

**Review of the Clearance and Authorisation Provisions under the  
Commerce Act 1986:  
Submission on MED's Discussion Document of May 2007**

**10 August 2007**



COMMERCE COMMISSION

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## **Executive Summary**

- 1 The following is a summary of the Commerce Commission's ('the Commission') responses to the issues raised in the discussion document entitled the *Review of the Clearance and Authorisation Provisions under the Commerce Act 1986*, released on 29 May 2007. A discussion of the issues and the reasons to support the Commission's responses are contained within the body of the paper.

### ***Issue A: The statutory time frame for merger clearance determinations***

- 2 The Commission considers that the statutory time frame should be increased from 10 working days to 40 working days, and that it should retain the ability to extend this deadline with the agreement of the applicants. A 40 working day time frame is appropriate because:
- the complexity of clearance applications has increased over time;
  - it will improve certainty for applicants because 40 working days is close to the average time taken by the Commission to make clearance decisions;
  - it remains challenging for the Commission to achieve as it is also the current performance measure set out in the Commission's Statement of Intent;
  - it will promote harmonisation with Australia, which has a 40 business day time frame for both its formal and informal notification procedures; and
  - extra resources may be required to meet a statutory time frame that is shorter than current practice.

### ***Issue B: The publication of written clearance decisions***

- 4 The appeal period should run from the date that the Commission makes its determination to:
- if the Commission advises it will not release written reasons for that determination, 20 working days from that date; otherwise
  - 20 working days from the date that the written reasons for that determination are released.<sup>1</sup>
- 5 In order to be operational, it would be necessary for the Commission to specify at the time that it announces its decision whether or not it intends to release written reasons for its determination.

### ***Issue C1: The enforceability of undertakings***

- 6 The Commission supports amending the Commerce Act 1986 ('the Act') to provide for enforceable undertakings for mergers before the High Court, separate from the main acquisition. In seeking such orders, the Commission should not have to establish that the undertaking is necessary to address the competition concerns resulting from the main

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<sup>1</sup> That is, the appeal period would be the number of working days between the date of the Commission's determination and the date it releases its written reasons plus an additional 20 working days.

acquisition. Rather, the proceedings should simply focus on whether or not the undertaking has been complied with.

***Issue C2: Variation of undertakings***

- 7 The Commission recommends that the Act should be amended to provide for variations of undertakings on application of the parties and with the consent of the Commission. The Commission considers that it is not necessary to limit the provision to only minor variations as there may be legitimate reasons that parties would seek to reconfigure the divestment undertakings given. If the proposed variation is significant, the Commission would carry out a full competition analysis of the implications of the variation, in the same manner in which the initial clearance or authorisation was considered. Given the potentially significant costs that may be incurred by the Commission, the parties should be required to pay an application fee to the Commission to have the variation considered.

***Issue D: Behavioural undertakings***

- 8 The Commission considers that it should not be empowered to accept behavioural undertakings for merger clearances and authorisations. Behavioural undertakings are effectively a form of company-specific regulation. Given the dynamic nature of markets, behavioural undertakings may not be effective over time and would require ongoing monitoring and enforcement. The damage to the economy could be irreparable if the merged entity does not comply with its behavioural undertaking. Even if the Commission has full discretion whether or not to accept behavioural undertakings, if applicants offer such undertakings the Commission would be bound to analyse their likely effect in the market, which could be costly and time-consuming. If the Commission declined to accept these undertakings, they would be a further matter for review or appeal to the court, which would add further complexity to the proceedings.
- 9 Therefore, the disadvantages of having a broad discretion to consider behavioural undertakings are likely to far outweigh the few cases where such undertakings would be beneficial.

***Issue E: Informal pre-merger processes***

- 10 The Commission considers that it should not introduce a pre-merger informal process. The benefits of a pre-merger informal process appear to be minimal, both in terms of providing a more cost-effective and timely process for business, and improving the Commission's monitoring and surveillance capability. Moreover, any benefits are unlikely to outweigh the costs and risks of introducing such a process.

***Issue F: A possible clearance process for trade practices***

- 11 The Commission considers that a clearance system for trade practices should not be introduced. The onus should be on business to comply with the Act on an ongoing basis. There would be little benefit in devoting resources to clearance applications that clearly did not substantially lessen competition.
- 12 If a clearance regime is introduced, the Commission considers that it should not be expanded to operate as an exemption regime in relation to conduct covered by the *per se*

prohibitions. Exemptions from the prohibitions should be assessed through the authorisation procedure in the Act.

- 13 If a clearance regime for restrictive trade practices is introduced, the Commission considers that it should be based on elements of the authorisation regime for trade practices, with any necessary modifications.

***Issue G: Collective bargaining notification***

- 14 The Commission considers that a collective bargaining notification system is not justified. The Commission has no evidence to suggest that SMEs are inhibited from engaging in pro-competitive collective bargaining schemes or collective bargaining schemes that would result in net public benefits. The ACCC has received only one notification since introducing its collective bargaining notification scheme in January 2007, which suggests that the demand for this scheme is limited.
- 15 However, if a collective bargaining scheme is introduced, it should be clearly targeted, transparent and certain, enable all interested parties to be involved and give the Commission sufficient time to obtain information and carry out a proper analysis.

***Issue H: the ‘lessening competition’ jurisdiction threshold***

- 16 The Commission considers that the ‘lessening of competition’ test to establish jurisdiction should be retained because it is a useful filter to ensure that the Commission’s resources are appropriately targeted. However, if a clearance regime for trade practices is introduced, the Commission considers that the jurisdiction test should be repealed, and applications for authorisation that would be unlikely to substantially lessen competition (or result in a deemed lessening of competition) would be granted clearance.

***Issue I: Power to revoke, amend or replace an authorisation***

- 17 The Commission’s power to vary, replace or revoke an authorisation if there has been a material change in circumstances should be retained so that the Commission can intervene ex post in relation to arrangements where significant public detriments have arisen following material changes in circumstances. The Commission would take into account the incentives for investment when exercising this discretion.
- 18 If desired, consideration could be given to introducing provisions similar to those in the Australian Trade Practices Act 1974 which make it explicit that the Commission must carry out a public benefits and detriments analysis before intervening, and which allow the parties to the agreement to apply to the Commission for minor variations to an authorisation.

***Issue J: Halting conduct***

- 19 The Commission considers that the mandatory requirement that conduct should be halted while it is considering an authorisation application should be retained. There should be a presumption that the contravening conduct is harmful, and therefore should be deterred. It is only once the net public benefits are demonstrated that the conduct should be sanctioned. However, the Commission should have the discretion to allow the conduct to continue in certain circumstances. The current threshold of ‘exceptional

hardship' to any of the parties could be lowered to accommodate other circumstances where the costs of halting may impose unreasonable costs.

- 20 The section should also be amended to make explicit the means by which the Commission may enforce the requirement for the conduct to halt. The Commission suggests that, if the parties do not cease the conduct and the Commission has not permitted the conduct to continue, the application should be deemed to lapse or deemed to be declined.

***Issue K1: The right of the applicant and specific third parties to call for a conference***

- 21 The Commission should have sole discretion to call a conference for restrictive trade practice proceedings. This discretion should be broadened so that the Commission may call conferences for fact finding purposes in relation to particular issues and not just after it has released a draft determination.
- 22 Section 61(3) of the Act provides that the Commission must take into account any submissions made to it by the applicant or any other person. In addition, as a matter of course, applicants or interested parties may request the Commission to hold a conference. Therefore, a statutory provision for applicants and interested parties to be able to request the Commission to hold a conference is not required.

***Issue K2: The time frames for restrictive trade practice authorisation conferences***

- 23 The Commission supports the option outlined in the discussion document and recommends that the statutory time limits in section 62 for holding conferences should be removed. The statutory time limits only relate to the middle of the Commission's process rather than the total time taken. As such, the time frames are arbitrary and, in addition, they can be impractical to implement.

***Issue L: Right to appeal Commission determinations – who can appeal***

- 24 In the case of Commission determinations relating to mergers, appeal rights for third parties who participate in Commission conferences should be repealed. Only the acquirer and the vendor of the assets should have rights of appeal. Third parties should only be able to initiate judicial review proceedings. In addition, third parties should retain the right to join an appeal if one of the parties to a determination appeals.
- 25 In the case of Commission determinations relating to restrictive trade practices, the case for change is less clear cut. The Commission has not formed a view on the matter. However, consideration could be given to amending third party appeal rights so they are based on making submissions to the Commission, rather than on participation in a Commission conference.

***Issue M: Specialist Competition Tribunal***

- 26 Unless a case can be made that the benefits of a specialist tribunal outweigh the costs, the current lay member system should remain unaltered. The Commission agrees with the preliminary view in the discussion document that the benefits are unlikely to outweigh the costs unless there were a decision to move to full appeals in relation to regulatory control and to establish a tribunal to hear those appeals. In principle, in the

event of such a tribunal being established, that tribunal may also hear Commerce Act matters in line with overseas tribunals.

***Issue N: Wider use of lay members***

- 27 The Commission agrees that any appeals on their merits should have lay members assisting the court as is the case today. A provision of wider discretion to courts to appoint lay members outside of merits review appeals is not necessary or desirable. Judges are experienced in dealing with judicial review, natural justice and procedural issues. Such legal issues are appropriately heard by the courts. The Commission therefore disagrees with the preliminary view in the discussion document that the current approach should be changed. The Commission is not aware of any other circumstances where there should be a wider discretion for judges to appoint lay members.

***Issue O: The assessment of efficiency gains and losses***

- 28 The Commission considers that its analytical framework for assessing public benefits and detriments adequately takes into account what would be likely to happen in the counterfactual, and that its approach is consistent with that of overseas competition authorities.

***Issue P: The treatment of international competitiveness claims***

- 29 The Commission considers that the public benefit test is sufficiently broad to take into consideration, and to give appropriate weight to, international competitiveness claims. Introducing international competitiveness provisions into the Act would result in inefficient market outcomes that would not be for the long-term benefit of consumers in New Zealand.

***Issue Q: Quantification of costs and benefits***

- 30 In almost all cases, measuring costs and benefits necessarily involves a mix of quantitative and qualitative assessments. The Commission undertakes a quantification assessment as a matter of good practice. Quantification acts as a discipline on the Commission by opening up to scrutiny the assumptions it has used in its analysis. However, this does not prevent the Commission having appropriate regard to those factors that may not be able to be quantified with any precision. Non-quantifiable factors are taken into account and given the appropriate weight.

***Issue R: Time frames over which costs and benefits are assessed***

- 31 The Commission considers that time frames over which costs and benefits are assessed vary depending upon the facts of each case. In particular, if specific factors warrant consideration of a longer time horizon, the Commission already has the capability to do this and has done so in practice.

***Issue S: Market definition***

- 32 The Commission considers that the approach it adopts for defining markets is consistent with that used by overseas competition agencies and is sufficiently flexible to define markets that best assist the competition analysis in each case.

***New issue: Withdrawal of applications before Commission***

- 33 The Commission requests that consideration be given to a further issue that has arisen with the operation of the clearance regime. The Commission considers that applicants should have to give five working days notice of their intention to withdraw a clearance application. This notice period would give the Commission sufficient time to inform itself of the reasons for the application being withdrawn and whether it will be necessary for it to initiate enforcement proceedings.

## Introduction

- 34 This submission is the Commerce Commission's ('the Commission') response to MED's discussion document entitled the *Review of the Clearance and Authorisation Provisions under the Commerce Act 1986*, released on 29 May 2007. The Commission welcomes the opportunity to present its views on the issues raised in the discussion document.
- 35 In many respects the clearance and authorisation regime in the Commerce Act 1986 ('the Act') is unique compared with overseas jurisdictions. The Act is based on internationally recognised competition principles and processes, but with some modifications to better fit the particular features of New Zealand's small economy.
- 36 In relation to mergers, unlike many OECD countries, New Zealand has a voluntary statutory clearance regime. The Commission may grant clearance to a proposed merger if it is satisfied that the merger is unlikely to substantially lessen competition in a market. A clearance confers immunity for the proposed merger from the prohibitions in the Act.
- 37 The release of the Commission's merger guidelines<sup>2</sup> and comprehensive written reasons for each of its determinations provides guidance to the business and legal community on how the Act is applied. The availability of such information is critical to the success of a voluntary regime, as it informs merging parties and, importantly, their professional advisors, on whether to not to apply to the Commission for clearance.
- 38 As parties become more familiar with the Act and the Commission's clearance processes, the Commission is increasingly dealing with merger applications at the margins of the competition threshold. In contrast to many overseas regimes, the Commission only considers 20 or so mergers a year, most of which raise complex or novel competition issues. This effective targeting of matters before the Commission means that its resources are used to maximum effect where the public interest is greatest.
- 39 In relation to authorisations, the Act requires that businesses prospectively apply to the Commission if they wish to enter into arrangements or make acquisitions that may lessen competition but that would otherwise have net public benefits. This is in contrast with some other jurisdictions where efficiency issues may only be raised as a defence to an enforcement proceeding. The Act requires the Commission to apply a total welfare standard to its assessment of public benefits and detriments. To the extent feasible, the Commission quantifies these benefits and detriments in its assessment.
- 40 Overall, the Commission considers that the clearance and authorisation regime is working well and major change is not required. Consequently, this submission focuses on means to enhance the effectiveness of the regime rather than to fundamentally reform it.
- 41 In this regard, the Commission supports the criteria used by MED in the discussion document to assess different proposals, such as high quality outcomes, clear and

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<sup>2</sup> Commerce Commission, *Mergers and Acquisitions Guidelines*, January 2004.

consistent legislation, cost effectiveness and timeliness, and also the impact of the proposals on Trans-Tasman business.

- 42 With this overall context in mind, this submission sets out the Commission's response to each of the questions posed in the discussion document.

### Public Submission

- 43 The Commission consents to this submission being made available to the public.

## Issues A – E: Merger Issues

### Issue A: Statutory Time Frame for Clearance Determinations

Question 1: *What should be the default number of working days for Commission consideration of merger clearance applications?*

#### *Current practice*

- 44 Section 66 (clearances for business acquisitions) of the Act provides that the Commission must make a determination on a clearance within 10 working days, or such longer period as the Commission and the applicant agree. In practice the 10 working day time frame is unrealistically short and extensions are agreed as a matter of course.
- 45 In 2006-07 the Commission used 0.8 full time equivalents (FTEs) on each case in order to make a determination within, on average, 45 working days. The Commission's performance measure set out in its Statement of Intent is to reach a decision, on average, within 40 working days. The table below shows merger clearance times, with updated data for the full 2006/7 financial year.

*Table One: Commerce Commission merger clearance times*

<b>Time taken</b>	<b>2004/5</b>	<b>2005/6</b>	<b>2006/7</b>	<b>Total</b>	<b>Cumulative Total</b>
1 to 10 days	0	0	1	1	1
11 to 20 days	2	3	1	6	7
21-30 days	7	7	5	19	26
31-40 days	3	3	5	11	37
41-50 days	1	1	1	3	40
51 days or more	5	6	5	16	56
<b>Total</b>	18	20	18	56	
Average number of days	37	37	45	40	
Percentage decided within 30 days	50%	50%	39%		46%
Percentage decided within 40 days	67%	65%	67%		66%

#### *Discussion of options*

- 46 The discussion document concludes that the statutory time frame should be increased to 30 working days, along with retention of the ability to extend the deadline, because:

- a challenging time frame is better than one that the Commission could meet most of the time;
- historic data shows that about half of decisions made in the past three years were made within 30 working days; and
- “30 days is not going to be any worse than 40 days and it could be better.”<sup>3</sup>

47 The Commission considers that the time frame of 10 working days is not achievable. Consequently, the Act does not provide businesses any guidance for planning purposes of the likely time the Commission requires to consider their application. The legislation should have a time frame that is both challenging and practical for the Commission and provides certainty for business.

48 However, the Commission considers that the analysis in the discussion document is static in its approach and, therefore, overly simplistic. The Commission considers that the statutory time frame should be increased to 40 working days because:

- overall, the complexity of clearance applications has increased over time, probably due to increased experience of the substantial lessening competition test, the increased concentration of markets, and technological changes, which have led to the emergence of new products and the blurring of market boundaries;
- it will improve certainty for applicants because 40 working days is close to the average time taken by the Commission to make clearance decisions;
- it remains challenging for the Commission to achieve as it is also the current performance measure set out in the Commission’s Statement of Intent;
- it will promote harmonisation with Australia, which has a 40 business day time frame for both its formal and informal notification procedures; and
- extra resources may be required to meet a statutory time frame that is shorter than current practice.

49 However, as each case is different, some may take less than 40 working days, while others will take longer. Therefore, the Commission considers that it should retain the ability to extend the deadline beyond the statutory time frame with the agreement of the applicant; otherwise there is a risk that it would have to decline applications because, due to resource constraints, it would not have time to be satisfied that there was not a substantial lessening of competition.

50 The Commission notes that any legislative changes to written reasons, conference proceedings and behavioural undertakings could also have an impact on time frames for clearance decisions.

### ***Commission preferred option***

51 The Commission considers that the statutory time frame should be increased from 10 working days to 40 working days, while retaining the ability to extend the deadline with the agreement of the applicant.

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<sup>3</sup> Ministry of Economic Development, *Review of the Clearance and Authorisation Provisions under the Commerce Act 1986: Discussion Document*, May 2007, paragraph 26, page 24.

## Issue B: Publication of Written Reasons

Question 2: *Is there a need to amend the Act in relation to the publication of written merger clearance decisions?*

### *Current practice*

- 52 The Commission is not required to give written reasons for its determinations under section 66 (clearance for mergers) of the Act. This contrasts with the requirements to give written reasons for determinations under sections 61 (authorisation for trade practices) and 67 (authorisation for mergers) of the Act.
- 53 In practice, the Commission prepares written reasons for all of its clearance determinations. The preparation of written reasons is useful for internal purposes to support the Commission's decision-making and knowledge management. Current practice is for a public version of these reasons to be posted on the Commission's website.
- 54 The Commission releases the written reasons for its determinations to the public for the following purposes:
- It provides parties to an application and other interested parties with transparency as to how their interests have been considered. The pro-active release of written reasons replaces the need to respond on a case-by-case basis to official information requests or, in the case of appeals or reviews, court orders for an affidavit of the Commission's reasons for its determinations.
  - It educates the business and legal communities as to how the Commission assesses the competitive effects of mergers, thereby informing their decisions as to whether or not to apply for clearance. While the Commission's *Mergers and Acquisitions Guidelines* outline the general analytical framework for assessing mergers, the case-by-case assessment continues to raise new issues and it clarifies how this framework is applied in practice.
- 55 However, the Commission makes a determination on a merger as soon as it is satisfied of the matters relevant to its decision, and this may be before the written reasons are finalised. Increasingly, there has been a delay between the date of the determination and the release of the public version of the written reasons on the Commission's website. This delay is not related to the complexity of the issues or whether or not the determination is a decline. Rather, it arises as a consequence of internal decisions relating to prioritising the use of Commission resources.
- 56 For example, staff involved in finalising the written reasons may be immediately reassigned following the making of a determination to another clearance, and the investigation phase of the second clearance application may take priority over completing the written reasons relating to the first clearance for public release. In other cases, the delay may arise while the staff work through confidentiality issues with the parties who provided information that is referenced in the written reasons prior to its public release.

### ***Relationship to appeal period***

- 57 The discussion document considers the implications of the delay between the determination and the release of the written reasons for appeal rights. Section 91 (appeals against Commission determinations) of the Act specifies that notices of appeal must be filed within 20 working days after the date of the Commission's determination, or within such further time as the Court may allow.
- 58 The discussion document outlines a concern that it can be difficult for a potential appellant to judge whether or not to lodge an appeal without having the Commission's written reasons. While the Commission may have advised the applicant of the nature of its competition concerns in the course of its determination, the implication is that this advice is not considered by the parties to be sufficiently detailed to inform the basis of an appeal. Consequently, the discussion document outlines that the delay in release of the written reasons may raise two issues:
- The appellant may be reliant upon the court's discretion for late appeals outside the 20 working day period, once the Commission has released its written reasons. This potentially diminishes the certainty of parties' appeal rights.
  - The time frame for reaching a final determination on the merger may be further delayed, as the court hearing of any appeal is subject to the Commission's release of those reasons.
- 59 The Commission considers that these concerns are unlikely to be significant in practice. In relation to the first issue, there has not been an instance of an eligible party being denied an appeal where their notice of appeal was filed within 20 working days of the release of the Commission's written reasons. The Commission does not object to appeals within this time frame.
- 60 In relation to the second issue, if parties are seeking a timely final determination by the court, and the release of the Commission's written reasons are delayed, the parties may still file notice of an appeal within 20 working days of the date of determination. In such cases, the court may order the Commission to produce an affidavit outlining its reasons for its determination in a timely manner in order to inform the appeal. This practice ensures that the appeal proceedings are not unduly delayed. The court has made such an order in the Woolworths Limited's appeal against Decision 607.<sup>4</sup>
- 61 However, while the concerns may not be significant in practice, the Commission agrees that the legislation could be amended to give the parties greater certainty.

### ***Discussion of options***

- 62 The discussion document outlines two options for change:
- requiring the Commission to give written reasons within a set time frame, or
  - amending the appeal provisions so that the notice of appeal must be made within 20 working days of the Commission publishing its written reasons.
- 63 Both of these options would make it mandatory for the Commission to release written reasons for all of its determinations. The Commission does not support this

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<sup>4</sup> Commerce Commission, *Decision No 607, Woolworths Limited / The Warehouse Group Limited*, 8 July 2007

requirement. While the Commission prepares written reasons for all of its decisions, the additional element of finalising those reasons for public release is relatively costly and time consuming. The Commission would prefer to retain flexibility as to whether it releases its reasons for all clearances in case it revises its practices in the future. For example, as experience with the merger regime increases, it is possible that full written reasons would only be issued where the proceedings resulted in a decline, raised novel issues or related to markets that the Commission had not previously considered.

- 64 Regardless of whether the release of written reasons becomes a mandatory requirement, the Commission does not favour the two options for appeal periods outlined in the discussion document.
- 65 Under the first option, if the time frame by which the Commission would be required to publish its reasons is unduly short, it may encourage the Commission to delay making decisions until the public version of the written reasons is nearly completed or, alternatively, reduce the comprehensiveness of the written reasons that are released. These outcomes are unlikely to be efficient.
- 66 The second option would protect the parties' appeal rights, but it would remove some of the disciplines that would ensure a timely appeal period and final determination of the merger. That is, currently the parties are able to seek orders from the court requiring the Commission to produce an affidavit of the reasons for its decision to inform the appeal proceedings, but under this option, this ability would be removed. The appeal period would only begin once the Commission released its written reasons.

***Commission preferred option***

- 67 Consequently, the Commission proposes an alternative option to address the concerns identified, while retaining flexibility for the Commission to manage its resources efficiently.
- 68 The appeal period should run from the date that the Commission makes its determination to:
- if the Commission advises it will not release written reasons for that determination, 20 working days from that date; otherwise
  - 20 working days from the date that the written reasons for that determination are released.<sup>5</sup>
- 69 In order to be operational, it would be necessary for the Commission to specify at the time that it announces its decision whether or not it intends to release written reasons for its determination.

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<sup>5</sup> That is, the appeal period would be the number of working days between the date of the Commission's determination and the date it releases its written reasons plus an additional 20 working days.

## Issue C1: Enforceability of Undertakings

Question 3: *Should the Act provide for the enforcement of undertakings to dispose of assets or shares?*

### *Current practice*

- 70 The Commission may accept undertakings to divest assets or shares in the course of considering a merger clearance or authorisation application. Under section 69 (undertakings) of the Act, the undertakings given are deemed to form part of the clearance or authorisation granted by the Commission. Once granted, the effect of the clearance or authorisation is to provide that nothing in sections 27 (arrangements substantially lessening competition) or 47 (anticompetitive mergers) of the Act applies to mergers carried out in accordance with the clearance or authorisation.<sup>6</sup>
- 71 Consequently, non-compliance with an undertaking means that the acquisition ceases to be immune from the prohibitions in the Act. While not explicitly stated in the Act, the Commission considers that the clearance or authorisation is invalid from the outset (i.e. void *ab initio*) regardless of whether the non-compliance occurred before, during or after the main acquisition.
- 72 However, as outlined in the discussion document, undertakings accepted under section 69 of the Act are not enforceable in themselves. Section 85 (court orders of divestiture) of the Act provides that the court must be satisfied of a contravention of section 47 before it may order divestiture in accordance with an undertaking given. Consequently, the Commission would be required to take enforcement proceedings under section 47 of the Act if the merger raised competition concerns. Such proceedings may be costly and are made more difficult by the passage of time since the Commission made its clearance determination.
- 73 The Commission's inability to enforce divestment undertakings quickly and efficiently could have two consequences:
- The Commission could place less reliance on any undertakings given as a remedy to address its competition concerns. This may result in more clearance applications being declined, thereby denying parties a pragmatic outcome.
  - The merging parties could submit divestment undertakings in order to obtain clearance, but have no intention of complying in full with the undertakings given. There is a risk that, even if the Commission is successful in taking an enforcement proceeding, the competitive harm may be irreversible given the passage of time.

### *Discussion of options*

- 74 The discussion document outlines options to allow the Commission to apply to the High Court to enforce undertakings to divest assets or shares separate from the main acquisition. These options would be based on sections 69J and 69K (undertakings) of the Securities Act 1978 or section 87B (enforcement of undertakings) of the Australian Trade Practices Act 1974. Under both options, the Court would be empowered to order the merged firm to:

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<sup>6</sup> Section 69 (effect of clearance or authorisation) of Act refers.

- comply with the undertaking;
- pay a pecuniary penalty to the Crown;
- compensate any other person who has suffered loss or damage; and/or
- comply with any other condition that the Court considered appropriate.

*Commission preferred option*

- 75 The Commission supports amending the Act to provide for enforceable undertakings for mergers before the High Court, separate from the main acquisition. In seeking such orders, the Commission should not have to establish that the undertaking is necessary to address the competition concerns resulting from the main acquisition. Rather the proceedings should simply focus on whether or not the undertaking has been complied with.
- 76 Section 87B of the Australian Trade Practices Act 1974 provides a useful model of a possible enforcement mechanism. Under this section the ACCC may accept a written undertaking in connection to a matter in relation to which it has a power or function under the Act, except Part X (international liner cargo shipping). If the undertaking is breached the ACCC may seek orders from the court directing compliance with the undertaking, the giving up of any financial benefit gained from the breach, compensation for any other loss or damage as a result of the breach, or any other appropriate orders. The ACCC keeps a public register of undertakings on its website.
- 77 An enforcement mechanism based on section 87B of the Trade Practices Act would address the concerns identified. In addition, it should be familiar to many competition lawyers and the trans-Tasman business community. The range of court enforcement orders that may be imposed under that section reflect the broad use of undertakings in relation to trade practice, fair trading and merger matters. However, the Commission queries whether the provision to seek compensation for any other person who has suffered loss or damage as a consequence of non-compliance is appropriate in the New Zealand context for enforcement of merger undertakings. In the case of mergers, compensation is ordinarily a matter dealt with in private proceedings or under section 89 (other court orders) of the Act.
- 78 In addition, there are a few key features of the clearance regime that should be retained:
- The undertakings should continue to be provided voluntarily by the parties and the Commission should not be able to impose conditions for mergers.
  - Failure to comply with an undertaking should still render the clearance or authorisation invalid from the outset. This mechanism ensures that the risk of third party proceedings places incentives on the merger parties to comply with any undertakings given in the first instance. Such a risk is independent of whether the Commission initiates proceedings.
- 79 These amendments would reduce the costs of enforcing undertakings before the High Court and give the Commission more certainty in accepting any undertakings offered.

## Issue C2: Variation of Undertakings

Question 4: *Should the original applicant be able to ask the Commission to make minor variations to undertakings to divest assets or shares?*

### *Current practice*

- 80 There is no provision in the Commerce Act enabling the variation of undertakings given under section 69A (merger undertakings) of the Act. However, the Commission's experience is that such a provision may be beneficial for some merger parties. This is particularly the case if the merger parties have entered into financing arrangements for a merger that are conditional on holding a clearance or authorisation.
- 81 Undertakings are most often varied to extend the time for divesting the assets or shares. Occasionally a party may also vary the nature of any asset to be divested or substitute an alternative purchaser where one has been specified in the divestment undertaking.
- 82 Given the absence of a provision enabling variations, a merger party who currently wishes to vary the terms of a divestment undertaking has three choices:
- comply with the undertaking in full (which may lead to suboptimal outcomes);
  - vary the undertaking but lose the protection of the clearance or authorisation for the merger; or
  - if the merger has not taken place, reapply to the Commission for clearance or authorisation subject to the proposed revised terms.
- 83 The Commission's experience is that the second option is the most common. If the variation is significant, the Commission may open an investigation under section 47 of the Act in relation to the acquisition with the varied undertakings.

### *Discussion of options*

- 84 The discussion document outlines that the Act should be amended to provide for minor variations to undertakings on application by the parties to the determination. The limitation to 'minor' variations is intended to reduce the opportunities for parties to relitigate matters that were critical to the Commission's initial decision to grant clearance or authorisation.
- 85 However, the Commission considers that it is not necessary to limit the power to vary in this way. There may be legitimate reasons that parties would seek to reconfigure the divestment undertakings given. If the proposed variation is significant, the Commission would carry out a full competition analysis of the implications of the variation, in the same manner in which the initial clearance or authorisation was considered. Such variations should only be permitted with the consent of the Commission.

### *Commission preferred option*

- 86 The Commission recommends that the Act should be amended to provide for variations of undertakings on application of the parties and with the consent of the Commission. Given the potential significant costs that may be incurred by the Commission, the parties

should be required to pay an application fee to the Commission to have the variation considered.

## **Issue D: Behavioural Undertakings**

Question 5: <i>Should the Commission be able to accept behavioural undertakings?</i>
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### ***Current practice***

- 87 Section 69A(1) of the Act provides that the Commission may accept a written undertaking from the person seeking clearance or authorisation for the divestiture of assets or shares. Section 69A(2) precludes the Commission from accepting any other type of undertaking, which includes behavioural undertakings.
- 88 These provisions contrast to section 61(2) of the Act, where trade practice authorisations may be granted subject to such conditions not inconsistent with the Act as the Commission thinks fit.

### ***Discussion of options***

- 89 The discussion document considers two options for change:
- allowing the Commission full discretion to accept any type of undertakings as it sees fit; or
  - allowing the Commission to accept behavioural undertakings in support of undertakings to divest shares or assets.
- 90 The Commission's experience and that of its overseas counterparts is that structural rather than behavioural undertakings are strongly preferred as a merger remedy. While there have been cases where the Commission has thought that a behavioural remedy may have been useful, these cases have been the exception rather than the rule.
- 91 The reasons that structural remedies are preferred for mergers are canvassed in the discussion document. In particular, behavioural undertakings are effectively a form of company-specific regulation. Markets are dynamic and behavioural undertakings that might be well targeted at the time of the merger may later turn out to be ineffective or counterproductive. In addition, the ongoing monitoring and enforcement costs to the Commission for these undertakings could be considerable. The damage to the economy could be irreparable if the merged entity does not comply with its behavioural undertaking.
- 92 Even if the Commission has full discretion whether or not to accept behavioural undertakings, if applicants offer such undertakings the Commission would be bound to analyse their likely effect in the market, which could be costly and time-consuming. If the Commission declined to accept these undertakings, they would be a further matter for review or appeal to the court, which would add further complexity to the proceedings.
- 93 Consequently, the Commission considers that the disadvantages of giving it a broad discretion to consider behavioural undertakings are likely to far outweigh the few cases where such undertakings would be beneficial.

***Commission preferred option***

- 94 The Commission considers that, on balance, the status quo should remain and it should not be empowered to accept behavioural undertakings for merger proposals.

**Issue E: Informal Pre-Merger Processes**

Question 6: *Should the Commission consider introducing an informal pre-merger letter of comfort system?*

***Current practice***

- 95 The Act confers upon the Commission a statutory role in adjudicating on applications for proposed mergers under the voluntary clearance regime. This role is separate from the Commission's enforcement function in respect of non-notified mergers.
- 96 The voluntary clearance regime is well-established in New Zealand and it is a clear and transparent regime. Key features include:
- publicly notifying applications for clearance of proposed mergers;
  - opportunities for merger parties and interested parties to make representations to the Commission to inform its consideration of applications;
  - the clearance confers full immunity to proposed mergers; and
  - merger parties and interested parties have rights of appeal or review.
- 97 Parties self-select whether to apply to the Commission for formal clearance. This decision may be informed by professional legal advice, the Commission's *Mergers and Acquisitions Guidelines*, and written reasons for previous decisions. In contrast to many overseas regimes, the Commission only considers 20 or so merger applications a year, most of which raise complex or novel issues. The Commission's experience is that the voluntary regime is effective in encouraging clearance applications where there are potentially significant competition issues. This ensures that the Commission's resources are well targeted.
- 98 In addition, the Commission encourages parties to informally notify it of any proposed mergers outside of the statutory clearance regime. Such notifications are more in the nature of courtesy calls to keep the Commission informed of market developments as part of its monitoring and surveillance programme, or to assist the Commission in planning for proposed clearance applications. Commission staff may indicate to parties if the proposed merger might raise competition issues, but it remains for the parties to assess any likely Commerce Act risk and whether or not to apply for clearance. The Commission does not give letters of comfort to prospective merger parties.

***Concerns with an informal process***

- 99 The discussion document considers the option of the Commission introducing an informal pre-merger process to supplement the statutory voluntary clearance regime. The reasons for considering this option are generally outlined as being:

- from the business perspective, it may provide a more cost effective and timely means than the current clearance regime to get comfort from the Commission that it will not intervene against the merger; and
  - from the Commission perspective, it may support the Commission's monitoring and surveillance activities by encouraging parties to come forward with information about prospective mergers where they would not otherwise have applied for clearance.
- 100 However, the Commission considers that these reasons are insufficient to justify a change in its practices, given the risks associated with the introduction of an informal letter of comfort process.
- 101 Businesses currently seek professional advice on the likely Commerce Act risk of a proposed merger to manage any uncertainty. Professional advisers carry out an important screening role. If the Commission introduced an informal pre-merger process it is likely that businesses would use this process as an advisory service instead of, or in addition to, seeking professional advice. This outcome is unlikely to be an effective use of the Commission's resources.
- 102 The Commission's assessment of the ACCC's informal merger review process is that some parties are using that process to get comfort from the ACCC when the merger proposals may not raise substantive competition issues. If the Commission has to consider more mergers under the informal process, this could result in it spending less time or delaying decisions on significant cases in relation to its enforcement function or the formal clearance process.
- 103 While an informal merger regime may result in the Commission receiving more information about proposed mergers in the market, the Commission considers that its current monitoring and surveillance programme is working effectively to identify non-notified mergers.
- 104 Furthermore, there would be process and outcome risks from introducing an informal merger process that would operate alongside a statutory clearance regime. There would be a lack of transparency as to how the interface between the processes would operate, and this would be compounded if full confidentiality was available for merger proposals under the informal procedure.<sup>7</sup>
- 105 For example, if the Commission declined to give comfort and the parties subsequently applied for clearance, there may be concerns that the Commission has pre-determined the matter. Alternatively, if the Commission provides comfort to merger parties in relation to a merger proposal, but subsequently seeks to take enforcement action based on new information, the Commission may be in a disadvantageous position before the court. The Commission could suffer reputational damage if it changes its view on any merger proposal, as the reasons for this change in view may be difficult to communicate to the public.

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<sup>7</sup> The ACCC advises that approximately half of the merger reviews carried out under its informal process are confidential (refer ACCC, *How to obtain approval for difficult mergers & acquisitions – and how you won't*, speech to the Lexus Nexis Trade Practices Law Conference, October 2006).

- 106 The United Kingdom's Office of Fair Trading (OFT), which operates a voluntary clearance regime, recently scaled back significantly its pre-merger processes of giving oral informal advice and/or written confidential guidance. This was because these processes detracted from the OFT's ability to conduct high quality reviews of merger cases in the public domain.
- 107 The OFT considered that informal advice often provided minimal added value beyond the parties' advisors own assessment. Experience suggested that it was dangerous to suppose that a limited review by officials, without proper review of the parties' or third parties' evidence, made the OFT any better placed than the parties' advisers to assess the transaction risk up front. The OFT's substantive merger guidance and the publication of its decisions provided business and professional advisers with transparency and guidance on how to apply competition law.<sup>8</sup>

### *Commission preferred option*

- 108 The Commission considers that it should not introduce a pre-merger informal process. The benefits of a pre-merger informal process appear to be minimal, both in terms of providing a more cost-effective and timely process for business, and improving the Commission's monitoring and surveillance capability. Moreover, any benefits are unlikely to outweigh the costs and risks of introducing such a process.

## **Issues F – K: Restrictive Trade Practices**

### **Issue F: A Possible Clearance Process for Trade Practices**

Question 7: <i>Should a clearance system be introduced for trade practices?</i>
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#### *Current practice*

- 109 The Act does not provide a clearance process for trade practices. Parties seeking guidance on the application of the Act will consult with professional advisers. If parties want to obtain protection from challenge under Part 2 of the Act (other than sections 36 and 36A) they must apply to the Commission for an authorisation and argue their case on public benefit grounds.

#### *Discussion of option*

- 110 The discussion document reaches a preliminary view that a clearance system for restrictive trade practices should be introduced, except for sections 36 and 36A (taking advantage of market power) of the Act. The discussion document suggests that the problem is twofold:
- firms may not be engaging in activities that are competitively benign or procompetitive because of uncertainty as to the application of the Act and concerns that they may attract a Commission investigation or litigation by the Commission or a private party; or

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<sup>8</sup> Interim advice for informal advice and pre-notification contacts, OFT, April 2006

- the *per se* prohibitions under the Act may be catching some conduct which is unlikely to substantially lessen competition.
- 111 Authorisation is currently available under the Act to address these two problems. Consequently, the Commission considers that an assessment of the need for a clearance regime for trade practices is directly related to issue H: the “lessening competition” jurisdiction test and the discussion relating to the authorisation process.
- 112 In terms of the perceived first problem relating to business uncertainty, the Commission considers that the onus should be on businesses to ensure that they are complying with the law on an ongoing basis. Businesses should take the Commerce Act risk into account in determining their conduct in the market, including the costs and benefits of obtaining professional advice to mitigate this risk. Transferring the burden of assessing this risk to the Commission would not be an efficient use of public resources. Such a regime may be justified for mergers, given the significant costs of unwinding a merger in the event that the merger is found to contravene the Act. However, these same issues do not apply for the vast majority of trade practices.
- 113 Moreover, business arrangements are not static but change over time. Given this, it would be difficult for the Commission to be satisfied that over time a particular arrangement would not be in breach of the Act. The authorisation process for restrictive trade practices is for exceptional cases where there are public benefits that outweigh the detriments arising from the loss of competition.
- 114 The Commission is not aware of any other jurisdiction which has a clearance system for restrictive trade practices. In a number of jurisdictions, such as the US, Canada, UK and the European Union, businesses can request advisory opinions on whether a trade practice is in breach of competition law but that this is only for novel questions of law for which there is no precedent. In New Zealand, businesses may seek such guidance from professional advisers or from the Commission under the authorisation process.
- 115 Australia had a clearance regime for restrictive trade practices under the Trade Practices Act 1974, but this provision was subsequently repealed in 1977 following the recommendations of the Swanson Committee. While the provision was in force, the ACCC (or Trade Practices Commission as it was then known) received a large number of applications for clearance, resulting in significant delays in decisions, and the consequential workload undermined the ACCC’s ability to perform its other functions. The Swanson Committee notes in its report:
- The Commission still has a backlog of applications relating to sections 45 and 47, dating back to the early 1975 period, which it has not yet made decisions upon in a final sense, although interim authorisations are running in many cases. The Committee was told that it will be at least another 12 months before this backlog of applications is cleared up, as the Commission is working through them on an industry-by-industry basis and in many cases detailed examination of industries is needed in order to make decisions. Indeed, we understand that much of the Commission’s work in the last twelve months has been in public hearings relating to some of these authorisation applications – hearings designed to establish industry-type information which can be the basis of resolving applications in a given number of cases.<sup>9</sup>

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<sup>9</sup> Trade Practices Act Review Committee, *Report to the Minister for Business and Consumer Affairs*, August 1976, paragraph 11.7, page 97.

116 In outlining its reasons for concluding that the clearance regime should be repealed, the Committee stated:

..the very existence of clearance provisions has meant that in a significant number of cases corporations previously engaging in anti-competitive conduct have sought clearance of that conduct rather than relying upon their own decisions as to whether the conduct was anti-competitive, and if it were so, was of such degree of anti-competitiveness that the Act was infringed. This has encouraged the practice of submitting for clearance by the Commission, patterns of business conduct which on any view of the law are likely to be only very marginally anti-competitive. In some measure the existence of the clearance opportunity in relation to section 45 and section 47-type conduct has deprived the community of the sort of self-reliance which competition-orientated legislation might be expected to encourage in a private enterprise system..<sup>10</sup>

117 Based on the Australian experience, the Commission considers that the discussion document underestimates the potential for there to be a substantial number of applications if a clearance system for restrictive trade practices is introduced. A substantial increase in budget would be required.

118 Unlike the clearance regime for mergers, the Commission does not have published guidelines for restrictive trade practices and Commission investigation reports are not generally made available to the public. This level of uncertainty suggests that there could be a significant amount of applications from risk-averse businesses. There is also a diverse range of behaviour that can potentially breach the Act. This again suggests that the potential volume of clearance applications will be significant. Businesses may also consider that a Commission clearance is important not simply to avoid potential litigation, but also so that they are perceived by the public and business community to be doing the right thing.

119 It is important that the Commission is sufficiently resourced to deal with the clearance regime because of the potential need to divert resources from enforcement work. It is crucial that the Commission continues to be an effective enforcement agency.

120 As well as dealing with applications, the Commission would need to devote resources to the following activities:

- Developing guidelines on the types of behaviour which are generally thought to raise restrictive trade practices. This would be a necessary precursor to the introduction of any regime.
- Monitoring of compliance with clearance terms and conditions after it has been granted, as businesses may claim the benefit of clearance but deviate from the terms on which it was granted. This could raise issues similar to those discussed above in Issue D: behavioural undertakings.

### *Commission view*

121 The Commission considers that a clearance system for trade practices should not be introduced. The onus should be on business to comply with the Act. There would be little benefit in devoting resources to clearance applications which clearly did not substantially lessen competition.

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<sup>10</sup> Ibid, paragraph 11.10, page 98.

Question 8: *Assuming a clearance system should be introduced, should it apply to price fixing and resale price maintenance?*

### ***Discussion of option***

- 122 In relation to the second perceived problem of technical contraventions of the *per se* provisions, the discussion document proposes that, if a clearance system is introduced, it could be extended to operate as an exemption regime for conduct that is caught by the *per se* offences. Exemptions would be granted if the conduct is unlikely to substantially lessen competition. However, the Commission does not support the use of the clearance mechanism for this purpose.
- 123 The discussion document makes comparisons with US jurisprudence where, in limited situations, the US courts have considered it necessary to ‘review the facts and undertake a market analysis’. Further analysis would be required as to whether these same ‘limited situations’ are caught within the *per se* prohibitions in the Commerce Act. Much of the US jurisprudence for when a ‘rule of reason’ approach is justified is reflected in New Zealand through the exemptions to the *per se* prohibitions, such as sections 31 and 33 relating to joint venture pricing and joint buying and promotion arrangements. The US courts only apply the ‘rule of reason’ approach in limited situations because it is recognised that, in virtually all instances, price fixing is plainly harmful to competition.
- 124 The discussion document does not recognise that offences are *per se* both in New Zealand and the US for the simple reason that in most instances there are no efficiency benefits arising that outweigh the obvious harm to the competitive process that results from the behaviour. Even though there may be some instances in which there is no harm to competition, they are not sufficient in number to warrant imposing a ‘rule of reason’ analysis through an expanded clearance regime. Authorisation is available for these rare instances.
- 125 The approach suggested in the discussion document assumes ‘hard-core cartels’ could not be granted clearance, or at least that the Commission would not be approached to grant clearance to a cartel. However, there is potential for parties to apply for clearance for a bald agreement relating to price that may not substantially lessen competition in the market due to the low markets shares of the parties to the price fixing agreement. Such behaviour, while perhaps not meeting the competition test in section 27, is not competitively benign, particularly if it becomes common practice. In this way the proposed amendment would go beyond the exceptions to the *per se* rule envisaged by the US Courts.

### ***Commission view***

- 126 If a clearance regime is introduced, the Commission considers that it should not be expanded to operate as an exemption regime in relation to conduct covered by the *per se* prohibitions. Exemptions from the *per se* prohibitions should be assessed through the authorisation procedure in the Act.

Question 9: *Assuming a clearance system is introduced, what features should it have in relation to such matters as time frames, undertakings, ability to vary, or revoke or replace a clearance regime?*

***Discussion of options***

- 127 If a clearance system is introduced, the Commission considers many of the current provisions relating to authorisation of restrictive trade practices should apply, with any necessary modifications.
- 128 For example, the statutory time frame for the Commission to consider applications for clearance for restrictive trade practices would need to reflect the complexity of the issues. In granting a clearance, the Commission would need the option of imposing conditions, including setting sunset clauses.
- 129 In addition, unlike merger clearances, the Commission would need the ability to vary, revoke or replace any trade practice clearance. If the clearance is granted at a time when the market participant has a low market share, but this market share subsequently significantly increases, then this may change the Commission's original analysis. It is important that the power to vary, revoke or replace a trade practice clearance is set out clearly so that the Commission is able respond to changes in the competitive nature of the market.
- 130 Consideration needs to be given as to which parties can appeal a clearance. Restrictive trade practices can affect third parties who are competitors, who could also be the complainants in the Commission's investigations. For example, competitors might complain about an exclusive dealing arrangement that potentially forecloses important retail space to them. Similar issues would arise as those discussed in Issue L in relation to appeals.

***Commission's view***

- 131 If a clearance regime for restrictive trade practices is introduced, the Commission considers that it should be based on elements of the authorisation regime for trade practices, with any necessary modifications.

**Issue G: Collective Bargaining Notification Regime**

Question 10: *Are SMEs inhibited from engaging in collective bargaining schemes? If so, please provide real examples.*

***Discussion of concern***

- 132 The discussion document notes that monopsony/oligopsony power is most likely to exist in relation to the agricultural or health sectors. The Commission has dealt with several cases in these sectors.
- The Commission considered equality of bargaining in the authorisation applications by the New Zealand Kiwifruit Exporter Association and the

New Zealand Grape Growers Council.<sup>11</sup> It noted that arguments relating to equality of bargaining power may have little substance.

- The Commission has also considered monopsony/oligopsony buying by supermarkets in wholesale food markets (Progressive Enterprises and Woolworths, Foodstuffs and The Warehouse, Woolworths and The Warehouse<sup>12</sup>) and noted that there appeared to be a degree of mutual reliance between supermarkets and their suppliers.
- The Commission examined monopsony buying by the Crown in The Pharmacy Guild of New Zealand.<sup>13</sup> Although the application for authorisation was subsequently withdrawn, in its draft determination the Commission did not accept the Guild's argument that an asymmetry of bargaining power lead to inefficient outcomes.

### *Commission view*

133 The Commission has no evidence to suggest that SMEs are inhibited from engaging in pro-competitive collective bargaining schemes or collective bargaining schemes that would result in net public benefits.

Question 11: *Should a collective bargaining notification system be introduced? Would your answer be different if a trade practices clearance system were to be introduced?*

### *Discussion of options*

- 134 The discussion document suggests that SMEs may be inhibited from engaging in collective bargaining schemes because of the high costs of applying for an authorisation. Consideration is given to adopting a process akin to the collective bargaining notification system for small business that was recently introduced by the ACCC on 1 January 2007. There has only been one application since this system was introduced, suggesting that the demand for such a system is limited.
- 135 The Act already provides for collective negotiation in markets in which the parties do not compete (or the collective negotiation is otherwise pursuant to a joint venture) and the collective negotiation would not substantially lessen competition. In those circumstances where collective negotiation may contravene Part 2 of the Act, parties can apply for an authorisation. It seems unlikely that the collective bargaining notification system would be quicker than the authorisation process because the Commission would need to carry out the same analysis as for an authorisation. If there is a concern that the Commission's current authorisation process is too costly for SMEs, this should be addressed within the authorisation regime rather than establishing a new procedure.

<sup>11</sup> Commerce Commission, *Decision No. 221: NZ Kiwifruit Exporters / NZ Kiwifruit Coolstores Association (Inc)*, 15 September 1988 and *Decision No. 263: Grape Growers Council of NZ (Inc)*, 14 March 1991.

<sup>12</sup> Commerce Commission, *Decision No. 438: Progressive Enterprises Limited / Woolworths (New Zealand) Limited*, 13 July 2001 and *Decision Nos. 606 & 607: Foodstuffs (Auckland) Limited, Foodstuffs (Wellington) Co-operative Society Limited, and Foodstuffs South Island Limited; and (separately) Woolworths Limited / The Warehouse Group Limited*, 8 June 2007.

- 136 The discussion document suggests the health and agriculture sectors are examples where concerns have been raised that SMEs are inhibited from engaging in collective bargaining. However, the Commission's experience of cases in these sectors is that the parties involved were not under-resourced SMEs. Nor were these cases where the public benefits of collective bargaining clearly outweighed the detriments. The arguments for public benefits as a result of collective bargaining are finely balanced and require a case by case assessment, which is often fact-specific and complex.
- 137 The Commission considers that the burden of proof should remain on those parties with knowledge of markets affected and who would benefit from authorisation. A collective bargaining notification system would shift the onus on to the Commission to establish that the public benefits of the proposed arrangement outweigh the detriments. This would shift costs that are normally borne by the applicant in the authorisation process to the Commission. In addition, the Commission may be at an information disadvantage relative to the applicant if a collective bargaining application is not required to be as detailed as an authorisation application.

***Commission preferred option***

- 138 The Commission considers that there is no justification for a collective bargaining notification system.

Question 12: *Assuming that a collective bargaining notification system was introduced, what comments do you have on the design features in Table 5? In particular, what criterion or criteria should be used to define conduct or firms that would be eligible for the system?*

***Discussion***

- 139 In the ACCC system, an agreement can be eligible for notification if the expected total value of transactions for each party is less than AUS\$3 million over a 12 month period. This seems poorly targeted because it could potentially capture larger firms. If a collective bargaining notification system was introduced, only smaller firms who are dealing with genuine monopsony or oligopsony buyers should be eligible to lodge a notification. Further work would need to be done to establish the eligibility criteria. Using the MED definition of an SME (a business with less than 19 people) would catch over 95 percent of New Zealand enterprises.<sup>14</sup> It is difficult to estimate how many notifications might be made but if a large proportion of firms were eligible to make notifications this could require significant Commission resources.

***Commission view***

- 140 If a collective bargaining scheme is introduced, it should be clearly targeted, transparent and certain, enable all interested parties to be involved and give the Commission sufficient time to obtain information and carry out a proper analysis.

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<sup>14</sup> MED, *SMEs in New Zealand: Structure and Dynamics* – 2006, 31 May 2006

## Issue H: The ‘Lessening Competition’ Jurisdiction Test

Question 13: *Assuming there will continue to be no clearance system for trade practices, should the ‘lessening of competition’ jurisdiction test for restrictive trade practice authorisations be retained or removed?*

### *Current practice*

141 The Commission considers that it does not have jurisdiction to grant an authorisation unless, in the first instance, the relevant conduct, undertaking, arrangement or provision would lessen competition. The threshold has operated as a filter to prevent the Commission from incurring major costs in considering an application where there are limited Commerce Act risks.

### *Discussion of concern*

142 The discussion document raises the issue of whether the “lessening of competition” jurisdiction test for restrictive trade practice authorisations has deterred some beneficial arrangements because the parties were concerned that they may still be exposed to Commerce Act risk.

143 The Commission considers that it is highly unlikely that, in the event that the Commission declined jurisdiction for a restrictive trade practice authorisation, that a third party could bring a successful private action. The fact that the Commission had considered the arrangement, and declined jurisdiction on the basis that it was satisfied the arrangement would not lessen competition, should of itself provide some certainty to the parties and reduce any perceived risks. A court would likely give deference to the Commission’s analysis. Consequently, in these cases the likely Commerce Act risk to the applicants would be slight. The Commission is not aware of an arrangement that has not proceeded where it declined jurisdiction.

144 The Commission considers that the concern identified in the discussion document would likely only arise if there was a risk of a material change in market conditions after the arrangement had been entered into that was not foreseeable by the merger parties or the Commission ex-ante. In addition, this material change would have to be so significant that there was a potential that the arrangement could substantially lessen competition.

145 If such a circumstance arose, however, the onus should be on the parties to consider if the arrangement could be amended to address the Commerce Act risks while retaining the public benefits. As discussed previously, arrangements are not static but change over time. However, if Commerce Act risks subsequently arise due to material changes, but the public benefits of the arrangement outweigh these competition detriments, the parties could seek authorisation from the Commission for the existing practice in accordance with section 59A of the Act.

146 In any case, regardless of whether there is a jurisdictional threshold, if the Commission had granted authorisation but there is subsequently an unforeseeable material change resulting in significant competition detriments, the fact that an authorisation had been granted would not necessarily preclude the Commission from intervening ex post under section 65 of the Act. This issue and the associated incentives for investment are discussed in more detail in Issue I of this submission.

### ***Option of removing threshold***

- 147 The discussion document considers the option of removing the jurisdictional threshold of ‘lessening competition’. As discussed, the ‘lessening competition’ test is a useful filter to ensure that the Commission’s resources are appropriately targeted. Without a filter, scarce resources may be diverted to deal with applications for authorisations that may not have any detrimental impact on competition. This is not considered to be an efficient use of public resources.
- 148 If this option is to be explored, consideration should be given to the applicants being required to make a greater contribution to the Commission’s costs of considering the application. The Commission estimates that this cost would be in the order of \$300,000 to \$800,000.

### ***Commission’s view***

- 149 The Commission considers that the ‘lessening of competition’ test to establish jurisdiction should be retained.

Question 14: *If there is to be a clearance system for trade practices, what implications are there for the “lessening of competition” jurisdiction test for restrictive trade practice authorisations?*

### ***Commission’s view***

- 150 If a clearance regime for trade practices is introduced, the Commission considers that the jurisdiction test would largely become redundant and could be repealed. Similar to merger authorisation applications, if the trade practice would be unlikely to substantially lessen competition, or unlikely to result in a deemed lessening of competition, the Act should be amended to provide that the Commission would grant clearance for the trade practice.

### **Issue I: Commission’s Power to Revoke, Amend or Replace Authorisations**

Question 15: *Should the Commission’s power to vary, replace or revoke an authorisation if there has been a material change of circumstances (i.e. section 65(1)(b)) be: retained; repealed; or replaced by a provision that allows the original applicant to ask the Commission to vary, replace or revoke an authorisation?*

### ***Current practice***

- 151 Section 65 of the Act outlines three grounds for the Commission to intervene once an authorisation for a trade practice has been granted to address competition concerns:
- the authorisation was granted on information that was false or misleading in a material particular;
  - there has been a material change of circumstances since the authorisation was granted; or
  - a condition upon which the authorisation was granted has not been complied with.

152 However, even if the Commission is satisfied that one of these grounds exists, it still has discretion as to whether to intervene. As outlined in the Commission's recent decision in relation to variation of the New Zealand Rugby Football Union authorisation:

The Commission is not obliged to amend, revoke, or revoke and substitute an authorisation. It may elect to do nothing, even though there may be grounds available to amend or revoke. Further any assessment of the appropriate remedy will always be based on the facts, circumstances, and merits of the particular case before the Commission.<sup>15</sup>

153 The Act does not outline the matters that the Commission should have regard to in exercising its discretion to intervene. The Commission's practice is to firstly consider whether the material change impacts on its original assessment of the public benefits and detriments undertaken at the time that the authorisation was granted. Depending on the extent of the impact on its original net public benefits analysis, the Commission considers whether or not to amend, revoke or revoke and replace the authorisation. The Commission has outlined its approach in making this decision in its determinations. In particular:

... the Commission must carry out the appropriate counterfactual analysis. That is, it must compare the future benefits and detriments both 'with and without' the authorisation, as follows:

- if mere revocation is being considered, the Commission should compare benefits and detriments in the future with the extant authorisation continuing in force, against benefits and detriments in the future with no authorisation in force; but
- if, substitution of the extant authorisation by a fresh authorisation is being considered, the Commission should compare benefits and detriments in the future with the extant authorisation continuing in force, with benefits and detriments in the future with a substitute new authorisation in force.

The Commission must be satisfied that the proposed amendment or substitution is necessary to ensure that the public benefits claimed for the conduct are in fact realised. This means that an amendment or a substitute authorisation should be tailored to meet the change in circumstances or change in benefits or detriments.<sup>16</sup>

154 The Commission has exercised its discretion to intervene on the basis of material change on three occasions. The most recent was the amendments to *Decision 580: New Zealand Rugby Union*. This amendment was initiated following an application for variation to the authorisation by the parties.

### ***Discussion of concern***

155 The concern raised in the discussion document is that taking away the protection of authorisation in situations where there has been a material change of circumstances that was not foreseeable at the time the arrangement was entered into creates risks and uncertainty for investments with long pay back periods, such as major infrastructure investments.

156 However, the Commission is mindful of the impact on ex ante incentives to invest in exercising its discretion under the Act. The Commission carries out a public benefits and detriments analysis to inform its decision on whether to vary, replace or revoke

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<sup>15</sup> Commerce Commission, *Decision No. 601: New Zealand Rugby Union*, 11 May 2007, page 23 paragraph 77.

<sup>16</sup> *Ibid*, page 28 paragraph 103.

authorisations as a result of a material changes. Consequently, the Commission considers that the investment risk is slight. In particular, the Commission considers that there was no impact on ex ante incentives in the *Pohokura* case<sup>17</sup> because, in practice, the authorisation was not necessary for the parties to carry out the arrangement. In this case the parties' marketing arrangements had significantly departed from that which had received authorisation.

157 If there are material changes that would negate the previous net public benefits that were relied upon to receive authorisation, then it is likely to be appropriate for the Commission to intervene to reconsider the arrangement. In such circumstances the authorisation may be revoked or substituted. If a new authorisation is substituted, the parties may continue to have immunity for the modified arrangement, while ensuring that the public benefits of the authorised conduct continue to be realised.

### *Discussion of options*

158 The discussion document asks whether the Commission's power to vary, replace or revoke an authorisation if there has been a material change of circumstances (i.e. section 65(1)(b)) should be:

- retained;
- repealed; or
- replaced by a provision that allows the original applicant to ask the Commission to vary, replace or revoke an authorisation?

159 The discussion document also proposes that parties should be able to apply for minor variations, as is possible under section 91A of the Australian Trade Practice Act.

160 As outlined above, the Commission considers that the repeal of the Commission's discretion to intervene in respect of existing authorisations on the basis of a material change in circumstances is not justified. The repeal of this provision would prevent the Commission from intervening ex post in relation to arrangements that do not involve long-term investments, but where significant public detriments have arisen following material changes in circumstances. Consequently, such an amendment would be poorly targeted.

161 Some of the concerns identified in the discussion document may be able to be addressed by making explicit in the Act the basis on which the Commission exercises its discretion to intervene. For example, sections 91B and 91C of the Australian Trade Practices Act explicitly provide that the ACCC could only intervene after carrying out a public benefits and detriments analysis. Such a provision may give additional assurance to the parties that the Commission takes into account the impacts of its intervention.

162 In the case of the option of amending the Act to provide for minor variations on application of the parties, such a provision may be useful in circumstances like those arising in respect of the New Zealand Rugby Union authorisation amendment. However, it would be desirable for the Act to clarify what is meant by 'minor' in that

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<sup>17</sup> Commerce Commission, *Decision No. 581: Revocation of Decision No. 505 - OMV New Zealand Limited/Shell Exploration New Zealand Limited/Shell (Petroleum Mining Company) Limited/Todd (Petroleum Mining Company) Limited*, 2 June 2006.

circumstance. Any uncertainty in the interpretation of the Act may impose legal risks on the Commission.

***Commission's view***

- 163 The Commission's right to vary, replace or revoke an authorisation if there has been a material change in circumstances should be retained.
- 164 If desired, consideration could be given to introducing provisions similar to that in the Australian Trade Practices Act that make it explicit that the Commission must carry out a public benefits and detriments analysis before intervening, and that allow the applicant to apply to the Commission for minor variations to an authorisation. If adopted, the meaning of 'minor' for the purposes of this provision should be clarified.

**Issue J: Halting Conduct While Authorisation Proceedings Underway For Existing Practices**

- Question 16: *Should the mandatory requirement to halt the conduct while the Commission is considering an application for authorisation (i.e. section 59A(2)) be retained; or removed?*
- Question 17: *If the mandatory requirement to halt the conduct is to be removed, do you consider that it would be better to repeal section 59A(2); or replace it with a provision that provides the Commission with the discretion to require that the conduct be halted?*

***Current practice***

- 165 Section 59A (when Commission may grant authorisation) of the Act clarifies that the Commission may in certain circumstances grant authorisation for existing restrictive trade practices. Subsections 59A(2) and 59A(3) require the parties to the restrictive trade practice to discontinue that conduct while the application is before the Commission, unless they are able to satisfy the Commission that discontinuing the practice would result in exceptional hardship to any of the parties. However, the Commission agrees that this section is not operating as intended.
- 166 The Commission considers that the provision does not permit nor entitle it to desist from further consideration of an application for authorisation if the parties to the arrangement fail to comply with section 59A(2) of the Act. However, if the conduct does not cease, the parties would not be protected by the lodging of the application from subsequent action if their conduct contravenes the Act.

***Discussion of options***

- 167 The discussion document outlines three alternatives:
- repeal of section 59A(2);
  - replace section 59A(2) with a provision that gives the Commission the discretion to order that the conduct be stopped while the application is being considered; or
  - lower the 'exceptional hardship' test in section 59A(3).

- 168 The Commission considers that there should be a mandatory requirement that existing conduct should be halted while it is considering an authorisation application. The presumption should be that contravening conduct is harmful, and therefore should be deterred. It is only once the net public benefits are demonstrated that the conduct should be sanctioned. Consequently, the Commission does not support the first two options outlined above.
- 169 However, the Commission agrees that there may be circumstances where a mandatory requirement for the parties to halt the conduct could result in significant costs. The current requirement for the parties to demonstrate ‘exceptional hardship’ to the Commission before the conduct may continue is likely to be a difficult threshold to meet and a lower threshold could be considered.
- 170 In addition, the Commission considers that the problem is broader than whether it has jurisdiction to require parties to halt the conduct while it is considering an application for authorisation. Not only can the Commission not decline jurisdiction on this grounds, but also it has no means by which to positively require parties to halt the conduct. It is also unclear what mechanism any private party could use to require parties to halt the conduct.
- 171 Consequently, the Commission recommends that the provision is amended to outline the mechanism by which the Commission may enforce the obligation on the parties to halt the conduct while it carries out its assessment of the application. For example, if the parties do not cease the conduct and the Commission has not permitted the conduct to continue, the application could be deemed to lapse or deemed to be declined.

#### *Commission’s view*

- 172 The Commission considers that the mandatory requirement that conduct should be halted while it is considering an authorisation application should be retained. However the Commission should have the discretion to allow the conduct to continue in certain circumstances. The Commission suggests that the current threshold of ‘exceptional hardship’ to any of the parties could be lowered to accommodate other circumstances where the costs of halting may impose unreasonable costs.
- 173 The section should also be amended to make explicit the means by which the Commission may enforce the requirement for the conduct to halt. The Commission suggests that, if the parties do not cease the conduct and the Commission has not permitted the conduct to continue, the application should be deemed to lapse or deemed to be declined.

#### **Issue K1: The Right of the Applicant and Specific Third Parties to Call for a Conference**

- Question 18: *Should the applicant and/or any third parties have the power to require the Commission to hold a conference or should the decision be the Commission’s alone?*
- Question 19: *Assuming the applicants and/or third parties were no longer able to require the Commission to call a conference, should the Act specify that they may request the Commission to hold a conference or does it go without saying?*

### *Current practice*

- 174 Section 62 of the Act provides rights for the applicant and specific third parties to call for a conference for restrictive trade practice authorisations. In addition, the Commission may call a conference on its own initiative. These provisions contrast to section 69B of the Act relating to conferences for mergers, where the Commission has sole discretion as to whether to hold a conference.
- 175 The purpose of the conference is to gather information to inform the Commission's consideration of an application. The Commission would always call a conference should there be a reasonable need to hold one. However, conferences are not necessarily the most effective way of gathering information. Direct interviews, written submissions and cross-submissions can be highly effective means of gathering information. Consequently, empowering other parties to have the right to call Commission conferences may not be an effective use of the Commission's time or resources.
- 176 In addition, given the current relationship between participation at a Commission conference and appeal rights for third parties, there may be poor incentives as to whether or not to call a conference, depending on the circumstances. This issue of the rights of appeal against a Commission determination is discussed in Issue L of this submission.
- 177 To date the Commission has not been required to hold a conference when it did not also consider that the conference would be of assistance. *Decision 580: New Zealand Rugby Union* authorisation is an example of an authorisation proceeding where neither the Commission nor the parties called a conference. Consequently, there may not be a problem in practice with this provision.

### *Discussion of options*

- 178 The discussion document outlines three options for amendment:
- to limit the right to call a conference to the Commission;
  - to limit conference rights to the Commission and the applicant; or
  - to allow the applicant and/or person to whom the draft determination has been sent to ask the Commission to call a conference, but leave it to the Commission to decide.
- 179 The Commission considers that, if appeal rights are not linked to participation in a conference, it should have sole discretion as to whether to hold a conference. This amendment would further align the trade practice proceedings with those applying for mergers, thus promoting clear and consistent legislation. In addition, the Commission's discretion to call a conference should be broadened so that the Commission may call a conference for fact finding purposes in relation to particular issues and not just after it has released a draft determination. While the Commission considers that this would not be a regular occurrence, a broader discretion to call a conference would be useful in certain cases.
- 180 The repeal of the right for parties to require a conference would not diminish their right to have their views taken into account by the Commission. Section 61(3) of the Act

provides that the Commission must take into account any submissions made to it by the applicant or any other person. In addition, applicants or interested parties may request the Commission to hold a conference. There is no need for a statutory provision for this to occur.

*Commission's view*

181 The Commission should have sole discretion to call a conference for restrictive trade practice proceedings. In addition, the Commission's discretion to call a conference should be broadened so that the Commission may call a conference for fact finding purposes in relation to particular issues and not just after it has released a draft determination. A statutory provision for applicants and interested parties to be able to request the Commission to hold a conference is not required.

**Issue K2: The Time Frames for Restrictive Trade Practice Authorisations**

Question 20: <i>Should the statutory time limits in section 62 be retained or removed?</i>
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*Current practice*

182 Section 62 of the Act provides strict time frames within which the Commission would be required to hold a conference following the release of its draft determination in the case of restrictive trade practice authorisation proceedings. The Commission must hold a conference within 20 working days of the expiration of a period of 10 working days from a date fixed by the Commission. The date fixed by the Commission is required to be a date not earlier than the day on which the Commission sent out its draft determination.

183 The Commission considers that these time frames are arbitrary and that there have been practical difficulties organising a conference within the time frames required. The statutory time frames are often not in the interests of applicant, especially where they place undue time pressure for getting experts and preparing a response to the draft determination. In addition, the inconsistency with time frames for merger authorisation applications creates problems when merger and restrictive trade practice procedures are conducted in parallel, for example, in the Air New Zealand/Qantas case.<sup>18</sup>

*Commission's view*

184 The Commission supports the option outlined in the discussion document and recommends that the statutory time limits in section 62 for holding conferences should be removed.

**Issues L – N: Joint Legal Process Issues**

**Issue L: Right to Appeal Commission Decisions – Who Can Appeal**

Question 21: <i>Should appeal rights for persons who participate in Commission conferences be retained or repealed?</i>
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<sup>18</sup> Commerce Commission, *Decision No. 511: Qantas Airways Limited / Air New Zealand Limited*, 23 October 2003.

Question 22: *Assuming that the High Court will be given the discretion to decide whether a third party may appeal, what criterion or criteria should appear in the Act?*

### ***Current practice***

- 185 Section 92 (persons entitled to appeal) of the Act provides for appeals against Commission determinations by the following persons:
- in the case of mergers, the acquirer and the vendor of the assets or shares;
  - in the case of restrictive trade practices, the parties to the agreement; and
  - any person who participated in a Commission conference in relation to that determination.
- 186 Section 91 of the Act provides that this appeal may be on the merits of the Commission's determination. In addition, all parties have a right of judicial review.
- 187 As conferences are rarely held for clearances, in practice third parties have not had a right of appeal, but only the right to seek judicial review. In the case of authorisations, third parties have exercised the right of appeal against Commission determinations.<sup>19</sup> In addition, it is not uncommon for third parties to join proceedings as respondents when the parties to the agreement have filed an appeal.<sup>20</sup>

### ***Discussion of concern***

- 188 The discussion document outlines a concern that the linking of appeal rights to participation in a conference is arbitrary. In addition it may cause excessive uncertainty for the applicant.
- 189 The Commission considers that the rationale for linking appeal rights to participation in a conference is not as arbitrary as may be indicated. This link ensures that only those parties that have stated their case to the Commission in the first instance have a right of appeal. The provision inhibits forum-shopping by third parties, where parties could attempt to raise new issues before the court in appeal that were not considered by the Commission. It ensures that the Commission is fully informed in its decision making. However, the focus on participation at a Commission conference ignores the other means by which third parties can make their views known to the Commission, such as through written submissions or interviews.
- 190 More generally, the Commission considers that defining appeal rights involves a trade-off between certainty in the marketplace and natural justice. Determinations by the Commission typically involve major transactions affecting the economy, and there is a premium on ensuring a timely outcome, particularly in the case of mergers. If third party appeal rights are overly broad this may impose significant costs on affected parties.
- 191 A particular concern with appeals on competition determinations is that competitors of the parties may often have skewed incentives in relation to appeals which may not be

<sup>19</sup> For example, *Rugby Union Players' Association v CC* [1997] 3 NZLR 79.

<sup>20</sup> For example, respondents in *Air New Zealand v CC* [2004] 11 TCLR 347 included Infratil Group, Virgin Blue and Gullivers Pacific.

aligned with the public interest. A pro-competitive determination enabling the parties to achieve efficiencies could tactically be challenged by competitors to the parties seeking delay, uncertainty or an overturning of the determination because of its competitive effects. Alternatively, if a determination erred and resulted in the parties acquiring market power, the competitors would generally benefit from the higher prices that would exist in the markets affected and they would not have incentives to appeal.

### *Discussion of options*

- 192 The discussion document suggests that the existing approach to appeal rights should be replaced and the High Court should decide standing to appeal based on:
- a general test – a third party would be allowed to appeal if the High Court thought fit; or
  - a specific test – a third party would be able to appeal if it has demonstrated that it has a material interest.
- 193 The Commission does not support the options outlined. The amendment would allow parties who may not have participated in the Commission’s processes to appeal to the courts. This may result in forum-shopping and undermine the Commission’s processes. In addition, in the case of mergers, this amendment would have the practical consequence of creating an appeal right that does not currently exist. It would shift the balance between certainty in the marketplace and natural justice, and may increase the costs of transacting for merger parties.
- 194 Consequently, the Commission considers that it is necessary to consider the trade-off between certainty in the marketplace and natural justice when considering the case for change.
- 195 In the case of mergers, there may be cases where it would be useful for the Commission to be able to hold a conference. In such instances, it is desirable that this decision is not linked to the creation of appeal rights. Consequently, consideration could be given to changing this provision. However, there is a risk that competitors may use appeal rights strategically to delay or raise the costs of an otherwise pro-competitive or efficient transaction. For example, in the ‘AMPS-A case’<sup>21</sup> it is possible that the right of appeal was used strategically by competitors. The priority in merger cases should be on achieving a timely decision to ensure certainty in the marketplace. Consequently, in the case of mergers, the right to seek judicial review should be sufficient to address third party concerns. The Commission recommends that third parties do not have a right of appeal on the merits for merger determinations.
- 196 In the case of restrictive trade practices, the case for change is not as clear. Achieving a timely decision may be less important than addressing natural justice issues, given that the costs and benefits resulting from the authorised conduct may be apportioned unevenly between third parties. In practice, there does not appear to be a problem with appeal rights for restrictive trade practices which suggests that the status quo could be retained. Alternatively, the appeal rights could be amended so that they are based on third parties making a submission to the Commission, rather than only participating in a conference. The Commission has not formed a view on this matter.

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<sup>21</sup> Telecom Corporation of New Zealand Ltd v CC (1991), 4 TCLR 473

197 The Commission also considers that a distinction should be made between a right to lodge an appeal and a right to join appeal proceedings. For the reasons outlined above, the Commission recommends that third parties should not have a right to lodge an appeal in relation to merger determinations. However, the Commission considers that third parties that participated in the Commission's processes should be able to join an appeal as a respondent. In this case, the court may benefit from hearing from the parties directly on how their interests would be impacted by the parties' appeal. This right to join appeals is consistent with current High Court Rules.<sup>22</sup>

### *Commission's view*

198 In the case of Commission determinations relating to mergers, appeal rights for third parties who participate in Commission conferences should be repealed. Only the acquirer and vendor of the assets should have rights of appeal. Third parties should only be able to initiate judicial review proceedings. In addition, third parties should retain the right to join an appeal if one of the parties to a determination appeals.

199 In the case of Commission determinations relating to restrictive trade practices, the case for change is less clear cut. The Commission has not formed a view on this matter. However, consideration could be given to amending third party appeal rights so that standing is conferred on parties that make a submission to the Commission in the course of its proceeding, rather than being based on participation in a Commission conference.

### **Issue M: Specialist Competition Tribunal**

Question 23: *Do you consider that a specialist competition tribunal should be established? Does your answer depend on whether there is to be appeals on the merit against regulatory control decisions by the Commerce Commission?*

### *Current practice*

200 Section 75 of the Act provides that the High Court has jurisdiction to determine enforcement proceedings under Parts 2 and 3 of the Act, and appeals from Commission determinations. As competition law matters are complex, New Zealand has put in place a process for the appointment of lay members under the Act as a cost-effective alternative to a specialist tribunal bearing in mind New Zealand's size and scale. This process assists the judge by providing expertise in economic and accounting matters that arise with competition law issues. The Commission considers that the lay member system is working well.

### *Discussion of options*

201 The discussion document raises the issue of whether a new specialist competition tribunal should replace the role of the High Court with a lay member.

202 The Commission considers that the establishment of a specialist competition tribunal for competition matters can bring significant benefits. However, these benefits have to be

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<sup>22</sup> R706(1)(c) provides that an appellant must "[serve] a copy of the notice of appeal on every other party directly affected by the appeal". This rule seems to envisage that such parties so served will or at least may become respondents to the appeal.

compared to the costs. In a small country like New Zealand, a specialist tribunal is unlikely to be cost effective. Only a small number of Commerce Act restrictive trade practice or merger cases make it to court each year. Accordingly, the costs of setting up a specialist tribunal solely for these cases are likely to outweigh any benefits this might bring.

- 203 If there is to be full appeal on the merits for economic regulation determinations, then the Commission has acknowledged in its submission on the companion MED discussion document that there may be case for having a specialist tribunal.<sup>23</sup> If in turn a specialist tribunal were established to hearing regulatory appeals, the Commission considers that there may be a stronger case for having this tribunal also consider Commerce Act matters.
- 204 If the costs of setting up a specialist tribunal continue to outweigh the benefits the Commission considers that the existing High Court regime should continue unaltered.

### *Commission's view*

- 205 Unless a case can be made that the benefits of a specialist tribunal outweigh the costs the current lay member system should remain unaltered. The Commission agrees with the preliminary view in the discussion document that the benefits are unlikely to outweigh the costs unless there were a decision to move to full appeals in relation to regulatory control and to establish a tribunal to hear those appeals. In principle, in the event of such a tribunal being established, that tribunal may also hear Commerce Act matters in line with overseas tribunals.

### **Issue N: Wider Use of Lay Members**

Question 24: *Should the High Court (or a replacement tribunal) have the discretion to appoint lay members in any proceeding where it is required to consider the merits of a report by the Commission?*

### *Current practice*

- 206 The current practice enables the appointment of lay members when dealing with appeals as opposed to procedural or judicial review matters. Lay members are required in some cases and may be appointed in certain others. The Act provides that the Court may act without lay members in cases involving procedure, orders that are not opposed, where the parties agree that the matter should be heard by a judge alone, proceedings where the issue is substantially a question of law only, and when the court is deciding whether to allow an appeal to the Court of Appeal.

### *Discussion of options*

- 207 The discussion document raises the issue of whether the High Court (or replacement tribunal) should have the discretion to appoint lay members in any proceedings where it is required to consider the merits of a report by the Commission. It reaches the view that the High Court should have such a discretion.

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<sup>23</sup> Commerce Commission, *Review of Regulatory Provisions under the Commerce Act 1986: Submission on MED's Discussion Document*, 6 July 2007.

- 208 The Commission agrees that the current approach is right. Appeals on their merits are assisted by the appointment of lay members.
- 209 By contrast, judicial review matters are concerned with the legality of the decision, namely that the decision was made in accordance with the law, fairly and reasonably. The Court's role is largely process focused. Procedural and judicial review matters have always been a matter for the courts. Even in countries where there are specialist tribunals, such as Australia, judicial review still goes to the courts. The issues to be addressed relate to questions of law and generally do not require the wider economic or commercial expertise that lay members bring to a full merits review rehearing.
- 210 The statements which are referred to in the discussion document made by the court in the *Powerco* case<sup>24</sup> appear to be a one-off occurrence, and, therefore, should not be considered to be indicative of a widespread concern. An analysis of the costs and benefits should be carried out before any decision is taken to extend the use of lay members into areas in which the Courts are traditionally experienced.

### *Commission view*

- 211 The Commission agrees that any appeals on their merits should have lay members assisting the court. This is the case today. The Commission does not see any case for change. A provision of wider discretion to courts to appoint lay members outside of merits review appeals is not necessary or desirable. Judges are experienced in dealing with judicial review, natural justice and procedural issues. Such legal issues are appropriately heard by the Courts. The Commission therefore disagrees with the preliminary view in the discussion document that the current approach be changed.

Question 25: *Are there other circumstances in which there should be wider discretion for judges to appoint lay members?*

- 212 The Commission is not aware of any other circumstances where there should be a wider discretion for judges to appoint lay members.

## **Issue O – S: Framework for Assessing Costs and Benefits**

### **Issue O: The Assessment of Efficiency Gains and Losses**

Question 26: *To what extent does the Commission's analytical framework adequately take account of what would happen if the proposed merger or arrangement did not go ahead (the counterfactual)?*

### *Current practice*

- 213 This issue set out in the discussion document relates to establishing the appropriate counterfactual for clearances. At present, the Commission makes a pragmatic and commercial assessment of what is likely to happen in the absence of the proposed acquisition. The counterfactual may not always be a continuation of the status quo. To ensure consistency, exactly the same approach to establishing the counterfactual is taken for restrictive trade practice investigations and authorisations.

<sup>24</sup> *Powerco Ltd v Commerce Commission* (HC Wellington, CIV 2005 485 1066, 9 June 2006 at paragraph 25.

***Discussion***

- 214 The discussion document seeks views on whether the analytical approach is well targeted.
- 215 The Commission recognises that defining the counterfactual involves forecasts that are difficult to make. The same difficulty occurs with defining the factual; the uncertainty associated with trying to forecast the future is intrinsic to the analysis. However, the Commission considers that its analytical framework does adequately take into account what would be likely to happen in the counterfactual, and that its approach is consistent with that of overseas competition authorities.

***Commission view***

- 216 The Commission considers that no change is required.

**Issue P: The Treatment of International Competitiveness Claims**

Question 27: *Is the public benefit test sufficiently broad to take international competitiveness claims into consideration and give them sufficient weighting?*

***Current practice***

- 217 The public benefit test allows the Commission to consider international competitiveness claims, such as increases in exports, and give them appropriate weight in its analysis.
- 218 For example, in the Air New Zealand/Qantas case, the Commission considered the claimed benefits from additional tourists to New Zealand, but did not find this to be an overall benefit because it resulted, in large part, from New Zealanders being deterred from travelling overseas and instead taking their holidays in New Zealand.

***Discussion of options***

- 219 The discussion document puts forward two alternative views:
- first, that a provision should be inserted into the Act which makes it as clear as possible that mergers that are likely to increase New Zealand's international competitiveness should be treated favourably; and
  - second, that there is a risk that identifying particular types of benefits may lead them to be given more weight than is merited.
- 220 The Commission's approach to measuring public benefits focuses on net benefits. For example, it does not measure gains as the dollar values of the prospective increase in exports, or of the prospective substitution of domestic products for imported ones, but simply as the extra economic profits earned from the additional exports or the domestic substitutes. This recognises that additional production of either uses up additional resources, which have an economic cost.
- 221 The Commission is strongly of the view that it should not give any more weight to international competitiveness claims than to any other factors, because this would bias its efficiency-based analysis, resulting in inefficient market outcomes that would not be for the long-term benefit of consumers in New Zealand. For example, it could result in

the Commission giving more weight to benefits from improvements in international competitiveness than benefits to consumers in New Zealand.

- 222 The Commission notes that, even though the Australian Trade Practices Act contains international competitiveness provisions, in practice the ACCC does not take a different approach to the Commission in assessing these possible benefits. If such provisions were inserted into the Act this would raise unduly expectations about the weight that the Commission would place on international competitiveness claims in future cases.

### *Commission's view*

- 223 No change is required. The Commission considers that the public benefit test is sufficiently broad to take into consideration, and to give appropriate weight to, international competitiveness claims. Introducing international competitiveness provisions into the Act would result in inefficient market outcomes that would not be for the long-term benefit of consumers in New Zealand.

### **Issue Q: Quantification of Costs and Benefits**

Question 28: *Does quantification restrict the consideration of dynamic or other difficult to measure economic effects?*

### *Current practice*

- 224 The Commission currently quantifies costs and benefits where possible. However, this does not restrict the consideration of factors, such as dynamic efficiencies that cannot be quantified with any precision.

### *Discussion of options*

- 225 The document suggests that there is a risk that too much emphasis may be placed on those costs and benefits that can be quantified at the expense of those for which quantification can be difficult. It notes that dynamic efficiencies can be the most important, but most difficult to measure, effect.
- 226 The discussion document states that it wishes to test with stakeholders whether the Commission has the scope to exercise judgements in relation to dynamic efficiency factors along with other costs and benefits that are not easily quantified.
- 227 The Commission considers that quantitative modelling has proved to be very useful in the regulatory context, for example, in the Mobile Termination decision. Here, it was used to assess the potential benefits, both from regulatory control compared to the counterfactual of no intervention, and in terms of assessing outcomes when companies have come back with voluntary commercial offers. These assessments would have been very difficult to do outside of a quantitative framework. Attempting to quantify effects also acts as a discipline on the Commission by opening up to scrutiny the assumptions it has used in its analysis.
- 228 The Commission considers that the problem is more that effects such as dynamic efficiency are difficult to predict, and may only be realised over the long-term. Consequently, they are often difficult to assess, regardless of whether a quantitative or a

qualitative approach is used. That said, the Commission suggests that in its experience, the efficiency benefits claimed in authorisation applications are more usually of the static (“productive”) efficiency kind, in terms of lower costs. Sometimes claims are made for new or improved services, which could be thought of as being ‘dynamic’. These are in principle capable of being quantified in an approximate way. For example, in *Decision 580: New Zealand Rugby Football Union Incorporated*, the Commission quantified in an approximate way the benefits of a salary cap in terms of greater spectator and viewer enjoyment.

229 The Commission’s assessment of dynamic efficiencies may have regard to a number of qualitative factors such as:

- the innovative potential of the industry, including the scope for product and process innovations, which varies widely depending on technological factors;
- the past innovation performance of the firms concerned, and what residual competitive pressures may encourage innovation post-acquisition or post-authorisation; and
- the fact that innovations are not cost- nor risk-free to develop and implement, and so have to be estimated on a net benefit basis.

230 In almost all cases, measuring costs and benefits necessarily involves a mix of quantitative and qualitative assessments. The Commission is mindful of the observation of Richardson J in the ‘AMPS-A case’ that it has a responsibility to attempt to quantify benefits and detriments so far as possible. It undertakes a quantification assessment in line with this observation and as a matter of good practice. However, some factors do not lend themselves readily to quantification. Without care, there could be a possibility that undue focus be given to those factors that can be quantified at the expense of those that cannot. Determining the appropriate weight that should be given to each can be difficult, but the Commission is confident that it has sufficient experience to undertake this weighting function appropriately.

### *Commission view*

231 Quantification, where possible, is helpful to the Commission’s decision making, but this does not prevent it also having appropriate regard to those factors that may not be able to be quantified with any precision. Non-quantifiable factors are taken into account and given the appropriate weight. Quantification also acts as a discipline on the Commission by opening to scrutiny the assumptions it has used in its analysis.

### **Issue R: Time Frames Over Which Costs and Benefits Are Assessed**

Question 29: *Are the time frames over which costs and benefits are assessed appropriate?*

### *Current practice*

232 The time frame used by the Commission to assess costs and benefits varies with the circumstances of each case. Benefits such as dynamic efficiencies that may arise beyond five years will be taken into account if these future benefits are shown to be sufficiently likely.

***Discussion of issue***

- 233 The discussion document notes that the Commission usually assesses the benefits and detriments looking forward no more than two to five years. It questions whether these time frames are sufficiently long to take dynamic efficiency into account.
- 234 The Commission does not share this view, as noted above. Where warranted, significantly longer time frames have been used to assess costs and benefits. For example, in *Decision 505*<sup>25</sup> (dated 1 September 2003) the Commission assessed the benefits and detriments from early production and joint marketing of Pohokura gas over the full period of production from the Pohokura field - i.e. from 2006 to 2019. The Commission recognised, however, the need to treat projections well into the future with appropriate caution because of the increasing amounts of speculation required to make these projections.

***Commission view***

- 235 The time frames over which costs and benefits are assessed vary depending upon the facts of each case. In particular, if specific factors warrant consideration of a longer time horizon, the Commission already has the capability to do this and has done so in practice.

**Issue S: Market Definition**

Question 30: *Is the approach to define markets appropriate?*

***Current practice***

- 236 The Commission uses the internationally accepted SSNIP test to define markets. This assumes the relevant market is the smallest space within which a hypothetical profit-maximising, sole supplier of a good or service, not constrained by the threat of entry, would be able to impose a small yet significant and non-transitory increase in price, assuming all other factors remain constant. Buyer and supplier reactions to a given price increase, when all other prices are held constant, are tested in hypothetical exercise, which assumes the creation of a total monopoly. The smallest space in which such market power may be exercised is defined in terms of a number of dimensions of a market e.g. product market, geographic market, functional market. The Commission generally considers a SSNIP to involve a five to ten per cent increase in price that is sustained for a period of one year.
- 237 The Commission also undertakes a reality check to ensure that it includes in the market goods and services that as a matter of fact and commercial commonsense are substitutable for each other.

***Discussion of issue***

- 238 The discussion document seeks stakeholders' views on whether the Commission's approach, including using the SSNIP test, is sufficiently flexible.

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<sup>25</sup> Commerce Commission, *Decision 505: Preussage Energie GMBH/Todd (Petroleum Mining Company) Limited/Shell Exploration New Zealand Limited/Shell (Petroleum Mining) Company Limited*, 1 September 2003

- 239 The Commission considers that the approach it adopts for defining markets is consistent with that used by overseas competition agencies, and is sufficiently flexible to define the markets that best assist the competition analysis in each case.
- 240 Under the Act, the Commission must define markets in New Zealand. However, this in no way prevents the Commission from considering competitive constraints from suppliers outside New Zealand. Section 3(3) of the Act requires the Commission to consider the effect on competition in a market by reference to all factors that affect competition in that market, including competition from goods or services supplied or likely to be supplied by persons not resident or not carrying on business in New Zealand.
- 241 For example, in the Air NZ/Qantas appeal, several of the market definitions involved routes between New Zealand and Australia, and between New Zealand and other overseas destinations. These route markets were all 'anchored' by having one point in New Zealand, and that was sufficient for the Commission to find a New Zealand market in each case, even though many of the customers would have purchased tickets outside New Zealand and there were overseas suppliers, such as Qantas, or potential entrants from overseas, such as Pacific Blue. The market definition was not a contentious point in the appeal.

#### *Commission view*

- 242 The Commission considers that the approach it adopts for defining markets is consistent with that used by major competition agencies and is sufficiently flexible to define markets that best assist the competition analysis in each case.

#### **New Issue: Withdrawal of Applications before Commission**

- 243 Finally, the Commission requests that officials consider a further issue that has arisen with the operation of the Act. This issue relates to the ability of parties to withdraw clearance applications and proceed with the merger before the Commission has made its final determination on the matter.

#### *Discussion of the issue*

- 244 Section 68(4) provides that an applicant may withdraw a clearance application before the Commission has made a determination. The Commission has had two recent occasions - *Telecom* and *New Zealand Bus* - where the applicants have withdrawn their application part way through the Commission's clearance proceedings following the Commission making the parties aware of its competition concerns.<sup>26</sup>
- 245 If an application is withdrawn, the Commission has to consider using expensive litigation to prevent a transaction proceeding while it is still to reach a determination on the merger proposal. This is administratively problematic and expensive.
- 246 There is also an added risk that the Commission may be discouraged from raising its competition concerns with the applicant during the course of a proceeding if it thinks

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<sup>26</sup> New Zealand Bus Limited / Mana Coach Services Limited and Telecom New Zealand Limited / Counties Power Limited

that the applicant may immediately withdraw the application. Such a consequence would limit the ability of the applicants generally to respond to conflicting evidence raised by third parties or Commission concerns.

*Options to deal with this issue*

- 247 One option to deal with this issue would be to insert a provision in the Act that requires parties to give the Commission five working days notice of their intention to withdraw a clearance application that is currently under consideration. This would send a clear signal to applicants of what is expected of them when they submit a clearance application to the Commission for consideration. The five day notice period would give the Commission sufficient time to inform itself of the reasons for the application being withdrawn and whether it will be necessary for it to initiate enforcement proceedings.
- 248 Consequently, the Commission requests that consideration be given to amending the Act to require applicants to give five working days notice of their intention to withdraw an application.