

Commerce Commission

Decision No. 322

Determination pursuant to the Commerce Act 1986 (the Act), and in accordance with a delegation given in terms of s 105 of the Act, in the matter of an application for clearance of a business acquisition involving:

WORKS CIVIL CONSTRUCTION LIMITED

and

BITUMIX LIMITED

The Commission:	T G Stapleton
Summary of Proposed Acquisition:	The proposed acquisition by Works Civil Construction Limited of the shares in or the assets and business of Bitumix Limited.
Working Day 10:	9 April 1998
Determination:	Pursuant to s 66(3)(a) of the Act, and in accordance with a delegation granted under s 105 of the Act, the Commission determines to give a clearance for the proposed acquisition.
Date of Determination:	7 April 1998

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THE PROPOSAL

- 1 On 26 March 1998, the Commission registered a notice pursuant to s 66(1) of the Commerce Act 1986 (“the Act”) seeking clearance for the acquisition by Works Civil Construction Limited (“Works Civil”) of the shares in or the assets and business of Bitumix Limited (“Bitumix”).
- 2 The vendor will be BP Oil New Zealand Ltd if the acquisition is a share purchase and Bitumix if the acquisition is an asset purchase.

THE PROCEDURES

- 3 Section 66(3) of the Act requires the Commission either to clear, or to decline to clear, a notice given under s 66(1) within 10 working days, unless the Commission and the person who gave the notice agree to a longer period. As no extension has been sought, a determination is required by 9 April 1998.
- 4 Pursuant to s 105 of the Act, the Commission delegated its powers to consider and determine the notice seeking clearance to Mr Terry Stapleton, a member of the Commission.
- 5 In the notice seeking clearance, Works Civil sought confidentiality for the fact of the proposed acquisition. Following discussions between Commission staff and the solicitors acting for Works Civil, it was agreed that, subject to Commission staff being able to contact Transfund New Zealand and Transit New Zealand for market information and comment on the proposed acquisition, a confidentiality order for the fact of the proposed acquisition would be made. Accordingly, an order under section 100 of the Act was made on that basis, providing for confidentiality for the fact of the proposal until the earlier of 20 working days from the Commission’s determination of the notice or public announcement of the proposal.
- 6 In addition, Works Civil sought confidentiality for certain information contained in the notice seeking clearance, and a confidentiality order was made in respect of that information for a period of 20 working days from the Commission’s determination of the notice. When the confidentiality order expires, the provisions of the Official Information Act will apply to that information.

- 7 This report concludes that Commission staff are satisfied that implementation of the proposed acquisition would not result, and would not be likely to result, in any person acquiring or strengthening a dominant position in a market. Accordingly, it is recommended that in terms of s 66(3)(a) of the Act, and in accordance with a delegation granted under s 105 of the Act, the Commission gives clearance for the proposed acquisition.

THE INVESTIGATION

- 8 Staff contacted the following parties in investigating the proposed acquisition:
- Existing competitors including Fulton Hogan Ltd, Technic New Zealand Ltd, and Higgins Contractors Ltd¹ ;
 - Transit New Zealand; and
 - Transfund New Zealand.
- 9 Additional information was also provided by the applicant (Works Civil).

THE PARTICIPANTS

Works Civil Construction Ltd (“Works Civil”)

- 10 Works Civil, based in Wellington, is a wholly owned subsidiary of Downer and Company Ltd and is involved in civil engineering activities in New Zealand including the following:
- State highway maintenance and construction;
 - Local authority road maintenance and construction;
 - Other specialist civil engineering and asset maintenance including private sector roading and special pavements, marine and river engineering, pipeline construction and rehabilitation, and oil industry engineering; and
 - Management and maintenance of other services for local authorities including water supply, sewage and waste water treatment, stormwater drainage, refuse disposal, street cleaning and tending of parks and gardens.
- 11 Downer Construction (New Zealand) Ltd (“Downer Construction”) is another wholly owned subsidiary of Downer and Company Ltd. Downer Construction’s principal business activity is construction, specifically:
- Civil engineering works such as road and bridge construction and thermal and hydro electric power plants;

- Building works including commercial buildings, shopping centres and apartments; and
- Special works such as port development and wharf construction.

Bitumix Limited (“Bitumix”)

- 12 Bitumix, based in Wellington, is a wholly owned subsidiary of BP Oil New Zealand Ltd which is ultimately owned by The British Petroleum Company plc. Bitumix’s principal business activity is the provision of road sealing services including the supply and spraying of bitumen and the production and laying of asphalt. Bitumix supplies bitumen and asphalt to other roading companies and also sub-contracts to these companies for the provision of sealing services.

OTHER RELEVANT PARTIES

Fulton Hogan Ltd (“Fulton Hogan”)

- 13 Fulton Hogan, based in Dunedin, is an unlisted public company in which Shell NZ Holding Company Ltd has a 37% shareholding. The balance of the shares in the company is held by staff and Fulton and Hogan family interests. Fulton Hogan is involved in civil engineering activities in New Zealand including state highway construction and maintenance and local authority road construction and maintenance.

Higgins Contractors Ltd (“Higgins”)

- 14 Higgins, based in Palmerston North, is a roading and general contractor and is involved in state highway and local authority road construction and maintenance.

Technic New Zealand Ltd (“Technic”)

- 15 Technic, based in New Plymouth, is also involved in state highway and local authority road construction and maintenance through various subsidiaries including Technic Taranaki Ltd, Technic Waikato Ltd, Technic Canterbury Ltd and South Taranaki Construction Ltd. Technic is also involved in the supply of bitumen products through Technic Industries Ltd and Technic Bitumen Ltd.

BACKGROUND INFORMATION

- 16 In 1991, Works Civil sought clearance to acquire the road maintenance assets used by Far North District Council. The Commission gave clearance for that acquisition. Commission staff also looked at the roading industry in 1992, and again in 1996, when investigating the possible sale of Works and Development Services Corporation (NZ) Ltd.²

RELEVANT LEGISLATION

- 17 Under the Transit New Zealand Act 1989, Transit New Zealand, a crown entity, was established with the principal objective of promoting policies and allocating resources to achieve a safe and efficient land transport system. In 1995, with the passing of the Transit New Zealand Amendment Act, Transit New Zealand's principal objective became that of operating a safe and efficient state highway system.
- 18 Under the 1995 Amendment Act, Transfund New Zealand was also established, functioning separately from Transit New Zealand. Transfund New Zealand is responsible for land transport system funding operations. Its objective is "to allocate road-user funds from the National Road Account to achieve a safer and more efficient roading system."³ Transfund New Zealand's functions include developing the National Roding Programme which proposes activities and allocates funds for roading and passenger transport. The organisation also undertakes reviews and audits of the activities of road controlling authorities, including Transit New Zealand, with respect to roading construction and maintenance and passenger transport funded from the National Road Account.
- 19 The Transit New Zealand Act 1989 requires all state highway construction and maintenance work to be put to open tender. This work is 100% funded by Transfund New Zealand. Local authorities must also put contracts out for competitive tender if they wish to receive Transfund New Zealand funding. If not offered for competitive tender, funding from Transfund New Zealand is not available.⁴ Transfund New Zealand contributes about 50% of the funding for local authority roading, with the balance provided by local authorities.

THE RELEVANT MARKETS

Introduction

- 20 The purpose of defining markets is to provide a framework within which the competition implications of a business acquisition can be analysed. The relevant markets are those in which competition may be affected by the acquisition being considered. Identification of the relevant markets enables the Commission to examine whether the acquisition would result, or would be likely to result, in the acquisition or strengthening of a dominant position in terms of s 47(1) of the Act in any of those markets.
- 21 Section 3(1A) of the Act provides that:
... the term 'market' is a reference to a market in New Zealand for goods and services as well as other goods and services that, as a matter of fact and commercial common sense, are substitutable for them.
- 22 In a 1984 decision, the Commission, drawing upon the Australian Trade Practices Tribunal decision in *Queensland Co-operative Milling Association*,⁵ defined a market as:
... a field of actual or potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given a sufficient price incentive.⁶
- 23 Markets are defined in relation to product type, geographical extent, and functional level. With the first two dimensions, market boundaries are determined by testing for substitutability, in terms of the response to a change in relative prices of the good or service in question and possible substitute goods or services. A properly defined market will include products which are regarded by buyers as being not too different ('product' dimension), and not too far away ('geographical' dimension), and are thus products to which they could switch if a small yet significant and *non-transitory* increase in price (*ssnip*) of the product in question was to occur. It will also include those suppliers currently in production who are likely, in the event of such a *ssnip*, to shift promptly to offer a suitable alternative product, even though they do not do so currently.
- 24 In addition, markets are also defined in relation to functional level. Typically, the production, distribution, and sale of products proceeds through a series of functional

levels. For example, that between manufacturers and wholesalers might be called the “manufacturing market”, while that between wholesalers and retailers is usually known as the “wholesaling market”.

Market Definition

- 25 The applicant submits that the proposed acquisition will result in aggregation of market shares in the market for roading construction and maintenance in New Zealand, as both companies are involved in tendering for state highway and local authority roading construction and maintenance contracts.
- 26 The applicant states that the core business activities of Works Civil and Bitumix are “complementary”, with Works Civil’s core business being roading construction and maintenance, and Bitumix’s core business being the supply and application of bitumen products. Works Civil is not currently involved in the supply and application of bitumen products and, in the past, has subcontracted this work out to Bitumix. The applicant notes that Works Civil is the only major roading contractor operating in New Zealand that does not have its own sealing capability.
- 27 The applicant states that construction contracts are for road and bridge construction, replacement and rehabilitation, with a large proportion of road construction contracts being for “shape correction”. Maintenance contracts primarily relate to surface maintenance such as pot hole repair, surface restabilisation, shoulder maintenance, snow/ice clearance and gritting. Roading contracts also involve emergency work such as dealing with floods and slips.
- 28 Obviously, minor maintenance work involves substantially less labour, equipment, and resources than major maintenance or construction work, but Commission staff do not consider it necessary to separate out these categories for the purpose of analysing the competition effects of the proposed acquisition. Further, the market participants contacted by Commission staff stated that the majority of roading contractors undertake both construction and maintenance work.
- 29 Commission staff, in the earlier surveillance report relating to the possible sale of Works and Development Services Corporation (NZ) Ltd⁷, defined the relevant market as that for the provision of civil engineering construction and maintenance contracting services (“the civil engineering construction market”). In relation to the provision of roading construction and maintenance services within that market, it was

considered that there were two segments – state highway construction and maintenance services and local roading construction and maintenance services.

- 30 Similarly, for the purposes of this report, Commission staff consider it appropriate to segment the market into state highway construction and maintenance services, and local authority road construction and maintenance services.
- 31 The roading construction and maintenance services market in New Zealand is driven mainly by the level of annual funding allocated by Government. As previously stated, this funding is administered by Transfund New Zealand. The main purchasers of roading construction and maintenance services are Transit New Zealand, in relation to state highway construction and maintenance, and local authorities, which are responsible for road construction and maintenance in their own areas.
- 32 All state highway construction and maintenance work is carried out under contracts awarded by Transit New Zealand through Transfund New Zealand’s Competitive Pricing Procedures (“CPP”). The contracts are awarded principally on the basis of the lowest price acceptable tender.
- 33 In relation to local authority roading construction and maintenance work, the applicant states that there are 59 district councils and 15 city councils in New Zealand, each of which has responsibility for road construction and maintenance in its own area. Transfund New Zealand provides approximately 50% of the funding for local authority roading.
- 34 Bitumen and roading aggregates are the main inputs in roading construction and maintenance. Bitumen is a by-product of petrol refining. As such, most bitumen available in New Zealand is produced at the Marsden Oil Refinery and is sold by Shell New Zealand Ltd (“Shell”), BP Oil New Zealand Ltd (“BP”) and Caltex New Zealand Ltd (“Caltex”). The applicant also submits that there is an increasing volume of bitumen imported into New Zealand.
- 35 In terms of geographic market definition, Commission staff consider that it is appropriate to define a national market. Works Civil, Bitumix and Fulton Hogan operate on a nationwide basis, and there are a number of other roading contractors operating on a relatively large scale; for example, Higgins and Technic. It is also noted that some Local Authority Trading Enterprises (LATEs) are expanding into different regions, and so are in an increasingly stronger position to tender for roading

work in a wider geographic area. For example, Excell Corporation, a LATE owned by the Manukau City Council, has acquired LATEs in Rotorua, Masterton, Nelson, and Buller. There is also a large number of smaller regional and local roading contractors operating in the market.

Conclusion on Market Definition

- 36 Commission staff conclude that the relevant market for the purpose of analysing the competition issues arising from the proposed acquisition is the market for the provision of roading construction and maintenance services in New Zealand (“the roading construction and maintenance market”).

ASSESSMENT OF DOMINANCE IN THE ROADING CONSTRUCTION AND MAINTENANCE MARKET

Overview

- 37 Section 66(3) of the Act, when read in conjunction with s 47(1) of the Act, requires the Commission to give clearance for a proposed acquisition if it is satisfied that the proposed acquisition would not result, and would not be likely to result, in a person acquiring or strengthening a dominant position in a market. If the Commission is not so satisfied, clearance must be declined.
- 38 Section 3(9) of the Act states that a person is in a “dominant position” in a market if:
- ... a person as a supplier or an acquirer of goods or services either alone or together with an interconnected or associated person is in a position to exercise a dominant influence over the production, acquisition, supply, or price of goods or services in that market ...
- 39 That section also states that a determination of dominance shall have regard to:
- market share, technical knowledge and access to materials or capital;
 - the constraint exercised by competitors or potential competitors; and
 - the constraint exercised by suppliers or acquirers.
- 40 In reaching a view on whether a person is in a position to exercise a dominant influence in a market, the Commission considers the foregoing non-exhaustive factors and any other relevant matters that may be found in a particular case.

41 In *Port Nelson Ltd v Commerce Commission* [1996] 3 NZLR 554, the Court of Appeal approved the following dominance standard, adopted by McGechan J in the High Court:

...dominance involves more than “high” market power; more than mere ability to behave “largely” independently of competitors; and more than power to effect “appreciable” changes in terms of trading. It involves a high degree of market *control*.

42 A dominance assessment for the roading construction and maintenance market follows.

Current Competition

43 As previously stated, Works Civil and Bitumix are involved in roading construction and maintenance on a national basis, as is Fulton Hogan. There is also a number of other roading contractors which operate at regional or local levels including Higgins, Technic, Local Authority Trading Enterprises (LATEs) and smaller private contractors.

44 The main customers in the roading construction and maintenance market are Transit New Zealand and local authorities. The applicant states that Transit New Zealand’s highway construction and maintenance work accounts for [] of Works Civil’s revenue, and local authority work accounts for []. Works Civil is also involved in roading work for forestry companies and residential subdivision developments.

45 From information published in the New Zealand Official Yearbook 1997, it is noted that there are 74 national and provincial state highways and motorways in New Zealand, comprising 10,453 kilometres of roading. In addition, there are 15,286 kilometres of urban roads and 66,137 kilometres of rural roads, a total of 91,876 kilometres of developed roading, which includes over 15,800 bridges.

46 In 1996, total public roading expenditure was \$624,097,000, with state highway expenditure accounting for \$363,131,000 or 58% and local authority roading expenditure accounting for \$256,726,000 or 41%. Of the expenditure on state highways, \$136,170,000 or 37% was spent on construction and improvement, and \$226,051,000 or 62% was spent on maintenance and repair. The balance was spent on bridges and other structures.

Market Shares

47 In the Commission’s view, a dominant position in a market is generally unlikely to be created or strengthened where, after the proposed acquisition, either of the following situations exist⁸ :

- the merged entity (including any interconnected or associated persons) has less than in the order of a 40% share of the relevant market;
- the merged entity (including any interconnected or associated persons) has less than in the order of a 60% share of the relevant market and faces competition from at least one other market participant having no less than in the order of a 15% market share.

48 Except in unusual circumstances, the Commission will not seek to intervene in business acquisitions which, given appropriate delineation of the relevant market(s) and measurement of market shares, fall within these “safe harbours”.

49 On the basis of information provided by the applicant and Transfund New Zealand, market shares for the year ended 30 June 1997 are calculated as follows:⁹

Contractor	Number of Contracts		Value (\$000)
Market Share (\$value)			
Works Civil	[]	[]	[]
Bitumix	[]	[]	[]
Downer Construction	[]	[]	[]
Combined Entity	[]	[]	[]
Fulton Hogan	[]	[]	[]
Higgins	[]	[]	[]
Technic	[]	[]	[]
Others	[]	[]	[]
Total	[]	[]	100%

50 As can be seen from the above table, the combined entity would have a market share of approximately [], facing strong competition from Fulton Hogan with a market share of approximately [] and from many smaller market participants. The combined entity’s market share would fall within both of the Commission’s “safe harbours”, having less than in the order of a 40% share of the market, and having less than in the order of a 60% share of the market and facing competition from at least one other market participant having no less than in the order of a 15% market

share.

51 Although the above market shares are calculated on the basis of roading contracts with a value of not less than \$50,000, it is considered that they are a realistic reflection of existing competition in the market. The applicant submits that the omission of contracts with a value of less than \$50,000 has no significant impact on market shares. Also, as Works Civil, Bitumix and Downer Construction are not particularly active at the lower end of the market, the inclusion of contracts with a value less than \$50,000 is likely to slightly reduce their market shares.

52 In relation to the state highway construction and maintenance segment of the market, market shares for the same period are calculated as follows:

Contractor	Number of Contracts		Value (\$000)
Market Share (\$value)			
Works Civil	[]	[]	[]
Bitumix	[]	[]	[]
Downer Construction	[]	[]	[]
Combined Entity	[]	[]	[]
Fulton Hogan	[]	[]	[]
Higgins	[]	[]	[]
Technic	[]	[]	[]
Others	[]	[]	[]
TOTAL	[]	[]	100%

53 Market shares for the local authority roading construction and maintenance segment of the market are calculated as follows:

Contractor	Number of Contracts		Value (\$000)
Market Share (\$value)			
Works Civil	[]	[]	[]
Bitumix	[]	[]	[]
Combined Entity	[]	[]	[]
Fulton Hogan	[]	[]	[]
Higgins	[]	[]	[]
Technic	[]	[]	[]
Others	[]	[]	[]
Total	[]	[]	100%

54 Market shares for the combined entity in both of these segments of the market would also fall within the Commission’s “safe harbours”.

- 55 The applicant submits, and Commission staff accept, that based on the market shares for the combined entity and other existing market participants, implementation of the proposed acquisition will not result in the combined entity acquiring or strengthening a dominant position in the market as it will continue to face strong national and regional competition from Fulton Hogan, Technic, Higgins, LATEs, and private contractors. Furthermore, the applicant submits that all market participants are constrained by the countervailing power in the hands of Transit New Zealand and local authorities.
- 56 Other market participants contacted by Commission staff, and Transfund New Zealand, also considered that there is strong competition in the roading construction and maintenance market.

Vertical Integration

- 57 Under the Commerce Act, vertical acquisitions are subject to the same tests as horizontal acquisitions. However, the Commission accepts that, in general, acquisitions leading to vertical integration are less likely to result in the acquisition or strengthening of a dominant position in a market than those which lead to horizontal integration. The Commission is of the view that, unless a situation of dominance exists at one of the levels affected by a vertical acquisition, such acquisitions are unlikely to lead to the acquisition of a dominant position in a market.¹⁰
- 58 Implementation of the proposal will result in vertical integration as Works Civil will acquire a supplier of bitumen products, one of the main inputs in roading construction and maintenance. Although Works Civil does not have any current involvement in the supply of bitumen, it already has some vertical integration in respect of roading aggregates, another input in roading construction and maintenance. Works Civil sources approximately 20% of its roading aggregates requirements from quarries which it leases.
- 59 Commission staff are of the view that the vertical integration resulting from implementation of the proposed acquisition is unlikely to result in the combined entity acquiring or strengthening a dominant position in any market. Works Civil is not currently involved in bitumen supply, and there are already a number of other vertically integrated roading contractors operating in the market, including Fulton Hogan, which sources its bitumen requirements from Shell, Technic, which is involved in importing bitumen into New Zealand, and Higgins, which sources its bitumen requirements from Caltex and Shell.

Conclusion on Assessment of Dominance in the Roading Construction and Maintenance Market

- 60 Commission staff conclude that the combined entity's market share would fall within both of the Commission's "safe harbours" and that the combined entity would face strong competition from Fulton Hogan and other existing market participants. Transit New Zealand and local authorities also have some countervailing power in the market. Accordingly, Commission staff conclude that implementation of the proposal would not result, and would not be likely to result, in the combined entity acquiring or strengthening a dominant position in the roading construction and maintenance market.

OVERALL CONCLUSION

- 61 Commission staff conclude that, having regard to the factors set out in s 3(9) of the Act and all other relevant factors, the proposed acquisition would not result, and would not be likely to result, in any person acquiring or strengthening a dominant position in the market for the provision of road construction and maintenance services in New Zealand.

RECOMMENDATION

- 62 It is recommended that, in terms of s 66(3)(a) of the Act, the Commission give clearance for the proposed acquisition.

John Preston
Chief Investigator

Jane Chilcott
Investigator

Jo Bransgrove
Manager

DETERMINATION ON NOTICE OF CLEARANCE:

WORKS CIVIL CONSTRUCTION LIMITED/BITUMIX LIMITED

I agree/disagree with the recommendation.

I am satisfied/not satisfied that implementation of the proposal would not result, and would not be likely to result, in any person acquiring or strengthening a dominant position in a market.

Accordingly, pursuant to s 66(3)(a) of the Commerce Act 1996 (the Act), and in accordance with a delegation granted under s105 of the Act, I hereby give/decline to give clearance for the proposed acquisition by Works Civil Construction Limited of the shares in or the assets and business of Bitumix Limited.

Dated this day of April 1998

T G Stapleton
Member

- ¹ No reference was made to the proposed acquisition in discussions with existing competitors.
- ² Refer surveillance reports BAE: 96 and BAE: 461.
- ³ New Zealand Official Yearbook 1997, p521.
- ⁴ Historically, local authorities maintained in-house operations for the majority of their road construction and maintenance work.
- ⁵ *Queensland Co-operative Milling Association* (1976) ATPR 40-012 at 17,247.
- ⁶ *Edmonds Food Industries/WF Tucker & Co Limited*, Decision No. 84, 21 June 1984.
- ⁷ Refer n2.
- ⁸ Refer Commerce Commission's Business Acquisitions Guidelines, 1996, p17.
- ⁹ Market shares are based on statistics supplied to Transfund New Zealand from all road controlling authorities. The information covers all roading contracts let which have a value of not less than \$50,000, and which are funded in whole/part by Transfund New Zealand.
- ¹⁰ Refer Commerce Commission's Business Acquisitions Guidelines, 1996, p23.

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