ANZ

9 February 2016

Targeted Commerce Act Review
Competition and Consumer Policy
Ministry of Business, Innovation and Employment
PO Box 1473
Wellington

By email: commerceact@mbie.govt.nz

To whom it may concern

**Submission on the Targeted Review of the Commerce Act 1986 - CONFIDENTIAL**

Thank you for the opportunity to provide feedback to the Ministry of Business, Innovation and Employment (**MBIE**) on the Targeted Review of the Commerce Act 1986 (**Issues Paper**).

ANZ notes the analysis by MBIE in the Issues Paper of the challenges associated with the rule against anti-competitive exclusionary conduct found in section 36 of the Commerce Act and believes that an opportunity for sensible reform of the rule exists.

ANZ acknowledges MBIE's work since the inception of the review, and appreciates its willingness to engage with businesses to obtain a diversity of views.

**Key Messages**

ANZ would like to specifically draw your attention to our key messages about the review set out below:

**Key messages**

- The policy underpinning section 36 as currently drafted is appropriate and should be retained.
- The current drafting and interpretation of section 36, including the requirement for counterfactual analysis, is effective in most circumstances.
- If counterfactual analysis is found to have limitations, then the best option is to improve that analysis incrementally rather than engage in wholesale reform.
- A formal market study power should not be introduced in New Zealand.

We have discussed each of these key messages in detail in Schedule 1 of this letter and have provided some factual information about regulator investigations ANZ is subject to.

**Request for confidentiality**

ANZ requests that this submission is kept in confidence by MBIE. Further, ANZ requests that section 4 of our submission, aside for the recommendation shown in the box on page 6, is kept permanently confidential by MBIE. This information is provided on an in confidence, without prejudice, basis.

**About ANZ**

ANZ is the largest financial institution in New Zealand. The ANZ group comprises brands such as ANZ, UDC Finance, ANZ Investments New Zealand, ANZ New Zealand Securities and Bonus Bonds.

ANZ offers a full range of financial products and services including a significant range of financial advisory services, personal banking, institutional banking and wealth management products and services.

**Contact for submission**

ANZ welcomes the opportunity to discuss any of our submissions directly with MBIE officials. Contact details for ANZ are Hannah Johnston, Head of Regulatory Affairs,

Once again, we thank MBIE for the opportunity to have input into the Commerce Act review.

Yours sincerely

Craig Mulholland

General Counsel and Company Secretary

## Schedule 1

## KEY MESSAGES

### 1. The policy underpinning section 36 as currently drafted is appropriate and should be retained.

**Recommendation**

The policy underpinning section 36 as currently formulated is that businesses with substantial market power should be prevented from using that market power in a manner that harms competitive markets. In particular, the policy position is that competitive dynamics should be protected, not individual competitors. This underlying policy position is appropriate, and should be retained.

Prohibitions on exclusionary conduct that harm competition is a difficult area of competition law to get right. In any discussion of possible reform, the first question to address is whether the underlying policy that section 36 is required to implement is appropriate for New Zealand's circumstances.

ANZ's view is that the current policy approach is appropriate for the New Zealand economy. That policy protects competition rather than individual competitors, which is the most effective means of delivering long-term benefits to consumers. This has been the standard approach under the Commerce Act since its inception, and we understand the Issues Paper is not contemplating fundamental changes to this underlying policy position.

One manifestation of this policy position is that the existence of substantial market power is not itself a breach of competition law. ANZ endorses MBIE's stated position in the Issues Paper that:

> *... striving to acquire market power is what encourages innovation, and firms should not be punished when they achieve it. Nor, having acquired market power, should they be prevented from innovating further. Consumers benefit from increased productivity and innovation.*

In practice, giving effect to the underlying policy relies on the substantial market power threshold as an initial sorting mechanism. This is an appropriate and effective means of screening for potentially harmful conduct:

- It is appropriate because it is the aggregation of substantial market power that, in certain circumstances, can prevent competitive dynamics operating in a workable manner. It is only in these circumstances where unilateral exclusionary conduct can be incompatible with competitive market outcomes.
- It is effective because the analysis turns on standard market definition techniques that are well known and used in New Zealand. These techniques are likely to be familiar to, and understood by, businesses to which section 36 might apply.

The Issues Paper raises the question of whether more than one person in a market can have substantial market power. This seems unlikely, but as the question has not been answered definitively in New Zealand under the current law there is a risk of departure from the underlying policy of protecting competition rather than competitors. More clarity over this area of the law would provide the business community with more confidence.

**2. The current drafting and interpretation of section 36, including the requirement for counterfactual analysis, is effective in most circumstances.**

**Recommendation**

Giving effect to this underlying policy requires a causal link to be established between the fact of substantial market power and harm to competition before a section 36 claim is made out. The current "counterfactual" or "comparative" approach required by the courts works well in terms of establishing this causal link – and therefore distinguishing between lawful and unlawful conduct – in most circumstances.

As we understand it, the causal connection test – which in New Zealand is primarily based on a type of "counterfactual" analysis – is the key driver for MBIE's publication of the Issues Paper. In line with the policy position outlined above, we consider the requirement to establish a causal connection between the use of substantial market power and harm to competition is essential for establishing anti-competitive exclusionary conduct.

Adopting a lower threshold, such as that which applies in the EU, would represent a departure from sound competition policy. It would also change the nature of the test completely in a way that creates additional risks from both a business and a policy perspective. Our major concern from a business perspective is that the main alternative to comparative analysis, what is often called an 'effects test', runs significant risk of being applied in hindsight. As a result, actual markets outcome could be used as a proxy for an assessment of competitive behaviour, which risks substantively different conclusions from what was foreseeable at the time the behaviour was undertaken. From a policy perspective, the risk with this type of approach is that liability attaches to impugned conduct as a result of factors that are unrelated to competitive harm caused by misuse of substantial market power.

ANZ considers that counterfactual analysis as developed and applied by the courts can and does work well to establish (or refute) the causal connection that is critical to valid application of the law in this area. Since 2010, counterfactual analysis has moved away from strict "but for" analysis towards a more nuanced comparative exercise. This clarification of the law has emphasised the role of cogent economic analysis in understanding the effect of unilateral conduct that relies on substantial market power. This new approach has been successfully applied by the High Court and the Court of Appeal in the only two section 36 cases heard since 2010, which indicates that the current law is both workable in theory and working in practice.

Given the successful experience with the current application of section 36, we consider that any case for reform would need to be based on an empirical assessment of conduct that has been endorsed by the courts that is inconsistent with New Zealand's policy in this area. We are not sure this can be done. Prominent examples of where the counterfactual test has not been satisfied (for example, *Carter Holt Harvey v Commerce Commission* 2004 11 TCLR 200 and *Commerce Commission v Telecom* (2010) 12 TCLR 843) have turned on questions of evidence rather than the application of the counterfactual analysis itself. The application of the law is consistent with the underlying policy it is set out to achieve. In fact, it is difficult to believe that an effects-based test would have returned a different result in these cases.

ANZ acknowledges that there is a tendency for academic commentators to express concern with the abstract, hypothetical nature of the counterfactual test. Taken to the extreme, this view holds that counterfactual analysis may be applied in a wholly fictional or unreal way that is divorced from the economic effect of the conduct under scrutiny. The specific concern from a practical perspective is that conduct that is harmful to competition precisely because it is undertaken by a firm that has substantial market power may be permitted under section 36 because there are no adverse consequences when the same conduct is undertaken by a non-dominant firm.

In ANZ's view, this concern is almost certainly overstated for two reasons:

- This is not a necessary consequence of counterfactual analysis. It may, however, suggest that the wrong sort of comparison is being made by the courts in some circumstances. This does not mean that the counterfactual test needs to be replaced, simply that it needs to be better (and more consistently) applied.
- The circumstances where this type of 'false negative' may occur are relatively few, and indeed are well known to economic theory. Application of the counterfactual test in light of the economic evidence will usually work to addresses these concerns.

As a result, the theoretical risks associated with counterfactual analysis are likely to be of little practical consequence. We prefer to rely on the current evidence derived from the New Zealand case law that the counterfactual test can distinguish lawful from harmful unilateral conduct, and usually performs that task well. If there remains a question over whether further fine-tuning is necessary, it is that question rather than fundamental reform that should be the focus of MBIE's current considerations.

We also add for completeness that we do not consider that there is much to be gained from the purpose/effect debate as framed in the Issues Paper. A focus on the language of the current New Zealand position may lead to an inaccurate view that purpose applies to the exclusion of an effects test. In reality, economic effects are considered under counterfactual analysis inherent in the causal connection nature of the test. In that respect, arguments for a more explicit "effects-based" test seem to point towards dissatisfaction with the way courts have decided particular cases in the past rather than with amending the type of analysis that is necessary to establish a causal connection.

Finally, ANZ notes that section 36 ought to be considered in its full context. The Commerce Act contains a number of provisions that could be used to bring enforcement action against anti-competitive exclusionary conduct. The most obvious is the prohibition against anti-competitive agreements in section 27, which addresses both unilateral and bilateral conduct where it applies. We note that the analysis in the Issues Paper of section 36's implementation by the courts does not appear to include a discussion of the enforcement track record of section 27, which in practice is often brought as a parallel cause of action in combination with section 36 and applies the substantial lessoning of competition test under consideration in the Issues Paper.

**3. If counterfactual analysis is found to have limitations, then the best option is to improve that analysis incrementally rather than engage in fundamental reform.**

**Recommendation**

There is currently no real evidence that counterfactual analysis, when properly applied, results in an unacceptable risk of false negatives in practice. For example, no specific types of exclusionary conduct have been identified as harmful to competition but permitted by the courts' counterfactual analysis. Even if such examples can be found, this suggests a case for incremental rather than fundamental reform. The counterfactual test should be retained but improved to ensure that it better promotes cogent economic analysis.

As stated above, there is currently a lack of evidence to support calls for reform of section 36. As a result, ANZ is concerned about the regulatory uncertainty that substantive reform may introduce. However, if MBIE's current consultation on the Issues Paper does reveal circumstances where counterfactual analysis could be improved, there may be a case for incremental rather than wholesale reform.

An approach based on incremental reform enables the courts to retain and build on those aspects of section 36 that currently work, rather than reinventing jurisprudence based on new statutory drafting. It ensures a high degree of consistency in the underlying policy position, which is likely to provide the courts with additional confidence where they are required to regulate business conduct.

It is usually poor application of counterfactual analysis rather than counterfactual analysis itself that is a cause for concern. Poor application of counterfactual analysis can lead to results that are opaque or counter-intuitive. Where counterfactual analysis is underpinned by cogent economic theory and evidence the prospect of poor results are greatly reduced.

For that reason, if any case for reform can be made it should focus on clarifying the need for cogent economic reasoning within the current counterfactual approach. This approach would represent modest reform only, and has the advantage of targeting only those aspects of the current legislation that result in genuine policy concerns.

ANZ also considers that incremental reform would avoid many of the disadvantages of more fundamental reform:

- Fundamental reform is likely to create acute uncertainty. Effects-based tests that are not based in counterfactual analysis risk large businesses being punished for unintended and unforeseeable consequences from apparently benign conduct. This goes over and above the standard uncertainty that follows any law change because even subsequent precedent developed by the courts is unlikely to provide a sufficient degree of certainty for responsible decision-making by large businesses.
- Fundamental reform may give rise to a need for explicit statutory defences or regulatory authorisations. These features are unnecessary under the current law, and would only serve to complicate business decision-making. The result would be a legal framework that is neither simply nor clear. While we acknowledge that a theoretical case could be made for an efficiencies defence, it is worth noting that many substantive elements of a defence are already considered in the counterfactual test.
- Fundamental reform is likely to up-end the currently settled policy position over the purpose of prohibitions on exclusionary conduct. Even if this is not intended by the drafters of new legislation, the courts may interpret any change as a signal to develop policy anew in this area of law. The greater the change, the greater the risk that new decisions are inconsistent with established parameters. Incremental reform is the best option for minimising this implementation risk.

### 4. A formal market study power should not be introduced in New Zealand

**Recommendation**

The case for the need for a formal market study power to be introduced in New Zealand has not been made out. There is no gap in New Zealand's institutional settings for promoting competition. In ANZ's view the cost associated with such studies outweighs the benefit to consumers. Many other regulators hold equivalent powers relevant to conducting a study in the particular industry.

ANZ does not support the introduction of a formal market study power in New Zealand. Both the Commerce Commission and the Productivity Commission have powers of inquiry which enable them to conduct market research. As noted in the Issues Paper, there are also other market studies functions which enable market studies to be conducted by other bodies, including government agencies. As a result, ANZ does not believe there is a gap in New Zealand's institutional settings for promoting competition.

ANZ considers that the Productivity Commission was likely established with at least the partial purpose of being able to conduct inquiries into competition law issues. The Productivity Commission is modelled on the Australian Productivity Commission, which has conducted inquiries focused on competition issues[1]. We note that the Productivity Commission has sufficient power of inquiry that enable it to inquire into whether markets are operating efficiently, and that they have in fact inquired into and made recommendations on competition law. The Productivity

[1] This includes a study *on Australian and New Zealand competition and consumer protection regimes* (13 January 2005) and an inquiry into whether Australia has the right balance between promoting competition and protecting intellectual property (18 August 2015).

Commission is well suited to conducting market inquiries related to competition law precisely because it was established to advise the government on improving productivity in New Zealand.

While we note that the Issues paper discusses the introduction of a market studies power in the context of considering whether competition within that market is inhibited or how competition could be improved, our view is that there is a significant risk that a regulator undertaking this study will deviate from this focus. For example, the study may become a fishing expedition simply because the regulator is conflicted through being both the policy setter and enforcement agency.

ANZ considers that the banking industry and the 'markets' within that industry are highly competitive, with a large number of participants providing a wide range of consumer choice. This perspective and an analysis of overseas experience indicate the cost of market studies is likely to outweigh any benefits to consumers. In the United Kingdom, market studies have been subject to criticism due to the amount of taxpayer resources they consume and the significant costs they impose on firms in the industries subject to the market studies[2]. Overseas experience also suggests that the burden of market studies tends to fall on particular industries that have a high profile with consumers (such as banking, insurance, groceries, energy and telecommunications). ANZ considers the costs of such market studies are likely to be borne by all market participants and inevitably passed on to consumers. Essentially, this leads to market studies being a tax on consumers in those industries, and as such, any benefit (or not) should be seriously considered before a introducing a power to initiate market studies.

s9(2)(b)(ii)

ANZ's view is that the introduction of voluntary information gathering powers would result in the same outcome as a mandatory power and that this is therefore not a sensible alternative. At the very least businesses would feel compelled to participate despite the voluntary request in order to ensure that the information received by the party completing the study was reflective of the industry as a whole.

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[2] Great Britain: Parliament: House of Commons: Trade and Industry Committee, "*The Work of the Office of Fair Trading: Twelfth Report of Session 2006-07 - Report, Together with Formal Minutes, Oral and Written Evidence*" (Paperback) at page EV52