



## EXECUTIVE OFFICE

21 July 2016

Targeted Commerce Act Review  
Competition and Consumer Policy  
Ministry of Business, Innovation and Employment

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### **Targeted review of the *Commerce Act 1986 (NZ)* – cross submission**

The Australian Competition and Consumer Commission (ACCC) welcomes the opportunity to make a second submission to the Targeted Review of the *Commerce Act 1986 NZ (CA)* (the Review). This submission should be read in conjunction with the ACCC's earlier submission to the Review.<sup>1</sup> While the Review canvasses a number of issues, this submission is confined to a consideration of the misuse of market power provision of the CA (section 36).

Australia's equivalent misuse of market power provision, section 46 of the *Competition and Consumer Act 2010 (CCA)*, has also been subject to review recently. On 16 March 2016 the Australian Government announced its intention to amend section 46 of the CCA by removing the take advantage element and adopting a substantial lessening of competition (SLC) test. However, the current text of the central provisions of section 36 of the CA and section 46 of the CCA are relevantly identical. As with the earlier submission, the ACCC makes this submission based on its experience enforcing section 46 of the CCA.

The ACCC has reviewed the submissions made to the Review by interested parties. The interested parties that oppose the removal of the take advantage element and / or the adoption of an SLC test raise a number of arguments, that are similar or identical to those made to the Australian Government during the review of section 46 of the CCA, and demonstrate a fundamental misunderstanding of the substantial market power element and misconstrue the operation of an SLC test.

The views expressed in opposition to reform can be summarised as follows:

1. The current section 36 adequately prevents anti-competitive unilateral conduct. Alternatively, even if section 36 is ineffective, the other provisions of the CA are sufficient to address anti-competitive unilateral conduct
2. An SLC test is a novel, and therefore uncertain, test in New Zealand law
3. A reformed section 36 will lead to the prohibition of pro-competitive conduct and / or otherwise 'chill' competition, innovation or investment
4. The removal of the take advantage element equates to the removal of the causal connection between a corporation's market power and its conduct
5. An SLC test would impose an unreasonable burden upon large businesses that is not imposed on small or medium enterprises.

The remainder of this submission will respond to these concerns.

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<sup>1</sup> [ACCC submission to the Targeted Review of the Commerce Act 1986 \(NZ\), February 2016](#)

1. Arguments that section 36 or alternately other provisions of the CA adequately addresses anti-competitive unilateral conduct

We regard the current section 46 of the CCA as deeply deficient. In short, it does not reliably address anti-competitive unilateral conduct and provides scope for anti-competitive conduct to go unchecked.

In part this follows from the drafting of section 46, which uses a series of indirect tests to filter pro and anti-competitive unilateral conduct rather than a direct test of whether the conduct was engaged in to cause, or caused, or is likely to cause, substantial harm to the competitive process.

*Purpose*

Section 46 currently proscribes purposes that relate to harming actual or potential rivals or otherwise limiting competitive conduct by those rivals. However, it is a natural consequence of robust competition that more efficient firms damage less efficient firms by attracting customers and increasing their market share. Striving to grow, succeed and acquire market share and potentially market power at the expense of one's rivals is what drives competition and innovation.

*Take advantage*

Therefore, the take advantage element has the role of filtering anti-competitive conduct from benign and pro-competitive conduct captured by the proscribed purpose element. Unfortunately, the take advantage element is a deeply flawed filter that pushes the provision to the other extreme by permitting serious anti-competitive conduct.

In seeking to use the take advantage element as a filter, the Australian and New Zealand Courts have undertaken complex counterfactual analyses that mean that to avoid liability for anti-competitive unilateral conduct a firm with substantial market power need only show that the conduct it engaged in is conduct that a small firm could also engage in. This is highly unsatisfactory as it ignores the very different consequences that flow from the conduct undertaken by a large firm compared to a small firm in same the market.<sup>2</sup>

We also note the take advantage element can produce outcomes that do not accord with the application of misuse of market power laws in other nations. In the US, Microsoft was prevented from forcing Windows users to install other Microsoft products, and excluding alternative software. Lifting these restrictions has led to the development of many diverse software offerings. In Australia the take advantage element would very likely not have been satisfied because firms without market power can bundle products in the way Microsoft did.

Given section 36 of the CA and section 46 of the CA are relevantly identical; these challenges are likely to be shared.

We have found that other provisions in the CCA are not able to cover the gap that exists in our law due to the current drafting of section 46. Equally, other provisions in the CA which are directed to multilateral conduct are unlikely to adequately address the harmful *unilateral* conduct that is intended to be addressed by section 36 of the CA.

**Attachment 1** provides examples of anti-competitive conduct that the current section 46 of the CCA may not be able to address.

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<sup>2</sup> Stuck, Cross, Douglas Richards, Weber Waller, *Use of Dominance, Unlawful Conduct, and Causation Under Section 36 of the New Zealand Commerce Act: A U.S. Perspective*, (2012) 18NZBLQ, 'whether firms with or without market power would have engaged in that conduct does not necessarily preclude anticompetitive purpose or effect', noting the court in *Berkey Photo, Inc. v. Eastman Kodak Co* (603 F.2d 263, 275 (2nd Cir. 1979)), 'Such conduct is illegal when taken by a monopolist because it tends to destroy competition, although in the hands of a smaller market participant it might be considered harmless, or even "honestly industrial".'

## 2. Arguments that an SLC test is novel or uncertain

An SLC test is neither novel nor uncertain. Quite the reverse; it is a well-established and well understood test that is applied in the majority of the other competition provisions of the CA, including anti-competitive agreements, covenants and acquisitions. It has a demonstrated ability to effectively filter anti-competitive from benign or pro-competitive conduct. The introduction of an SLC test into section 36 will merely allow the New Zealand Commerce Commission and the Courts to apply this clear and effective test to a broader range of conduct than they currently can.

The use of an SLC test in section 36 will require that dominant New Zealand businesses assess their conduct in a similar way to that in which they already assess their contracts, covenants and acquisitions. Further, it is a test applied internationally to unilateral conduct and multinational firms in New Zealand will be well-versed with it.

## 3. Arguments that adopting an SLC test will prevent or deter competition

The adoption of an SLC test will not restrain large businesses from competing on their merits, reduce productivity, chill investment or lead to higher prices. The adoption of an SLC test will better protect pro-competitive conduct and appropriately target anti-competitive conduct. Conduct that enhances competition or is benign, by definition, does not substantially lessen competition and will not be captured.

Competition, by its very nature, is deliberate and ruthless. Advantages gained through research and development, innovation or economies of scale do not lessen competition, even if the conduct causes competitors harm or forces them to exit a market.

- Investing in improved technology and lowering prices is a normal part of the competitive process that increases efficiency and will increase rather than lessen competition.
- Passing on lower prices to consumers that a firm is able to offer as a result of increased efficiency is a normal part of the competitive process and will increase rather than lessen competition. This is the case even where the prices are at a level that competitors find hard to sustainably match. Retailers adopt pricing strategies to promote their competitive position and increase their share of the contestable market; such strategies can include loss leading and national pricing where a chain retailer may offer a form of price guarantee. This conduct can be undertaken by firms with market power and those seeking to gain market share. In the majority of cases such pricing strategies stimulate competition and are pro-competitive. Section 46 with an SLC test will only capture pricing strategies undertaken by a firm with substantial market power where that strategy has damaged the competitive process by substantially lessening competition.
- Expansion by a firm into a new geographic area or into a complementary market that, because of the efficiency or technical expertise of the entering firm, causes others to exit or decide not to enter, is a normal part of the competitive process and will increase, not lessen competition.

## 4. Arguments that removal of the causal connection between market power and conduct

The ACCC accepts that the removal of the take advantage element and adoption of an SLC test would mean the law would no longer allow dominant firms to engage in conduct because of the mere fact that the conduct is of a kind that a non-dominant firm could theoretically engage in. Indeed, this is one of the key benefits of the proposed reform.

One of the reasons that section 46 of the CCA and section 36 of the CA exist is to take account of the very different competitive and consumer harms that result from anti-competitive conduct by firms with substantial market power as compared to those without. Therefore, it is very undesirable that, as set out in paragraphs 15 – 25 of the NZCC's 2 June

2016 letter,<sup>3</sup> the current section 36 effectively provides a safe harbour for firms with market power to engage in anti-competitive conduct without regard to the consequences of the conduct on the competitive process.

5. Arguments that amending section 36 would impose an unreasonable burden upon large business

The ACCC accepts that amending section 36 to remove the take advantage element and insert an SLC test will expose a very small number of firms – those with substantial market power – to more scrutiny. This additional responsibility is imposed upon firms with substantial market power because of the drastic competitive consequences that flow from anti-competitive unilateral conduct by a firm with substantial market power.

However, their conduct will only be restrained when their conduct crosses an international recognised marker of anti-competitive conduct, when the conduct has the purpose, effect, or likely effect of substantially lessening competition.

Given the similarities between section 46 of the CCA and section 36 of the CA, the ACCC anticipates that the removal of the take advantage and current proscribed purpose elements, and the substitution of an SLC test would improve the efficacy of section 36 of the CA, and therefore the efficiency and effectiveness of the New Zealand economy.

Yours sincerely



Rod Sims  
Chairman

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<sup>3</sup> [New Zealand Commerce Commission Letter to the New Zealand Minister of Commerce, 2 June 2016](#)

**Attachment 1 – examples of conduct that the current law may not appropriately address**

Conduct	Why current law unlikely to apply	Why an SLC test will help
<p><b>A</b></p> <p><b>Land banking</b> A retailer operates six out of eight retail fuel sites in a major town. The local planning authority has designated four other sites in the town as suitable for the establishment of new retail sites. The retailer buys the first option to purchase all four of the sites before this can occur.</p>	<p>Unlikely to be taking advantage of market power because a firm without substantial market power could also buy the option. In other words, conduct that is designed to protect market power but could be undertaken by a firm without substantial market power is unlikely to breach the current section 46 (<i>Rural Press</i>).</p> <p>There are likely to be legal difficulties with this conduct being captured as an ‘acquisition’ for the purposes of the merger provisions and with the acquisition having an SLC effect.</p>	<p>An SLC test would allow an assessment of whether the conduct has an anti-competitive purpose or effect in the relevant market, including by way of the higher barriers to entry that the conduct is likely to erect.</p> <p>Even if the conduct could be assessed using the ‘effect’ of SLC under the merger provisions, the revised section 46 would allow ‘purpose’ of SLC to also be assessed.</p>
<p><b>B</b></p> <p><b>Locking up supplies</b> A firm with 60% total sales in a market enters into long term agreements to lock up 90% of all supplies of an essential ingredient in its production process.</p>	<p>Unlikely to be taking advantage of substantial market power as a firm without market power could enter into such agreements (see <i>Cement Australia</i>). In other words, conduct that is designed to protect market power but could be undertaken by a firm without substantial market power is unlikely to breach the current section 46 (<i>Rural Press</i>).</p>	<p>An SLC test would allow an assessment of whether the conduct has an anti-competitive effect (or purpose) in the relevant market, including by preventing competing producers from growing their production thereby competing with the firm.</p>
<p><b>C</b></p> <p><b>Restricting supplies of essential materials</b> A vertically integrated firm with substantial market power refusing to supply downstream competitors</p>	<p>Depends very much on the details but likely to be caught by the current law, although there could be some difficulties in showing take advantage and / or purpose (see and compare <i>Queensland Wire</i> and <i>Melways</i>).</p>	<p>An SLC test would allow an assessment of whether the conduct has an anti-competitive effect, without the complicated use of a counterfactual test to assess whether the conduct constituted taking advantage of a firm’s market power.</p> <p>Assessing whether the conduct has the purpose or effect of substantially lessening competition (rather than whether it amounts to taking advantage of substantial market power) provides a clearer and more predictable test for</p>



			assessing whether the refusal to deal is based on genuine business concerns (such as the credit worthiness of the buyer) or being in engaged in to prevent rivalry.
<b>D</b>	<p><b>Retaliatory threats</b> A firm is the only distributor of newspapers to newsagents and convenience stores in town. A distributor of newspapers in a neighbouring town expands its distribution area to compete with the firm. The firm threatens to commence operating in the entrant's distribution area unless the entrant keeps to its own area.</p>	Unlikely to be taking advantage of market power as the firm is using its assets as a distributor to make a threat of retaliation credible, i.e. using its financial power rather than market power (see <i>Rural Press</i> ). Further, if the entrant does not accede to the threat, then there would be no section 45 agreement to assess under the SLC test.	An SLC test would allow an assessment of whether the conduct has an anti-competitive purpose or effect in the relevant market, including by eliminating the threat of entry from a neighbouring distributor (In <i>Rural Press</i> – an SLC was found but no breach of section 46).
<b>E</b>	<p><b>Joint marketing fee</b> A retailer with more than 60% of sales in a market asks its suppliers to pay it 20% of sales price in a joint marketing fee. It doesn't impose this requirement on suppliers of products it sells under its home brand.</p>	Unlikely to be taking advantage of market power as any retailer could ask suppliers to contribute to marketing expenses.	An SLC test would allow an assessment of whether the conduct has an anti-competitive purpose or effect in the relevant market, including by imposing considerable additional costs on suppliers that compete with home brand suppliers.
<b>F</b>	<p><b>Freezing out competing suppliers from retail display and demonstration opportunities</b> A retailer with more than 60% of sales in a market discriminates in favour of its own brand products in relation to in-store placement and promotions.</p>	There may be difficulties with showing taking advantage and / or purpose. Alternatively, an unconscionable conduct case where the targets of the conduct are large suppliers of proprietary brands would be challenging (and not available at all where the suppliers are listed companies).	An SLC test would allow an assessment of whether the conduct has an anti-competitive purpose or effect in the relevant market, including by making it more difficult for suppliers of proprietary brands to compete with home brand products.
<b>G</b>	<p><b>Targeted price discounting strategies by an incumbent, designed to dissuade new entrants in a region</b> Possible predatory pricing by a dominant firm.</p>	If truly predatory, i.e. below relevant costs of supply and targeted at potential competitors, this conduct would be picked up by the current law.	An SLC test would allow an assessment of whether the conduct has an anti-competitive purpose or effect, without the complexities of demonstrating below cost pricing. Assessing whether the conduct has the purpose or effect of substantially lessening competition (rather than whether it amounts to taking advantage of

			<p>substantial market power) provides a clearer and more predictable test for assessing whether the price discounting is a genuine competitive response or being in engaged in to prevent rivalry.</p>
<p>H</p>	<p><b>Tying up customers in long term contracts with anti-competitive rebates</b></p>	<p>Depending on the detail this could fall within the current law.</p>	<p>An SLC test would allow an assessment of the conduct through the prism of the SLC test.</p> <p>Assessing whether the conduct has the purpose or effect of substantially lessening competition (rather than whether it amounts to taking advantage of substantial market power) provides a clearer and more predictable test for assessing whether the use of rebates is competitive conduct or being in engaged in to prevent rivalry.</p>