



6 July 2007

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Commerce Act Review
Ministry of Economic Development
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Dear Sir

REVIEW OF THE REGULATORY CONTROL PARTS OF THE COMMERCE ACT

We are grateful for the opportunity to comment on the Ministry of Economic Development's ("MED's") Review of Regulatory Control Provisions under the Commerce Act 1986: Discussion Document ("**the Discussion Document**"). This letter sets out the submissions of the New Zealand Shipping Federation (" **the NZSF**"), and we are happy for this letter to be published on the MED's website. This submission is also supported "in principle" by the members of the New Zealand Shippers Council¹

About the NZSF

The NZSF is an organisation that advocates on behalf of a range of significant New Zealand businesses with interests in passenger and cargo shipping, oil and fuel and cement distribution. NZSF's members include Pacifica Shipping, Silver Fern Shipping Limited, Holcim NZ Limited, Toll - The Interislander, Strait Shipping Limited and Golden Bay Cement. Broadly speaking, NZSF's members are major acquirers of services from New Zealand's ports.

Historically, NZSF and its members have engaged with Government in relation to the contestability of port services. In particular, NZSF's members led submissions, from an acquirer's perspective in relation to the 2002 Ministry of Transport ("**MOT**") review of the market power of ports. The finding of the MOT review was that while the ports sector as a whole was subject to competitive constraints, there were areas of port operations for which competitive pressures were limited and the customers of those services were described as having been "captured".

¹ List of Shipper's Council members can be found at www.shipperscouncil.co.nz

Since the release of the MOT review, the port companies have become sensitive to the concerns raised and, in general, a positive working relationship has emerged between NZSF and the port companies. Having said this, some competition bottlenecks remain and the NZSF is of the view that the ports sector as a whole is intrinsically vulnerable to competition risks emerging if it is left for too long without regulatory scrutiny.

In addition, NZSF is of the view that the performance of the ports sector could be improved if there was greater transparency and if regulatory agencies such as the Commerce Commission had a greater array of options at their disposal to address problems as they emerge. Increasing the regulatory pressures on the ports to improve their efficiency and to pass on the gains of that efficiency would assist with the growth of New Zealand's export driven economy.

NZSF has monitored the progression of the MED's review of the regulatory control parts of the Commerce Act 1986 ("**the Act**") with interest and has exchanged correspondence with the Minister of Commerce prior to the release of the Discussion Document. Essentially, NZSF endorses many of the MED's proposals, however it has some specific points which are set out below.

Focus on Investment in Infrastructure

NZSF notes that the Discussion Document places great emphasis on promoting investment in infrastructure. This is reflected in the reasons for the review, the principles underpinning review and in the proposal for the purpose statement of the regulatory control parts of the Act to make explicit reference to retaining incentives to invest. NZSF has some particular comments in relation to this general theme, which are set out below.

While deficiencies in infrastructure may be real and immediate problems for some sectors (for example in the electricity and telecommunications sectors), other issues may be more important for other sectors. For example, in the ports sector the creation of better incentives to export, or make use of domestic maritime transport, through more efficient pricing of port services. Major New Zealand Shippers represented by the New Zealand Shippers Council state in support of this submission that infrastructure investment needs to be aligned to shippers requirements and to be flexible over time. These factors may align better with Government's priorities than having further or sub-optimal investment in ports infrastructure. Growing New Zealand's export sector is a key issue of national importance which Government is committed to resolving and is on an equal footing with the provision of infrastructure. Similarly, the facilitation of improved domestic freight transport is critical to achieving the aims of sustainability and efficiency of New Zealand's surface transport networks.

Further, assuming that any new legislation arising from the review is intended to last into the long term, it is important that the resultant regulatory framework should be flexible enough to allow emergent issues to supersede the priority currently being given to promoting investment in infrastructure, which NZSF sees being particularly germane to specific sectors only. For example, addressing climate change, improving surface transport networks, growing New Zealand's export sector or creating incentives for businesses to innovate are likely to become as important in the future as stimulating investment in infrastructure is today.

Another point is that the Discussion Document only contemplates the importance of investment from the perspective of the monopoly supplier. Acquirers are themselves often businesses which provide essential services or infrastructure, which create valuable innovations or which contribute to New Zealand's economy in critical ways e.g. by driving the export led economy, by employing large numbers of staff and generating revenues. These businesses also need to retain incentives to invest. Such incentives to invest diminish if the regulatory balance is tilted too much in favour of monopoly suppliers. For instance there is little value in New Zealand having world class ports and a run down coastal shipping fleet.

Overall, in NZSF's view the Discussion Document's proposals appear to overly compensate for investment deficiencies that are apparent in specific sectors. While NZSF agrees that the regulatory framework should be able to address underinvestment in infrastructure where it is needed, we think it would be a mistake to accord such importance to that one issue that it trumps more important issues in other sectors that may be current or emerge over time. Certainly, it would be difficult to avoid this outcome if incentives to invest were to be given statutory recognition, whilst issues such as growing the export economy, creating incentives to innovate or dealing with other emergent issue were not.

Purpose Statement

NZSF endorses the concept of a clear purpose statement for the regulatory control parts of the Act. However, NZSF has concerns about attempting to list particular, and conflicting, criteria as being the key issues to consider in all regulatory decision making. As discussed above the most important factors to consider will change for different sectors and overtime.

NZSF suggests that the overarching goal for the regulatory control parts of the Act should be "regulation for the long term benefits of New Zealand consumers" and the Act should then be flexible as to what this entails in respect of different sectors and circumstances.

Competition Test

The MED has sought submissions on the appropriate "competition" test for identifying businesses that can be regulated under the regulatory control parts of the Act.

In NZSF's view, the test for regulation should focus on specific services rather than businesses as a whole. This would enable the regulator to take a more effective surgical approach to investigation and regulation. It would also protect the contestable services that a business offers.

For example, ports offer a range of services some of them are contestable, some of them are not. It would be useful if the regulator could focus only on the services for which there are "captured" customers.

NZSF is also of the view that the nature of a service should be taken into account making a decision as to whether it should be subject to regulation. In particular, access to essential services should be more readily subject to regulatory scrutiny, than the provision of a non

essential goods or service supplied by a firm with market power. Such an approach would be consistent with Australia's access regime under Part IIIA of Australia's Trade Practices Act 1974.

"Lighter Handed" options for regulating

NZSF endorses the introduction of a wider suite of regulatory options for resolving concerns in markets where there is limited competition that are more cost effective and less invasive than control.

The introduction of information disclosure and regulated negotiate arbitrate/mechanisms would also potentially enable acquirers of services to play a more active role in disciplining markets and potentially remove some of that responsibility for this function from the regulator.

In addition, the deployment of "lighter handed" options would be particularly appropriate in respect of sectors where there is contestability for some services, which could be lost if control were to be imposed. For example in the ports sector the imposition of control would potentially damage the many areas of the operation of ports, which are contestable. On the other hand, greater information transparency could enhance the ports progress to contestability.

Sector review

NZSF endorses the introduction of a power for sector wide review it would make the review of certain sectors far more efficient and cost effective.

Simultaneous consideration of "whether" and "how" to regulate

NZSF endorses the proposal for simultaneous consideration of "Whether" and "How" to regulate. There are two reasons for this. Firstly it is difficult for a decision maker to have the confidence to make a decision to regulate if it is not clear what the outcome of imposing regulation would be. Secondly, retaining a two stage process would add significantly to the costs of following through with regulation.

Both of these issues are apparent in a letter from the Minister of Commerce to the Captive Port Customers Group (a group related to the NZSF) dated 13 October 2003:

"You are correct that, following my decision on the control inquiry into airfield activities, I requested the Ministry of Economic Development to carry out a review of Parts 4 and 5 of the Commerce Act. My particular concern was the inability of the Commerce Commission to advise me on what form of control

they may impose so as to inform my decision on the relative costs and benefits of control. The practical effect was that, had I recommended control be imposed on airfield activities, the Commerce Commission would have had to undertake a further inquiry of similar complexity to determine what form of control to impose. I considered this to be highly inefficient."

Tests for whether to impose "lighter handed" regulation

NZSF endorses the proposal that "lighter handed" options regulation should not require quantitative cost benefit analysis for three reasons:

- (i) Previous experience with regulatory control inquiries has shown that quantitative cost benefit analysis is problematic in general, and no other jurisdiction uses it;
- (ii) Allowing qualitative analysis would reduce the cost and complexity of the regulatory process in relation to the imposition of less invasive forms of regulation; and
- (iii) Decisions on the benefits of lighter handed options do not lend themselves to quantitative cost benefit analysis because it is impossible to calculate what the counterfactual would be, as the outcome would be driven by the market rather than the regulator.

Guidance papers

NZSF is of the view that it would assist acquirers of services if the Commerce Commission were to publish more papers or guidelines on key issues, such as appropriate WACC ranges for sectors. These papers could be used as reference points for negotiations. The proliferation of guidance might assist acquirers to help themselves and reduce the need to rely on the regulator to intervene. NZSF suggests that the Act should be amended so that this function is an explicit part of the Commerce Commission's role. This would allow the Commerce Commission to seek appropriate resources to carry out this work.

Merits review

NZSF is of the view that if a supplier of services is entitled to seek merits review of a regulatory decision, then acquirers directly affected by the review should be able to join proceedings and make submissions.

Overall process for regulatory decision making

NZFS is concerned to ensure that the overall process for regulating a business does not become so cumbersome as to make any regulatory inquiry undesirable and burdensome for all parties.

There is a danger that the proposed process for regulatory decision making may have this effect if implemented. It is proposed that there be a criteria assessment stage, a key inputs consultation stage, a putting the key inputs into regulation stage, an inquiry stage, a Ministerial decision stage, a customised control stage and a merits review stage. This process might also involve various bodies having different roles.

NZSF asks that that whatever the final process for regulating is determined to be, it should be relatively efficient. This is particularly important where a fairly low level of regulatory intervention is being contemplated, such as an information disclosure regime. Perhaps in these circumstances it is not necessary to have lengthy key inputs processes for example.

In addition, if the MED is considering placing increasing weight on efficiencies in regulatory analysis than on distributional benefits, it would be inappropriate for the MED to propose legislating a mechanism for regulating that was highly costly and inefficient.

We hope that these comments have been of assistance.

Yours faithfully

A handwritten signature in black ink, appearing to read 'Paul Nicholas', with a stylized flourish at the beginning.

Paul Nicholas
Manager