

10 August 2007

Commerce Act Review
Ministry of Economic Development
PO Box 1473
WELLINGTON

Dear Sir/Madam

**Submission to the Ministry of Economic Development -
Review of the Clearance and Authorisation Provisions under the Commerce
Act 1986 – Discussion Document May 2007**

1. **The New Zealand Fair Trading Coalition (“NZFTC”)** is an informal group of like-minded organisations promoting best business practice, sound business ethics, and fair and vigorous competition. NZFTC members comprise a total of 13 business and trade associations, representing approximately 30,000 individual businesses, and close to 200,000 employees. A list of organisations comprising the Fair Trading Coalition can be found on the NZFTC website www.nzftc.org.nz
2. Our function is the pursuit of legislative reforms in a number of key target areas within business law. NZFTC believes that a central issue facing our economy is the releasing of the full potential of all business to contribute to growth.

This has significant implications both for competitiveness and adaptation to necessary change within a global economy.

NZFTC believes that small and medium enterprises (SMEs) have a significant role in this. SMEs make a critical contribution to any economy particularly smaller economies such as New Zealand.

The NZFTC is **not** requesting that government prop up inefficient SMEs nor protect SMEs from competition. The NZFTC merely wants a level playing field for SMEs to begin with.

SMEs represent a New Zealand mainstream, comprising 97 per cent of all businesses and engaging a substantial proportion of our workforce. They also bring that spirit of innovation and entrepreneurship that is vital to our economy, small and remote by global standards.

Energising the full potential of this dynamic resource makes sense, both economically and socially. Consumer interests will also benefit.

However the NZFTC believes that there are real obstacles to this. The playing field is not level.

There are substantial and unfair barriers that constrain SMEs. There are inadequacies in New Zealand law governing aspects of commercial practice that leave SMEs disadvantaged in their relations with organisations that have market power. This can threaten the viability of SMEs, smother their vitality, and hinder their capacity to grow and contribute fully to our national economic growth.

NZFTC has thoroughly researched avenues for liberating the potential of SMEs through legislative reforms in a number of key target areas.

Our research is comprehensive, our experience of the difficulties of the current business environment is both real and first-hand, and the solutions well considered.

The legislative changes we are proposing have been benchmarked against those of other jurisdictions with deregulated competition frameworks, and have received the endorsement of several overseas commentators whose own experience provides them the insight into the real benefits of analogous reforms.

NZFTC believes it is fundamental that both the spirit and the practice of free competition be allowed to thrive in our economy.

However, this competition must also be fair so that the potential contribution of all sectors, large and small, may be realized to their fullest extent, underpinning business sustainability, industry productivity, and consumer interest.

The legislative reforms proposed by NZFTC are founded on principles of fairness for all business, and have at their heart irrevocable principles of strong business ethics and "Best Practice" that encourage free enterprise.

Sadly, New Zealand lags behind other OECD member countries in the area of fairness in competition law. Australia by contrast has made recent significant advances and which, various commentators have observed, support the viewpoint that such reforms have benefited consumers, SMEs, and industry at large.

3. We therefore welcome the opportunity to make this submission, because the issue of Collective Bargaining is one of the four key target areas that comprise the main thrust of our objectives in legislative reform. The other key areas include the outlawing of Unconscionable Conduct, the introduction of Franchise Law, and also industry-led regulation via Codes of Practice
4. We support the introduction of a collective bargaining notification system as proposed in Issue G of the Discussion Document.

SMEs will generally lack bargaining power when negotiating the terms and conditions of supply or purchase with other, larger, organisations. Often, as a result of this imbalance, they are forced to accept terms in agreements that they would not otherwise accept, were there greater equality of bargaining power which impacts adversely on allocative and dynamic efficiency. The larger organisations are able to impose their will, rather than accommodate the innovations of the SMEs. The collective bargaining notification system proposed would allow SMEs to join together and bargain as a group, allowing them to exercise a degree of countervailing market power to that of the larger organisation with whom they are negotiating.

The NZFTC believes that the adoption of the proposed system would be a positive step towards securing a fairer and more competitive trading environment for all businesses, leading to greater dynamic efficiency which will benefit consumers and the New Zealand public.

5. The Appendix sets out the full analysis of the issues that arise in many sectors of New Zealand industry, and illustrates how a collective bargaining regime could assist in conduct of business within these, with considerable potential to lead to more efficient and more effective outcomes. The Appendix also provides answers to the questions raised in the Discussion Document.

6. We would welcome the opportunity to discuss these issues with officials as required.

Yours sincerely

Stephen Matthews
Chairman

APPENDIX

1 Introduction

- 1.1 Issue G: “A Possible Collective Bargaining Agreement Notification Process” in the Review of the Clearance and Authorisation Provisions under the Commerce Act 1986 – Discussion Document May 2007 (the “Discussion Document”) proposes the possibility of putting in place a collective bargaining notification system for small to medium sized firms (“SMEs”) that would provide immunity from court action in certain circumstances.
- 1.2 That section of the Discussion Document sought submissions that provide real examples of issues that have arisen under the current system that could be addressed by the introduction of a collective bargaining notification system.
- 1.3 The **New Zealand Fair Trading Coalition (“NZFTC”)** supports the Commission’s proposal in Issue G of the Discussion Document, and addresses the questions put forward on page 45 of the Discussion Document in the sections below, which includes the highlighting of where such a system would be of considerable benefit, based upon the experiences of our member organisations within the broad range of industry sectors they represent, and which will be incorporated as real examples in individual organisation submissions on this Discussion Document.

2 Are SMEs inhibited from engaging in efficient collective bargaining schemes? If so, please provide real examples.

- 2.1 In many industries, small and medium enterprises (“SME”s) must negotiate with large organisations over terms and conditions related to the purchase or supply of various goods and services. Given their relative size, SMEs are often exposed to negotiation situations in which they have little or no bargaining power and are, as a result, often forced to accept unfavourable terms and conditions including those in relation to price. In order to improve their position, SMEs may seek to join together and to bargain as a collective group, thereby exercising a degree of countervailing power to that of the large organisation. Collective bargaining is seen as an effective strategy to employ in order to achieve more appropriate commercial terms and conditions, including terms and conditions in relation to the price paid for goods and services.
- 2.2 Despite being an effective strategy, arrangements where competitors in an industry get together (either directly or through the election of a representative to negotiate on their behalf) to discuss and agree upon terms and conditions for the supply or acquisition of goods or services in markets in which they compete, or attempt to collectively negotiate those terms, are likely to breach the Commerce Act 1986 (the “Act”).
- 2.3 Section 27 of the Act prohibits collusive conduct in the form of contracts, arrangements or understandings which have the purpose, effect or likely effect of substantially lessening competition. Section 30, in effect, deems a price fixing agreement to be in breach of section 27. Accordingly, any agreement between competitors to fix, control or maintain prices for goods or services is prohibited regardless of its purpose or effect on competition. Collective bargaining, even where its focus is on terms other than price, is likely to amount to a prohibited agreement under the Act.
- 2.4 In addition, section 29 prohibits any contract, arrangement or understanding which contains an exclusionary provision. Relevant in the present context, the aim of section 29

is to prevent behaviour such as a collective boycott (i.e. the deliberate exclusion of a person from participating in a market). A collective bargaining arrangement that involves the possibility of the group collectively refusing to deal with a particular business or individual might be held to be an exclusionary provision under section 29.

- 2.5 There is scope within the Act for collective bargaining or collective boycott arrangements to be authorised.¹ The Commerce Commission (the "Commission") has the power to grant immunity from legal action where an overall benefit to the public in doing so is established. This power comes through the authorisation process contained in Part V of the Act and permits collective bargaining arrangements that would otherwise breach the Act. Collective bargaining can be authorised by the Commission in circumstances where the public benefit outweighs the detriment to competition that would arise from the collective bargaining behaviour (i.e. the Commission applies the 'net public benefit' test). The Act requires the Commission to have regard to the overall efficiencies that will result from the collective bargaining conduct when it is assessing net public benefits.² This focus on economic efficiency is evident in the Pharmacy Guild Draft Determination.³
- 2.6 However, as recognised at paragraph 100 of the Discussion Document, the existing authorisation process is lengthy, costly and has a level of uncertainty attached to it which as a result, means that this is a process which, from a practical and commercial perspective, SMEs are unable to undertake. In order to obtain an authorisation, there is an initial filing fee of \$10,000 plus GST, substantial legal and other professional costs, and a lengthy consultation process which must be undertaken by the Commission before any authorisation can be granted. Other than the application by the Pharmacy Guild (which was withdrawn prior to the final determination), there have been no other applications to the Commission for authorisation of collective bargaining arrangements. The low number of applications reflects the cost, time and uncertainty associated with an authorisation application. This is particularly discouraging for SMEs which often do not have the resources required to undertake the authorisation process.
- 2.7 Therefore, collective bargaining by SMEs in New Zealand is not currently a viable option due to:
- a. the risk of the agreement breaching the Act; and
 - b. the cost, complexity, delay and uncertainty associated with the authorisation process.

3 **Should a collective bargaining system be introduced? Would your answer be different if a trade practices clearance system were introduced?**

- 3.1 We support the introduction of a collective bargaining notification system as proposed in Issue G of the Discussion Document, and submit on the questions raised below.

¹ Refer to section 4.

² Section 3A Commerce Act.

³ New Zealand Commerce Commission, *The Pharmacy Guild of New Zealand (Inc)*, Draft Determination, page 50.

3.2 There are many public benefits that would result from the ability of SMEs to collectively bargain. It is difficult to measure public benefits in precise quantitative terms and the Commission requires credible evidence to illustrate any claimed public benefits. Unique issues arise in different situations; however, there are numerous common public benefits that would arise. These include:

- a. **Improved bargaining power:** Public benefit arguments around improved bargaining power centre on the attempt to shift the balance of power between the parties to a proposed agreement. An increase in bargaining power is typically sought by SMEs individually and achieved through a collection of those SMEs forming a group and attempting, through a collective agreement, to improve their bargaining position in relation to that of the organisation (which is often larger) with whom they are negotiating.

There are numerous factors which, in some circumstances, result in SMEs having very little bargaining power compared with larger organisations. For example:

- A monopoly supplier or monopsony purchaser has the ability to compel acceptance of terms and conditions, with the only alternative being the SME ceasing supply or purchase potentially pushing the SME out of business.
- The percentage of the business the SME provides to or requires from the other party.
- The limited product or service range of the SME.
- The respective resources of the parties.
- The level of negotiation expertise of the parties.

The consequences of an imbalance in bargaining positions can be:

- The offering of standard form contracts.
- Terms dictated by (and likely to benefit) the offering party (including limited, if any, scope for the SME to have input into the terms of the contract).
- Agreements offered on a 'take it or leave it' basis.

However, by bargaining collectively, SMEs may be able to achieve competitive parity with the large organisation with whom they are negotiating and realise more favourable and more appropriate terms and conditions through, for example, the opportunity to have input into agreements.

- b. **Transaction cost savings:** Transaction costs arise in all markets and cannot be avoided. However, it is likely that transaction costs would be lower where an acquirer or supplier is able to conduct negotiations only once (in this case with a group of businesses) as opposed to situations where separate agreements must be entered into with every business with whom they deal. This is because parties can avoid the unnecessary duplication of legal fees, specialist consultant fees and the cost of the time involved in negotiations. On the other side, smaller

parties are able to share the cost of the negotiation process as opposed to bearing it in its entirety.

- c. **Redistribution of monopoly or monopsony profits:** The ability for SMEs to collectively negotiate lower prices for goods and services means that the level of overall profit received by each party is likely to shift, with the SMEs gaining a better advantage than they had previously. In turn, this benefit may well be passed on to consumers in terms of lower prices paid for goods or services given the level of price competition that generally exists between suppliers in a market. However, even where SMEs operate in a market where there is no price competition (for example, where price is regulated) it is still possible that any change in the price negotiated will result in a public benefit in the form of increases to salaries and other aspects of business that will remain competitive. This leads to improved service levels and, therefore, the quality adjusted price of the good or service would decrease for consumers resulting in a public benefit.⁴
- d. **Easing the transition to industry deregulation:** The ACCC has accepted arguments that there is a public benefit in mechanisms, including collective bargaining schemes, that facilitate the transition from a regulated to a deregulated environment given that such mechanisms help to avoid dislocation in the functioning of a market that might otherwise be caused by such change in regulation. However, industries seeking to collectively bargain, must demonstrate a clear commitment and movement towards operating in a deregulated market. Collective bargaining arrangements which effectively seek to replace one set of regulated arrangements with another are unlikely to produce a net public benefit and would, therefore, be unacceptable.

This matter was considered by the Dawson Committee which commented:

“If notification were to be introduced as an alternative to authorisation, it should not be allowed to become a de facto mechanism for the re-establishment of the statutory marketing arrangements. Notification should not be seen as an alternative form of industry policy.”⁵

- e. **Continued viability of small businesses:** There is a public benefit in increasing the viability of efficient SMEs (efficiency must be able to be demonstrated as there is unlikely to be a public benefit in the maintenance of inefficient SMEs). In some situations, allowing SMEs to bargain collectively will help to ensure the continued viability of the businesses involved.
- f. **Opening up new marketing opportunities:** Collective bargaining may enable the exploration of increased marketing opportunities for the SMEs involved. Opportunities could include better use of spot markets, the ability to supply different companies and the ability to have agreements with more than one company.

This is particularly relevant in the agriculture industries. In Australia, in an application by the Australian Dairy Farmers Federation, the ACCC accepted that, by allowing farmers in a collective bargaining group to aggregate their milk, this could increase the viability of such farmers competing to supply processors that they would previously have been excluded from supplying (due to the high cost

⁴ This argument was accepted by the ACCC in their assessment of the TAB agents and TAB Limited.

⁵ Dawson Committee Report, page 118.

and logistics of individual farmers transporting relatively small volumes of raw milk). The ACCC concluded that this would result in considerable public benefit.

- g. **Reduced risk of unconscionable conduct:** Many SMEs seeking to redress a perceived imbalance in bargaining power with a larger organisation argue that allowing them to collectively bargain will reduce the risk of the larger organisation inserting harsh, unfair or unreasonable terms into their contracts.

The ACCC has accepted that reducing the risk of SMEs being treated unconscionably is a public benefit where it can be demonstrated that there is a genuine likelihood that such conduct will occur absent of the collective bargaining arrangements; and that bargaining collectively will reduce such a risk. However, in the absence of any evidence of unconscionable dealings, it is unlikely that collective bargaining arrangements will be accepted as they will not necessarily result in a reduced risk of unconscionable conduct occurring.

This public benefit is likely to be of increased relevance in the New Zealand environment because there is no general prohibition on unconscionable conduct.⁶ The Australian provisions are designed to assist SMEs that find themselves the victims of harsh or unfair behaviour by larger businesses; and specifically prohibits one business dealing unconscionably with another in the supply or acquisition of goods or services. In New Zealand, collective bargaining would mean there was less opportunity for large organisations to engage in unconscionable conduct.

- h. **Improved industrial harmony:** Industry representative bodies, by engaging in collective bargaining on behalf of their members, may result in increased industry harmony. There must, however, be evidence which clearly establishes that the granting of an authorisation to collectively bargain will lead to significantly greater industry harmony in the future than currently exists.

- i. **Facilitation of industry association representation:** The granting of authorisation for collective bargaining by an industry representative association has many public benefits, including:

- Increasing and assisting the association's capacity to represent its members' interests.
- Enabling the association to act as an advocate for members.
- Preventing risk of breaching the Act by associations in representing their members collectively without an authorisation.
- Facilitating the exchange of information and discussion of issues common to participants in the industry.
- Encouraging informed markets.

In some situations, the ACCC considered that the associations were likely to continue to play the roles outlined above, regardless of whether authorisation for collective bargaining was granted. In those cases, the ACCC did not accept that any public benefits flowing from an industry association's other activities in acting on behalf of its members would be lost if no authorisation was granted.

⁶ In Australia, unconscionable conduct is prohibited under section IVA of the TPA.

3.3 We also recognise that there are also a number of potential public detriments that could result from the introduction of a collective bargaining system including the following which have been identified in the Australian context:

- a. Lost efficiencies resulting from collusion.
- b. Effect on competitors outside the bargaining group
- c. Reduced scope for new market entry
- d. Potential for collective activity beyond that authorised

However in the situation faced by SMEs, and when a system is in place that limited the collective bargaining to businesses of a certain size and profit capacity, these detriments are outweighed by the public benefits.

3.4 As noted by the Discussion Document, a collective bargaining notification system has been put in place in Australia. The anti-trust legislation and the business environment in Australia is very similar to that of New Zealand, and the amendments to the Trade Practices Act highlight the necessity of allowing collective bargaining for SMEs. New Zealand should follow the Australian approach and implement a similar system.

3.5 There are a number of ways that the concerns facing SMEs in relation to the prohibition against collective bargaining in the Act could be addressed. These include:

- a. Implementing a range of administrative improvements i.e. more guidance and explanation regarding the authorization process;
- b. Making amendments to the existing authorization process i.e. amend the public benefit test, reduce authorization fees for SMEs, or impose time limits;
- c. Enacting a general legislative exemption that permits small business collective bargaining;
- d. Establishing a trade practices clearance system; or
- e. Establishing a new process for granting immunity for collective bargaining, including a notification process.

3.6 We have conducted an assessment of the options on the basis that immunity for SMEs from the relevant competition law provisions to facilitate collective bargaining should:

- a. provide a mechanism to ensure that immunity is only granted where conduct is likely to operate in the public interest; and
- b. minimise the regulatory burden on small businesses seeking immunity from the Commerce Act to collectively bargain with large businesses with a substantial degree of market power.

3.7 In addition the option chosen should adhere to the principles that are the fundamental to competition law in New Zealand must be adhered to. These principles are:

- a. In a market economy, competition is generally the means of maximising national economic welfare.

- b. The competition provisions of the Commerce Act should prohibit market participants from engaging in anti-competitive conduct.
 - c. These prohibitions should apply equally to all market participants.
 - d. The Commerce Act should have sufficient flexibility to ensure that it permits conduct that results in a net public benefit.
 - e. Exemptions for anti-competitive conduct should only be granted when the conduct results in a net public benefit.
 - f. Any process for granting exemptions for anti-competitive conduct on public benefit grounds should be transparent and offer procedural fairness and natural justice to those affected.
- 3.8 We support the option of establishing a new process for granting immunity for collective bargaining through a notification process, as this is not only consistent with the overall objectives of competition law, but would be the most effective and efficient policy option.
- 3.9 We believe that a collective bargaining notification process is preferable to a trade practices clearance system. We would prefer the introduction of a notification system as such a system would place the burden of proof on the Commission. Whilst recognising that the Commission does have limited resources, a trade practices clearance system would involve extra costs and is therefore less likely to be utilised by SMEs which are the types of organisations the proposal is aimed at assisting.

4 Assuming that a collective bargaining notification system were introduced, what comments do you have on the design features discussed in Table 5? In particular, what criterion or criteria should be used to define conduct or firms that will be eligible for the system?

- 4.1 If a collective bargaining notification system was adopted to address SME collective bargaining, it would need to take into account the anti-competitive potential associated with collective bargaining and should incorporate the notification provisions of section 93 of the Trade Practices Act (the exclusive dealing provisions). The broad features that we would expect to be contained in such a notification process are set out below:
- a. In order for the Commission to assess the potential public benefit and anti-competitive effect, the notification should contain certain information, including information identifying who is giving the notification, details of the notified conduct and details of the class or classes of persons to which the conduct relates.
 - b. The Commission should maintain a public register of notifications.
 - c. The Commission should be entitled to revoke immunity under a notification if it is satisfied that the likely public benefit from the notified conduct will not outweigh the likely detriment to the public from the notified conduct.

- d. Before issuing a notice revoking immunity, the Commission should be obliged to issue a draft notice and give interested parties the opportunity to call a conference to discuss the draft notice.
- e. If the Commission issues a notice revoking the immunity under a notification, interested persons dissatisfied with the Commission's decision should have the right to apply to the High Court to review the Commission's decision.
- f. Immunity under a notification should come into effect automatically following a specified time after the notification is lodged, unless the Commission has formally commenced the process of revoking the notification by issuing a draft notice.
- g. The Commission should be entitled to use its powers to obtain information under section 98 of the Act to obtain information relevant to making a decision to issue a notice or a draft notice revoking immunity.

4.2 In addition, the following features should be incorporated into the notification system for collective bargaining conduct to ensure that the process is workable and operates in the public interest:

- a. The notification should provide immunity for section 27 conduct, including price fixing and the prohibition on primary boycotts.
- b. Immunity should not come into effect until 15 days (or 30 days in the case of complex matters) after the notification is lodged to ensure the Commission has sufficient time to assess the likely effect of the notified conduct. We note that in paragraph 114 of the Discussion Document the Commission advocates a period of 40 days, we think that unless the notification involves a complex matter this period is too long.
- c. The Commission should be able to prevent a notification from coming into force where substantial competition and public interest concerns are raised by interested parties or where the notification does not contain sufficient information to enable the Commission to make an informed decision about the notification.
- d. The Commission should be able to impose conditions on notifications.
- e. Immunity under a notification should operate for three years, after which parties will have to lodge a new notification if they wish the immunity to continue.
- f. The notification process should be subject to eligibility criteria to ensure that only SMEs collectively bargaining with large businesses with a substantial degree of market power are eligible to lodge a notification.

4.3 We recommend that collective bargaining notification system is a mechanism for automatic immunity from the relevant competition provisions of the Act unless and until that immunity is revoked by the Commission. Under the notification process, sufficient checks should ensure that this mechanism cannot be used to gain immunity inappropriately (albeit temporarily) for highly anti-competitive conduct. This is particularly important in the case of inappropriate collective bargaining arrangements which have the potential to cause significant commercial damage in a relatively short time, especially if used strategically during commercial negotiations.

5 **Conclusion**

- 5.1 In our experience there is a need for SMEs to be able to collectively bargain when negotiating with large organisations in New Zealand in an efficient and cost effective manner. The current authorisation process under the Act is lengthy and prohibitively expensive meaning that such SMEs are unable to form such collective bargaining groups.
- 5.2 We support the introduction of a collective bargaining notification system as proposed in Issue G of the Discussion Document.