SUBMISSION TO
THE MINISTRY OF ECONOMIC DEVELOPMENT

Review of the Clearance and Authorisation Provisions under the Commerce Act

10 August 2007

On behalf of the Chief Executives of 15 **Port Companies**

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SUBMISSION ON REVIEW OF CLEARANCE AND AUTHORISATION PROVISIONS UNDER THE COMMERCE ACT

Introduction

1 This submission is made on behalf of 15 Port Company Chief Executives[1] who work together on public policy issues, in response to the discussion document entitled *Review of the Clearance and Authorisation Provisions under the Commerce Act 1986* released by the Ministry of Economic Development (*MED*) in May 2007 (the *Discussion Document*).

Summary

2 The Discussion Document addresses a range of possible changes to Part 5 of the Commerce Act. The port industry has limited its comments to a number of key issues. In summary:

2.1 ***The statutory timeframe for merger clearance determinations.*** A party making a clearance application needs certainty around timeframes for various commercial reasons. Any revised timeframes should realistically reflect the time within which the Commission is likely to make a decision, and the Commission should be incented to meet the statutory timeframe.

2.2 ***Behavioural undertakings.*** The Commission should be able to accept behavioural undertakings where a merger would be authorised *but for* a particular area of concern which can be adequately addressed through such undertakings.

2.3 ***A possible clearance system for trade practices.*** There is merit in establishing a clearance system for trade practices. Firms that have avoided a particular practice to date due to Commerce Act uncertainty can get valuable guidance and so may be able to proceed.

2.4 ***Power to revoke, amend or replace an authorisation.*** The Commission should not be able to revoke, amend or replace an authorisation because there has been a material change in circumstances. While there will always be some risk that a change in circumstances will have unforeseen consequences, businesses would benefit greatly from the certainty of an authorisation continuing to be effective.

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[1] The Port Companies are: Northport Limited, Ports of Auckland Limited, Port of Tauranga Limited, Eastland Port Limited, Port of Napier Limited, CentrePort Limited, Port Taranaki, Port Nelson Limited, Port Marlborough NZ Limited, Lyttelton Port of Christchurch Limited, PrimePort Timaru Limited, Port Otago Limited, South Port New Zealand Limited, Port of Greymouth and Buller Port Services (Westport).

2.5 ***The assessment of costs and benefits.*** The Commission's current approach to cost benefit analysis is satisfactory. However greater regard should be given to claims of international competitiveness.

Our comments

3 The Discussion Document covers a variety of issues. By and large, the port industry agrees with the MED's reasoning and conclusions. However, we do have specific comments on a number of the MED's proposed changes which have particular relevance to the port industry.

The statutory timeframe for merger clearance determinations

4 The clearance regime should be a quick and efficient process for determining whether a proposed merger (or trade practice) raises competition issues. A party seeking clearance is often working to a commercially constrained timeframe – such as a time bound offer, where timeliness and certainty are critical.

5 The Commission should assume that any statutory timeframe for making a clearance decision is indicative not only of the time within which it should reach a decision (irrespective of any powers to extend that timeframe), but also the extent of the analysis expected to underpin the Commission's decision. The temptation for the Commission to "gold plate" the decision-making process is understandable, but in practice gives rise to significant delay which is ultimately counter-productive.

6 There is a perception that the Commission seeks to "appeal-proof" its decisions. But the Commission should be indifferent to the outcome of an appeal. If a court, with the luxury of time, takes a more considered approach and reaches a different outcome, so be it. It is not possible to future-proof competition, and there will be times when, even after the most elaborate investigation, the Commission gets it wrong. That risk is unavoidable in any process where the analytical framework is inherently speculative. Prolonged delay though is avoidable – it simply requires the Commission to recalibrate its processes so as to deliver decisions in a timeframe that accords with normal business imperatives.

7 The port industry believes that the approval process (for both clearance and authorisation) should be as quick and efficient as possible. In practice, the existing 10 working day timeframe has proven to be unworkable. Data suggests that a 30 working day timeframe is more realistic. While still not ideal, that may well constitute a sensible compromise.

8 If the MED decides to amend the statutory clearance timeframe, then:

8.1 There should be a clear signal that the timeframe should invariably be met. This could be achieved either by a statutory requirement that the majority of clearances be completed within the required timeframe, or some form of performance measure for the Commission to meet; and

8.2 The Commission needs to be cognisant that the statutory timeframe guides the level of detail that they need to go into when making a clearance decision. A 30 day timeframe would suggest that a "no stones unturned" approach is inappropriate.

Behavioural undertakings.

9 Contrary to the MED's conclusion, the port industry believes that there is merit in allowing the Commission to accept behavioural undertakings in support of a case for merger.

10 It is quite conceivable that potentially welfare-enhancing mergers cannot proceed simply because the Commission is unable to accept behavioural undertakings to address specific issues. So this technical constraint can operate to deny the public the clear benefit of a merger. New Zealand cannot afford to risk leaving money on the table in this way.

11 The MED has traversed a number of concerns about behavioural undertakings. Most of the concerns that the MED has raised go to the possible cost and risks of allowing an authorisation on the basis of undertakings. The Commission can weigh any of these costs and risks against the associated benefits when analysing the case for authorisation. In particular, by reference to the MED's stated concerns:

11.1 ***"Regulation by another name".*** Regulation is often far reaching, and seeks to address a number of concerns. A behavioural undertaking for a merger need not be so intrusive. It could be confined in scope to address particular aspects of a merged entity's behaviour. In marginal cases, behavioural undertakings may allow the public to benefit from a welfare-enhancing merger with minimal and targeted intervention to provide a degree of certainty that the benefit identified will in practice accrue.

11.2 ***Market circumstances change over time.*** This risk exists with any merger, irrespective of whether an undertaking is given.

11.3 ***Behavioural undertakings may not be fully effective.*** The Commission will have the opportunity to assess any undertaking and determine whether it will be effective. If the Commission doubts the likely effectiveness of an undertaking, that goes to the primary

decision whether or not to approve. But it does not necessarily follow that there will never be a place for such undertakings.

11.4 ***Damage to the economy if breached.*** The MED's proposal that the Commission be given the power to enforce undertakings should minimise any effect on the economy if the undertaking is breached. The power to enforce will in itself act as a deterrent;

11.5 ***Subjectivity and cost.*** Behavioural undertakings can be designed with clear measurables. This would reduce subjectivity and monitoring costs. Again, if the Commission is unclear that an undertaking would address an issue, then that goes to the outcome of the application.

12 The concerns that the MED has identified apply equally to authorisations of trade practices. Yet, section 61(2) allows the Commission to impose conditions on a trade practice authorisation – these conditions have the same effect as behavioural undertakings. It makes sense to align the trade practices and merger provisions, and equally allow behavioural undertakings for mergers. We note the MED has not proposed to remove the ability to impose conditions under section 61(2).

13 There is a strong case for allowing behavioural undertakings. They have been used successfully implemented in both Australia and the UK and are potentially of even greater value in a smaller economy where there is clearly less scope for competition in major network infrastructure industries.

14 The Commerce Act largely in its current form has been in place for over 20 years now. Both the regime and the Commission's role in the regime have matured. The Commission now has wider expertise in performing a "regulatory" role. It is equipped to assess the likely effectiveness of undertakings, and to monitor and enforce compliance with them. Allowing it to accept behavioural undertakings will help facilitate welfare enhancing outcomes.

A possible clearance system for trade practices

15 The port industry agrees that there is merit in introducing a clearance process for trade practices.

16 In most circumstances, the law is clear enough to guide a firm's behaviour. However, in marginal cases, firms may be inclined not to act because of the risk of incurring large penalties for breaching the Act. A clearance process provides the opportunity to gain certainty, and immunity from prosecution,

which increases the prospects of firms pursuing value enhancing strategies which do not in fact unduly impact on competition.

17 For ports, it is conceivable that industry rationalisation may be pursued in part by non-structural arrangements either at the horizontal level (i.e. between port companies which may be perceived to be in competition with one another) or at a vertical level (i.e. between a port company and a third party – for example, a customer or a strategic investor. It would potentially be of great benefit for ports to be able to test formally the competition law implications of any such arrangement.

18 It is unlikely that there would be a flood of clearance applications for trade practices in the long run if the proposal is implemented. Firms have established practices around what is and is not acceptable practice under the trade practice provisions of the Act. It will only be the marginal cases where clearance would be sought.

Power to revoke, amend or replace an authorisation

19 The port industry agrees that the Commission should not have the power to revoke, amend or replace an authorisation if there is a material change in circumstances, and that s65(1)(b) should therefore be revoked.

20 There will always be a risk that circumstances will change. However, that risk applies equally to authorisations that are rejected and those that are accepted. The regime is not intended to ensure that the Commission gets it right 100% of the time. It needs to give appropriate weight to the pro-competitive effect of providing an adequate degree of certainty.

The assessment of costs and benefits

21 The following briefly summarises the port industry's view on issues addressed by the MED in relation to assessing costs and benefits:

21.1 ***Assessment of efficiency gains and losses.*** The port industry agrees with the counterfactual approach to assessing competition. However, it is critical that the assessment is realistic, and that the Commission identifies a counterfactual that is likely to occur, and not a counterfactual that is a mere possibility.

21.2 ***Treatment of international competitiveness claims.*** There is particular merit, from a port's perspective, in specifically requiring the Commission to take international competitions into account. Ports are pivotal in the supply chain. Improvements in the efficiency of the supply chain in turn improve New Zealand's overall international competitiveness. This is especially the case for a geographically isolated country with [x]% of exports leaving via

ports. Any proposal for rationalisation in the port industry would ultimately be directed at enhancing the overall efficiency of the supply chain. This is potentially hugely significant in the long-term interests of New Zealand consumers and accordingly must be appropriately accounted for.

21.3 ***Quantification of costs and benefits*** The quantification of costs and benefits can be a helpful process – especially for "hard cases". However, it is always vital that all costs and benefits - both qualitative and quantitative - are pragmatically factored into the Commission's analysis. Quantification can be useful, but its limitations must be acknowledged and more qualitative factors must be given due weight in the final determination.

21.4 ***Markets*** The Commission's approach to defining markets is well established, and consistent with international practice. It also provides a useful reference point for assessing risks before approaching the Commission. However, it is important for the Commission to take a real world view when applying its assessment under s3(1A).

Further information available

22 For further elaboration or additional information on any of the submissions above, please contact either of the following:

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