last financial year.

Table 3: Fleet management market shares based on revenue

Operator	Revenue (Last Financial Year)	Market Share (Revenue of last financial year) (%)
Custom Fleet	[ ]	[ ]
GE Fleet	[ ][34]	[ ]
Combined Entity	*[ ]*	[ ]
Fleetsmart (Cardlink)	[ ]	[ ]
Leaseplan	[ ]	[ ]
Fleetwise	[ ]	[ ]
Esanda	[ ]	[ ]
Other	[ ]	[ ]
Total	**[ ]**	100

133. The tables above illustrate that market share figures for fleet management differ significantly depending on the measure used. This is because fleet management can encompass a variety of services, and while some fleet management specialists offer a fully comprehensive package of services, other companies offer a much narrower fleet management product. For instance, GE Fleet stated that its management of [ ].

134. The difference in the variety of services offered becomes clearer on examination of the average revenue derived per vehicle for each company. Table 4 shows that companies such as [ ] and [ ] have a much higher average revenue per vehicle, which suggests that they typically offer a more comprehensive fleet management package than other companies.

Table 4: Average revenue per vehicle

Operator	Fleet Management: Average Revenue per Vehicle
Custom Fleet	[ ]
GE Fleet	[ ]
Fleetsmart (Cardlink)	[ ]
Fleetwise	[ ]
Leaseplan	[ ]
Esanda	[ ]

135. Based on number of vehicles, the combined entity would have a market share of [ ] % and the three-firm concentration ratio would be [ ] %. These figures fall outside of the Commission's safe harbour guidelines. Based on revenue, Table 3 indicates that the combined entity would have a market share of [ ] %, and the

[34] GE Fleet introduced a Fleet Management service in March 2006. Figures are extrapolated to 12 months.

three-firm concentration ratio would be [ ] %. These figures are inside the Commission's safe harbours.

136. According to industry participants, the major competitors in the fleet management market are Fleetsmart, Custom Fleet, Fleetwise, and Leaseplan. These companies all provide a fully comprehensive fleet management package to customers.

137. Fleetwise and Fleetsmart are the only major fleet management specialists in New Zealand. In addition to the standard fleet management services offered such as servicing, maintenance, WOF, registrations, accident management, insurance, and fuel cards, these fleet management specialists can organise the acquisition of vehicles or lease of vehicles for a customer. Not having their own leasing division, Fleetwise and Fleetsmart are able to run tenders on behalf of customers, and have relationships with all the major lease companies for this purpose. They also frequently undertake cost-benefit analyses for customers on lease-versus-buy options. The other major fleet leasing companies, which also offer management services, typically promote their own lease product. Ben Unger, CEO, Fleetsmart, stated that this independence was Fleetsmart's main point of difference in the market.

138. In addition to the fleet management companies listed above, other fleet leasing companies have some involvement in fleet management. Fleet leasing companies such as [ ] offer standard FMOLs which include an element of fleet management (i.e. the leasing company organises WOF, registrations, maintenance and servicing).

139. Major competitors such as Fleetsmart, Leaseplan, and Fleetwise advised the Commission that GE Fleet is not a significant competitor in the fleet management market. GE Fleet stated that it has only recently rolled out a fleet management product, [ ].

140. Industry participants advised the Commission that it is quite common for customers with smaller fleets (fewer than 50 vehicles) to manage their fleets in-house. Typically, these customers will have FMOLs with a lease company, which would include the service and maintenance of the vehicles. Any other fleet management services would be undertaken in-house.

141. Custom Fleet stated that rental companies, which typically have very large fleets of vehicles, tend to favour non-maintained operating leases and undertake all aspects of fleet management in-house.

142. The Applicant stated that of the 200,000[35] estimated commercial and government vehicles on the road in New Zealand, it estimates that [ ][36] vehicles are managed by a fleet management company. This represents approximately [ ], suggesting that a significant number of vehicles continue to be managed in-house, or do not require management services beyond the standard maintenance and servicing offered by FMOLs.

143. [ ] was that when market penetration of fleet leasing and management

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[35] The Applicant obtained this estimate from LTNZ.

[36] The Applicant's estimate differs from the actual figures obtained by the Commission, which add to a total of [ ].

companies reached 50-55% of all corporate vehicles, the market became saturated. This suggests that there will always be approximately 45-50% of vehicles which are owned and managed in-house, rather than by lease companies.

Conclusion on Competition in the national fleet management market

144. Industry participants and GE Fleet advised the Commission that GE Fleet does not currently provide a comprehensive fleet management service in New Zealand. The [ ]. Industry participants did not consider GE Fleet to be a significant competitor in the fleet management market in New Zealand.

145. The Commission considers that there would continue to be significant existing competition in the fleet management market in the factual and the counterfactual due to major competitors such as Leaseplan, Fleetwise, and Fleetsmart.

OVERALL CONCLUSION

146. The Commission has considered the probable nature and extent of competition that would exist, subsequent to the proposed acquisition, in the national market for fleet leasing and the national market for fleet management.

147. The Commission considers that the counterfactual is that Custom Fleet would be acquired by another company, either one with a significant presence in the New Zealand fleet leasing and fleet management markets, or an overseas company not already present in the New Zealand market.

148. In the national fleet leasing market, the Commission considers that there would continue to be significant existing competition in the factual scenario, compared to the counterfactual scenario. In the factual and the counterfactual, there would be major competitors such as Esanda, Orix, and Leaseplan, as well as limited competition from a number of other small lease companies and finance companies.

149. With respect to the national fleet management market, the Commission considers that there would continue to be significant existing competition in the factual and the counterfactual due to major competitors such as Leaseplan, Fleetlease, and Fleetsmart.

150. The Commission is therefore satisfied that the proposed acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in any market.

DETERMINATION ON NOTICE OF CLEARANCE

151. Pursuant to section 66(3) (a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition by GE Fleet of the business of Custom Fleet.

Dated this 5 July 2006

David Caygill

Deputy Chair
Commerce Commission