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Commerce Commission  
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## **Anytime NZ Limited – Submission in response to Statement of Issues**

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### **Introduction**

1. This submission responds to the 22 December 2021 Statement of Issues (confidential version to Anytime NZ Limited) (**Sol**) prepared by the Commerce Commission (**Commission**).
2. The Sol was issued in response to Anytime NZ Limited's (**Applicant**) 20 September 2021 application for clearance under section 65A of the Commerce Act 1986 (**Act**) for proposed agreements with its franchisees that contain or may contain cartel provisions (**Application**).
3. The Applicant has proposed reintroducing a pricing policy binding on Anytime Fitness franchisees that sets minimum and maximum prices for gym memberships from time to time (**Proposed Agreement**). The Proposed Agreement is proposed due to problems that have arisen with the franchise's reciprocity policy that allows members to access any of the Anytime Fitness networks gyms (**Reciprocity Policy**). The Proposed Agreement and the issues with the Reciprocity Policy are set out in more detail in the Application.

### **Summary of Commission's current views from Sol**

4. The Commission's current views are that the following criteria are met<sup>1</sup>:
  - (a) the Proposed Agreement between the Applicant and franchisees is likely to contain cartel provisions and some of those parties are in competition with each other;
  - (b) the Applicant and the franchisees are or will be involved in a collaborative activity; and
  - (c) the entry into the Proposed Agreement is unlikely to have the effect of substantially lessening competition in a market.
5. The Commission's primary concern is whether every cartel provision in the Proposed Agreement is reasonably necessary for the purpose(s) of the cartel activity<sup>2</sup>. In assessing this, the Commission also considered the available alternatives that would allow the parties to pursue the collaborative activity.
6. We address the issue of whether the Proposed Agreement is reasonably necessary and respond to the alternatives suggested by the Commission below.

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<sup>1</sup> At paragraph 8 and 19 to 58 of the Sol.

<sup>2</sup> At paragraph 7 and 59 to 116 of the Sol.

### Proposed Agreement reasonably necessary for the purposes of the collaborative activity

7. The Commission assessed the reasonable necessity of the Proposed Agreement against the following purposes<sup>3</sup>:
  - (a) provision of a strong network of club facilities in good locations to members;
  - (b) ensuring the focus of franchisees is on the provision of excellent facilities and services so that the chain can best compete with other gyms; and
  - (c) improvement of the equitable allocation of membership fees as between franchisees.
8. The Commission was not yet satisfied the Proposed Agreement is reasonably necessary for any of these purposes. We respond to the Commission's preliminary views regarding each purpose below.
9. The Applicant agrees with the Commission's view at paragraph 60 of the Sol that *where a collaborative activity has multiple substantial purposes, a cartel provision that is reasonably necessary for at least one of the substantial purposes will satisfy the "reasonably necessary" test.*
10. Accordingly, even if the reasonable necessity test fails in respect of one purpose, this does not mean that clearance cannot be granted.

#### *Reasonably necessary to provide a strong network of gyms*

11. With respect to the first purpose, the Commission says it is not yet satisfied that the Proposed Agreement is necessary for the Applicant to provide a strong network of gym facilities in good locations to members.
12. In the Applicant's view there will not be a strong network of franchisees if franchisees [ ], rather than cooperating to better compete with other gym networks such as Les Mills, Snap Fitness and Flex Fitness.
13. It is self-evident that Anytime Fitness franchisees will not be able to effectively compete with other gym providers if their focus is [ ] rather than competition with other gym networks.
14. A franchise network cannot operate effectively unless there is collaboration between the members. [
  - (a)
  - (b)
 ]
15. [ ]

4 ]

<sup>3</sup> At paragraph 72 of the Sol.

<sup>4</sup> See for example paragraphs 3.13 - 3.14 and 3.17 of the Application.

16. [ ]

17. [ ]

- (a) [ ]
  - (i)
  - (ii)
  - (iii) ]

(b) [ ]

(c) [ ]

(d) [ ]

18. The Commission refers in the Sol to the expansion plans of Anytime Fitness<sup>5</sup>.

19. The Applicant considers that the growth of the network is what is causing issues under the Reciprocity Policy.

20. It is when franchisees are close to each other that the Reciprocity Policy causes problems in the absence of common pricing limits.

21. [ ]

<sup>5</sup> At paragraph 74 of the Sol.

22. [ ] therefore, the network will [ ] not be as effective as it could be in providing a coordinated common front that will compete well with the likes of Les Mills, Flex Fitness and others gym networks.

23. The Applicant submits that the pricing policy in the Proposed Agreement is reasonably necessary for that purpose.

Growth of Anytime Fitness network

24. It is important to consider not just the number of new clubs projected but their locations with regarding to existing clubs. Please note that the Applicant’s plans as to the number and locations of future Anytime Fitness gyms are particularly commercially sensitive and confidential.

25. [ ]

(a) [ ]

]

(b) [ ]

]

26. [ ]

].

27. [ ]

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Franchisee interviews and surveys

28. In reaching its preliminary views, the Commission was influenced by the fact that many of the franchisees the Commission contacted advised that they were not negatively affected by the Reciprocity Policy.

29. In response to this, the Applicant submits the following.

(a) Franchisees are very aware, due to training conducted by the Applicant, that it is potentially a criminal offence to discuss pricing with other franchisees. Franchisees are also aware that the Commission is the investigator and enforcer of the Act. [ ]

(i) [ ]

]

(ii) [ ]

]

(b) [ ]

]

(c) While some franchisees may not have had issues with the Reciprocity Policy to date, [

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*Reasonably necessary for high quality facilities and services*

30. At paragraph 83 of the Sol, the Commission says that the proposed agreement is not reasonably necessary to encourage franchisees to continue to provide high quality facilities and services.
31. In the Applicant's view, the incentive to invest in excellent services is dampened substantially if a franchisee knows that members of a neighbouring franchisee can take advantage of those facilities if a neighbouring franchisee offers lesser prices to members who then use the better facilities of the first franchisee under the Reciprocity Policy.
32. [
- ]
33. The Commission acknowledged that there are benefits in franchisees aligning with each other to ensure high quality branding, equipment and services. However, the Commission refers to quality inspections by the franchisor as a way of upholding quality standards.
34. The Applicant would suggest that quality inspections are no substitute (or match) for economic incentives.
35. The economic incentive created by having closely situated fellow franchisees who undercut prices and free-ride on your better facilities is necessarily to reduce the incentive to invest in such better facilities. The free-riding means that the investment in better facilities and services becomes financially unprofitable.
36. If franchisees all priced their services within a band, there would be a strong economic incentive for franchisees to invest in their facilities as a way to attract and retain members. [

]

*Reasonably necessary for equitable allocation of membership fees*

37. At paragraph 87 of the Sol, the Commission says the [
- ]
38. [
- ]
39. [
- ]
40. A major driver for the Proposed Agreement and the Application is the fact that the [

(a)

- (b) ]
41. [ ]
42. At paragraph 90 of the Sol, the Commission refers to the comments of “most” Anytime Fitness franchisees not seeing an issue on this point. Anytime Fitness does not have visibility of which franchisees have been interviewed. [ ], for most franchisees [ ]
43. [ ]
44. [ ]
45. [ ]
46. At paragraph 108 of the Sol the Commission suggests better enforcement of the 30-day cooldown period would assist in preventing the gaming of the Reciprocity Policy. [ ]
47. In paragraph 101 of the Sol the Commission refers to [ ] and queried whether this would create the possibility [ ] the Proposed Agreement.
48. The Applicant confirms that [ ]

#### **Alternatives raised by the Commission**

49. The Commission has asked at paragraph 113 of the Sol whether various alternatives could be an alternative to using a cartel provision. The Applicant has considered the practicality of the alternatives and responds below.

#### *Apportioning members fees based on use prior to transfer*

50. The Commission asks if the apportionment of membership payments during the 60 day period (prior to transfer) to clubs based on usage is practical?<sup>6</sup>
51. [ ]

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<sup>6</sup> At 113.1 of the Sol.

52. [

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53. Such an apportionment of membership payments would also be impossible to police fairly or effectively. For example, would members coming in for coffee or a chat with a trainer count as visits? Clubs might encourage members just to swipe in (even if they do not stay for a work out) just so it counts as use of the club. Clubs would want to police what other clubs were doing to ensure they were not incorrectly counting visits, which would result in [ ]. Clubs would unproductively spend time monitoring gym usage and potentially the time spent on individual gym visits.
54. Instead, the time and effort of franchisees is better spent on improving services and competing with other gym networks.
55. This approach would also make it harder for franchisees to accurately forecast revenue as gyms could not predict how members they signed up would behave in terms of use of their home gym compared to other Anytime Fitness gyms. This inability to forecast revenue would have negative consequences, for example if the club wished to borrow to improve its facilities.
56. The fact that gym members travel from around the world would also add to the impracticality of any proposal to apportion membership payments.
57. [ ] It would seriously detract from the Anytime Fitness “*Anytime, Anywhere*” philosophy to have clubs focusing on which gyms members are visiting and for how long.
58. An apportionment mechanism of this kind would simply divert the focus and attention of franchisees away from the collective efforts of the Anytime Fitness network to compete with other gym networks.

*Reducing the geographic scope or duration of the Proposed Agreement*

59. The Commission asks if the policy could be limited to those areas where the Reciprocity Policy is giving rise to problems?<sup>7</sup>
60. The issue of the [ ] the compounding problems with the Reciprocity Policy has been discussed at paragraphs 24 to 27 above. [ ]
61. There is also the concern that if the policy applied to say [ ] of clubs there is a risk that the ability of the remaining small numbers of clubs to diverge from the policy might undermine the perception of Anytime Fitness as a common network with consistent policies and procedures. Different positioning of the brand in a few locations would jeopardise the common look of the Anytime Fitness network.
62. An accepted benefit of franchising as a business method is to provide a common customer experience. Having a few clubs that had prices significantly higher or lower than those at the great majority of the network would detract from that benefit of franchising the network.

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<sup>7</sup> At 113.2 of the Sol.

*Better explanation to members of pricing changes on transfer*

63. The Commission asks if a better explanation to members of the possibility for pricing to change on transfer of club would help?<sup>8</sup>
64. The negative perception of some members might be ameliorated by such an explanation. However, it is still human nature to feel aggrieved when attracted by a particular low price and then find that the price is then increased (whether on a transfer or otherwise). Such a situation does not make for a good customer experience (regardless of whether a warning was originally provided) and creates a negative perception of the Anytime Fitness brand.
65. Further, given that price fixing is a criminal offence, Anytime Fitness is cautious to undertake training with members that could be seen as creating greater price uniformity by stealth. This is one of the reasons why the Applicant has applied for clearance. There is a fine line between explaining to clubs that they must emphasise to members the possibility for pricing to change on transfer of club, and risking liability under section 80 for aiding and abetting a section 30 breach.

*Requirement relating to extent of members use of their home club*

66. The Commission asks whether the Reciprocity Policy and transfer system could be modified to introduce a requirement on members to use their home club for at least a specific percentage during a 30 day period?<sup>9</sup>
67. Such a policy would be inconsistent with the Anytime Fitness model, which is the same worldwide and is based on members being able to use other clubs freely (until a transfer is triggered). A key aspect of Anytime Fitness's market positioning is a convenience model ("*Anytime, Anywhere*"). Restrictions on flexible use by member would be inconsistent with that market positioning- the network would no longer truly be Anytime Fitness. [

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11 ]

*Shortening the period before a transfer is triggered*

68. Similarly the suggestion of shortening the period before a transfer is triggered<sup>12</sup> is also [

13 ]

69. Accordingly, while the Applicant appreciates the Commission's offering of alternative proposals to the pricing policy in the Proposed Agreement, the Applicant does not consider any of those alternatives are practical or could achieve the objectives to be achieved by the pricing policy.

**Conclusion on reasonably necessary test**

70. In conclusion, for the reasons discussed above, the Proposed Agreement for which clearance has been sought is reasonably necessary to ensure:

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<sup>8</sup> At 113.3 of the Sol.

<sup>9</sup> At 113.4.3 of the Sol.

<sup>10</sup> [ ]

<sup>11</sup> [ ]

<sup>12</sup> At 113.4.4 of the Sol.

<sup>13</sup> [ ]



- (a) a strong franchise network characterised by cooperation [ ];
- (b) appropriate incentives towards high quality gym services consistent with Anytime Fitness's desired market positioning; and
- (c) ensuring equitable allocation of membership fees (rather than an allocation of fees under the present rules which will create perverse incentives to reduce rather than enhance the quality of gym services).

**Application of clearance following expansion of franchise network and application to future franchisees**

71. Commission staff in an email dated 10 February 2022 have asked the Applicant to provide a submission on the question of whether the collaborative activity clearance (if granted) could continue to apply after new parties are added to this agreement (i.e. new franchisees join the network).
72. Commission staff have referred to the absence of a provision equivalent to section 58B(2) of the Act in the provisions relating to collaborative activity clearances, and to the implications of addition of new parties to the Commission's assessment of whether giving effect to an agreement will have the effect or likely effect of substantially lessening competition under section 65A(2)(c).
73. The Applicant submits that a clearance given to Anytime Fitness would continue to apply if additional franchisees are appointed and become party to the arrangement, and further that those additional franchisees would also gain the benefit of the clearance.
74. In particular the Applicant submits that:
- (a) section 65B applies to all parties to an arrangement (whether a party to the arrangement at the time of clearance or not);
  - (b) for the purpose of deciding whether to grant a clearance, the Commission should be forward looking in its assessment of whether an arrangement will have the likely effect of substantially lessen competition in any market;
  - (c) however, any clearance granted is subject to the Commission's power to revoke the clearance for material changes in circumstances;
  - (d) an unanticipated substantial change in the composition of a franchise network could potentially in some cases amount to a material change in circumstances if the change in network composition would have made a material difference to the Commission's assessment whether to grant a clearance (e.g. the change would have cast doubt on the Commission's view that a provision was "*reasonably necessary*" or its view on whether an agreement was likely to substantially lessen competition in a market); and
  - (e) this submission is discussed in more detail in the following paragraphs.
75. Section 65B does not limit its application to persons that were parties to an arrangement at the time of the application for clearance. It is clear that the person applying for clearance must be a person who proposes to enter into the arrangement (see section 65A). However, once a clearance is given, any "*party*" who enters into the arrangement does not breach section 27 or section 30 by doing so (section 65B(a)) without there being a requirement as to *when* the party enters into the arrangement. Further, once a clearance is given, a "*person*" who gives effect to the arrangement does not breach section 27 or section 30 by doing so (section 65B(b)) without there being a requirement that the person was in fact an original party to the arrangement.
76. The legislative history supports an interpretation that allows members to a franchise chain to be able to rely on the collaborative activity exception and seek clearance where appropriate. It is well known that franchise networks grow (sometimes substantially) over time, and that the identity of franchisees in a franchise network will change from year to year. Some franchise networks are very large involving hundreds of franchisees (for example, the likes of McDonalds). It would be surprising in the extreme

if a collaborative activity in the form of a franchise network contained the same franchisee members in say year four that it did in year one. Yet despite that, franchise agreements were always considered to be a prime example of collaborative activities that would be capable of relying on the collaborative activity exception and the ability to seek clearance.

77. First, in the Commerce Select Committee's final report of 13 May 2013 on the Commerce (Cartels and Other Matters Bill) at page 7 the Committee discussed franchise arrangements specifically and suggested that the Commission in its guidelines provide more certainty as to whether the collaborative activity exception might be applied to particular franchise arrangements. Secondly, the driver for the amendment to the Bill to include section 31(3) (dealing with restraints of trade following termination of involvement in a collaborative activity), was the fact that such restraints were common in franchise agreements.
78. An interpretation of the Act that did not permit the parties to a franchise network from time to time to be able to rely on a clearance of provisions in a standard franchise agreement would largely render nugatory the benefits of the clearance procedure for what is one of the most common form of collaborative business activities in New Zealand business, the franchise business method. Clearly, that was not Parliament's intention as the Select Committee's report suggests.
79. At the time that the Commerce (Cartels and Other Matters Bill) was passed in 2017, franchising was a rapidly growing method of collaborative activity in New Zealand. A 2017 survey of NZ franchising conducted by Massey University (Auckland) and Griffith University (Queensland, Australia)<sup>14</sup> noted the importance of franchising as a business format in New Zealand including the following:
  - (a) there were 631 business format franchisors in NZ compared with 446 in 2012;
  - (b) it was estimated that franchised businesses contribute about \$27.6 billion to the NZ economy;
  - (c) 124,200 people were employed in NZ franchises; and
  - (d) 72% of franchises in operation in New Zealand were NZ founded.
80. That market position is important background context to the specific noting by the Select Committee of franchises as a form of business collaboration that could be expected (in appropriate circumstances) to be able to rely on the collaborative activity exception and the clearance procedure.
81. The Select Committee in the same report referred to above (which discussed the potential ability of franchises to rely on the collaborative activity exception) also at page 4 recommended the insertion of section 65D allowing the Commission to revoke a clearance after a "*material change in circumstances*". This in fact is the provision that provides a necessary safeguard in situations where either the market situation has changed substantially, or perhaps the parties to an arrangement have changed substantially, so that the Commission considers a clearance previously given should no longer stay in place.
82. The Applicant would accept that if a change in market or parties substantially affected the assessment of whether cartel provisions were reasonably necessary, or the consideration of whether an arrangement substantially lessened competition, then the Commission could potentially revoke a clearance under section 65D(1)(b) on the basis that there had been a material change in circumstances.
83. The Commission's revocation power therefore provides a necessary safeguard to the Commission and the public interest, without the need to eviscerate the clearance procedure in such a way that it could not achieve its objective in relation to perhaps the most common form of collaborative activity in New Zealand.

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<sup>14</sup> A copy of the survey can be found at <https://s3-ap-southeast-2.amazonaws.com/wh1.thewebconsole.com/wh/726/images/FINAL-REPORT-web-version-compressed.pdf>

84. A provision of similar nature to section 58B(2) in relation to authorisations was simply not required for clearances. Section 58B(1) expressly limits the persons who can rely on an authorisation to those who are named in the application for authorisation- it only allows authorisation to the person applying and “*to every other person named or referred to in the application for authorisation*”. Therefore section 58(2) was needed to allow the Commission to grant a wider form of authorisation to parties not mentioned in the application for authorisation.
85. By contrast, s65B does **not** limit the parties who can rely on a clearance in the same way as section 58B(1). It applies to “*a party*” (section 65B(1)) and to “*a person*” (section 65B(2)) without limiting those parties/ persons to those persons named in the application. Therefore no provision similar to section 58(2) was necessary.
86. The Commission, in considering an application for a collaborative activity clearance, can properly look forward in time and consider whether the expected expansion of a franchise chain makes a difference to its assessment of whether a cartel provision is reasonably necessary or whether it substantially lessens competition. That is to be expected with common forms of collaborative activity like business format franchise networks.
87. However, if the franchise network expansion proceeds in a way that the Commission did not expect then there is the possible remedy/ safeguard of revocation as discussed above.

### Confidentiality

88. Confidentiality is requested for the information in this submission that is contained in square brackets and highlighted in yellow on the basis that:
- (a) the information is commercially sensitive and valuable information which is confidential to the Applicant and/or the franchisees and the disclosure of which would be likely unreasonably to prejudice the commercial position of the Applicant and/or the franchisees, or the person who is the subject to the information; or
  - (b) to make the information public would be likely to result in its disclosure or use for improper gain or advantage.
89. The Applicant requests that it be notified if a request is made to the Commission under the Official Information Act 1982 for the release of the information for which confidentiality has been claimed, and given a chance to provide submissions to the Commission on whether it should make disclosure prior to any such disclosure taking place.
90. Confidential and public versions of this submission have been provided to the Commission.

Yours faithfully  
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**Appendix 1 – [ ]**

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**Appendix 2 – [ ]**

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