SUBMISSION TO THE MINISTRY OF ECONOMIC DEVELOPMENT ON THE EXPOSURE DRAFT COMMERCE (CARTELS AND OTHER MATTERS) AMENDMENT BILL 22 JULY 2011

RUSSELL McVEAGH

1. INTRODUCTION

1.1 This submission responds to the Ministry of Economic Development's ("**MED**") invitation for submissions on its *Exposure Draft Commerce (Cartels and Other Matters) Amendment Bill* released in June 2011 ("**draft Bill**").

1.2 As a frequent advisor to clients on the Commerce Act 1986 ("**Commerce Act**") and the use of the New Zealand Commerce Commission's ("**Commission**") processes, Russell McVeagh has advised key corporate clients accused of cartel conduct and is also familiar with the use of the criminalisation process in other jurisdictions.

1.3 Our key submissions are that we have not, in our experience, seen compelling evidence that, from a purely local New Zealand deterrence perspective, criminalisation is necessary nor that the broader New Zealand public's view of cartel conduct demands this move. Indeed, research conducted by the Commission suggests small to medium sized enterprises ("**SMEs**") in the construction sector do not even believe the Commerce Act applies to their behaviour. If international comity and the trans-Tasman single economic market agenda ("**SEM**") demands cartel criminalisation, then the MED must sufficiently resource the Commission to ensure that New Zealand's small businesses understand their obligations before criminal sanctions take effect. Such public education programs would also necessitate the Commission publishing detailed guidelines on the new offences and defences and detailed and binding guidance on when criminal enforcement action will be taken. This submission attaches specific directions on the issues that would need to be addressed in such guidelines at Schedule One.

1.4 Please contact the below partners in respect of any queries in relation to this submission:

Andrew Peterson
Partner
Russell McVeagh
Ph: 09 367 8315
andrew.peterson@russellmcveagh.com

Sarah Keene
Partner
Russell McVeagh
Ph: 09 367 8133
sarah.keene@russellmcveagh.com

2. EXECUTIVE SUMMARY

2.1 Russell McVeagh considers the key reforms proposed in the draft Bill comprise the:

(a) new cartel prohibition;

(b) new "collaborative activities" defence;

(c) new bid rigging defence;

(d) new clearance regime; and

(e) introduction of criminal sanctions.

2.2 We will consider each of these reforms in detail in the submissions that follow.

2.3 We consider there are three further important issues raised by the reform proposal, and we express our views on each at the end of our submission:

(a) the new regime for mergers outside New Zealand;

(b) a dramatic increase in the penalties for offences under s 103 of the Commerce Act; and

(c) no reform of the extraterritorial reach of the Act.

2.4 Before delving into detailed submissions on each of these issues, we outline a high level response to the design decisions set out at paragraph 8 of the MED's explanatory materials:

(a) **Parallel criminal/civil provision**: the criminal prohibition and civil prohibition should be distinguished such that the criminal prohibition stipulates that the provision must have the purpose of price fixing, restricting output, market allocation or bid rigging whereas the civil prohibition prohibits provisions with the purpose, effect, and/or likely effect of pricing fixing, restricting output, market allocation or bid rigging;

(b) **Prosecutorial discretion**: the decision to bring a criminal prosecution should be one of prosecutorial discretion. We do not consider that it needs to be fettered by factors set out in legislation. However guidelines setting out the proposed exercise of that prosecutorial discretion must be consulted on and in place prior to the regime coming in force;

(c) **Cartel prohibition, conduct vs outcome**: in our view the per se prohibition should define the form of conduct that is illegal rather than the outcome. For that reason we are supportive of the proposed approach to the new prohibition on cartel conduct;

(d) **Collaborative activities exemption: substance vs form**: the exemption should focus on the substance of the collaboration rather than defining acceptable forms. Again, for this reason, we are supportive of the proposed collaborative activities exemption;

(e) **Clearance regime**: we are supportive of the concept of a clearance regime, and believe this is long overdue for restrictive trade practices;

(f) **Clearance regime design**: our views on the clearance regime are that it should broadly align with the notification process for collective bargaining and exclusive dealing in Australia. We will expand on the proposed regime design further in our submission.

2.5 In the event that criminalisation is not introduced, we are strongly of the view that the draft Bill proposes a number of positive amendments to the Commerce Act, which we are broadly supportive of regardless of whether cartel conduct is criminalised.

3. PRICE FIXING

3.1 We are generally supportive of the proposed redraft of s 30. It expressly incorporates the Organisation for Economic Co-operation and Development's ("**OECD**") categories of hard core cartel conduct,[1] being price fixing, restricting output, market allocation and bid rigging. The new provision aligns the substantive elements of the prohibition with Australia, in accordance with SEM objectives. Alignment with the Australian provision will also contribute to the certainty of the regime, as judicial interpretation of the Australian provision can be used to guide its likely application in New Zealand.

Definition of cartel conduct

3.2 Section 30 as it currently stands is widely regarded as being uncertain in scope. For example, commentators and practitioners disagree whether s 30 extends to prohibit market allocation, a non-price related cartel arrangement. Some lawyers and an academic[2] suggest that customer allocation is not price fixing. However, the penalty decision in *Commerce Commission v Eli Lily*[3], Commission speeches[4] and commentary under the Australian Competition and Consumer Act 2010 ("**Competition and Consumer Act**") suggest that market allocation is capable of "maintaining price", and thus susceptible to the per se prohibition on price fixing. This is just one example of unacceptable uncertainty under the existing price fixing prohibition, which has not been alleviated by guidelines from the Commission on the substantive application of the prohibition. It is trite that criminalisation of an uncertain provision would be contrary to the rule of law. It is therefore positive that the proposed prohibition more clearly articulates the conduct captured and better facilitates adoption of international precedent. Under the proposed redraft of s 30, businesses will at least be in a better position to assess whether such conduct risks breaching the Act.

3.3 While the proposed cartel definition is, on balance, an improvement on the existing price fixing prohibition, we are nonetheless concerned that businesses are not sufficiently aware of the type of conduct that will be caught by the prohibition. There is likely to be considerable debate around the edges of the prohibition. One area of the law that readily springs to mind is the debate surrounding input pricing; specifically, whether a price fixing arrangement in an upstream market has the ability to fix, control or maintain prices in a downstream market.

3.4 On a technical view, any agreement between A and B (whether it relates to prices or not) which incidentally controls the prices at which they both either acquire or supply in competition with each other, will be deemed to contravene s 30.[5] The Commission adopted this position in the Interchange Proceedings, which concerned the interchange service fee agreed between major retail banks and credit card providers, Mastercard and Visa.

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[1] International Competition Network, "*Defining Hard Core Cartel Conduct: Building Blocks for Effective Anti Cartel Regimes*", presented at ICN 4th Annual Conference, Bonn, Germany, 6-8 June 2005.

[2] Scott, Paul, 'Unresolved Issues in Price Fixing: Market Division, the Meaning of Control and Characterisation', 12 *Canterbury Law Review* 197 at 199.

[3] *Commerce Commission v Eli Lily* High Court, Auckland, Fisher J, 30/4/99.

[4] Paula Rebstock "Speech to the New Zealand Institute of Management", 21 March 2007, (available at www.comcom.govt.nz/MediaCentre/Speeches/speechtothenewzealand instituteofma.aspx):

> ...section 30 of the Act... prohibits price fixing, **market sharing** and bid rigging...

[5] This reasoning is based on *ACCC v Concrete Constructions (NSW)* (1999) 92 FCR 375; 165 ALR 468.

3.5 This interpretation of s 30 is widely regarded as problematic, in that it appears to capture as a per se breach conduct that is not likely to substantially lessen competition. In a paper entitled, "*Dare to Deem - Does s 45A Trade Practices Act Prohibit "Pro-Competitive" Price Fixing?*", the authors Aldo Nicotra and James O'Regan,[6] argue that the application of s 45A of the Trade Practices Act 1974 (now the Competition and Consumer Act 2010) to input supply arrangements catches conduct that does not fit within society's conception of the archetypal cartel arrangement. "Input supply arrangements" describe the not uncommon scenario where parties to an arrangement, while not competitors with respect to the supply of the input, are competitors with respect to the downstream or final product. On the current interpretation of the law, such arrangements risk per se liability under the Act, despite the fact that the "input" component may represent a fraction of the price of the downstream or final product. The authors persuasively argue that input supply arrangements are unlikely to control or maintain price unless the parties collectively have market power in the market for the downstream product, however the per se nature of the prohibition does not allow for this degree of flexibility in interpretation.

3.6 The debate on input pricing illustrates the difficulty, particularly for lay people, in understanding how concepts like price fixing apply to ordinary business practices. We will return to this point in more detail in our submission on the merits of criminalising cartel conduct, however do flag this definitional complexity as a real issue, particularly when criminal liability is at stake.

Purpose only test

3.7 Under the proposed cartel prohibition, the provision must have the purpose (not effect) of substantially lessening competition. While this may reduce need for economic evidence, and decrease the length and complexity of trials, analysis of "purpose" can be fraught. While it is clear that is the purpose of the *provision* and not the person that is relevant, particular difficulty surrounds the objective/subjective nature of the test. In *ANZCO Foods Waitara Ltd v AFFCO New Zealand Ltd*,[7] the objective test was upheld. Under this test, you are presumed to have the purpose of intending the likely consequences of your actions. We comment that an objective test brings the analysis quite close to an "effects" test, as it requires an assessment of what the likely consequences of your actions are.

Parallel civil/criminal provision

3.8 As currently drafted, the draft Bill contains a parallel civil/criminal cartel prohibition. This mirrors the design of the Australian prohibition. While we support a combined purpose/knowledge threshold for the criminal prohibition, we submit that the civil prohibition should retain the references to purpose, effect or likely effect in the existing s 30. The reasons for this proposed distinction are threefold:

(a) where the Commission decides to proceed civilly, it is often a defendant's position in a settlement that the defendant did not have the *purpose* of substantially lessening competition or price fixing as the case may be, but that the provision may have inadvertently or "technically" had that effect. This flexibility should be retained;

(b) in the criminal context it is likely that establishing purpose will require a high threshold test, which may conversely set the bar high in civil proceedings. For this reason it is better to have a distinguishing standard for the civil prohibition; and

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[6] At the time of publication, both authors were partners at Blake Dawson Waldron. Aldo Nicotra is now a partner at Johnson Winter & Slattery.

[7] *ANZCO Foods Waitara Ltd v AFFCO New Zealand Ltd* [2006] 3 NZLR 351 (CA).

(c) in the criminal context we agree that purpose and knowledge as a combination are the appropriate touchstones for determining criminal liability, and agree with the reasoning set out by the MED regarding the removal of effect/likely effect as a basis for imposing criminal liability.

Prosecutorial discretion

3.9 At a high level, we agree that the decision of whether to initiate civil or criminal proceedings should be a matter of prosecutorial discretion. This aligns with the practice in relation to similar criminal offences (for example, offences under the Securities Act 1978 and the Securities Markets Act 1988), and is the approach taken in Australia.

3.10 The explanatory materials indicate that guidelines for the exercise of prosecutorial discretion will be developed by the Commission along the lines of those published by the Australian Competition and Consumer Commission ("**ACCC**"). Our initial concern is that the ACCC guidelines are neither binding on the Commission, or subsequent Commissions, nor exhaustive. It is crucial to have a clear and transparent decision making process when the outcome could affect a person's liberty. We support prosecutorial guidelines so long as they are exhaustive, clear and binding on both this Commission, and subsequent Commissions. We agree that it is not necessary to prescribe factors in the legislation.

3.11 We set out our initial views on the appropriate factors to be included in the prosecutorial guidelines at Schedule One.

4. COLLABORATIVE ACTIVITIES EXEMPTION

4.1 We are broadly supportive of the new collaborative activities exemption.

4.2 Provided it is applied as it appears to be conceived, it would be a marked improvement on the current joint venture exemption, which is unacceptably uncertain in scope and application, and has been much maligned by academics, practitioners and the business community. There is little in the way of conclusive case law on the provision and, despite being in force for 25 years and high profile cases showing differences in interpretation, the Commission has not published guidelines on its application.

4.3 In particular, we believe that the substance over form approach to drafting the collaborative activities exemption is desirable. This recognises that collaborative activities can take many forms, and allows business to help shape the scope of what is a pro-competitive collaborative activity, rather than structuring their arrangements to fit within a proscribed form.

4.4 The proposed exemption appears, on its face, to be sufficiently flexible to cover a wide range of activities. The flipside to the broad wording of the exemption is that it may be unclear what its precise parameters are. However, it is likely that this issue can be addressed by the publication of detailed guidelines from the Commission on its intended scope and application.

4.5 We expand on our very real concerns regarding the reverse onus for establishing the exemption in the discussion on criminalisation.

4.6 We note that the collaborative activities defence is inconsistent with the Australian joint venture exemption. While this detracts from trans-Tasman alignment and SEM objectives, the Australian joint venture defence has been criticised as being too restrictive to permit legitimate collaborative activities. In particular, criticism has been directed at the fact that it requires the collaboration to be in the form of a joint venture,

where there are of course many forms of pro-competitive collaboration between competitors that are not joint ventures. The Australian joint venture exemption is also unduly limited to contracts (or where the parties reasonably believed that they had entered into a contract), and to production or supply joint ventures (as distinct from joint ventures for acquisitions). Accordingly, we support the MED's decision to diverge from the Australian approach in this respect.

Comparison with ancillary restraint doctrine

4.7 We understand that the MED has modelled the collaborative activities exemption on the doctrine of ancillary restraint, prevalent in antitrust law in the United States and Canada. Given the analogies between the ancillary restraints doctrine and the proposed collaborative activities exemption, it is likely that jurisprudence from the United States and Canada will assist the interpretation of the exemption in New Zealand.

4.8 The "ancillary restraint" defence was establish in United States case law, and has since been adopted and codified by Canada in the Competition Act 1985 (CA).[8]

4.9 An agreement is ancillary if it is "subordinate and collateral to another legitimate transaction and necessary to make that transaction effective".[9] Ancillary is a question of fact on which the defendant has the burden of proof.

4.10 In the United States, for a restraint to be ancillary it should be "reasonably necessary" to achieve a pro-competitive objective.[10] This test is reflected in the wording of the s 45 of the Competition Act 1985, and s 31(b) of the draft Bill. The Department of Justice *Antitrust Guidelines for Collaborations Among Competitors* state:

> An agreement may be "reasonably necessary" without being essential. However, **if the participants could achieve an equivalent or comparable efficiency-enhancing integration through practical, significantly less restrictive means, then the Agencies conclude that the agreement is not reasonably necessary.** In making this assessment, except in unusual circumstances, the Agencies consider whether practical, significantly less restrictive means were reasonably available when the agreement was entered into, but do not search for a theoretically less restrictive alternative that was not practical given the business realties. [emphasis added]

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[8] Section 45(4):

> No person shall be convicted of an offence under subsection (1) in respect of a conspiracy, agreement or arrangement that would otherwise contravene that subsection if
>
> (a) that person establishes, on a balance of probabilities, that
>
> (i) it is ancillary to a broader or separate agreement or arrangement that includes the same parties, and
>
> (ii) it is directly related to, and reasonably necessary for giving effect to, the objective of that broader or separate agreement or arrangement; and
>
> (b) the broader or separate agreement or arrangement, considered alone, does not contravene that subsection.

[9] *Dagher v Saudi Refining, Inc*, 369 F 3d. 1108 (2004); overturned on appeal *Texaco Inc v Dagher* 547 U.S. 1 (2006).

[10] *Los Angeles Memorial Coliseum Comm'n v. National Football League*, 726 F. 2d 1381, 1395-1396.

4.11 The ancillary restraints defence has been problematic. *Dagher v Saudi Refining, Inc*,[11] a decision of the United States Court of Appeals for the Ninth Circuit, wrongly applied the ancillary restraints doctrine to an agreement solely relating to the joint venture's own conduct. That judgment suggested that joint venture partners could be required to justify every choice they make about what the venture does or how it is done as reasonably necessary to the achievement of pro-competitive ends. Conversely, the position arrived at by the United States Supreme Court on appeal,[12] exempting "core" constraints, is ill-defined and a recipe for evasion.

Reasonably necessary

4.12 We are concerned that the "reasonably necessary" threshold could lead to the Commission second guessing commercial decisions. In our view, the Commission is poorly placed to make detailed assessments of what would or would not be sufficient restraints for a commercial transaction to proceed on terms acceptable to parties.

4.13 The explanatory materials indicate the reasonably necessary threshold is designed to follow the "least restrictive alternative" test from United States jurisprudence. That test involves a consideration of whether the purpose of the collaborative activity could be achieved without the restriction imposed by the cartel provision. Unlike the counterfactual analysis, which requires a broad assessment of likely market structure and dynamics in the future, this type of analysis is more akin to a "line by line" scrutiny of how the parties could, or should, have conducted their affairs. We note that the Commission already conducts a similar analysis in the merger context when applying the "Failing Firms Guidelines". The Commission is not always well placed to determine whether a firm is actually failing, leading to an arguably overly conservative approach to that question being adopted by the Commission. This is particularly evident when compared with the standard business understanding of when a firm is "failing".

4.14 While we are wary that an application of the reasonable necessity test could lead to inappropriate interference with commercial decision making, we acknowledge that this will always be a matter of practical implementation, hence our insistence that guidelines must be issued on the exact scope of the exemption prior to it coming into force.

For the dominant purpose of lessening competition

4.15 The wording of limb 31(2)(b) of the collaborative activities exemption appears to reflect the view put forward by Beaton-Wells and Fisse in the text, *Australian Cartel Regulation*.[13] The authors (at pp 293-294) express the view that the Australian joint venture exemption should be amended to cover the broader concept of "collaborative ventures". Beaton-Wells and Fisse propose that the exemption should be drafted "specifically to exclude cases where the common purpose is unlawful or the dominant purpose of a cartel provision is to cease or avoid competition between the parties to the venture".

4.16 We agree that the collaborative activities exemption needs to distinguish legitimate and genuine forms of co-operation from "sham" ventures, which are designed to avoid the per se prohibition on cartel conduct. In our view, the "dominant purpose" requirement in s 31(2)(b) is likely to assist a court in drawing on the "sham" test in United States jurisprudence, which requires the Court to assess whether the collaboration has a genuine or legitimate purpose.

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[11] *Dagher v Saudi Refining, Inc*, 369 F 3d. 1108 (2004).

[12] *Texaco Inc v Dagher* 547 U.S. 1 (2006).

[13] Beaton- Wells, C, and Fisse, B, *Australian Cartel Regulation: Law, Policy and Practice in an International Context*, Cambridge University Press, New York, 2011.

4.17 We do, however, consider that requiring the purpose to be a "dominant purpose" adds uncertainty to the exemption. Once it is established that an arrangement has a purpose of lessening competition, it is very difficult to then determine whether that purpose was in fact a dominant purpose. It is likely to be difficult to differentiate between hierarchies of purpose and any analysis will also be highly fact dependant. In our view, it will be difficult to advise with any certainty on the distinction between "purpose" and "dominant purpose" and, accordingly, consider that the word dominant should be removed.

In a market?

4.18 We also consider that the collaborative activities exemption should include a reference to lessening competition **in a market.** This is because collaborative arrangements can often have the purpose of lessening competition as between the two parties to the arrangement but not the purpose and/or effect of lessening competition in the market as a whole. It is important that the collaborative activities exemption applies easily to arrangements that do not have the purpose of lessening competition in the market as a whole. We are aware that the MED did not want to import a competition test to the exemption, to retain its per se nature. However, in our experience parties often have a view about the pro-competitive effects of a collaborative arrangement but may readily admit a purpose of the arrangement is to reduce competition between those two parties in certain limited respects. For this reason, we think the test should be not for the purpose of substantially lessening competition "in a market" (and believe that the words "in a market" are most likely to be read in by a court in any event).

5. VERTICAL SUPPLY ARRANGEMENTS

5.1 The new cartel prohibition is clearly targeted at horizontal conduct, ie arrangements between competitors. However, we submit that the prohibition could be prone to overreach as it does not exclude vertical arrangements, despite the MED recording the view that vertical conduct between entities in different parts of the supply chain can be pro-competitive and should not be prohibited.[14]

5.2 Section 30B defines a competitor broadly to include interconnected bodies corporate:

> **30B Additional interpretation relating to cartel provisions**
>
> (1) in this Act, in relation to a cartel provision, -
>
> (a) if a person is a party to a contract, arrangement or understanding, each of the person's interconnected bodies corporate is taken to be a party to the contract, arrangement or understanding; and
>
> (b) **if a person (person A) or any of person A's interconnected bodies corporate acquires or supplies goods or services in competition with another person (person B) or any of person B's interconnected bodies corporate, person A is taken to acquire or supply those goods or services in competition with person B.**
>
> (2) In this Act, in relation to a cartel provision, a reference to persons in competition with each other includes a reference to persons who, but for the cartel provision, would, or would be likely to, be in competition with each other in a market. [emphasis added]

5.3 Section 30B extends the definition of "in competition" by providing that if any of person A's interconnected bodies corporate compete with person B or any of person B's interconnected bodies corporate, person A is taken to be in competition with person B. A classic example would be a manufacturer/supplier with a downstream retail presence.

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[14] MED, Explanatory materials, 3.4.3, paragraph 38.

In our practice, we commonly come across supply arrangements with vertically integrated companies that risk liability under the per se price fixing provisions in the Commerce Act, despite in many cases being unlikely to substantially lessen competition.

5.4 For example, in 1998, the Commission took action in respect of an inadvertent breach of s 30 by a vertically integrated company.[15] The company was a wholesaler that also had a presence in the downstream retail market. The Commission was concerned that a maximum price provision in the company's wholesale supply agreements with other retailers would have the effect of "controlling" price in the retail market, in which that vertically integrated company was also a competitor. In this case, the Commission accepted a settlement whereby the company concerned agreed to remove the maximum price provision from its terms of trade with participating retailers.

5.5 In our experience, this technical approach to s 30 risks chilling legitimate and even pro-competitive conduct. The effect of the view taken by the Commission in relation to that wholesaler's supply arrangements is that vertically integrated companies cannot set a maximum retail price in supply agreements, even, for example, when that company is giving discounts for a promotional period.

5.6 The MED acknowledges that vertical supply arrangements are commonplace and generally considered to enhance consumer welfare. While the draft Bill does not currently provide a specific exemption for vertical supply arrangements, the MED states that a specific exemption may be necessary if the exemption for collaborative activities does not capture these arrangements.[16]

5.7 In our view, it is not clear that the collaborative activities exemption can extend to cover vertical arrangements. This is primarily because a vertical arrangement is not *an activity carried on in cooperation by two or more persons*, as required by s 31(2)(a), because interconnected bodies corporate are taken to be the same person. It is also unlikely that vertical supply arrangements meet the threshold of "reasonably necessary for the purpose of the collaborative activity" (s 31(1)(b)).

5.8 Accordingly, to address this issue, there needs to be a specific exemption from the cartel prohibition for vertical conduct.

6. BID RIGGING DEFENCE

6.1 Our feedback on the new bid rigging defence is generally positive. It allows parties to form bidding consortia and submit syndicated bids if they have obtained prior approval from the vendor. Bidding consortia and syndicated bidding are recognised as potentially pro-competitive by enabling greater participation in tenders by firms that are too small to "go it alone". This increases the competitive tension in the bid process, and can dislodge incumbents by introducing dynamic competition to the market.

6.2 The vendor approval process makes the defence transparent, and doubles as an anti-avoidance mechanism. However this transparency could also create unintended liability for bidders. If a vendor refuses to consent to a bid rigging proposal, there is a risk that the bidders could be subject to proceedings for cartel conduct arising from their subsequent actions. For example, in the case that either:

(a) neither party bids independently; or

(b) only one party proceeds with a bid (assuming the bid is less favourable to the vendor).

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[15] See Commerce Commission media release of 14 August 1998.

[16] MED, Explanatory Materials, at 3.7.4, paragraph 62.

the Commission could allege that the parties were so acting in accordance with an understanding to only bid at a certain price by way of a joint bid. Evidence of this understanding would be that the parties submitted a joint bid, and then acted in accordance with a prior understanding by either failing to bid independently, or bidding at a higher price than proposed under the joint bid.

6.3 It would be inappropriate to affix bidders with criminal liability for this type of conduct, particularly as it is anything but covert. Accordingly, the Commission's proposed approach to this scenario must be addressed in guidelines on the application of the bid rigging exemption.

Other jurisdictions

6.4 While Australia does not have an equivalent defence,[17] the Canadian legislation provides a carve out for notified bid rigging conduct:

> **COMPETITION ACT 1985 (CA)**
>
> **47. Definition of "bid-rigging"**
>
> (1) In this section, "bid-rigging" means
>
> > (a) an agreement or arrangement between or among two or more persons whereby one or more of those persons agrees or undertakes not to submit a bid or tender in response to a call or request for bids or tenders, or agrees or undertakes to withdraw a bid or tender submitted in response to such a call or request, or
> >
> > (b) the submission, in response to a call or request for bids or tenders, of bids or tenders that are arrived at by agreement or arrangement between or among two or more bidders or tenderers, **where the agreement or arrangement is not made known to the person calling for or requesting the bids or tenders** at or before the time when any bid or tender is submitted or withdrawn, as the case may be, by any person who is a party to the agreement or arrangement.
>
> (2) Every person who is a party to bid-rigging is guilty of an indictable offence and liable on conviction to a fine in the discretion of the court or to imprisonment for a term not exceeding 14 years, or to both.

6.5 The Canadian provision is framed differently to the proposed bid rigging exemption in New Zealand. Rather than having a separately defined prohibition and exemption, the definition of the bid rigging prohibition itself contains a carve-out for agreements that are notified to the person calling for the bids.

6.6 If New Zealand were to adopt the design of the Canadian legislation, this would likely avoid the issue raised above at paragraph 6.2 regarding liability for prior understandings.

7. CLEARANCE REGIME

7.1 While under the current law parties can seek authorisation for restrictive trade practices, the Commerce Act does not provide a clearance procedure for restrictive trade practices. Russell McVeagh supports the concept of a new clearance regime for collaborative activities; however we make a number of submissions on regime design.

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[17] Commentators in Australia have observed that the lack of such defence could subject potentially legitimate conduct to per se criminal liability.

7.2 The proposed clearance regime for collaborative activities has two limbs:

(a) the cartel provision must be "reasonably necessary" for the purposes of a collaborative activity; and

(b) the collaborative activity would not have, or would not be likely to have, the effect of substantially lessening competition.

7.3 The proposed regime is similar in many respects to the merger clearance regime in that:

(a) it is prospective (ie obtained *before* engaging in the conduct);

(b) the applicant parties must show that the collaborative activity would not have, or would not be likely to have, the effect of substantially lessening competition; and

(c) the procedure for obtaining a clearance is publicly notified.

7.4 Like the mergers regime, the proposed clearance procedure is likely to assist the Commission to become more familiar with commercial conduct. If well utilised, it also has the potential to develop a body of (non-binding) precedent, which will help create clarity and certainty under the new law, and may provide guidance for future arrangements.

Clearance vs collaborative activities exemption

7.5 The key difference between clearance and the collaborative activities exemption is that clearance provides protection against prosecutions under sections 27 (substantial lessening of competition), 29 (exclusionary provisions) and 30 (cartel prohibition), whereas the collaborative activities exemption only provides protection against prosecutions under s 30 (cartel prohibition).

7.6 Commensurate with the greater protection extended, to gain clearance the applicant must satisfy a higher threshold than is required to fit under the collaborative activities exemption. Clearance will be granted if the applicant satisfies the Commission that the provision does not have the purpose of substantially lessening competition, whereas the collaborative activities exemption provides a defence (from s 30 only) if the dominant purpose of the provision is not to lessen competition.

7.7 While we appreciate that the threshold for the collaborative activities exemption (dominant purpose of lessening competition) is set deliberately low, we consider the departure from the established test (ie substantial lessening of competition) could create undesirable uncertainty.

Clearance for existing arrangements

7.8 While there is a transitional regime for agreements entered into in the six months before the proposed amendments come into force, it is not possible to obtain clearance to give effect to agreements entered into before the transitional period.

7.9 We oppose the position set out in the draft Bill whereby the Commission cannot grant clearance for existing arrangements. It is arguable that the new cartel prohibition significantly extends the scope of the existing prohibition in s 30. Accordingly, parties who have taken the view that their conduct is not caught by s 30 as it is currently drafted may come to a different view under the new provision.

7.10 To address this issue, we consider that the draft Bill should be altered so that parties to existing arrangements are either:

(a) able to obtain clearance for the existing arrangement; or

(b) exempt from the new cartel prohibition in respect of the implementation of that existing arrangement.

7.11 An alternative approach would be to limit liability for giving effect to a cartel provision in a contract, arrangement or understanding to contracts, arrangements or understandings entered into after, say 1 July 2011, and to enable clearance to be sought for any contracts arrangements or understandings entered into after that date.

7.12 Other possible issues associated with the clearance regime include:

(a) the public nature of the process: our experience suggests that a significant drawback of the authorisation procedure for restrictive trade practices is the extensively public nature of the process. In our experience, commercial parties do not wish to expose their commercial arrangements to a high degree of public scrutiny. In this regard, clearances for restrictive trade practices are different to clearances for business acquisitions. Acquisitions are deserving of greater scrutiny as they affect the *structure* of a market, whereas arrangements made under s 30 may be temporary;

(b) the parties to the arrangement must admit that the arrangement contains a cartel provision;

(c) the proposed regime contains no provision for behavioural undertakings; and

(d) parties cannot get clearance for resale price maintenance ("**RPM**").

Alignment with Australia

7.13 In Australia, there is a process whereby parties can notify the ACCC of exclusive dealing or collective bargaining arrangements. If the ACCC does not issue an objection notice (which it may do at any time) the parties are free to engage in the notified conduct for a period of three years with comfort that the ACCC will not prosecute under the competition provisions of the Competition and Consumer Act 2010.

Process

7.14 Two key benefits of the notification process are the low cost (application fee of between $100 and $2,500) and the short timeframes.

Exclusive dealing

7.15 Pursuant to s 93(1) of the Competition and Consumer Act, a corporation that engages, or proposes to engage in exclusionary conduct (prohibited by s 47), may give the ACCC a notice setting out particulars of that conduct.

7.16 The ACCC may issue an objection notice if it is satisfied that the conduct would have the purpose, effect or likely effect of substantially lessening competition, and that the public benefits of the conduct do not outweigh the detriments (s 93(3) and 93(3A)).

7.17 If the ACCC does not formally object, immunity for the conduct will commence 14 days after the notification is lodged for notifications involving third line forcing, or from the date of notification for notifications involving exclusive dealing conduct other than third line forcing.

Collective bargaining

7.18 Pursuant to s 93AB of the Competition and Consumer Act, a corporation can give notice to the ACCC that it has made or proposes to make, or proposes to give effect to a contract (**initial contract**) containing a cartel provision, or a provision that has the purpose or has or would be likely to have the effect of substantially lessening competition. There are three provisos:

(a) the initial contract between the contracting parties must relate to the supply or acquisition of particular goods or services to or from another person (the **target**);

(b) the corporation must reasonably expect that it will make one or more contracts with the target about the supply or acquisition of one or more of those goods or services;

(c) the corporation must reasonably expect that the value of the contract(s) will not exceed $3,000,000 in any 12 month period.

7.19 Upon receipt of the notice, the ACCC may issue an objection notice if it considers that either (s 93AC):

(a) in respect of a cartel or per se provision, the benefits of the provision do not outweigh its detriments; or

(b) in respect of a competition provision, the provision has or would have the purpose, effect or likely effect of substantially lessening competition *and* the benefits of the provision do not outweigh its detriments.

7.20 If the ACCC does not issue an objection notice within 14 business days of receipt of the notice, or determine to hold a conference in respect of the collective bargaining notice within the same period, the contracting parties are immune to challenge from the ACCC under the competition provisions of the Competition and Consumer Act in respect of the notified conduct. This immunity lasts for three years, although the ACCC can object to the notified conduct at any time during the three year period (s 93AD(3)(b)).

7.21 The ACCC is required to keep a public registrar of the notifications it receives. Each notification is published on the ACCC website, with a short description of the notified arrangement, and brief commentary on the markets affected and the reasons for or against granting immunity from ACCC prosecution.

7.22 If there is a valid notification in place, there is no breach of a cartel prohibition (s 44ZZRL, Competition and Consumer Act). This provides immunity from third party actions.

7.23 We consider many aspects of the Australian exclusive dealing and collective bargaining notification process to be superior in many respects to the proposed clearance regime. Russell McVeagh supports the introduction of a similar regime in New Zealand, not least due to the trans-Tasman synergies it would create, but also for the certainty it would afford businesses, without the attendant costs and publicity associated with the authorisation process.

8. SHOULD CARTELS BE CRIMINALISED IN NEW ZEALAND?

8.1 Our submissions on the merits of criminalisation echo our previous submission on the MED's Discussion Document. While we accept the benefits arising from greater international co-operation and alignment with Australia, we are not convinced that the

claimed deterrent effect of criminalisation outweighs or compensates for the chilling effect it will have on pro-competitive behaviour and the increased costs of doing business in New Zealand. Criminal sanctions are unlikely to be used frequently by the Commission, and on a strict cost / benefit analysis, we doubt that the costs of implementing a criminal regime are justified given the size and characteristics of the New Zealand economy. In particular, we consider the administration and enforcement costs may be disproportionate to the benefit of criminal sanctions.

8.2 Without a compelling case based on international comity, it is not something that we think New Zealand requires when looked at in isolation. It is possible there is a case for it from an international and SEM perspective. For example, the ability to cooperate with key trading partners (such as the United States, the United Kingdom and Australia), and extradite New Zealand nationals that engage in cartel conduct in those countries may to a benefit arising from cartel criminalisation. However, if these reforms are justifiably driven by those international objectives, it is surprising the Commission has not made this point in support of the draft Bill to date.[18] We are also concerned that our perception of the lack of understanding in the New Zealand business community of the case for cartel criminalisation based on international comity and SEM objectives indicates that the MED has not properly articulated those benefits.

8.3 As the MED recognises, criminalisation is an extraordinarily onerous remedy, and imports considerations under the Bill of Rights Act 1990 (**"Bill of Rights"**), and requires that procedures are duly followed to ensure a fair trial results. We understand the Commission has informally acknowledged that this means they will have to open practically all investigations as criminal investigations, which makes their internal processes more cumbersome.

8.4 Even with the proposed reforms that clarify and simplify the test for cartel conduct, which we endorse, our discussion of the "grey areas" surrounding the prohibition demonstrate that it is not a simple matter. There are two key issues that in our view must be carefully considered in the context of the policy decision to criminalise cartel conduct:

(a) Complexity and uncertainty of the prohibition; and

(b) Limited knowledge and awareness of the prohibition in the business community.

8.5 The feedback we have received from clients suggests that the prospect of criminalisation is even more of an issue for SME's than it is for larger entities, which generally have in-house legal teams and a more sophisticated understanding of the laws that apply to business. Given that SMEs represent a significantly larger proportion of our economy than in many other countries, this is a real concern.

Complexity and uncertainty

8.6 As a general comment, it is well recognised that matters under the Commerce Act are inherently complex. In *NZ Bus v Commerce Commission*,[19] Hammond J comments on

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[18] We note that the Cabinet Paper on Criminalisation of Cartels records (at paragraph 17):

> In order to reduce barriers to trans-Tasman trade, the Government has committed to a high-level outcome under the Single Economic Market agenda of ensuring that those who engage in anti-competitive behaviour in Australia or New Zealand face the same penalties [ERD Min (09) 10/1].

[19] *Commerce Commission v NZ Bus* [2008] 3 NZLR 433.

the jurisprudential difficulties of imposing significant penalties under the Commerce Act in this context:[20]

> [195] At the other end of the scale, **there may be some uncertainty in the definition of the prohibited conduct or the application of that definition to particular cases. Heavy penalties may have the effect of deterring lawful conduct at the margin**, requiring potential defendants to steer too far clear of the intended zone.
>
> [196] These sorts of issues have given rise to a vast law and economics literature, and some of the more complex techniques of analysis ever employed in a legal context. [emphasis added]

8.7 Few would disagree that it is unsound to impose criminal liability in circumstances where the bounds of legitimate and illegitimate conduct are not clearly delineated. As articulated by Lord Bingham of Cornhill:[21]

> No one should be punished under a law unless it is sufficiently clear and certain to enable him to know what conduct is forbidden before he does it.

8.8 In light of the uncertain and complex nature of determining liability under the Commerce Act, we submit that the decision to criminalise cartel conduct is not one that should be taken lightly.

Lack of understanding/knowledge

8.9 The Commission's survey of the construction sector in 2010[22] aptly demonstrates the limited awareness of the Commerce Act and how it applies to businesses. Of those businesses surveyed who were aware of the Commission (close to 95 per cent), only 58 per cent believed the Commerce Act applied to them compared to 83 per cent for the Fair Trading Act 1986 ("**FTA**"). The Commission's findings were that, despite engaging in or being familiar with cover bidding (bid rigging), most thought cartels were only engaged in by large, international organisations. This is alarming, but hardly surprising, given the Commission's exclusive focus on enforcement in the cartel space is against large international companies.

8.10 This lack of understanding and knowledge is unlikely to be confined to the construction sector. It is trite that conduct should only attract significant criminal sanctions if society considers that conduct to be harmful or morally wrong. If the Commission's survey of the construction sector is a proxy for small business's perception and understanding of the Commerce Act, this is a significant concern for the proposed reform.

8.11 Certainly if criminalisation is introduced (and even if it is not), it is essential that the Commission is properly resourced to educate, and is encouraged to enforce the law not only against large international corporations.

9. MENTAL ELEMENT FOR ESTABLISHING CRIMINAL LIABILITY

9.1 We agree that purpose and knowledge is the appropriate touchstone for finding a person criminally liable for cartel conduct.

9.2 It is accepted that to be criminally liable, a person must have knowledge of the essential facts giving rise to the contravention, but need not be conscious that the facts establish

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[20] Ibid, [195]-[196].

[21] *R v Goldstein: R v Rimmington* [2005] UK HL 63; [2006] 2 All ER 257; [2006] 1 AC 459; [2005] 3 WLR 982 at [33].

[22] Commerce Commission, *Construction Sector Research - Key Findings*, 2010, available at http://www.comcom.govt.nz/construction-sector-research-key-findings/

a contravention of the Act. This test accords with the fundamental principle that ignorance of the law is no excuse (Crimes Act 1961 ("**Crimes Act**"), s 25).

9.3 A more difficult question concerns the standard of knowledge that is required to affix criminal liability. The test under existing (civil) provisions of the Commerce Act is stated in the Court of Appeal commentary on "knowingly concerned" in *NZ Bus*:

(a) the court rejected the "degrees of knowledge" approach as unworkable;

(b) Hammond J preferred "dishonest participation" as the touchstone for determining accessory liability; and

(c) Arnold J took the more orthodox view that intentional participation (ie knowledge of the essential facts which constitute the breach) was sufficient to find accessory liability.

9.4 In our view, dishonest participation is not an appropriate standard for assessing liability under the cartel prohibition.

9.5 We observe that other statutes imposing criminal sanctions for regulatory/economic crimes do not require a uniform standard of knowledge. For example, under the Securities Markets Act 1988 ("**SMA**"), offences for insider trading etc require actual knowledge, whereas offences under the FTA are strict liability offences.

9.6 In terms of seriousness, cartel offences are much more akin to offences under the SMA than those under the FTA. Accordingly, we consider that a similarly high standard of knowledge should be required to establish criminal liability for cartel offences. Further, while we are not convinced that society is sufficiently aware of the wrongfulness or harm caused by cartel conduct, a high threshold test is also required to justify criminal sanctions to accord with the policy that you should only be criminally liable for conduct that you know to be wrong or harmful. In our view, criminal liability for cartel offences should only be imposed when a person has **actual knowledge** of the essential facts giving rise to the contravention.

10. REVERSE BURDEN

10.1 We are strongly of the view that the reverse onus provision proposed by s 82B(2) is not appropriate. Section 82B(2) provides:

> If a defendant wishes to rely on the exemption relating to cartel provisions in section 31 [the collaborative activities exemption], it is for the defendant to prove, on the balance of probabilities, that -
>
> (a) the exemption applies; or
>
> (b) the person believed, at the time when the contract or arrangement was entered into, or the understanding was arrived at, or when the cartel provision was given effect to (as the case may be), that -
>
> (i) the parties were involved in a collaborative activity; and
>
> (ii) the cartel provision contained in the contract, arrangement or understanding was reasonably necessary for the purpose of the collaborative activity.

10.2 When faced with the substantial resources of the State, it is unfair for a defendant in cartel proceedings to bear the burden of proving, even on the balance of probabilities,

that their conduct is exempt under the Act. While it would be sensible for the defendant to bear an evidential onus, the prosecution should bear the burden of proving that the collaborative activity exemption does not apply on the facts of any given case. This would align with the position in Australia, where there is no reverse onus for the joint venture exemptions.

10.3 The MED contends that "the departure from the ordinary burden of proof on the prosecution in criminal cases seems justified because the exemption involves complex arrangements which are within the peculiar business knowledge of the defendant".[23] In our view, the extensive information gathering powers afforded to the Commission under the Commerce Act weighs against this justification. Conversely, it is likely to be administratively difficult for defendants to assert that their conduct was reasonably necessary to achieve the purpose of the arrangement, as this will presumably require the defendant to prove that there was no practical alternative to the cartel provision at the time of entering into the arrangement.

10.4 We submit that not only will the reverse burden chill potentially pro-competitive activity, it also runs into Bill of Rights issues.

10.5 Reverse onus provisions are generally regarded to breach the presumption of innocence in s 25(c) of the Bill of Rights, and there is considerable debate as to whether reverse onus provisions can ever constitute a reasonable and justified limitation on this right.[24]

10.6 The reverse onus provision in s 6(6) of the Misuse of Drugs Act 1975 was subject to intense judicial scrutiny in a series of decisions culminating with the Supreme Court's decision in *Hansen v R*.[25] There, the Supreme Court found that the reverse onus provision was inconsistent with the Bill of Rights, and, further, did not constitute a reasonable limitation that could be demonstrably justified in a free and democratic society. While, applying s 4 of the Bill of Rights, s 6(6) of the Misuse of Drugs Act was allowed to stand in this case, the Supreme Court clearly articulated its disapproval of reverse onus provisions.

10.7 We are not aware of another criminal offence, with a seven year maximum, which contains such a reverse onus. The essence of the offence is the conscious entering into or giving effect to a cartel provision. Inherent in that is the absence of an honest belief that the acts were a collaborative activity and the cartel provision was reasonably necessary for that purpose. That absence of an honest belief should be an essential element for the prosecution to prove. The situation is the same in offences involving dishonesty or offences involving an absence of claim of right (an honest but mistaken belief that the act was lawful).

10.8 It is argued that reversing the onus of proof of the collaborative activities exemption is justified as the defendant will be the person with the best ability to prove this. Such an argument is misguided in our view. First, the same could easily be said of dishonesty or claim of right in fraud offending. Neither are required to be proved by the defendant, for reasons already discussed. Second, the defence has two limbs. The first of which is to prove that the exemption actually applies. This requires proof of a complex matter the substance of which the Commission will have investigated and has far greater expertise and resource to do so. There is no good reason for reversing that onus. The second limb is the belief that the exemption applies. Again, the essence of the criminality is the absence of an honest belief or a belief that the acts were lawful. It is oppressive to require the individual defendant to have to prove that, faced with the expertise, personnel and resources of the state, and in the position of having to deal with the

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[23] MED, Explanatory Materials, 3.7.6, paragraph 65.

[24] As required by s 5 of the Bill of Rights Act.

[25] *Hansen v R* [2007] NZSC 7.

already immense burden of defending oneself against what will likely be lengthy and complex prosecutions.

10.9 The risk is that the Commission will take prosecutions without having fully investigated whether the exemption applies or whether the defendant believed it did. It will be for the defendant to prove that, which can only occur at the end of a lengthy, expensive and highly stressful prosecution (there being no earlier time at which the defendant will be able to prove his/her innocence). That in turn, will involve a huge cost burden on a defendant in circumstances where, (if the exemption applies or the defendant believed it did), the case should not have been prosecuted. The prosecution should have to investigate and properly consider that defence in advance. The conventional burden of proof will ensure that occurs before a prosecution is commenced.

11. ACQUISITIONS BY OVERSEAS PERSONS

11.1 The draft Bill proposes to repeal s 4(3) of the Act and establish a new regime for acquisitions by overseas persons. The MED is concerned that s 4(3) is overly broad as the Commission is unable to enforce proceedings against overseas persons that make acquisitions in breach of the Commerce Act.

11.2 As preliminary point, we have not encountered any issues with overseas persons avoiding the Commerce Act by reference to s 4(3) or otherwise. Indeed, even acknowledging enforcement issues, in our experience, overseas parties have recognised the need for the Commission to be able to capture mergers that take place overseas but which have an affect on a market in New Zealand. Practicalities of enforcement should not limit what is an unobjectable provision in the first instance.

11.3 The MED's explanatory materials state that one of the reasons why multinationals voluntarily seek Commission clearance for their acquisitions in New Zealand is to ensure they are perceived as law abiding global citizens, even though the Commission might not have recourse against them if the merger resulted in a substantial lessening of competition in New Zealand. That might be a motivating factor, but the ability for the Commission to name the overseas person in proceedings for a breach of s 47 is also a factor, even if ultimately because of the structure of their New Zealand holdings, no remedies can be obtained against them. To the extent that is the case it seems perverse to create a regime that might be perceived as permitting a 'form over substance' approach which would encourage parties to adopt a legalistic approach as to why a foreign to foreign merger is not caught. We see the removal of s 4(3) and the new declaratory process as likely to encourage companies to structure their acquisitions such that the New Zealand entity of a global group of companies does not make the acquisition, in order to avoid s 47.

Proposal

11.4 The draft Bill proposes that foreign to foreign mergers will not be subject to the prohibition on mergers that are likely to substantially lessen competition unless the acquirer is a person resident or carrying on business in New Zealand, although the vendor may be an overseas person with a business in New Zealand.

11.5 The new regime is modelled on the equivalent regime in Australia; although the MED explanatory materials note that s 50A of the Competition and Consumer Act (the Australian provision upon which the proposed s 47A is based) has never been invoked.

11.6 The draft Bill sets out a new declaratory process allowing the Commission to obtain an order that the foreign company cease carrying on business in New Zealand. The proposed regime no longer allows (even in theory) the Commission to apply for injunctions, divestment orders or penalties against any New Zealand held assets of a

global business that may be an acquirer of another business that has New Zealand operations. Instead the remedy is to create the reduction in number of competitors the merger is targeted at. It is an 'own goal'.

12. NEW PENALTIES UNDER S 103

12.1 The draft Bill proposes dramatic increases to the penalties under s 103 of the Act. Section 103 makes it an offence to:

> (1)(c) Resist, obstruct or delay an employee of the Commission acting pursuant to a warrant under s 98A of the Act; or
>
> (2) Attempt to deceive or knowingly mislead the Commission in any matters before it; or
>
> (3) When required to appear before the Commission pursuant to s 98(c) of the Act:
>
> > (a) Without reasonable excuse, refuse or fail to appear before the Commission to give evidence; or
> >
> > (b) Refuse to take an oath or make an affirmation as a witness; or
> >
> > (c) Refuse to answer any question; or
> >
> > (d) Refuse to produce to the Commission any book or document that that person is required to produce.

12.2 Current penalties under s 103 are $10,000 for an individual, or $30,000 in the case of a body corporate. The draft Bill proposes to increase these penalties to:

(a) up to 18 months imprisonment for an individual, and

(b) $1 million for a body corporate.

12.3 In the case of bodies corporate, the proposed penalty represents roughly 33 times the current maximum. Of greater concern, for individuals, a modest fine has been substituted with a possible 18 month prison sentence.

12.4 We consider the proposed penalties to be disproportionately harsh, and out of step with equivalent penalties in other jurisdictions. For example, in Australia, while the equivalent offence carries a maximum prison sentence of 12 months, the maximum monetary penalty is only AU$220,000.

12.5 In our view, the proposed penalties are demonstrably excessive, and out of line with equivalent jurisdictions.

13. JURISDICTION

13.1 The extra territorial application of the Commerce Act was recently considered by the Supreme Court in *Poynter v Commerce Commission*.[26] Following *Poynter*, it is clear that s 4 provides an exhaustive test for determining whether conduct engaged in outside New Zealand can be subject to the Commerce Act. Essentially, the Act will only apply to conduct outside New Zealand where:

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[26] *Poynter v Commerce Commission* [2010] NZSC 38.

(a) it is carried on by a person who is either resident or carries on business in New Zealand, *and*

(b) that conduct affects a market in New Zealand.

13.2 The MED appears to regard the extra territorial application of the Act as overly restrictive:[27]

> The jurisdiction requirements mean that individuals or corporate entities may enter into anticompetitive arrangements overseas directed at a New Zealand market and can avoid the jurisdiction of the Commerce Act by operating through local entities and taking care not to hold meetings in, or send communications to, New Zealand.

13.3 Certainly, the large number of jurisdictional challenges the Commission receives points to a disconnect between the Commission's view of the jurisdictional reach of the Commerce Act and the view held by the challenging parties of what ought to be within the Commission's enforcement reach.

13.4 However, the Supreme Court in *Poynter*, unlike the Court of Appeal, was not prepared to extend the extraterritorial application of the Act on policy grounds. It emphasised that it is a matter of comity between states that each will not interfere in the internal governance of another,[28] and provisions that give statutes extraterritorial effect should be read narrowly in line with this principle.

13.5 This view is consistent with legislative practices, for example, the Legislative Advisory Guidelines, May 2001 ("**Advisory Guidelines**") provide (at p 344-5, 349):[29]

> **Considerable restraint is however appropriate in applying New Zealand legislation to conduct occurring wholly outside New Zealand, solely on the grounds of effects produced in New Zealand**: such rules have the potential to interfere with the domestic jurisdiction of other States, and can place those subject to them in the difficult position of being subject to multiple overlapping legal requirements, or worse still to inconsistent requirements.
>
> A clear justification is needed for the application of substantive New Zealand law (civil or criminal) to conduct occurring outside New Zealand. [emphasis added]

13.6 The Advisory Guidelines discuss the different ways in which legislation can establish extraterritorial application, called common connecting factors. Examples cited are:

(a) whether certain conduct or events occurred in New Zealand;

(b) whether a person is present/resident/habitually resident/ordinarily resident/domiciled in New Zealand at the time of certain events, or at the time proceedings (civil or criminal) are commenced against them, or the relevant process is served on them;

(c) whether a person is a New Zealand national;

(d) whether a transaction is governed by New Zealand law;

(e) whether certain property is situated in New Zealand; and

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[27] MED, Explanatory Materials, 5.1, paragraph 81.
[28] *Poynter*, at paragraph [30].
[29] Legislation Advisory Committee Guidelines, May 2001.

(f) whether certain consequences occur in New Zealand, and the level of knowledge of the person concerned as to whether those consequences would occur in New Zealand.

13.7 Section 4(1) of the Act extends jurisdiction by conjunctively referring to factors (b)/(c) (attributes of the person) and (f) (attributes of the conduct).

13.8 It is and should be insufficient to establish jurisdiction if the entire body of conduct forming and implementing the anticompetitive arrangement occurs overseas, and that conduct is alleged to have an indirect economic effect on a market in New Zealand (being the approach in the United States). In recent cases, even the United States has resiled from its aggressive pursuance of conduct with this tenuous jurisdictional basis.

13.9 Rather, if there is a need to amend s 4(1) at all, then it should only be to remove the characteristics of the person but retain a requirement of implementation and effect. The test must require a factual nexus between the overseas conduct and conduct in a market in New Zealand. Ultimately, given similar laws in developed countries, it is difficult to argue with the proposition that a foreign person can be liable under New Zealand law for implementing a cartel in New Zealand, even if implementation is achieved through an innocent agent or intermediary in New Zealand. Such conduct is directed towards and affects a market in New Zealand, and should be subject to the Act.

13.10 Ultimately we are of the view that s 4(1) strikes the correct balance and does not require amendment. Extraterritorial jurisdiction was not extended for the cartel offence when cartel criminalisation was introduced in Australia. However, if the MED are inclined to extend the jurisdictional reach of the criminal offence to the extent provided in s 7 of the Crimes Act then it would produce perverse results if s 30 did not have a similar reach. If would be both arbitrary and counterintuitive if the Commission could prosecute criminally a broader range of conduct than it could proceed against civilly. We are particularly concerned that this disconnect may create an incentive for the Commission to proceed criminally when it is unsure of its jurisdiction to proceed civilly, given the restrictions imposed by s 4(1) of the Commerce Act.

13.11 Accordingly, if the MED does choose to propose to amend the jurisdictional reach of the criminal provisions to match s 7 of the Crimes Act, a new s 4(4) ought to extend the extraterritorial application of s 30 in the same terms as s 7 of the Crimes Act.

Russell McVeagh

22 July 2011

1. SCHEDULE ONE - GUIDELINES REQUIRED

1.1 Given the novel nature of many of the proposed reforms, we consider it essential that the Commission consult upon and publish detailed guidelines with respect to how it intends to apply the new law. In our view, these guidelines should be in place before the reforms come into force.

1.2 Where appropriate, we comment on what we would expect from specific guidelines, below.

Cartel prohibition

1.3 It would be useful for the Commission to publish guidelines which comment on and give examples of conduct that would fall under the prohibitions on price fixing, restricting output, market allocation and bid rigging.

Prosecutorial discretion

1.4 Our preliminary view of the requirements for proceeding down the criminal prosecution track is as follows:

(a) The conduct must be covert, steps must have been taken to keep the arrangement secret;

(b) The conduct must have had at least the potential for an impact in a market in New Zealand of $10,000,000 or more;

(c) A significant number of customers must have been potentially affected by the conduct (ie more than one);

(d) The conduct took place over an extended period of time (ie more than 5 years);

(e) Criminal prosecution will be more appropriate where the parties have made some attempt to mislead the Commission in its investigative process; and

(f) Recalcitrant offenders should more readily be subject to criminal sanctions.

Collaborative activities

1.5 We would expect guidance on the new collaborative activities exemption to comment on the phrases "reasonably necessary" and "dominant purpose of lessening competition".

1.6 Specifically, it would be useful for the Commission to include examples of the circumstances in which it would and would not consider a provision to be reasonably necessary in respect of all four categories of identified conduct (ie price fixing, output restriction, market allocation and bid rigging).

Bid rigging

1.7 As set out in our submission, we are concerned that prior understandings could be subject to liability under the Act.

1.8 We would expect the Commission to release guidelines on the circumstances in which it will elect to investigate prior understandings.