COMMERCE COMMISSION NEW ZEALAND
Te Komihana Tauhokohoko

Submission on Commerce Amendment Bill

Submitted to: Economic Development, Science and Innovation Committee

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Introduction

1. The Commerce Commission (the **Commission**) is New Zealand's primary competition, fair trading, consumer credit and economic regulatory agency. The Commission is responsible for enforcing the Commerce Act 1986 (**the Act**), the purpose of which is to promote competition in markets for the long-term benefit of New Zealand consumers.

2. This submission sets out the Commission's views on the Commerce Amendment Bill (9-1) (**the Bill**). The Commission appreciates the opportunity to make this submission. Given the importance of the Act to its functions, powers and duties, the Commission would welcome the opportunity to appear before the Committee to further engage on the changes.

3. The Commission is supportive of the Bill and the core changes it makes to the Act, including the reform of the misuse of market power prohibition, the removal of exceptions relating to intellectual property, clarifications of the application of the Act to land and covenants and an increase in pecuniary penalties for unlawful business acquisitions and mergers. The Commission is also supportive of the increase in the maximum number of Commissioners and formalising the Commission's ability to share information. Both will assist the Commission to enforce the Act. The latter will enhance collaborative working and prioritisation amongst domestic enforcement agencies.

Misuse of market power prohibition (clause 14)

An effects-based test is appropriate

4. The Commission welcomes the change to the misuse of market power prohibition to include a 'substantial lessening of competition' effects test (**SLC test**). The Commission has long advocated for a change to the misuse of market power prohibition. In summary, we consider that:

    4.1. the current prohibition does not meet the Act's purpose to promote competition in markets for the long-term benefit of consumers. The current interpretation necessitates a hypothetical counterfactual test that fails to capture all anti-competitive conduct. It is complex, and difficult to apply and to enforce, and the effect the conduct has on competition is not a core line of inquiry;

    4.2. an SLC test will protect the competitive process by ensuring that firms with substantial market power do not engage in exclusionary conduct that prevents competitors from entering and expanding based on the merits of their own products and service. It will not prevent firms with substantial market power from improving their market position at the expense of smaller rivals if this is achieved by outperforming those rivals in terms of efficiency, innovation and/or better value goods and services;

4.3. the SLC test is well understood in New Zealand. It has already been applied in the context of anticompetitive agreements (section 27 of the Act) and anticompetitive mergers (section 47 of the Act) since 1986 and 2001 respectively;

4.4. the SLC test is consistent with the approach taken in comparable competition law jurisdictions. Of particular relevance is the equivalent test in Australia, where the market power provision was amended to a SLC test in 2017 (see further below); and

4.5. New Zealand's relatively small population and its concentrated markets require a well functioning rule against unilateral anti-competitive conduct. MBIE has noted that there is likely to be a greater number of dominant players in markets in New Zealand.[1] Therefore, it is vital to have an effective rule against unilateral conduct by firms with substantial market power to deter exclusionary conduct.

5. More detail on the appropriateness of the SLC test is set out in the Commission's previous submissions on this issue, a selection of which are attached.[2]

Alignment with Australia

6. As set out in the Explanatory Note, the change aligns the prohibition with section 46 of the Competition and Consumer Act 2010 (Cth), the equivalent prohibition in Australian competition law. This alignment reduces the uncertainty which might typically arise from the introduction of the new threshold. It will allow New Zealand businesses, the Commission, and the New Zealand courts to benefit from Australian case law and guidance, together with the case law and guidance from the many other jurisdictions that have adopted a similar effects test.

7. Consistency of the competition law framework between New Zealand and Australia will also make it easier for a business operating (or wanting to operate) in both markets. In particular, those businesses with substantial market power will face substantively the same provisions when undertaking unilateral conduct in both New Zealand and Australia, where that conduct has the potential to affect markets in both countries. For example, in digital markets the activities of large digital companies have cross border implications and the enforcement response in Australia and New Zealand could currently be quite different.

8. The Bill does not include provisions equivalent to subsections 46(4)-(6) of the Australian provision. The Commission agrees that these sections are not required, as they simply

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[1] Ministry of Business, Innovation & Employment "Discussion Paper: Review of Section 36 of the Commerce Act and other matters" (January 2019), at [44].

[2] These submissions are Annexed to this submission and are publicly available:

- Commerce Commission, Targeted Commerce Act Review Issues Paper, Submission to MBIE, 10 February 2016 (see paragraphs 4 – 12 on misuse of market power);
- Commerce Commission, Targeted Review of the Commerce Act 1986, Cross-submission to MBIE;
- Commerce Commission, Review of section 36 of the Commerce Act and other matters, 1 April 2019 (see paragraphs 10 – 40. Paragraphs 41 – 47 also refer to the intellectual property exception).

state factors that would be expected to be considered in an assessment of market power. Subsection 46(7) of the Australian provision clarified that it is possible for more than one person in any market to have market power. The Commission recommends that an equivalent clause be adopted in New Zealand to remove doubt on this issue.

9. The Explanatory Memorandum introducing the current Australian provision also explained the meaning of the "indirect" supply and acquisition of goods and services:[3]

> *This 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.*

10. The concept of indirect supply or acquisition is found in subsection 36(1)(b)(ii), clause 14 of the Bill. The Commission understands that it was intended by officials that the same approach to that of Australia be taken in the New Zealand legislation. The Commission agrees this is desirable but is concerned that this intention may not be clear on the face of the legislation. A definition of supply or acquisition "indirectly through one or more persons" may assist. The Commission recommends that the Bill be amended to ensure clarity and consistency with the Australian provision.

Business justification and other defences

11. The Commission does not support adding a "business justification" (or similar) defence to the misuse of market power prohibition.

12. As set out in paragraph 4.2 above, the SLC test will protect the competitive process by ensuring that firms with substantial market power do not engage in exclusionary conduct that prevents competitors from entering and expanding based on the merits of their own products and service. This does not prevent firms with substantial market power from improving their market position. Legitimate competitive conduct that enhances competition will not be captured by the SLC test. Firms can gain market share at the expense of smaller rivals if this is achieved through increased efficiency, innovation and/or better value goods and services, all of which are at the heart of competitive conduct. The Commission is already familiar with these concepts, as it undertakes a similar assessment of competition in relation to both the prohibition on anticompetitive arrangements (section 27 of the Act) and in its assessment of mergers (section 47 of the Act).[4]

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[3] Competition and Consumer Act 2010 (Cth), sections 46(1)(b)(ii) and 46(1)(c)(ii).

[4] See the Commission's guidance on efficiencies in the merger context: Commerce Commission, Mergers and Acquisitions Guidelines, July 2019 (paragraphs 3.118 – 3.125).

13. To the extent that there are public benefits from a firm's conduct that do not fall within those described above, the firm can apply to the Commission for authorisation of the conduct. This could be the case, for example, where efficiencies arise that do not occur within the market in which competition is affected. This provides sufficient protection for firms wishing to engage in conduct that might otherwise breach the prohibition in limited circumstances. The commencement of the authorisation process six months after the passing of the Bill will give the Commission time to prepare for potential applications.

14. Any material departure from the SLC test as set out in the Bill will make the prohibition inconsistent with the Australian prohibition, negating the benefits discussed in paragraphs 6 and 7 above. It will also take New Zealand out of step with comparable overseas jurisdictions and re-introduce many of the problems that the Explanatory Note identifies with the current prohibition. It will add cost and complexity, reduce the incentive for compliance and make it more difficult for the Commission and the courts to enforce.

The intellectual property exception (clause 15)

15. The Commission agrees with the Bill's repeal of the exceptions for intellectual property and with the reasons for repeal set out in the Explanatory Note. The intersection of intellectual property rights and competition law is becoming particularly important in relation to digital markets.

16. There is no strong rationale for treating intellectual property rights differently to any other form of property or assets under competition law. The removal of the exception does not diminish the rights of intellectual property holders, it simply ensures that they are not used in an anti-competitive manner, similar to any other form of property or assets under competition law.

17. Where the Commission has dealt with the exception, it has found that the scope of the exception is often misunderstood by the parties, creating confusion relating to its application.

18. The change will bring New Zealand closer to comparable jurisdictions. Australia has recently repealed an equivalent intellectual property-related exception in its competition laws. The Harper Review[5] noted that most comparable jurisdictions have no intellectual property exception. The removal of the equivalent exception in Australia was on similar grounds to those set out above and in the Explanatory Note.

19. The four year transitional period for existing statutory intellectual property rights (three years after the Commencement Date) is relatively long, particularly given the lack of a strong rationale for the exception and the fact that the exception is so rarely relied

[5] Professor Ian Harper, Peter Anderson, Su McCluskey and Michael O'Bryan QC "Competition Policy Review: Final Report" (March 2015) at 109.

upon. This can be compared to Australia, where the intellectual property exceptions fell away six months after the amending legislation was passed.

20. The Commission is concerned that the transition period applies to contracts, arrangements or understandings entered into in the period after the Royal assent for the Bill but before the Commencement Date. This will allow parties to enter into arrangements knowing that they would be illegal but for the transitional period – this is inconsistent with what appears to be the purpose of the transitional provision, being to allow existing agreements to continue to be enforced.

Information exchange (clause 32)

21. The Commission welcomes formalising its ability to share information with other government agencies. The Commission works with a number of regulatory agencies with overlapping and/or complementary functions to that of the Commission.

22. The exchange of information with these regulators is important to ensure the efficient exercise of the Commission's functions, powers and duties, and those of its partner agencies. As described in the Commission's Vision and Strategy, in order to ensure the Commission has the greatest impact it first needs to decide whether an issue would be better addressed by an agency other than the Commission.[6] This often necessitates sharing information with other regulators to determine who is best placed to investigate an issue.

23. The Commission already limits the extent to which it shares information with other regulators. The Commission's Investigation Guidelines set out how and in what circumstances the Commission will share information with other New Zealand or overseas law enforcement or government departments.[7]

24. When the Commission does share information with other agencies it does so lawfully (including in compliance with the Privacy Act), with appropriate controls and consideration of confidentiality, and in accordance with information sharing agreements, as set out in the Commission's Transparency Statement.[8] The proposed amendment contains adequate safeguards and processes related to the future sharing of this information.

Other amendments

25. *Membership of Commission (clause 7):* The Commission supports the proposed amendments to subsections 9(1) and (2) of the Act to increase by two the maximum number of full members that make up the membership of the Commission. With increasing functions, powers and duties arising for the Commission under the Act and a number of different statutes (including in the Telecommunications Act 2001, the Fuel Industry Act 2020, and the Credit Contracts and Consumer Finance Act 2003) it is

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6 Commerce Commission, Our Vision and Strategy 2017 – 2022, section 3.2.

7 Commerce Commission, Competition and Consumer Investigation Guidelines, July 2018, page 33.

8 Commerce Commission, Transparency Statement,

beneficial for the Governor General to be able to appoint additional full members of the Commission who can work on all matters, as an alternative to the appointment by the Minister of an Associate Member to work only in relation to “a matter or class of matters” (see subsection 11(2) of the Act).

26. *Covenants (clauses 9, Schedule):* the Commission supports the inclusion of covenants in the cartel prohibition. The Commission understands that the removal of covenants was most likely an oversight in the context of the previous amendments to the cartel prohibitions. Its absence creates a potential loophole for cartel behaviour and there does not appear to be a good reason for its exclusion. The Australia equivalent prohibition already includes covenants within the scope of its cartel prohibition.

27. The transition period for the inclusion of covenants in the cartel prohibition is for a similarly long period as that for the intellectual property exception. It also allows parties to enter into covenants between the passing of the Bill and the commencement date. To the extent that the current exclusion of covenants does provide a loophole for cartel behaviour, this will allow parties to exploit this loophole right up to the Commencement Date, and benefit from the exception for another three years thereafter.

28. *Penalties (clause 28):* the Commission supports the increase in penalties for anti-competitive mergers to bring them into line with the penalties for anticompetitive agreements. As currently drafted, it is not clear how the turnover threshold will be calculated in the amended subsection 83(3)(b)(ii)(B) of the Act. The amendment refers to turnover “in each accounting period in which the contravention occurred”. However, a merger is typically a single act, as opposed to the continued contravention related to giving effect to anticompetitive agreements. The Commission suggests that the amendment instead refers to accounting periods since the completion of the merger (including the accounting period in which the merger occurred).

ANNEX

Previous Commerce Commission submissions

(see separate pdf document attached)