



## COMMERCE COMMISSION

### Decision No. 462

Determination pursuant to the Commerce Act 1986 in the matter of an application for clearance of a business acquisition involving:

**ANCHOR INVESTMENTS LIMITED**

**and**

**GRATED CHEESE COMPANY**

**The Commission:** MJ Belgrave  
D Bates QC  
P JM Taylor

**Summary of Application:** The application by Fonterra Co-operative Group Limited for the acquisition by Anchor Investments Limited, a wholly owned subsidiary of Fonterra, or any of its interconnected bodies corporate, of the remaining 50% of the shares in Grated Cheese Co Limited from Chad Holdings Limited.

**Determination:** Pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition.

**Date of Determination:** 29 April 2002

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## THE PROPOSAL

1. On 15 April 2002 Fonterra Co-operative Group Limited ("Fonterra") registered a notice with the Commission seeking clearance under s66 (1) of the Commerce Act 1986 ("the Act")<sup>1</sup> for Anchor Investments Limited ("AIL"), a wholly owned subsidiary of Fonterra, or any of its interconnected bodies corporate, to buy the remaining 50% of the shares in Grated Cheese Co Limited ("GCC") from Chad Holdings Limited ("Chad").

## THE PROCEDURES

2. Section 66(3) requires the Commission either to clear or to decline to clear a notice given under s66(1) within 10 working days, unless the Commission and the person who gave notice agree to a longer period. Accordingly, a decision on the application was required by 30 April 2002.
3. In its application, Fonterra sought an order under s100 to prohibit disclosure of certain information confidential in the application. A s100 order was made on 17 April 2002 in respect of certain information for a period expiring 20 working days after the Commission's determination notice. When the s100 order expires, the Official Information Act 1982 will apply to that information.
4. The Commission's determination is based on an investigation conducted by Commission staff.
5. The Commission's approach is based on principles set out in the Commission's *Practice Note 4*.<sup>2</sup>

## GCC

6. GCC was established in 1982 in Auckland. 50% of GCC's shares are owned by AIL and 50% by Chad.
7. GCC produces a range of grated, shredded and diced cheeses from cheese manufactured by Fonterra (Cheddar, Mozzarella, Colby, Edam, Gouda, Parmesan).
8. In New Zealand, GCC sells to food service wholesalers, New Zealand Dairy Foods Limited ("NZDF"), food manufacturers, supermarkets and other food retailers. These customers resell grated cheese at wholesale or retail or to use it as ingredients in food products.
9. GCC also fills the New Zealand Dairy Board's export contracts for both food service and consumer packed grated cheese products for markets in Australia, Asia, Latin America and the Middle East. Approximately [ ] of GCC's product is exported.

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<sup>1</sup> For the purpose of this determination, references to sections will be to sections of the Act unless otherwise stated.

<sup>2</sup> Commerce Commission, *Practice note 4: The Commission's Approach to Adjudicating on Business Acquisitions Under the Changed Threshold in section 47 – A Test of Substantially Lessening Competition*, May 2001.

**AIL**

10. AIL is a company incorporated in New Zealand and registered under the Companies Act 1993. It is wholly owned by Fonterra, which, through AIL, owns 50% of the shares in GCC.
11. Fonterra plans to on-sell its interest in GCC to Australian Food Holdings Limited (“AFHL”) which is majority owned by Fonterra.

**Chad**

12. Chad is the shareholding company that owns the other 50% of the shares in GCC. The two shareholders of Chad, Mal Smith and Bill Walker, are also the joint managing directors of GCC. Both wish to exit their shareholding in GCC.

**AFHL**

13. AFHL is Fonterra's principal investment vehicle into New Zealand and Australian consumer dairy markets. 81.81% of AFHL's shareholding is owned by Fonterra, with the remaining shareholding split relatively equally between Aorangi Laboratories Limited (associated with the McConnon family) and Lait family interests.

**OTHER RELEVANT PARTIES****Mainland**

14. Mainland Products Limited (“Mainland”) is a subsidiary of Australasian Food Holdings Limited, incorporated in New Zealand.
15. Its dairy products division manufactures a full range of cheeses, butter, speciality cheeses, yoghurt, dairy foods, other cultured products, fresh milk and other beverages. Its brands include Mainland®, Tararua®, Meadow Fresh®, Ferndale®, and Galaxy®.

**NZDF**

16. 50.0004% of NZDF's shareholding is owned by Fonterra and 49.9996% by other independent shareholders (mostly farmers). In accordance with the divestment requirement contained in section 9 of the DIRA, Fonterra has entered into a sale and purchase agreement with Rank Group Limited (“Rank”) under which Fonterra has irrevocably undertaken to sell to Rank all of Fonterra's NZDF shares. Notice of the sale was served on NZDF by Rank on Friday, 5 April 2002. The sale is conditional on no material adverse event occurring before the date on which the offer is due to be made and the offer itself is subject to a number of conditions relating to the operation of NZDF and NZDF's level of debt. Fonterra expects that all of the conditions will be satisfied and that its NZDF shares will be sold to Rank.
17. NZDF has a long-term supply contract with Fonterra for bulk cheese, block cheese and grated cheese. [

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18. NZDF currently purchases cheese and other packaged dairy products from Fonterra, GCC and other companies and on-sells them to food service customers, supermarkets and other food outlets. It also owns the Puhoi Valley Cheese Company, which makes specialty cheeses.

### **Bonlac Foods Limited and Bonland Limited**

19. Fonterra has a 25% shareholding in an Australian company, Bonlac Foods Limited (“Bonlac”) and a 50% shareholding in a joint venture company with Bonlac called Bonland Limited (“Bonland”).
20. Bonland supplies cheese, butter and dairy ingredients in Australia and exports some of these products to New Zealand. Its exports of cheeses are under the Perfect and Bega brands.

### **ASSOCIATED PERSONS**

21. Companies that are part of the same corporate grouping, or have similar strong relationships, cannot be relied upon to provide an effective competitive constraint to one another. Other less formal relationships between companies may also give rise to limitations on the extent of rivalry between them. Relationships between persons in the relevant market and other businesses may also affect rivalry in a market.
22. In determining whether two or more persons are associated, s 47(2) provides as follows:

*“for the purpose of this section, a person is associated with another person if that person is able, whether directly or indirectly, to exert a substantial degree of influence over the activities of the other.”*

#### *Analysis of substantial degree of influence*

23. The Commission considers that a “substantial degree of influence” means “able to bring real pressure to bear on the decision-making process of the other”<sup>3</sup>. The Commission also accepts the rebuttable presumptions postulated by Berry and Riley<sup>4</sup> as a useful working approach. In each case, however, it is necessary to stand back and look at all the facts in light of s47(2).

24. The Commission’s approach to association is:

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<sup>3</sup> See Commerce Commission, *Decision No. 278: Air New Zealand/Ansett Holdings/Bodas*, 3 April 1996, especially paragraph 180

<sup>4</sup> MN Berry & A Riley, “Beware the new business acquisition provisions in the Commerce Amendment Act 1990”, (1991) 21 VUWLR, 91 at 111. Within this article, the authors put forward the following rebuttable presumptions for the analysis of association:

- (a) a shareholding between 30% and 50% is likely to give rise to a substantial influence, without any other contributing factors.
- (b) a shareholding between 20% and 30% is likely to give rise to a substantial influence only if there are “other factors”. These other factors would include the distribution of other shareholdings, the ability to defeat shareholder resolutions, board representation, and the ability to influence the target’s management and policy.
- (c) a shareholding between 15% and 20% is unlikely to give rise to a substantial influence unless there are special circumstances.
- (d) a shareholding of less than 15% does not give rise to the necessary degree of influence.

“ in considering whether persons are associated in terms of s47(2), (the Commission) has regard to all relevant factors and considers as a whole the total effect, actual or likely, of all elements of the relationship between the parties. These factors include:

- (a) the historical basis of the relationship and reciprocal connections
- (b) actual and prospective shareholdings
- (c) board membership and representation
- (d) motivation and expectation of parties
- (e) any premiums or concessions paid or provided to pursue the relationship
- (f) distribution of other shareholdings, and
- (g) evidence of influence on management and policy.”<sup>5</sup>

25. Applying that approach to the present application, the Commission notes the following points:

- Fonterra holds 50% of the shares in GCC through its wholly owned subsidiaries AIL. Under clause 3.1 of GCC's Constitution, [

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- (a) Under clause 26.1 of GCC's Constitution, Chad and Fonterra may each appoint three directors to the GCC board of directors, with one of the Fonterra appointed directors being the Chairman (with no casting vote).
- (b) Directors' and shareholders' decisions are made by simple majority (although there must be at least one director present representing the two classes of shares - Fonterra and Chad - clause 32.10 of the Shareholders' agreement). This provides the Fonterra directors and Chad directors each with a power of veto.
- (c) Under the Shareholders' Agreement between Fonterra and Chad, [ ]

26. The Commission considers that the above factors demonstrate that Fonterra can exercise a substantial degree of influence over the activities of GCC and that Fonterra and GCC are associated.

27. AS GCC is associated with Fonterra, it cannot be relied upon to provide competitive constraint on Fonterra.

## **CONTERFACTUAL**

28. The applicant submits that the two Chad shareholders, Mal Smith and Bill Walker wish to exit their shareholding in GCC as [ ] It would appear that a sale of Chad's GCC shares is inevitable.

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<sup>5</sup> See *Air New Zealand/Ansett Holdings* decision

29. Consequently, the counterfactual is the situation where Chad's GCC shares are sold to a party not associated with Fonterra and Fonterra keeps its 50% shareholding in GCC, that is, Fonterra would remain associated with GCC.
30. On this basis, GCC cannot be relied upon to provide competitive constraint on Fonterra in the counterfactual.

## **CONCLUSION**

31. As Fonterra and GCC are currently associated, GCC cannot be relied upon to provide competitive constraint on Fonterra. The acquisition by Fonterra of Chad's GCC shareholding is not likely to result in any real substantial lessening of competition in a market in New Zealand. The competitive situation would remain effectively the same.
32. The same situation would prevail under the counterfactual.
33. As there is the same situation under the proposed acquisition and the counterfactual, the Commission is satisfied that the proposed acquisition will not have, nor would be likely to have, the effect of substantially lessening competition in a market.
34. Because the Commission has reached this conclusion on the basis of the relationships between the parties to the transaction, it has not been necessary to consider a competition analysis.

## **DETERMINATION ON NOTICE OF CLEARANCE**

35. Accordingly, pursuant to section 66(3)(a), the Commission determines to give clearance for the acquisition by Anchor Investments Limited, a wholly owned subsidiary of Fonterra Co-operative Group Limited, or any of its interconnected bodies corporate, of the remaining 50% of the shares in the Grated Cheese Company Limited from Chad Holdings Limited.

Dated this

John Belgrave  
Chair  
Commerce Commission