

DRAFT FOR CONSULTATION - 18 OCTOBER 2022

Misuse of Market Power Guidelines



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Introduction

- 1 The purpose of the Commerce Act 1986 (Commerce Act) is to promote competition in markets for the long-term benefit of consumers within New Zealand.¹ Effective competition plays an important role in driving the performance of New Zealand's economy. Competition delivers lower prices, higher quality, and more choice for consumers. It gives firms increased incentives to innovate, and results in a better allocation of resources.

Prohibition on the Misuse of Market Power

- 2 One of the ways the Commerce Act promotes competition is by prohibiting firms with substantial market power from misusing that market power to harm competition, including by maintaining or extending their market power in a way that limits the ability of other firms to compete.
- 3 The Commerce Amendment Act 2022 (Amendment Act) amends New Zealand's laws on the misuse of market power, set out in section 36 of the Commerce Act. The Amendment Act strengthens the prohibition on the misuse of market power by prohibiting conduct by persons with substantial market power that has the purpose, effect, or likely effect of substantially lessening competition in markets. The Amendment Act also brings New Zealand's test back in line with the Australian misuse of market power test, following its amendment in 2017.
- 4 Parliament intended the Amendment Act to address concerns that the previous prohibition was costly and complex to enforce, unpredictable, and failed to deter or penalise some forms of anti-competitive conduct.² The amended prohibition is therefore likely to capture anti-competitive conduct that was not previously prohibited.

Authorisation

- 5 The Commerce Act recognises that competition is not an end in itself, but a means by which to promote the long-term interests of New Zealand consumers.³ The Amendment Act extends the authorisation provisions of the Commerce Act to conduct that might or will breach section 36. Where conduct gives rise to such a public benefit that it should be permitted, it may be authorised by the Commission.⁴

Transitional Provisions

- 6 The amended misuse of market power prohibition takes effect on 5 April 2023 and applies to all conduct from that date onward. The previous provision applies to conduct prior to that date.

1 Commerce Act 1986, s 1A.

2 Commerce Amendment Bill 2021 (9-1) (Explanatory note) at 1.

3 *Godfrey Hirst NZ Ltd v Commerce Commission* (2011) 9 NZBLC 103,396 (HC) at [46].

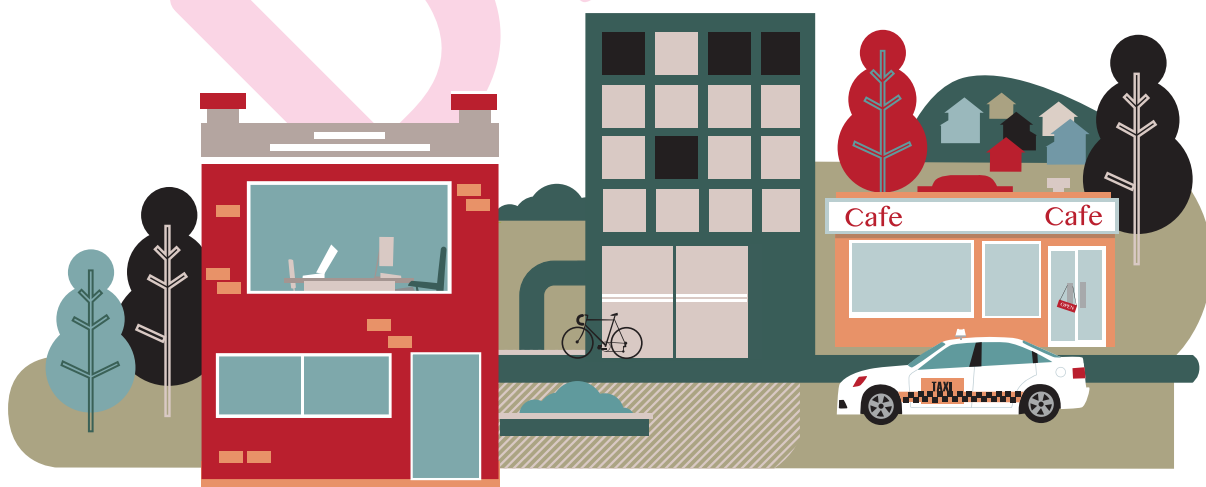
4 Commerce Act, s 61(8).

Role of the Guidelines

- 7 These Guidelines provide a broad overview of our proposed approach to the amended prohibition. The Guidelines are necessarily general and are not an attempt to codify the Commission’s approach. We will exercise our judgement on how best to apply them to the facts of each case but will depart from them where there is good reason to do so.
- 8 These Guidelines are not law and are not legally binding. They do not replace legal advice. The specific facts of each case will determine how the Commerce Act applies and you should seek legal advice on the application of the Commerce Act to your circumstances.
- 9 These Guidelines also do not bind the courts. It is ultimately up to the courts to determine whether conduct breaches the misuse of market power prohibition.

Our Approach Will Evolve Over Time

- 10 The amendments to the Commerce Act introduce a new prohibition, based on existing concepts used in other prohibitions in the Commerce Act. The Guidelines represent our interpretation of how those existing concepts apply to single firm conduct at this point in time.
- 11 We expect our approach will evolve over time. We will gain valuable experience working with the new provisions as new issues come before us. And as matters come before the courts we will benefit from clarity about the interpretation and application of the new concepts.
- 12 The amendments are intended to align New Zealand’s misuse of market power prohibition with the equivalent prohibition in Australia.⁵ We will also benefit from the cases that are decided in that jurisdiction.
- 13 Changes to our approach and new case law may result in changes to the Guidelines.



5 Commerce Amendment Bill 2021 (9-1) (Explanatory note) at 1.

Misuse of Substantial Market Power

Competition and Market Power

- 14 Competition is the process through which firms compete to win customers based on price, quality, service, or any other parameter of competition.
- 15 The Commerce Act defines competition as “workable or effective competition”.⁶ As the High Court has noted:⁷

...workable competition means a market framework in which the presence of other participants (or the existence of potential new entrants) is sufficient to ensure that each participant is constrained to act efficiently and in its planning to take account of those other participants or likely entrants as unknown quantities. To that end there must be an opportunity for each participant or new entrant to achieve an equal footing with the efficient participants in the market by having equivalent access to the means of entry, sources of supply, outlets for product, information, expertise and finance. This is not to say that particular instances of the items on that list must be available to all. That would be impossible. For example, a particular customer is not at any one time freely available to all suppliers. Workable competition exists when there is an opportunity for sufficient influences to exist in any market, which must be taken into account by each participant and which constrain its behaviour.

- 16 Market power is the antithesis of competition.⁸ A firm has market power if it has the ability to act to some extent without competitive constraint.⁹ Both suppliers of goods and services and acquirers of goods and services can have market power. Market power enables a firm to take more and give less.

Section 36 – The Prohibition on the Misuse of Market Power

- 17 Section 36 of the Commerce Act provides:

36 Misuse of market power

- (1) A person that has a substantial degree of power in a market must not engage in conduct that has the purpose, or has or is likely to have the effect, of substantially lessening competition in—
 - (a) that market; or
 - (b) any other market in which the person, or an interconnected person,—
 - (i) supplies or acquires, or is likely to supply or acquire, goods or services; or
 - (ii) supplies or acquires, or is likely to supply or acquire, goods or services indirectly through 1 or more other persons.

⁶ Commerce Act, s 3(1).

⁷ Bruce G Donald and JD Heydon *Trade Practices Law: Restrictive Trade Practices, Deceptive Conduct and Consumer Protection* (Law Book Co, Sydney, 1978) as cited in *Auckland Regional Authority v Mutual Rental Cars (Auckland Airport) Ltd* [1987] 2 NZLR 647 (HC) at 671; and *Fisher & Paykel Ltd v Commerce Commission* [1990] 2 NZLR 731 (HC) at 757-758.

⁸ *Re Queensland Co-operative Milling Association Ltd* (1976) 8 ALR 481 (Trade Practices Tribunal) at 515.

⁹ *Commerce Commission v Telecom Corporation of New Zealand Ltd* [2010] NZSC 111, [2011] 1 NZLR 577 at [33].

Why Firms with Substantial Market Power are Prohibited from Misusing It

- 18 The process of competition encourages firms to innovate, to be efficient, and to offer a range of products,¹⁰ at prices and quality levels that respond to demand from consumers. Competition delivers benefits to New Zealanders in both the short and long run, by driving firms to offer consumers greater choice of goods and services. Competition will often result in a diversity of offerings to meet different consumer demands, including different prices or different degrees of quality for the same products.
- 19 Section 36 does not prohibit firms with substantial market power from ‘out-competing’ their competitors through superior innovation, better products, lower prices and/or efficiency. Firms that compete by, for example, undertaking a successful promotional campaign, undertaking research and development which results in better products or more efficient processes, or passing savings through to consumers as lower prices will generally be enhancing competition, not lessening it.
- 20 Section 36 prohibits a firm with substantial market power from damaging the competitive process by restricting or undermining its rivals’ ability to compete, rather than offering a more attractive product. Such conduct undermines the effective operation of markets and the economy. A firm with market power may be able to damage the competitive process if it can sufficiently hinder its current rivals, restricting their ability to compete, or prevent them from competing entirely. It may also be able to deter potential rivals, impose barriers to slow down entry or expansion of current and potential rivals, or entirely prevent them from entering a market.
- 21 In some cases, conduct may be harmful to competition when undertaken by a firm with substantial market power, but not when undertaken by a firm without. Recognising this fact was one of the reasons for amending section 36.
- 22 Harming the competitive process in this way can result in higher prices, lower quality, fewer choices, inefficiency, and reduced innovation. These outcomes are not in the long-term interests of New Zealand consumers.
- 23 The aim of the misuse of market power provision is to prohibit such activity and ensure firms with substantial market power compete on their merits.
- 24 The Courts in New Zealand have noted on many occasions that prohibitions on misuse of market power exist to protect the competitive process, not to protect individual competitors. Lessening the effectiveness of a competitor is not necessarily the same as lessening competition.¹¹ However, in some circumstances, protecting the process of competition may have the effect of protecting a competitor.¹²

10 In these guidelines we use ‘product’ as shorthand for goods and services.

11 *Port Nelson Ltd v Commerce Commission* [1996] 3 NZLR 554 (CA) (*Port Nelson (CA)*) at 564-565.

12 *Commerce Commission v Fletcher Challenge Ltd* [1989] 2 NZLR 554 (HC) at 604; and *Union Shipping NZ Ltd v Port Nelson Ltd* [1990] 2 NZLR 662 at 700.

How Markets are Assessed in a Misuse of Market Power Case

Markets

- 25 A market is the place in which the competitive process, or potential competitive process, takes place. The identification of the relevant market/s is the first step in the assessment of a firm's market power, and the effect of any unilateral conduct that might lessen competition.¹³
- 26 The market definition exercise is not an end in itself. It is a tool for analysing the competitive issues of interest, revealing the effective constraints upon a firm's behaviour.¹⁴
- 27 In relation to section 36, market definition assists with two questions:
 - 27.1 Whether a firm has substantial market power; and
 - 27.2 Whether the conduct has the purpose, effect, or likely effect of substantially lessening competition in a market.
- 28 A market is a description of an area or space for transactions for a product or service.¹⁵ It includes both actual and potential transactions. A market includes not only the products and services under analysis, but any other products or services that, as a matter of fact and commercial common sense, are substitutable for them.¹⁶ The market seeks to capture the factors that directly shape and constrain the rivalry between firms supplying the relevant products or services.¹⁷
- 29 Generally, the more closely substitutable two products are, the closer the competition and the greater the competitive constraint between those products. When assessing the degree of substitutability, the dimensions that we are likely to consider can include:
 - 29.1 The products supplied and purchased (the product dimension);
 - 29.2 The geographic area from which the products are obtained, or within which the products are supplied (the geographic dimension);
 - 29.3 The level in the supply chain at which the firm in question operates (the supply chain level dimension);
 - 29.4 The different customer types (the customer dimension); and
 - 29.5 The time within which the market operates (the time dimension).
- 30 Our approach to market definition is set out in detail in our Mergers and Acquisitions Guidelines.¹⁸ We define markets in a way that best isolates the key competition issues under investigation. Market definition is not an exact science, and it is not always possible or necessary to identify precise boundaries.
- 31 Defining markets where a firm has an existing substantial degree of market power can add complexity. This is because a firm with market power may set prices at levels that increase the range of substitutable products. This may give a false impression that the firm lacks market power. Consequently, it may be more appropriate to consider the range of substitutable products if prices were instead set at competitive levels, ie in the absence of market power.

13 *Tru Tone Ltd v Festival Records Retail Marketing Ltd* [1988] 2 NZLR 352 (CA) at 358.

14 *Commerce Commission v Bay of Plenty Electricity Ltd* HC Wellington CIV-2001-485-917, 13 December 2007 at [282]; and *Commerce Commission v New Zealand Bus Ltd* (2006) 11 TCLR 679 (HC) at [123].

15 *Commerce Commission v New Zealand Bus Ltd*, above n 14, at [123].

16 Commerce Act, s 3(1A).

17 *Commerce Commission v Air New Zealand Ltd* [2011] NZHC 1285 at [124].

18 *Commerce Commission Mergers and Acquisitions Guidelines* (May 2022) at [3.7]-[3.47].

Indirect Supply

- 32 Where a firm has substantial market power, section 36 applies to its conduct affecting the market in which it has substantial market power. It also applies to conduct affecting markets where the firm does not have substantial market power, but:
- 32.1 Supplies or acquires goods or services (whether directly or indirectly through one or more other persons); or
- 32.2 Is likely to supply or acquire goods or services, (whether directly or indirectly through one or more other persons).
- 33 The concept of indirectly supplying or acquiring in section 36 mirrors the equivalent Australian provision in section 46 of the Competition and Consumer Act 2010 (Cth). When those amendments were introduced, it was noted that the concept of indirect supply:¹⁹

... allows for the application of [the prohibition] to increasingly common situations in which a corporation does not act through a related body corporate, but nonetheless exercises a degree of influence or control, such as through contractual or intellectual property rights, over another entity which itself is directly engaged in activities in an upstream or downstream market.

The phrase 'indirectly through one or more persons' includes situations where a corporation is indirectly supplying or acquiring in a single market through multiple other persons. This phrase also includes situations where the relevant indirect supply or acquisition takes place in multiple markets.

- 34 Indirect supply may include supply through a wholesaler, distributor, reseller, franchisee, licensee, or agent who is not an interconnected body corporate of the firm with substantial market power. It also includes supply on a platform controlled by a firm with substantial market power, where that control gives the firm a degree of influence or control over the sellers or buyers on the platform.
- 35 Generally, a firm with substantial market power would be unlikely to substantially lessen competition in a market in which it does not supply or acquire goods (and is not likely to do so), as it would receive no benefit from doing so. The concept of indirect supply was introduced to deal with situations where firms with a substantial degree of market power may be indirectly involved in a market such that they have an incentive to lessen competition. Examples might include:
- 35.1 A firm with substantial market power that owns a platform on which other firms operate; or
- 35.2 A firm with substantial market power that conducts an aspect of another firm's business, in return for a portion of their revenue.

19 Competition and Consumer Amendment (Misuse of Market Power) Bill 2017 (Cth) (Explanatory Memorandum) at [1.44].

Indirect supply

An Operating System (OS) Provider controls the app store on mobile devices using that OS.

A number of markets are significantly or entirely dependent on access to the app store. That is, competitors in those markets may be unviable without the ability to list their mobile apps on the app store. An example of one such market might be the online food delivery app market.

OS Provider itself may not operate or compete in the markets at issue. However, if OS Provider excluded competing online food delivery apps from the app store and decided to permit only one food delivery app, this could lessen competition in the online food delivery app market.

In such a situation, it is possible that OS Provider could be characterised as indirectly supplying online food delivery services:

- Through its operation of the app store, and the terms it imposes, OS Provider may be able to effectively influence and/or control the operators in these markets.
- OS Provider also benefits from the app revenue, as it receives a portion of all revenue through the App. If a revenue maximising strategy on the part of one online food delivery apps was to reduce competition on or between those platforms, OS Provider might benefit from this.



Person with Substantial Market Power

Person

- 36 The prohibition in Section 36 applies to any person with substantial market power. The Commerce Act defines ‘person’ broadly, including individuals, companies, local authorities, and any association of persons whether incorporated or not.²⁰ This includes trade and professional bodies and non-profit organisations. The Commerce Act also applies to the Crown and Crown Entities, when they are engaged in trade.²¹
- 37 A firm’s market power may be considered together with other firms in the same interconnected group of companies.

Substantial Market Power

- 38 Market power comes from a lack of effective competitive constraint. Any firm that is substantially unconstrained by competitive pressures has “substantial” market power.²² It does not, however, require that a firm has a monopoly, or that a firm is dominant in the sense of substantially controlling the market. A firm with substantial market power may still face some constraint from the conduct of competitors, suppliers, and customers.
- 39 A firm’s market power is most often described as, in the case of a supplier, a firm’s ability to raise prices to above competitive levels for a non-transitory period of time without its rivals taking away sufficient customers to make the price increase unprofitable. A firm may also have market power as a purchaser of goods and services. A firm with substantial purchasing market power might have the ability to worsen prices or terms of trade to sellers.
- 40 More than one firm may have a substantial degree of power in a market.

What Factors Contribute to a Firm’s Market Power?

- 41 There are a range of factors that can influence the degree of competitive constraint faced by a firm, and therefore how much market power it is likely to have. As noted above, both suppliers and purchasers can have substantial market power.
- 42 When assessing whether a firm has substantial market power, we consider the market share of the firm, and how much existing and potential competitive constraint the firm faces. This will include looking at the conditions for entry and expansion. We also look at other factors such as how much countervailing power buyers (or suppliers, in purchasing markets) have.
- 43 Other factors that can influence market power include:²³
 - 43.1 The extent to which the products of the industry are characterised by product differentiation and sales promotion; and
 - 43.2 The character of ‘vertical relationships’ with customers and with suppliers and the extent of vertical integration and/or vertical restraints.

20 Commerce Act, s 2.

21 Commerce Act, ss 5 and 6.

22 *Commerce Commission v Telecom Corporation of New Zealand Ltd*, above n 9, at [33].

23 *Re Queensland Co-operative Milling Association Ltd* (1976), above n 8, at 516.

Market Share

- 44 All other things being equal, the larger the sustained share of the market held by a firm, the more likely it is that the firm will have a substantial degree of market power.
- 45 Market share is not, however, the sole indicator of market power. While substantial market power is frequently accompanied by a substantial market share, other relevant factors must be considered. The most important of these will be the conditions for entry and expansion in the market:
 - 45.1 If the barriers to entry and expansion are low, a high market share does not necessarily indicate substantial market power;²⁴ and
 - 45.2 If the barriers to entry and expansion are high, a persistently high market share is likely to indicate substantial market power.
- 46 Market power is a question to be determined on a case-by-case basis. There is no market share threshold above which a firm will be considered to have substantial market power. There have been cases where a firm with below 30 per cent market share has been found to have substantial market power.²⁵ This is consistent with our view that more than one firm can have substantial market power in the same market.

Existing Competition

- 47 Generally speaking, the larger the number of independent competitors in the market, and the lower the concentration of the market, the less likely it is that a firm will have a substantial degree of market power.
- 48 The Commission will also consider the competitive constraint applied by existing competitors, including whether competitors exert constraint on price, quality and service levels, or encourage the firm to continue to innovate. The ability of customers to import similar products at similar prices from overseas may also be relevant. The greater the constraint applied by existing competitors, the less likely it is that a firm will be found to have a substantial degree of market power.

Potential Entry and Expansion

- 49 The conditions for potential entry or expansion can be decisive in determining whether a firm has substantial market power. If new entry that would place competitive pressure on a firm is likely if the firm were to increase prices or reduce quality, it is less likely that a firm would be found to hold substantial market power. It has been said that:²⁶

Of all [the] elements of market structure, no doubt the most important is... the condition of entry. For it is the ease with which firms may enter which establishes the possibilities of market concentration over time; and it is the threat of the entry of a new firm or a new plant into a market which operates as the ultimate regulator of competitive conduct.

- 50 Conditions of entry may be structural, regulatory, or strategic.
- 51 **Structural** conditions are associated with industry conditions, including the technologies, resources or inputs a firm would need to enter or expand. These include:
 - 51.1 Economies of scale, which reduce per unit costs when production of a single product increases;
 - 51.2 Economies of scope, which reduce per unit costs when more than one product is produced (or transported);
 - 51.3 Industry demand, and whether it is expected to grow, remain at current levels, or decline;

24 *Southern Cross Medical Care Society v Commerce Commission* (2001) 10 TCLR 25 (HC) at [85]; *aff'd Commerce Commission v Southern Cross Medical Care Society* (2001) 10 TCLR 269 (CA).

25 See *Australian Competition & Consumer Commission v Australian Safeway Stores Pty Limited* [2003] FCAFC 149 at [307].

26 *Re Queensland Co-operative Milling Association Ltd*, above n 8, at 516.

- 51.4 Switching costs, which are costs a customer incurs when switching to use a new supplier and costs arising from product compatibility issues;
 - 51.5 Network effects, which refer to when a product or service becomes more valuable the more users it attracts (for example, a new entrant may be at a disadvantage to a competitor that already has a well-established customer base);
 - 51.6 Sunk costs, which are costs that cannot be recovered and raise the costs and risks of failed entry; and
 - 51.7 The difficulties a firm would face in accessing required inputs (which could include access to intellectual property rights) or product distribution channels.
- 52 **Regulatory** conditions include:
- 52.1 Resource management or other planning consent requirements;
 - 52.2 Licensing requirements for a firm or product; and
 - 52.3 Regulations governing standards and quality.
- 53 **Strategic** conditions can also create barriers to entry where incumbent firms take action to discourage prospective entrants or expansion. These could include conditions which disincentivise switching, including charges imposed on customers to terminate a supply contract.
- 54 When considering entry and/or expansion through imports, additional conditions to those identified above include:
- 54.1 Access to the New Zealand market (including tariffs, quotas, import licences/duties, anti-dumping regulations and other laws);
 - 54.2 Customer preference for a New Zealand supplier (reasons for this could include, among others, that customers need to buy other associated services from a New Zealand supplier, or because customers need a supplier to be able to supply on a 'just-in-time' basis); and
 - 54.3 The costs of, and obstacles to, transporting the product in relation to the price of the product, which would depend on factors including:
 - 54.3.1 The logistics of shipping the product and the establishment of distribution networks;
 - 54.3.2 Any need for minimum shipping quantities to ensure economic supply; and
 - 54.3.3 The perishability of the relevant products.

Countervailing Buyer Power

- 55 Generally speaking, where customers have countervailing buyer power, a firm is less likely to be found to have market power. Customers generally have countervailing power where customers have the ability to take action to prevent a firm from increasing prices or reducing quality,²⁷ for example, by:
- 55.1 Sponsoring another firm to enter, for example, by promising a long-term contract to the firm if it entered;
 - 55.2 Entering the market themselves; or
 - 55.3 Credibly threatening to switch to another supplier in relation to another product, or in a different geographic market, where the firm does not have substantial market power.
- 56 If only some customers have countervailing buyer power, this may be an insufficient constraint on a firm to protect all customers and a firm may still be found to have market power.²⁸

²⁷ *Commerce Commission v New Zealand Bus Ltd*, above n 14, at [193].

²⁸ *Commerce Commission v New Zealand Bus Ltd*, above n 14, at [192].

Conduct with the Purpose, Effect, or Likely Effect of Substantially Lessening Competition

- 57 The misuse of market power prohibition does not make it illegal for a firm to have substantial market power. Section 36 only applies where a firm with substantial market power engages in conduct with the purpose, effect, or likely effect of substantially lessening competition.

Engaging in Conduct

- 58 Engaging in conduct includes both doing any act or refusing to do any act.²⁹ Refusing to do an act includes making it known that an act will not be done.³⁰

Purpose, Effect, Likely Effect

- 59 When assessing a firm's conduct, the Commission considers the nature and extent of that conduct, including the firm's commercial rationale.
- 60 The purpose of conduct is the firm's object or aim, what it was intended to achieve.³¹ If the conduct was engaged in for multiple reasons, it will be sufficient if one of the firm's motivating purposes is anticompetitive.³² Once an anti-competitive purpose is established, the existence of some other motive is irrelevant.³³
- 61 Conduct can have a purpose of substantially lessening competition in a market even if it does not have that effect or is not likely to have that effect.³⁴
- 62 Whether a provision has the actual or likely effect of substantially lessening competition is a question of fact.
- 62.1 'Effect' refers to the consequence of a firm's conduct. This is determined objectively by examining the actual impact on the competitive process and the relevant market.
- 62.2 'Likely effect' involves considering results that may happen or could have happened.³⁵ 'Likely' means that there is a real chance or possibility that is not remote. Conduct may have the likely effect of substantially lessening competition at the time it occurs, even though it does not in fact result in a substantial lessening of competition.³⁶

Lessening Competition

- 63 A lessening of competition means that the rivalry between firms has been diminished or lessened, or the competitive process has been compromised or impacted. A lessening of competition includes a hindering and/or prevention of the process of competition.³⁷ Hindering competition includes delaying it.³⁸
- 64 A firm may lessen competition by creating barriers to entry and expansion that mean its competitors are less able to enter, expand or compete based on the merits of their own products. A lessening of competition may manifest in several ways, including higher prices, lower quality, reduced services, reduced choice, and reduced innovation.

29 Commerce Act, s 2(2)(a).

30 Commerce Act, s 2(2)(c). See also *Turners & Growers Ltd v Zespri Group Ltd* (2011) 13 TCLR 286 (HC) at [338].

31 *Union Shipping NZ Ltd v Port Nelson Ltd*, above n 12, at 707.

32 Commerce Act, s 2(5).

33 *Queensland Wire Industries Pty Ltd v Broken Hill Pty Co Ltd* (1989) 167 CLR 177 at [28].

34 *ANZCO Foods Waitara Ltd v AFFCO New Zealand Ltd* [2006] 3 NZLR 351 (CA) at [152]-[154] per William Young J, and [302] per Anderson P.

35 *Commerce Commission v Bay of Plenty Electricity Ltd*, above n 14, at [342].

36 *Port Nelson (CA)*, above n 11, at 567.

37 Commerce Act, s 3(2).

38 *Commerce Commission v Port Nelson Ltd* (1995) 6 TCLR 406 (HC) (*Port Nelson (HC)*) at 434.

- 65 The substantial lessening of competition test is a relative standard. We ask whether conduct would increase a firm’s market power relative to its market power without the conduct. That is, has the firm’s market power moved along the spectrum away from perfect competition towards monopoly? To say that competition has been lessened is equivalent to saying that market power has increased.³⁹ A lessening of competition could also include a firm maintaining market power in circumstances that would not have been possible without the conduct.

Substantial

- 66 Only a lessening of competition that is substantial is prohibited. A lessening of competition will be substantial if it is real, of substance, or more than nominal.⁴⁰ Some courts have used the word material to describe a lessening of competition that is substantial.⁴¹ Others have focussed on whether the lessening is “meaningful or relevant to the competitive process”.⁴²
- 67 No bright line separates a lessening of competition that is substantial from one which is not. What is substantial is a matter of judgement and depends on the facts of each case. The effect of a lessening of competition may be to increase or maintain prices or margins. The percentage price increase that gives rise to a substantial lessening of competition may vary from market to market. Where goods are supplied at low margins but frequently, small increases in prices can lead to significant increased revenue to the supplier and significant consumer harm. An equivalent impact on other dimensions of competition, including quality, range, service or innovation, is likely to be substantial if it endures beyond the short term.
- 68 A lessening of competition does not need to be felt across an entire market or relate to all dimensions of competition in a market, for that lessening to be substantial. A lessening of competition that adversely affects a significant section of the market may be enough to amount to a substantial lessening of competition.⁴³

How We Analyse Competitive Effects and Likely Effects

- 69 To assess whether conduct has substantially lessened competition, or is likely to do so, requires us to compare the likely state of competition with the conduct (often referred to as the factual) with the state of competition without the conduct (often referred to as the counterfactual).⁴⁴ This is often referred to as a “with-or-without” test.
- 70 The question whether a substantial lessening of competition has an actual or likely effect is determined by means of a counterfactual analysis comparing:⁴⁵
- 70.1 In the case of an “effect”, the actual state of competition in the market with the state of competition that would have occurred in the absence of the conduct; and
 - 70.2 In the case of “likely effect”, the likely state of competition if the conduct is engaged in with the likely state of competition if it is not.

39 *Woolworths Ltd v Commerce Commission* (2008) 8 NZBLC 102,128 (HC) at [127].

40 At [127].

41 At [129].

42 *Rural Press Ltd v Australian Competition & Consumer Commission* [2003] HCA 75, (2003) 216 CLR 53 at [41]; and *Universal Music Australia Pty Ltd v Australian Competition & Consumer Commission* [2003] FCAFC 193, (2003) 131 FCR 529 at [242].

43 *Dandy Power Equipment Pty Ltd v Mercury Marine Pty Ltd* (1982) 44 ALR 173 (FCA) at 191.

44 At 191.

45 *Commerce Commission v Bay of Plenty Electricity Ltd*, above n 14, at [349].

- 71 Past conduct may have had the likely effect of substantially lessening competition even though it did not, in fact, have that effect.⁴⁶
- 72 Although the test is not a “before and after” test, the state of competition in the market prior to the conduct will often reflect the state of competition that would have occurred in the market had the conduct not been engaged in. Equally, in the case of proposed conduct, or conduct that has only recently occurred, the status quo may provide a guide as to the likely future state of competition in the market absent the conduct.
- 73 A substantial lessening of competition may arise where the conduct makes entry and expansion more difficult, or otherwise reduces the ability or incentive of competitors to provide a competitive constraint. Conduct does not need to force a competitor, or competitors, to exit the market to have this effect.
- 74 Conduct may affect competition even if it affects only some competitors in a market. The impact on competition may depend on the nature of the competitors:
- 74.1 Where the conduct affects the ability or incentive of a particularly aggressive or destabilising competitor to provide a competitive constraint, a substantial lessening of competition is more likely.
- 74.2 Where there remain other effective competitors who are unaffected by the conduct, the conduct will often be less likely to substantially lessen competition.
- 75 The ultimate question is whether the conduct has lessened, or is likely to lessen, the constraints that operate on the firm with market power, or that would have emerged absent the conduct. In answering that, several other questions may be asked:⁴⁷
- 75.1 To what extent are customers or inputs foreclosed by the conduct, and what alternatives do customers or competitors in the market have?
- 75.2 To what extent does the conduct impose costs on competitors or potential entrants that are not faced by the firm in question?
- 75.3 Does the conduct have the effect of harming incentives to innovate by other competitors in the market?
- 75.4 Does the conduct have the effect of causing competitors in the market to compete less vigorously?
- 75.5 Does the conduct make it harder for potential entrants to enter the market in question in response to profitable opportunities to do so?
- 75.6 Does the conduct enable the firm in question to exercise power over suppliers, customers or competitors?
- 75.7 How long are these effects likely to continue?
- 76 A substantial effect on competition is more likely to occur where:
- 76.1 the existing competition is limited; and/or
- 76.2 conditions for entry or expansion are difficult.
- 77 In assessing whether the conduct has, or is likely to have, the effect of substantially lessening competition, we will consider any pro-competitive effects of the conduct that the parties identify to the Commission.

⁴⁶ *Port Nelson (CA)*, above n 11, at 567.

⁴⁷ *Re Weddel Crown Corp Ltd* (1987) 2 TCLR 215 at 227.

Types of Conduct That May Substantially Lessen Competition

- 78 The types of unilateral conduct that may substantially lessen competition are potentially very broad. The misuse of market power prohibition applies to any conduct by firms with substantial market power that has the purpose, effect or likely effect of substantially lessening competition.
- 79 Assistance can be gained from considering the types of conduct that are prohibited or permitted in other jurisdictions, and in what circumstances that conduct is prohibited or permitted. Care should be taken, however, not to substitute overseas approaches to particular types of conduct for the statutory test.⁴⁸
- 80 In particular:
- 80.1 The prohibition is not limited to conduct that lessens competition by full or partial exclusion of existing or potential competitors. The prohibition would also cover conduct that substantially lessened competition by reducing competitors' incentive or ability to compete.
- 80.2 The prohibition does not cover "exploitative conduct", where existing market power is used against customers.
- 81 It is also important to bear in mind that the categories of conduct can frequently overlap. What matters is their combined actual or potential impact on competition, rather than how the conduct is characterised.
- 82 Conduct that involves a contract, arrangement, understanding or covenant can contravene both section 36 of the Act and the prohibitions in sections 27 and 28 of the Act. However, the same conduct may only be penalised once.⁴⁹
- 83 It is not possible to precisely and exhaustively identify and categorise all types of conduct that may substantially lessen competition. We can, however, identify some conduct that is at increased risk of substantially lessening competition based on New Zealand and overseas experience. These include:
- 83.1 Refusal to supply an input;
- 83.2 Margin/price squeezing;
- 83.3 Exclusive dealing;
- 83.4 Loyalty rebates; and/or
- 83.5 Tying and bundling.

Refusal to Supply an Input

- 84 Firms are generally entitled to choose who they will supply. However, when a firm with substantial market power refuses to supply an input to downstream firm(s), it may hinder or prevent those firms from competing in the downstream market.⁵⁰ In passing the amended misuse of market power prohibition, Parliament made clear that a refusal to supply by a firm with substantial market power may contravene the amended section 36, where that refusal has the purpose, effect, or likely effect of substantially lessening competition.⁵¹

48 *Auckland Regional Authority v Mutual Rental Cars (Auckland Airport) Ltd*, above n 7, at 665; *Port Nelson (CA)*, above n 11, at 569; *Fisher & Paykel Ltd v Commerce Commission*, above n 7, at 756-757.

49 Commerce Act, s 80(6).

50 This situation most commonly arises when the firm with substantial market power is vertically integrated and competes in the downstream market.

51 Commerce Amendment Bill 2021 (9-1) (Explanatory note) at 1.

- 85 A firm with substantial market power may in some circumstances therefore be required to supply a wholesale input to a downstream competitor.⁵²
- 86 A refusal to supply can include:
- 86.1 A literal refusal in response to a request for supply;
 - 86.2 A constructive refusal to supply, for example by responding with a request for supply with terms that no competitor would reasonably be willing to accept; or
 - 86.3 Making it known that, if a request for supply was made, it would be refused (or that supply would only be made on terms that no competitor would reasonably be willing to accept).
- 87 Two factors are likely to significantly influence whether a refusal to supply has the purpose, effect, or likely effect of substantially lessening competition:
- 87.1 The extent to which the input is required for competition in the relevant market. If there are sufficiently close substitute inputs, or alternative methods that do not require the input, competition is less likely to be affected by a refusal to supply. The closer the input is to essential, the more likely it is that competition will be lessened.
 - 87.2 The extent to which there are alternative sources of competitive supply of the input, including through entry. If the input is available from other sources on similar terms, or could become available with commercially viable investment within a reasonable timeframe, competition is less likely to be affected. Where there are few or no viable alternatives for supply, it is more likely that competition will be lessened.
- 88 A refusal to supply may substantially lessen competition without completely preventing the downstream rival from competing. For example, a refusal to supply might raise rivals' costs significantly because the rival must use a more costly alternative, thus reducing their competitive constraint and enabling a firm with substantial market power to increase its prices or reduce quality and innovation.



52 *Telecom Corporation of New Zealand v Commerce Commission* [2012] NZCA 278 at [129]-[132]; *Queensland Wire Industries Pty Ltd v Broken Hill Pty Co Ltd*, above n 35, at [28]-[29] per Mason CJ and Wilson J, and [10]-[11] per Deane J.; *NT Power Generation v Power and Water Authority* [2004] HCA 48; 219 CLR 90 at [85] and [115]; and note also *Commerce Commission v Bay of Plenty Electricity Ltd*, above n 14, at [387]-[388].

Example: Refusal to Supply

Company A supplies festivals with the processing system and hardware to offer cashless payments on festival branded wristbands supplied by Company A. Company A's wristbands have become very popular and are used in around three quarters of major festivals in New Zealand.

Company A does not charge festival organisers to supply wristband payment systems, but charges customers fees when they put money onto their wristband. It also takes a percentage of all payments made through the system.

Company B provides mobile phone payment services to businesses and has its own payments processing system.

Company B writes to Company A seeking an arrangement to interoperate its payments processing system with Company A's wristbands so that it can also process payments for customers when they are supplying festivals. It is technically feasible for Company A to interconnect its wristband payment system with Company B's payments processing system.

Company A indicates it would be happy to consider an arrangement, but requests extensive information from Company B over several months. When Company B declines to provide commercially sensitive details of its interconnection arrangements with other financial institutions and details of Company B's intellectual property, Company A declines Company B's request.

Company B complains to the Commission.

- Although Company A may be the only supplier of the processing system and hardware for wristbands, it is not clear whether that results in it having a substantial degree of market power. Festival organisers have other payment alternatives, including contactless payments like Paywave, cash, mobile EFTPOS terminals, and online payment systems. The Commission would consider whether these alternatives constrained Company A to the point that it did not have substantial market power.
- If Company A did have substantial market power, it may be relatively unconstrained by competition. Unless the threat of entry is extremely strong, entry by Company B would be likely to substantially increase competition.
- If Company A did have substantial market power, then its conduct may risk contravening the Act. Imposing significant burdens on an access seeker that relate only to terms and conditions necessary to enable access can amount to a constructive refusal to supply.

Price Squeeze

- 89 A price/margin squeeze is generally considered to occur when a vertically integrated firm with substantial market power sets prices in the upstream wholesale market in a manner that prevents efficient competitors from profitably operating in the downstream retail market.⁵³ In some situations, a price squeeze may also be viewed as a constructive refusal to deal.
- 90 A firm with substantial market power in the supply of an important input can disadvantage its competitors in downstream markets by charging a high wholesale price that reduces the margin available to these competitors in the downstream market.
- 91 Where competitors in the downstream market require the input and have limited alternative sources of competitive supply, a margin or price squeeze has the potential to prevent efficient competitors in the downstream market from competing with the firm in that market on their merits, or prevent competing firms from gaining sufficient size and scale to achieve an equal footing with existing participants in the market.
- 92 Whether a substantial lessening of competition is likely will depend on the circumstances of the case. Two factors are likely to significantly influence whether alleged price squeezing conduct has the purpose, effect, or likely effect of substantially lessening competition:
- 92.1 First, the extent to which the input is required for competition in the relevant market. To the extent there are substitute inputs, or alternative methods that do not require the input, competition is less likely to be affected.
- 92.2 Second, the extent to which there are alternative sources of supply of the input, including through entry. Competition is unlikely to be substantially lessened if the input is available at a competitive price from other firms, or could become available, with economically rational investment.
- 93 Where there are limited competitive alternatives to the input, and the available retail margin would be insufficient to enable efficient competitors from profitably operating in the downstream market, or to facilitate newer entrants from achieving an equal footing with existing competitors, competition is likely to be substantially lessened.



53 *Telecom Corporation of New Zealand Ltd v Commerce Commission*, above n 54, at [2].

Price Squeeze

Manufacturer A is New Zealand's only domestic producer of steel products, including extruded steel bars that can be turned into fence posts, which are used throughout New Zealand. The relatively low value of steel bars compared to their weight means imports are not cost effective and are therefore uncommon.

The cost of converting steel bar into fence posts is around 20c per post at the volume Manufacturer A produces. Manufacturer A's sister company sells building and farming products include fencing products. The retail price of fences posts depends on the height of the fence, but ranges between \$5.50 and \$7.70 a metre.

Company B imports wire and installs fences throughout the Northland region. It approaches Manufacturer A to purchase steel bars that it can process into fence posts. Manufacturing its own posts will enable Company B to provide more innovative products, such as insulated wire attachments for use with electric fences, and potentially offer more cost competitive fence posts for its customers.

Manufacturer A offers to sell Company B steel bars at a delivered price of \$6.50 per linear metre. It will also provide finished fence posts at its retail list price.

NFL complains to the Commission.

- Manufacturer A likely has substantial market power in some markets for steel manufacturing, given the practical barriers to entry associated with building another steel mill, and the economies of scale and scope Manufacturer A's steel mill has. The Commission would investigate the extent to which imports may constrain Manufacturer A.
- The price Manufacturer A is proposing to charge for steel bars would be close to or above the retail price for some lengths of fence post, potentially reducing the margin available to Company B. This could be of concern if Manufacturer A's conduct disincentivised entry by Company B, or prevented Company B from engaging in competition on the merits (for example, competing on price with Manufacturer A or engaging in innovation).
- The Commission would consider the likely cost of manufacturing fence posts for Manufacturer A and Company B. The Commission would also consider the extent to which other substitutes are available (for example, the extent to which wooden fence posts were an effective alternative, or Company B is able to import posts or steel bars).

Exclusive Dealing

- 94 Broadly speaking, exclusive dealing occurs when a firm trading with another imposes some restrictions on the other's freedom to choose with whom they deal.
- 95 Exclusive dealing generally involves a buyer agreeing (or being induced) to purchase certain goods or services only or primarily from a particular seller from a period of time. For example, a retailer could be prevented from stocking a competing product; or a manufacturer could be prevented from using a competitor's component as an input in the production of goods. Exclusive dealing may foreclose rivals' access to customers or distribution channels, hindering or preventing them from competing in the relevant market.
- 96 Exclusive dealing may similarly involve a supplier agreeing to supply only or primarily to a particular firm and not to rival retailers or manufacturers. This could foreclose rivals' access to an input, hindering or preventing them from competing in the relevant market.

- 97 Exclusive dealing may be achieved through contractual means or through economic inducements. For example, loyalty rebate or conditional discount schemes may incentivise exclusive dealing arrangements.
- 98 Exclusive dealing by a firm with substantial market power is more likely to substantially lessen competition where it continues for a significant period and:
- 98.1 The exclusive dealing will deny competitors access to an input for which there are limited substitutes, and which are not available cost-effectively from other firms; or
 - 98.2 The exclusive dealing will deny competitors access to a downstream facility or service, such as an important distribution channel, for which there are limited cost-effective substitutes; or
 - 98.3 The exclusive dealing will deny competitors access to a sufficient share of customers or inputs to achieve the scale needed to compete effectively.
- 99 The greater the degree of foreclosure, the more likely it is to substantially lessen competition. Exclusive dealing can, however, substantially lessen competition without completely foreclosing access. For example, exclusive dealing might raise rivals' costs significantly, reducing their competitive constraint and enabling a firm with substantial market power to maintain or increase its prices.

Examples

Exclusive dealing 1

Company A is a manufacturer of electronics, including televisions and computers. It is a major supplier to the New Zealand market with a strong, positive reputation with New Zealand customers. Company A primarily supplies via the retail channel. It has a market share in the retail channel in various product markets of approximately 60%.

Company A's distribution agreements with retailers as a matter of practice include provisions that require retailers not to stock more than 40% of their products from any other brand name. Retailers also obtain significant discounts if more than 70% of their television offerings come from Company A.

Company A also includes provisions requiring retailers to obtain Company A's consent in respect of the other brands that retailers may stock. Company A states that this practice is to maintain the reputation of its product as a "premium" product. Company A does not wish to supply its product to retail stores that also sell non-premium products.

- The Commission would consider whether Company A has substantial market power in the supply of electronics, and any relevant sub-markets, to the retail channel. The Commission would consider the significance of Company A's products in the relevant markets (including whether the products comprise 'must stock' products), the level of competitive constraint applied by competing brands, and any countervailing power exerted by retailers.
- If Company A has substantial market power, its conduct may be of concern if, as a result of Company A's contracting practices, insufficient retail volumes remain available to competitors, such that competitors are foreclosed or prevented from entering or expanding. Company A's conduct may be of particular concern if lower cost competitors are disproportionately excluded from the retail market, softening price competition at the retail level. The duration of the distribution agreements and any ability on the part of the retailers to terminate the contract early will also be relevant to the analysis.

Exclusive Dealing 2

Manufacturer A is New Zealand's only manufacturer of high-quality glass for construction purposes. Imports of glass are not common due to the delicacy of glass, but some imports do occur.

Glass manufacturing requires high quality silica sand. High quality silica sand makes up a small fraction of all sand and requires resource consent to extract. Manufacturer A currently has the exclusive rights to the only sand deposit in New Zealand.

A Mining Company has obtained resource consent for a quarry and will remove large quantities of high-quality silica to expand the quarry. Appropriately disposing of the sand is a condition of Mining Company's resource consent. Manufacturer A enters into an exclusive agreement with Mining Company to buy all the sand at the new quarry, despite already having many years of supply at its existing sand depot.

Manufacturer B is a major manufacturer of building products. Manufacturer B does not make glass, but imports it from time to time when a client requests it. It had been considering whether to enter glass manufacturing, and contacts Mining Company to find out the cost of its high-quality sand. Upon learning of the exclusive contract, Manufacturer B complains to the Commission.

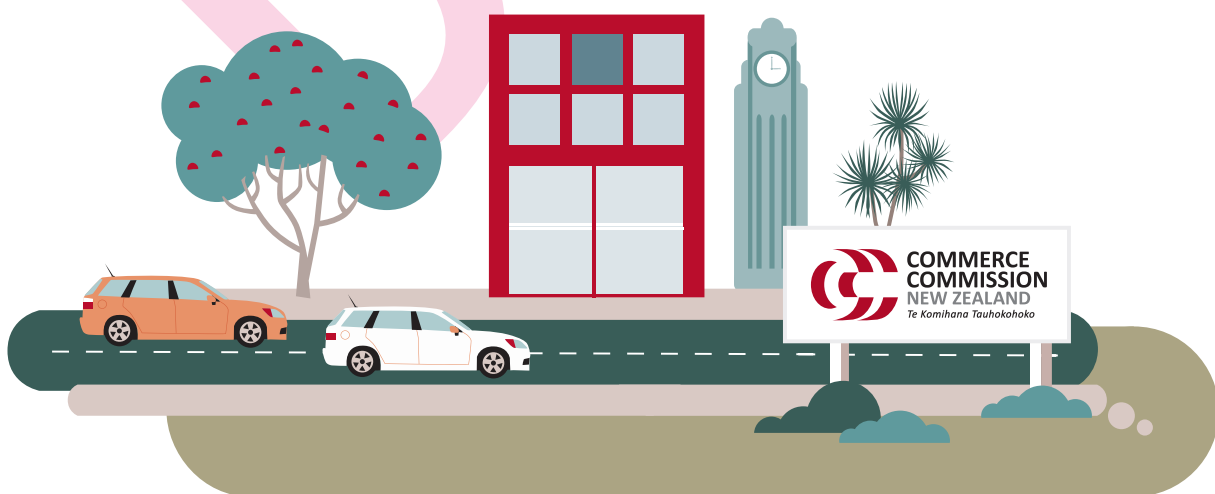
- Manufacturer A likely has substantial market power in the market for glass manufacturing, although the Commission would consider the extent to which imports operate as a constraint. New entry is likely to be difficult given the scarcity of the main input (high quality silica sand).
- The exclusive arrangement between Mining Company and Manufacturer A has the potential to substantially lessen competition. The Commission would consider the availability of alternative sources of supply, and where they are absent, uncommon or involve significant cost/quality compromises, an exclusive arrangement is more likely to raise competition issues.
- In establishing the effect and likely effect of the exclusivity arrangement, the Commission would consider the arrangement that would have been reached absent that exclusivity arrangement. Here, Mining Company would still need to dispose of the sand. The Commission would then consider whether it was likely that Manufacturer B would, absent the exclusivity, have entered the market if silica sand supply was available.

Loyalty Rebates and Conditional Discounts

- 100 A loyalty rebate is a post-purchase discount given by a supplier to a purchaser under certain conditions. Conditional discounts involve a supplier offering customers a pre-purchase discount if they meet certain conditions. For example, customers may be required to purchase a certain proportion of their stock or certain volumes from the firm to qualify for the rebate or discount.
- 101 Rebates and discounts offered to retailers or distributors by a supplier with substantial market power can harm competition by reducing the ability of other suppliers to compete effectively. Some rebate schemes may induce strong incentives for buyers to achieve a minimum level of sales of the firm's products, or a given market share. This can hinder smaller rivals from competing by raising their costs and restricting their access to sufficient distribution channels, and ultimately end consumers, to achieve necessary scale.
- 102 Loyalty rebates and conditional discounts may even encourage partial or full exclusivity and can therefore have the same potential to foreclose customers as an exclusive dealing arrangement.⁵⁴

⁵⁴ For this reason, the framework for considering loyalty rebates and conditional discounts is likely to be similar for considering exclusive dealing.

- 103 The anti-competitive effects of rebates are likely to be strongest where the firm offering the rebate has a large assured or captive supply base. This means that only a portion of the market is ‘contestable’ to rivals. If rivals can compete for all of the market (because the firm offering the rebate does not have a ‘must have’ product or large assured supply base) rebates are less likely to have an anti-competitive effect, as rivals can match or improve the offer provided by the firm offering the rebate.
- 104 There is also the potential for the use of rebates by a majority of suppliers in a market that has a small number of similar sized players to harm competition by facilitating accommodating behaviour.
- 105 In assessing rebates, the Commission will have regard to:
- 105.1 The type of rebate. Different rebate structures are likely to affect competition to differing extents. For example, rebates may be structured in a way which makes it very costly for a purchaser to switch even small amounts of volume away from the established supplier. This disincentivises switching to an alternative supplier. This is sometimes referred to as ‘quantity forcing’. In order to entice a buyer to switch, an alternative supplier attempting to win even a small share of supply would have to offer buyers a relatively greater discount to compensate for the loss of the rebate on the share of the buyer’s purchases which remain with the incumbent supplier;
 - 105.2 The size of rebate (i.e., how large the discount is for the contestable share of the market);
 - 105.3 The extent to which the rebate structures are targeted at different customers’ requirements; and
 - 105.4 The extent to which alternative distribution options are available to rival suppliers.



Tying and Bundling

- 106 'Tying' occurs when a supplier sells one good or service on the condition that the purchaser buys another good or service from the supplier. In other words, product A is only available if the buyer also agrees to buy product B.
- 107 'Bundling' occurs when a supplier offers two or more products for a lower price if the products are purchased as a package.
- 108 Selling products together in this way can often be good for both consumers and suppliers but, sometimes, tying and bundling can harm competition. For example, if a firm has substantial market power in the supply of product A, but faces competition in the supply of B, then by tying the supply of A and B together the firm may be able to use its power in A to prevent other suppliers from competing effectively in the supply of B.

Examples

Tying

Big Book Ltd (BBL) is a supplier of textbooks, particularly to universities. It is one of several major textbook suppliers but, due to an arrangement with the governing body for legal education in New Zealand, is the only supplier of textbooks on New Zealand law.

University A conducts tenders for textbooks split by Department. The textbooks of the successful tenderer for each Department will be made the compulsory texts at University A and will be supplied through the university bookshop.

The law school at University A sits within the Humanities Department. BBL's tender to the Humanities Department includes law textbooks, but only if University A agrees to award BBL all its broader Humanities Department textbook requirements.

University A accepts this arrangement, and a competitor complains to the Commission.

- BBL likely has substantial market power in the market for legal textbooks, if that is an appropriate market.
- The Commission would consider the size of the remaining portion of the market. The conduct could be particularly problematic if rival suppliers were also foreclosed from supplying other universities in New Zealand and Departments at University A. The Commission would investigate whether BBL's tendering practices were utilised at other universities.

Bundling

In the above fact scenario, BBL instead responds to the Humanities Department tender by offering a significant discount from the standard retail price on all textbooks required by the Humanities Department if they are bought together in a bundle. Otherwise, University A must purchase textbooks from BBL at standard retail price, which includes very high prices for law textbooks.

- In addition to the above, the Commission would consider whether suppliers of other Humanities Department textbooks were able to offer a competing bundle or individual products at a sufficiently low price to compensate for the loss of the bundled discount offered by BBL.

Predation

- 109 Firms compete by providing more compelling offers to consumers than their competitors. This often involves firms undercutting prices offered by rivals. In almost all circumstances low pricing is beneficial for consumers and is part of the competitive process. However, very low pricing by a firm with substantial market power may in some situations be predatory.
- 110 Predatory pricing occurs when a firm substantially reduces its prices for a sustained period or at strategic times to induce exit or deter entry. Predatory pricing may prevent competing firms from gaining sufficient size and scale to achieve an equal footing with existing participants in the market. Predatory pricing can lessen competition in at least one of three ways:
- 110.1 By causing one or more competitors to exit the market, reducing the constraint that they place on the firm with substantial market power;
- 110.2 By discouraging potential competitors from entering the market, reducing the constraint the firm with substantial market power faces from the threat of entry in the future; and
- 110.3 Disciplining or damaging existing competitors for competing aggressively, discouraging them from engaging in such conduct in the future.
- 111 Predatory pricing may result in a firm, or division of a firm (for example in relation to a particular product line or geographic area), investing in the prospect of changing the market structure in the future by foregoing profit in the short to medium term. If competition has been lessened, then the firm would expect to recover this in the longer term by charging higher prices and maintaining or increasing its market share.
- 112 However, while evidence of actual or potential recoupment may be evidence of a lessening of competition, it is not required if the Court is satisfied that competition has been lessened.⁵⁵
- 113 However, as the Court of Appeal has noted, merely supplying below cost is not unlawful:⁵⁶

It is not a contravention ... to offer or sell goods or services at less than cost. The section requires proof of the substantial lessening of competition – not merely aggressive competitive conduct. The purpose or (likely) effect must be more than short term and must impact upon the competitive process in the particular market structure. The mere fact that a participant operates in the market at a loss, and even fails, will not necessarily lessen competition.

55 *Port Nelson (CA)*, above n 11, at 571.

56 At 571 (made in the context of section 27 of the Commerce Act).

Predation

Company A supplies payment processing systems such as EFTPOS terminals to taxi drivers in New Zealand. It also offers other products and services, such as taxi meters, booking and dispatch services, and charge cards offered by taxis to frequent customers.

Company A does not charge taxis upfront for supplying payment processing terminals, but levies a 10% service fee on all payments made using its payment processing systems. Company A supplies 90% of New Zealand taxis with payment processing systems.

Company B is a rival supplier of payment processing systems and taxi meters and has recently entered the market. It has acquired a 10% share in the supply of payment processing systems and taxi meters.

To further grow its market share, Company B offers new customers a 25% discount on the service fee for its payment processing systems. Company A responds by offering a 50% discount on its service fee, including for its pre-existing customers, that Company B cannot profitably match. Company A returns its service fees to their usual levels once Company B's offer expires.

Company B attempts to offer similar discount schemes several times during a 2 year period, and each time is met with a deep discounting response by Company A. Eventually, Company B ceases offering discounts and its market share remains around 10%.

Company B complaints to the Commission.

- Company A likely has substantial market power in the market for payment processing systems for taxis (if this is the appropriate market) due to its share of the market.
- The Commission would consider whether Company A has an anticompetitive purpose; and as part of that will consider any legitimate business justifications for the discounting put forward by Company A.
- The Commission would consider whether the deep discounting by Company A in response to Company B's discounting has had the effect of preventing expansion by Company B, with the effect of substantially lessening competition.
- The Commission would also consider whether the deep discounting may have had the effect of signalling to Company B that discounting to win market share will be met with similar deep discounts, softening competition and resulting in higher service fees for taxi companies; with flow on impacts for the cost of taxi services for end customers
- The deep discounting in response to Company B's discounting may have had the effect of signalling to other potential competitors that attempts to enter and win market share will be met with similar deep discounts. This may discourage entry, which may substantially lessen competition. The Commission would consider the conditions of entry and whether there were likely additional entrants absent the discounts.

Other Conduct

- 114 As noted above, it is not possible to precisely and exhaustively identify and categorise all types of conduct that may substantially lessen competition. Some other ways in which conduct may be harmful include (but are not limited to):
- 114.1 **Raising regulatory barriers:** conduct by a firm with substantial market power can make the conditions for entry more difficult by encouraging the creation or maintenance of regulatory barriers. This may reduce the constraint that entry places on the firm with substantial market power. This can include standard setting, where standards exclude actual or potential competitors.
 - 114.2 **Abuse of legal rights:** a firm with substantial market power may utilise legal or regulatory proceedings in an unreasonable or vexatious manner in order to hinder or exclude rivals or potential entrants.
 - 114.3 **Restricting interoperability:** conduct by a firm with substantial market power can restrict the ability of its products to operate with the products of its competitors. This can hamper customer switching, reducing existing competition and making entry more difficult.
 - 114.4 **Self-preferencing:** Self-preferencing involves conduct by firm with substantial market power that is designed to favour its own products or services over those of its competitors. For example, an online market may preferentially show products of the platform owner even where these are not the best fit for the customer's search terms.
 - 114.5 **Brand proliferation/saturation:** Brand proliferation involves conduct by a firm with substantial market power that produces a large number of substitutable brands for the same product. This can increase the brand investment required by a new entrant to sustainably enter the market.
 - 114.6 **Forced Free Riding:** Forced free riding involves conduct by a firm with substantial market power to appropriate the innovation or effort undertaken by rival firms. For example, an online platform may use data or content generated by rivals use of the platform in order to produce rival products that divert sales or traffic away from those rivals.

Examples

Raising Rivals Costs / Regulatory Barriers

LinePower owns the local electricity distribution network in Region A. LinePower's primary business is in owning and maintaining the local electricity lines network. LinePower has a subsidiary - LinePower Electrical (LPE) - that (amongst other electrical services) undertakes connections to LinePower's lines network on behalf of LinePower.

Big City Electrical is a competing electrical business that (amongst other services) offers electrical connections. Big City Electrical wants to enter the connections market in Region A. It requests that LinePower allow its electricians to undertake connections to the LinePower lines network.

LinePower agrees to allow Big City Electrical electricians to connect to the LinePower network but requires Big City Electrical to submit extensive connection plans to LinePower at least 90 days before each connection so that LinePower can ensure that its quality and safety standards are met; and pay LinePower a fee of 15% of the total cost of the electrical works to facilitate a connection.

Big City Electrical complains that it is unable to offer a competitive service due to the administrative requirements associated with submitting connection plans, and the 15% fee (which LPE is not required to pay).

- LinePower likely has substantial market power in the market for electricity distribution and connection services in Region A, given the practical impossibility of replicating or bypassing its network.
- Imposing reasonable measures to safeguard quality and safety standards is unlikely to substantially reduce competition but could raise concerns if LinePower sought to impose quality or safety requirements that were unnecessary, or which impacted Big City Electrical's ability to compete (by increasing cost or reducing the scope for innovation).
- Imposing additional administrative hurdles on a new entrant could raise concerns if they are significantly more onerous than the administrative hurdles faced when customers use the services of the firm with substantial market power. The Commission would test whether LinePower imposed similar requirements or procedures on LPE.
- The 15% fee imposed on Big City Electrical for connections could raise concerns where the fee is significantly larger than the cost LinePower would charge customers who used LPE. The Commission would consider any legitimate business justification offered by LinePower regarding the imposition of this fee.

Types of Conduct That are Unlikely to Substantially Lessen Competition

- 115 The Commission aims to distinguish between desirable vigorous competition, which may harm individual competitors but which delivers good outcomes for consumers, and conduct that harms the competitive process and results in consumer harm.
- 116 Section 36 does not prohibit a firm from having substantial market power. A firm with substantial market power may continue to possess market power, provided it does not engage in conduct to substantially lessen competition.
- 117 Section 36 also does not prohibit a firm from charging high prices to end consumers.
- 118 It is not unlawful for a firm with substantial market power to compete strongly, even where that causes competitors to lose sales or even to exit. Competition is unlikely to be substantially lessened by:
 - 118.1 Genuine innovation, including the offering of new products or better or more efficient ways of delivering existing products;
 - 118.2 Conduct that improves efficiency and drives down costs and prices to consumers; and
 - 118.3 Firms responding to competitive offerings in the market by sustainably improving the quality or price of their product.
- 119 Firms and advisors should reassess their position at appropriate intervals, and consider whether conduct remains unlikely to breach s 36 of the Commerce Act, for example where there have been significant changes in market dynamics and/or the firm's market power.

Types of conduct that are unlikely to SLC

Transport Bay of Plenty (TBP) is the provider of public transport services for the Bay of Plenty. It is the only body able to access subsidies from central government, and no firm could compete without access to those subsidies.

TBP proposes to hold a round of tenders for bus routes for a period of 5 years. It proposes to consolidate the number of routes, potentially reducing the number of firms that will be able to provide services. Bus patronage has declined following a greater move to “working from home”, and TBP’s expectation is that this will deliver cost savings and greater efficiencies that avoid any need to cut bus routes.

A local transport firm complains that the tendering process will substantially lessen competition because a number of local firms will miss out on routes.

- TBP likely has a substantial degree of market power in relation to the purchase of Public Transport in the Bay of Plenty.
- Although the tender may reduce the number of operators in the market, it has not reduced competition for the market at the point of tender.
- It is unlikely that TBP would intentionally lessen competition in the tendering market in which it acquires services. Doing so would expose TBP, in future years, to price increases, reduced innovation, and/or lower levels of services.
- Although some firms may cease providing services following the tender, competition for the market at the time of the next tendering round will not be lessened provided that there are likely to remain sufficient firms who can compete.
- Absent evidence to the contrary, the Commission would expect TBP to be well incentivised, in the factual, to conduct its procurement process to ensure sufficient tenders are received.



Types of conduct that are unlikely to SLC

HOPNZ is a domestic grower of hops for use in the production of high value craft beer. The flavours in hops are very time sensitive, meaning fresh hops are only available for short time in Autumn each year, with the balance being dried or pelletised.

In response to increased demand for “fresh hop” beers, HOPNZ develops technology that enables it to supply hops to produce “fresh hop” beers regularly throughout the year. As a result it is able to charge a substantial premium for its hops, and demand for dried hops is somewhat reduced in the period that “fresh” hops are available.

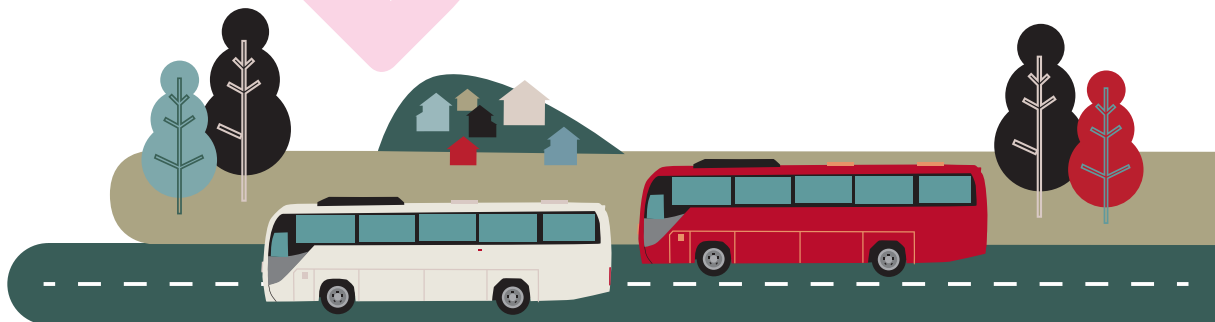
HOPNZ declines to license its innovation to other hop growers, who must accordingly discount their comparable hop varieties. A rival grower complains that HOPNZ conduct is substantially lessening competition.

- HOPNZ’s ability to charge more for its hops does not mean it has a substantial degree of market power. HOPNZ is providing brewers with a higher quality product that may justify the increased price premium.
- HOPNZ’s product does not appear to be essential as rivals are able to supply brewers with alternative hops, albeit at a lower price. Other hop growers may be required to invest in innovations, such as a new flavours, or make efficiency gains to enable them to maintain existing levels of profitability.
- HOPNZ’s refusal to license could raise issues over time if market dynamics were to shift such that fresh hops beer became sufficiently desirable as to give rise to its own product market, or a substantial part of a market.

Statutory Authorisation

120 Conduct that is specifically authorised or required by another Act will not contravene the Commerce Act.⁵⁷

121 There are many Acts that contain specific exceptions to the Commerce Act. A list of these, as at the date of publication, is included as an appendix to these guidelines.



⁵⁷ Commerce Act, s 43.

Authorisation

- 122 Authorisation provides protection against legal action for future conduct that might breach the Commerce Act including the misuse of market power prohibition.
- 123 A firm can apply to the Commission for authorisation where they believe that there is some risk that the conduct they propose to engage in would or may breach s 36 of the Commerce Act.
- 124 We must authorise conduct breaching s 36 of the Commerce Act where we are satisfied that engaging in the conduct will be likely to result in a benefit to the public that would outweigh the lessening in competition (the 'public benefit' test).⁵⁸
- 125 When we receive an authorisation application, we must first assess whether the conduct is likely to lessen competition. We call this the 'competition threshold'.⁵⁹
- 126 If we determine that conduct does not meet the competition threshold, it will not be necessary for the Commission to consider whether to grant authorisation. If we determine that conduct meets this competition threshold, we apply the public benefit test to determine whether to authorise the agreement.
- 127 The applicant bears the burden of demonstrating to the Commission that the public benefit test is satisfied.
- 128 Authorisation may be appropriate where:
 - 128.1 Conduct may lessen competition in one market but promote competition in another market.
 - 128.2 Conduct may lessen competition, but lead to desirable social benefits, which could include improved efficiency.
- 129 Authorisation is a formal and public process. The application and submissions on it will be available on the Commission's website. Our draft and final determination including the reasons for the decision are also publicly available.
- 130 We cannot retrospectively grant authorisation for conduct that has already occurred. Parties are encouraged to contact us if they have any concerns about future or ongoing conduct. The Commission can provide, in appropriate circumstances, interim authorisation that will apply to conduct during the consideration of an authorisation application.
- 131 Although the amended misuse of market power prohibition does not take effect until 5 April 2023, our power to grant authorisation comes into force earlier, from 5 October 2022. From that day, we may grant authorisation where we are satisfied the conduct is likely to result in such a benefit to the public that the matter should be permitted.
- 132 Further detailed information on the authorisation process is available in the Commission's *Authorisation Guidelines*.⁶⁰

58 Commerce Act, s 61(6).

59 Commerce Commission *Authorisation Guidelines* (December 2020) at [19].

60 These are available at https://comcom.govt.nz/__data/assets/pdf_file/0012/91011/Authorisation-Guidelines-December-2020.pdf.

The Commission's Approach to Investigating Alleged Breaches of the Commerce Act

- 133 Our purpose is to achieve the best possible outcomes in competitive and regulated markets for the long-term benefit of New Zealanders. We are committed to ensuring that New Zealand businesses and consumers understand our activities and the ways in which we exercise our powers and functions.
- 134 When determining whether and how to investigate a particular matter, we do not apply a rigid formula. Rather, we weigh all competing considerations and exercise our judgement.
- 135 Wherever possible, we prefer to encourage compliance with the law through the use of non-enforcement options. We prioritise our limited enforcement resources to focus on matters where the greatest harm exists or may occur. We will also try to respond promptly to changing or emerging market problems, so we will focus on making timely responses to problems as they arise.
- 136 Detailed information on the Commission's approach to investigations is available in the Commission's *Competition and Consumer Investigation Guidelines*.⁶¹
- 137 In determining what matters to investigate or prioritise for enforcement, we consider our published *Enforcement Criteria*.⁶²

Remedies

- 138 The Commerce Act provides a range of remedies in relation to misuse of market power. The remedies provided under the Commerce Act serve several purposes:
 - 138.1 Stopping or preventing harm to competition;
 - 138.2 Deterring firms with substantial market power from harming competition; and
 - 138.3 Compensating people who suffer loss or damage because of the unlawful conduct of firms with substantial market power.
- 139 The Commission will apply its usual enforcement approach to alleged misuses of market power. Further detailed information on the Commission's approach is available in the Commission's *Enforcement Response Guidelines*.⁶³

Interim and Permanent Injunctions

- 140 The Commission and private parties can apply the High Court for an injunction restraining a person from engaging in conduct that constitutes, or would constitute, a breach of section 36.⁶⁴
- 141 This includes the power to restrain a person from doing or refusing to do something.⁶⁵ For example, the Court could restrain a person from refusing to supply products.
- 142 The Court may also grant an interim injunction, where it considers it desirable to do so.⁶⁶ In deciding whether to grant an interim injunction, the Court must consider the interests of consumers.

61 These are available at https://comcom.govt.nz/__data/assets/pdf_file/0028/89821/Competition-and-Consumer-Investigation-Guidelines-July-2018.pdf.

62 These are available at <https://comcom.govt.nz/about-us/our-policies-and-guidelines/investigations-and-enforcement/enforcement-criteria>.

63 These are available at https://comcom.govt.nz/__data/assets/pdf_file/0030/62589/Enforcement-Response-Guidelines-October-2013.pdf.

64 Commerce Act, s 81.

65 Commerce Act, s 2(2) defines engaging in conduct as doing or refusing to do any act. See also *Port Nelson (HC)*, above n 40, at 559-560.

66 Commerce Act, s 88.

- 143 Where the Court finds that a person who is a party to the proceedings has suffered, or is likely to suffer, loss or damage, the court may make such order or orders as it thinks appropriate against the person who engaged in the conduct.⁶⁷

Penalties

- 144 The Commission may also apply to the Court for a civil pecuniary penalty. If the Court finds an individual or firm has breached the Commerce Act significant penalties can be imposed:

144.1 For an individual the maximum penalty is \$500,000.

144.2 The maximum penalty for a firm is, the greater of:

144.2.1 \$10 million, or

144.2.2 Three times the commercial gain, or

144.2.3 If this cannot be easily established, 10 percent of turnover in each accounting period in which the breach occurred.

- 145 Penalties can also be imposed on firms or individuals who are directly or indirectly involved in another person's breach of the Commerce Act.

- 146 Every separate breach of the Commerce Act (even if done by the same person) may incur a penalty.

Damages

- 147 Where the Court finds that a person who is a party to the proceedings has suffered, or is likely to suffer, loss or damage, as a result of a contravention, the Court may make such orders as it thinks appropriate against the person who engaged in the conduct.⁶⁸ The Court can also make orders varying or cancelling any contract that, if given effect to, would contravene the Act.⁶⁹ In addition, where a contravention has caused loss or damage to a person, the Court may make orders awarding compensation to that person.⁷⁰

Enforceable Undertakings

- 148 The Commission may accept an enforceable undertaking in relation to a breach, or possible breach, of section 36.⁷¹ Enforceable undertakings are a form of out-of-court negotiated settlement that a party may offer to the Commission. If the party does not keep to their undertaking, the Commission may apply to the Court to enforce it.

- 149 Enforceable undertakings are a flexible tool, and can include a firm undertaking to:

149.1 Cease conduct that contravenes, or may contravene, the Commerce Act;

149.2 Pay compensation to any person who has suffered, or is likely to suffer, loss as a result of their conduct;

149.3 Take action to avoid, remedy, or mitigate any actual or likely adverse effects of their conduct;

149.4 Monitor and report on its conduct in the future;

149.5 Put in place a programme to ensure compliance with the Commerce Act in the future, which may include ensuring its employees undertake training in relation to the Commerce Act; and/or

149.6 Pay to the Commission all or part of the Commission's costs incurred in investigating, or bringing proceedings in relation to, its conduct.

67 Commerce Act, s 89(1).

68 Commerce Act, s 89(1).

69 Commerce Act, s 89(2).

70 Commerce Act, s 82.

71 Commerce Act, s 74A.

Appendix

- 150 There are many Acts that contain exceptions to the Commerce Act. New acts and regulations will be introduced from time to time however the below provides a guide as of 11 October 2022 to the exceptions found in other legislation.
- 150.1 Certain charges by an airport company:** Nothing in section 43 of the Commerce Act 1986 applies in relation to the setting and charging of charges by an airport company (s4A(3) of the Airport Authorities Act).
- 150.2 Civil aviation levies:** Imposition of levies by the Civil Aviation Authority to fund the Authority to carry out its functions are specific authorisations for the purposes of s43 of the Commerce Act (s 42D of the Civil Aviation Act 1990).
- 150.3 International carriage by air:** Part 9 of the Civil Aviation Act 1990 provides a specific regime for agreements such as capacity sharing, tariff schedules and service agreements between airlines. As long as they are authorised by the Minister of Transport, they are exempt from Part 2 of the Commerce Act.
- 150.4 Electricity industry and gas industry:** The actions of the respective electricity and gas governance bodies and any acts in compliance with rules set by them are specifically authorised for the purposes of section 43 of the Commerce Act (section 130 of the Electricity Industry Act 2010 and section 43ZZR of the Gas Act 1992). Section 47 of the Commerce Act does not apply to any transfer of assets undertaken by a state generator pursuant to a direction given under s117 of the Electricity Industry Act 2010.
- 150.5 Telecommunication industry:** Part 2 of the Commerce Act does not apply to TSO instruments to facilitate the supply of certain telecommunications services to groups of end-users within New Zealand to whom those telecommunications services may not otherwise be supplied on a commercial basis or at a price that is considered by the Minister to be affordable to those groups of end-users.
- 150.6 Agricultural producer boards:** Agricultural producer boards are exempt from Part 2 of the Commerce Act to enable them to undertake their activities such as setting a levy to fund the Board's activities (section 14 Pork Industry Board Act 1997) and set quota allocations (part 3 of the Meat Board Act 2004).
- 150.7 Tertiary education:** Nothing in the Commerce Act applies to the Tertiary Education Commission except to the extent that the Commission engages in supplying goods and services for which it charges (section 159K Education (Tertiary Reform) Amendment Act 2002).
- 150.8 Fisheries:** The Ministry of Fisheries may devolve certain fisheries management to other service providers where efficient. The outsourcing arrangements are exempt from the Commerce Act (section 296C Fisheries Act 1996).

150.9 Health care: There are a number of Commerce Act exceptions for health care services.

150.9.1 Arrangements between public health providers: certain public health providers are treated as interconnected bodies corporate under s2(7) of the Commerce Act which exempts arrangements wholly between these parties.

150.9.2 Blood products: arrangements in relation to blood or controlled human substances approved by the Governor General or Order in Council (section 64 Human Tissue Act 2008).

150.9.3 Emergency ambulance services: joint purchasing arrangements between the Ministry of Health and Health New Zealand for emergency ambulance services are exempt from Part 2 of the Commerce Act, other than sections 36 and 36A (section 305 Accident Compensation Act 2001).

150.9.4 Pharmaceutical subsidies: nothing in Part 2 of the Commerce Act applies to any agreement to which Pharmac is a party and that relates to pharmaceuticals for which full or part payments may be made (section 53 New Zealand Public Health and Disability Act 2000).

151 Crown exceptions: the Commerce Act only applies to the Crown and Crown Corporations when they engage in trade.⁷²



72 Commerce Act, ss 5 and 6.

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This is a guideline only and reflects the Commission's view. It is not intended to be definitive and should not be used in place of legal advice. You are responsible for staying up to date with legislative changes.

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