COMMERCE COMMISSION NEW ZEALAND
Te Komihana Tauhokohoko

10 February 2016

Targeted Commerce Act Review
Competition and Consumer Policy
Ministry of Business, Innovation and Employment
Wellington

Dear Review Team

Commerce Commission submission to Targeted Commerce Act Review Issues Paper

1. We welcome the opportunity to submit to this stage of the review and look forward to our engagement with MBIE going forward.

2. As a general comment, we consider that the Issues Paper appropriately identifies the policy issues and considerations relevant to: reform of section 36 (s 36) of the Commerce Act; an evaluation of the Commerce Act's enforcement mechanisms; and the question of whether market studies should be introduced to New Zealand.

3. As a result, we have not addressed every question posed in the Issues Paper. Rather, we have offered some observations and perspectives on the three topics addressed in the paper.

Section 36

4. We support reform of s 36 and the Commission's current preference is to move s 36 to a substantial lessening of competition (SLC) test. This view is consistent with the view we expressed in our submission to the Australian Competition Policy Review (Harper Review).[1]

5. New Zealand is a small economy, some distance from many of its trading partners. We appreciate that these features can make it challenging for New Zealand businesses to acquire the scale they believe they need to operate efficiently and compete effectively in global markets. It is perhaps for these reasons that the level of aggregation often tolerated in New Zealand's domestic markets is higher than in some larger economies.

6. Some argue that New Zealand's small size and apparent need for increased scale also necessitate a more relaxed attitude towards single firm conduct in New Zealand markets. We disagree. As discussed in the relevant literature[2], we consider that any

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1 http://competitionpolicyreview.gov.au/files/2014/11/NZCC.pdf

2 Michal Gal *Competition Policy for Small Market Economies* (Harvard University Press, Cambridge, 2003) at 93.

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tolerance for higher market shares in domestic markets reinforces rather than undermines the need for effective rules prohibiting anti-competitive practices by firms with substantial market power. That is, an effective s 36 is needed to ensure that competition in New Zealand domestic markets serves the long term interests of consumers.

7. Section 36 does not achieve this. Simply put, it is not effective at identifying single firm conduct that is harmful to competition and the New Zealand economy. The reason is primarily the way the courts have interpreted the "taking advantage" part of s 36, by introducing a counterfactual test.

8. The purposes in s 36 are phrased in terms that might suggest that s 36 is directed to protecting competitors rather than competition. Courts have been concerned that all firms act with the purpose of harming their competitors. There is a need therefore to distinguish between conduct by a firm which, while designed to harm its competitors can be regarded as vigorous 'competitive' conduct (ie, that which promotes competition) as opposed to 'anti-competitive' conduct (ie, that which diminishes competition). New Zealand courts have done this through their interpretation of the taking advantage limb of s 36. The counterfactual test, as interpreted by the courts, examines the conduct of a firm with a substantial degree of market power compared to the likely conduct of a firm without such market power.

9. The result of this interpretation of the counterfactual test is that conduct by a firm with substantial market power, which has the effect of a SLC (substantially lessening competition) in a New Zealand market, may not be prohibited even though New Zealand consumers will more than likely be worse off. The test is, therefore, at odds with an underlying foundation of competition law that what matters is the impact of a firm's conduct on competition, because of the benefits that competition brings to an economy.

10. Neglecting the effect of the conduct is not in keeping with rest of New Zealand's competition law. Other sections of the Commerce Act look at the effect of the conduct on the relevant market.[3] These sections provide a good base for a revised 36. Section 36 is also misaligned with international best practice in considering unilateral conduct.[4] The only country with a similar provision is Australia,[5] and there the Harper Review recommended reform to remove "taking advantage" and adopt an SLC based provision.

Potential options for reform of section 36

11. Having said all this, we recognise that the challenge is to frame a law that captures anti-competitive unilateral behaviour but does not constrain vigorous competitive conduct.

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3 For example, s 27 looks at whether the conduct has the purpose, or has or is likely to have the effect, of substantially lessening competition in a market.

4 Andrew Gavil "Imagining a Counterfactual Section 36: Rebalancing New Zealand's Competition Law Framework" (2015) 46 VUWLR

5 Competition and Consumer Act 2010 (Australia), Section 46

12. We note the potential options on page 32 of the Issues Paper. As set out above our preferred option at this point is option 4 – a SLC test. We consider this test would capture anti-competitive unilateral behaviour while enabling firms to compete vigorously on the merits of their products and services, including in international markets. It would also shift the focus to protecting the competitive process and not competitors.

Alternative enforcement mechanisms

Cease and Desist

13. The Commission supports the repeal of the cease and desist regime. In the Commission's assessment, injunctions provide a more cost effective and efficient method of stopping harmful conduct.

14. This is because, as illustrated by Table 4 in the Issues Paper, the Commission has to navigate more procedural and practical hurdles to secure a Cease and Desist Order than it does to secure an interim injunction. In addition, a Cease and Desist Order is appealable to the High Court, at which point litigation commences in another forum.

15. For example, to secure a Cease and Desist Order, the Commission must establish a prima facie case of breach, a standard which is likely higher than the serious question to be tried threshold for an interim injunction. The practical implication of having to reach a prima facie case standard (and the requirement that a report be submitted to Commissioners before an order is sought) means that it may be difficult for the Commission to obtain a Cease and Desist Order quickly, as more extensive investigation will be required to meet the prima facie case threshold. [6] This then raises the question of whether at the time a Cease and Desist Order is sought (after comprehensive investigation), the Commission could satisfy the "necessary to act urgently" limb of the test.

	Interim Injunction[7]	**Cease and desist order**
Legal threshold	• There is a serious question to be tried • The balance of convenience favours the granting of an injunction • It is in the interest of justice to grant the injunction	• A prima facie case of conduct that breaches the Act (this is the same standard the Commission uses for warnings). • Necessary to act urgently to prevent serious loss or damage to a particular person or consumers. • It is in the interests of the public to grant the order.
Key procedural steps	• Staff investigation to indicate serious question to be tried • Recommendation to	• Staff investigation to indicate prima facie breach of the Act • Recommendation to Commerce

6 Of course, appropriate evidence would still need to be adduced before the Court to obtain an interim injunction.

7 See generally McGechan on Procedure at [7.53].

	Commerce Commissioners to apply for an injunction. • Application for injunction • Usually service of application followed by opposed hearing • Interim injunction may be sought in some circumstances without notice (HCR 7.46).	Commissioners to apply for a Cease and Desist order. • Application to a Cease and Desist Commissioner • Service of proposed order • Mandatory opportunity to be heard. • Appealable to High Court.

16. The (lack of) utility of Cease and Desist Orders is illustrated by the fact that the Commission has only used the Cease and Desist regime once since its enactment in 2001.[8] For various reasons, including those explained above, we do not believe that the Commission could have used these orders more regularly. We do not believe that the lack of use of these orders has affected the Commission's ability to achieve appropriate enforcement outcomes.

Settlements

17. The Commission does not believe it is accurate to describe the current settlement process as 'weak', or the lack of administrative settlements as being indicative of a problem with the system. In most cases the Commission regards conduct as requiring a court approved settlement involving admissions of breach. Administrative settlements occur in the minority of Commerce Act matters. Moreover, we have not faced a situation where a party to a settlement agreement (administrative or court approved) has ultimately reneged on the agreement, when faced with steps to enforce the settlement in Court.

18. Having said that, we do consider that enforceable undertakings would be a useful addition to our enforcement toolkit. The Commission was granted these powers in recent amendments to the Fair Trading and Credit Contracts and Consumer Finance Acts and has already entered into these undertakings a number of times. This has been beneficial as a way to promptly effect change in a trader's behaviour, and to benefit consumers.

19. In the Commerce Act context, while we do not believe that the number of administrative settlements/enforceable undertakings would be likely to increase at the expense of court approved settlements, there would be some benefit in being able to settle some matters involving future behavioural changes without needing recourse to the courts.

20. An example of this is a recent warning we issued to Consolidated Alloys (N.Z) Limited as a result of an agreement it had reached with one its competitors. The agreement contained a restrictive clause (which had yet to have an anti-competitive effect, but

[8] http://www.comcom.govt.nz/the-commission/media-centre/media-releases/2006/firsteverceaseanddesistorderissued

would have had in the future), which the parties agreed not to enforce as a result of our investigation. The Commission considered the parties decision not to enforce the clause as part of its enforcement response. However, an enforceable undertaking would have allowed the Commission to have had more certainty and a straight forward remedy in the case that the parties subsequently gave effect to the clause.

21. There is also benefit in the fact that these undertakings can also be amended by agreement with the Commission. This would allows the Commission to agree changes that both parties see as positive but that were not foreseen at the time the original undertaking was given.

Market Studies

22. We believe there may be a gap in New Zealand's competition framework that could be filled by market studies. These studies would allow an agency to analyse competition in a market in a more holistic way. The result of a study could range from policy change to remove anti-competitive regulation to Commerce Act enforcement.

23. At this point the Commission has no policy position on who should conduct market studies if a market study regime is introduced. We think this matter is best left to discussion at the options paper stage. However, we provide some general comment to assist officials in determining which options should be considered.

Is there a gap?

24. In short, the Commission's current power to undertake inquiries or studies similar to market studies is fairly narrow. Specifically, it is confined to formal questions about whether a market should be regulated, and matters related to the telecommunications and dairy industries.

25. Several other agencies such as the Productivity Commission and MBIE undertake studies of markets, and while competition issues feature they are not the focus of these studies.

26. The Commission may undertake studies and publish reports and information regarding matters affecting the interests of consumers under section 6(b) of the Fair Trading Act 1986 (FTA). A recent example is the Commission's report into mobile traders.[9] The Commission's ability to undertake studies into matters affecting consumer interests provides some scope to look at particular competition concerns (when linked to consumer matters), but it is unlikely to provide the power to look at all determinants of competition in a particular market.

Structure of a regime

27. The agency receiving market studies powers would need to be adequately funded for these studies. We consider that the funding required would be significant. Based on our experience of 'market study type investigations' (eg, the current DIRA Review),

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9 Commerce Commission *Mobile Trader 2014/2015 Project* (2015) available at http://www.comcom.govt.nz/the-commission/consumer-reports/mobile-trader-201415-project/.

market studies are a specialised activity that will require staff, contractors and experts with relevant experience and a specialised skillset. This would require additional funding in order for market studies to be conducted without affecting the agency's other responsibilities.

Powers

28. We believe that the responsible agency does need powers to compel information. In order for the regime to be effective, the agency needs to be able to gather the information required to conduct its analysis. There may be instances where market participants will be unwilling or unable absent being compelled to provide information.

29. We also consider that there should be adequate safeguards on the use of those powers. We consider that the current formulation and interpretation of s 98 of the Commerce Act provides adequate safeguards. If the Commission were to receive market study powers, then we consider they should simply form part of the Commission's s 98 powers rather than introducing a new and unknown framework. Similar considerations should apply to any other agency that was to receive a market study power.

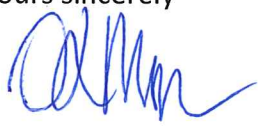
Outcome of the study

30. We do not believe that a remedies based market studies system is appropriate in a New Zealand context.[10] We believe the best option is a recommendation based system where the agency makes recommendations to the government. To ensure this system is effective, we suggest there should be a statutory requirement for the government to respond in a certain timeframe.

Conclusion

31. We hope this response is useful in your deliberations. Commission staff are happy to continue to engage with MBIE in relation to this review. If you have specific questions on this submission please contact Dáire Queenan, Advocacy Adviser on 04 924 3744 or daire.queenan@comcom.govt.nz in the first instance.

Yours sincerely



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[10] Example of such a system would be the UK (Part 4 Enterprise Act 2002).