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Targeted Review of the Commerce Act 1986

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Metals New Zealand (Metals NZ) is an incorporated society serving the needs of New Zealand's metals related industry. Launched in 2011, it consists of Organization Members made up from metals related industry sub associations. Its Executive consists largely of leaders of New Zealand's major organizations operating in the metals based sectors.

The NZ metals-based industry is actively involved with and supports many other industries, such as food processing, energy generation, agriculture and building & construction. As such, industry-specific figures are difficult to pinpoint, but the last research completed in 2010 reported:

- Contributes over 7% to Annual NZ GDP
- Direct metals-based product manufacturing employs more than 26,000 people
- Over $7.3 billion worth of metals-based product manufactured annually
- More than $2.6 billion of product exported, representing 5.6% of total NZ exports

Further information can be gained by visiting the website ***http://www.metals.org.nz***

Introduction;

This MetalsNZ submission is a principles-based one in which we make comment on the issues emerging from the key questions in the Issues Paper. We address those questions we consider most directly pertinent to our industry, but leave open the opportunity for comment during any broader option discussions at a later time.

MetalsNZ believes, in response to numerous questions, that the issues paper has been well prepared and outlines the pertinent issues in consideration.

MetalsNZ fully supports the Governments Free Trade Agenda and Competition Policy both from domestic and from international sources that is fair and conducted on a level playing field basis.

The macro and microeconomic reforms initiated by the current government, in a much broader international context, are now playing out in rapid and currently uninterrupted economic growth and wealth creation in this country.

New Zealand markets are generally small and distant from highly referenced & governed international markets such as US/EU. International competition is present here with few barriers to trade. The fact that we are adjacent to the fastest growing region in the world, ASEAN & Nth Asia, we would also support the call for a well structured and operational competition regulatory regime.

Size and scale bring substantial benefits through efficiencies that lead to lower prices and we must be careful to automatically assume high market shares, or large scaled businesses are bad in the sense of competition & therefore benefit to consumers.

Without sufficient scale, many New Zealand businesses will find it exceedingly difficult to compete and survive against international entrants that have scale which dwarfs even the largest NZ firms in their respective sectors. Pointing to the benefits of scale is not to argue for government policies to facilitate scale or restrict competition. To the contrary, it is an argument against policy interventions that inhibit competition.

NZ consumers can now purchase many of the goods and services, including metals products or raw materials, they desire directly from international providers, located virtually anywhere in the world, using any computer or mobile device.

This is the real world in which many metals businesses increasingly operate and compete.

It is most obvious in the burgeoning online economy, but also in the proliferation of international traders/retailers moving into our markets. This has potentially profound but seemingly overlooked ramifications for taxation receipts for government, direct and indirect employment in the domestic economy and the flow-on community benefits that can result from both.

It is not an argument for protection, but a recognition our domestically based industries and businesses are subject to ever greater competition in an increasingly internationalised market and should be allowed and encouraged to compete as vigorously as possible.

The concept that a firm must have a physical presence to be a major participant in a market is being challenged today. An increasing number of businesses have no outlets at all, merely distribution centres or call centres which may be located anywhere in the world. The corollary of this development is that any belief that a business establishing or maintaining a substantial physical presence in a market must therefore be exerting too much market power is increasingly redundant. In many parts of the world this virtual competition extends to metals products.

Metals NZ recognises there is unquestionably a role for government in regulating business and industry. Good governance is vital to a healthy economy, but regulation and support must serve to protect competition, not strangle it or protect uncompetitive participants.

Demands for increased bureaucratic intrusion into and regulation of competitive markets will not increase national wealth; but rather challenge it & likely diminish it.

MetalsNZ endorses the international best practice principles . These principles are important not only to ensure the highest standard framework, but also to facilitate the domestic entry of international competitors and the expansion of NZ businesses overseas through consistency in competition principles.

A competition framework that is consistent with international best practice will provide efficiencies and increase competition for the benefit of NZ consumers.

However, the purpose of competition policy law should be to protect competition for the benefit of consumers. Proposed amendments to the Commerce Act 1986 should be assessed on the basis of whether they protect competition or competitors and not just that they align with international practice.

MetalsNZ is a diverse group of companies that thrive on competition. These companies are ready and willing to compete against all comers in sensibly regulated markets and do not support competition policies that, in fact, restrict competition.

At the same time, MetalsNZ acknowledges that competition laws are essential to safeguard against businesses with a substantial degree of market power from misusing that power. Competition laws are necessary to prevent anti-competitive practices such as cartels, collusion and the misuse of market power preventing the entry of competitors into markets or substantially lessening competition. Metals NZ believes that generally the current Policies work well in promoting and protecting competition.

Nevertheless, MetalsNZ would consider on their merits any proposals to amend the Commerce Act 1986 in ways that removed impediments to competition without having unintended anti-competitive effects and which kept compliance costs to a reasonable level.

Amendments that may have the deliberate or unintended consequence of protecting businesses from competition to the detriment of consumers must be considered & rejected, these proposals fail the principal objective of competition law, which should be to promote and protect competitive processes and behaviour for the benefit of consumers.

It is clear that that globalization of markets has accelerated in very recent times given implementation of GPA, TPP and Free Trade Agreement initiatives.

However, we do need to be mindful of what offshore practices are and continue to assess various options. Metals NZ must be sure that we understand the Problem Statement and Risk Assess the various options in Policy decision making.

To this end, whilst we may be able to offer up some shortcomings in the existing Policy, or application thereof, there must be clear evidence that alternatives will provide cost beneficial outcomes and simply aligning our Policies with those held internationally might be the short answer but it's not the right answer.

In this issues paper, MBIE is pointing to a type of 'effects test' that hasn't been road tested anywhere in the world, not to mention suggesting releasing it on a country that is small and therefore characterized by some specialized large firms with high market share. In short, MetalsNZ doesn't support being the guinea pig on this issue without further detailed consideration given what adverse effects could result.

In terms of Market Studies, clearly it has been suggested there is a gap in the framework and so option studies to strength this area may well be appropriate but concerns for the workload this may place on our businesses is real.

<u>Anti-competitive Exclusionary Conduct</u>

1. The Ministry has accurately described the type of conduct that countries typically seek to prohibit.
2. Yes, accurate descriptions of different approaches to rules have been made.

2.5 Assessment of the New Zealand regime Do you agree that section 36 may not effectively assure the long-term benefit of consumers? If you agree, are there any sectors of the economy where you consider this to be well illustrated? If you disagree, please explain why. 9 Is it fair to say that businesses will generally know if they are acting in a way that they would not in a competitive market – i.e. that the current test is sufficiently predictable? 10 Do you agree that section 36 – as applied by the courts – is too complex to ensure that it is cost-effective and timely? 11 Do you agree that section 36 – as applied by the courts – is not well aligned with other relevant provisions? 12 Given your view on the correct implication of having a small and remote economy, do you consider that section 36 appropriately reflects that implication? 13

The Issues Paper sums up MBIE's preliminary conclusion on s36 since it appears:

- to be failing to maximise the long-term benefit of consumers, by failing to punish anticompetitive conduct by powerful firms;
- to be too complex to allow for cost-effective and timely application; and

- to be misaligned with other prohibitions in the Commerce Act (sections 27 and 47 both of which include an “effects test” while section 36 relies on a “purpose test”) and with equivalent provisions in a number of foreign jurisdictions (the US, the EU and Canada do not require a powerful firm to “take advantage” of its market power).

MetalsNZ disagrees with the conclusions reached in the Issues Paper because:

- there is no evidence to suggest there has been a failure to punish anti competitive behaviour by dominant firms.
- There is a widely held misunderstandings about what constitutes ‘dominant’ and that ‘ big is bad’ in the eyes of the consumer
-the minimal number of cases judged to be anti competitive has been very small in number should in no way be an indication as to the effectiveness of ensuring consumer wellbeing.
-to be Policy aligned with Australia is preferred so as to harmonize the business environment to lower business risk, but international.....even given the current significant trends in globalization of trade the lack of alignment argument is just not relevant in this case.

2 2.3 The New Zealand regime Has the Ministry accurately described the main elements of New Zealand’s rule against anti-competitive exclusionary conduct? 3 In your opinion, what justifications can there be for requiring that a firm with a substantial degree of market power “take advantage” of that power? 4 What justifications can there be for a purpose-based (rather than effects based) approach? Why do you think Australia adopted such an approach with its Trade Practices Act 1974? 5 Does section 36(1) make sense, given that authorisations do not apply to section 36(2)?

The determination that a firm with a substantial degree of market power ‘take advantage’ of that power is an important one.

The fact that NZ is somewhat geographically remote and small by international standards is a very important consideration in this review and the very example cited that a business operator in NZ may find itself having significant market power in NZ through no fault of its own is a pertinent one.

Driving through innovative management decision making needs to be encouraged rather than bridled otherwise, step change improvements in cost, quality or service would be sub optimized and ultimately not in the best interests of consumers.

The justification for the Purpose based test over any other effects test is that it does not invite considerations of any legitimate business conduct thereby not challenging the fundamental competitive process itself...this is important.

A business that competes hard on price, to the benefit of consumers, can damage or eliminate a rival, or make it uncommercial for a potential rival to enter a market. Since the competitively behaving business cannot know in advance what effect its competitive behaviour might have on an actual rival or on a potential rival that is not even in the market at the time, it could breach the law by behaving competitively.

The competitive business could be deterred from keeping its prices low, from finding efficiencies that enabled it to drive prices lower and possibly even from offering quality and service that had the effect or likely effect of damaging a rival or preventing a potential rival from entering a market.

Opening a new MEGA hardware store could increase competition in the home improvement market in an area, provide a great outcome for consumers in range and value, but also have the eventual effect of seeing an existing hardware retailer competitor hardware business close.

Boards and managers of businesses with a substantial degree of market power could be breaching the law by competing hard on price, and possibly also on quality and service. However, they would not know at the time they were making these decisions whether they were acting unlawfully, since under an effects test it could depend on the response of actual or potential competitors, including rivals that might not even exist at the time management decisions were made. Management of a business may be reluctant to put itself in such a position, with a consequent lessening, not strengthening, of competition.

- Removing "taking advantage" ... Businesses always have the purpose of 'winning' - damage to competitors is inherent in the process of competition (ie getting ahead at competitors' expense). To prohibit firms with market power from engaging in conduct with the purpose of damaging competitors, without requiring proof that such conduct is linked to that market power or would not occur in a competitive market, would require powerful firms to be more competitively conservative than other less powerful competitors. This would be a very poor policy outcome - especially for a small economy like New Zealand's which requires large efficient businesses to be as competitive as possible.
- Moving to an effects based test makes it difficult for a powerful firm to determine *in advance* whether its conduct is lawful. In the s 27 / s 47 context, the "effect" of an agreement can be assessed at a later point in time after the agreement has been entered into. In the misuse of market power context, this would mean a firm with market power won't know until some months or years later whether its conduct was illegal or not.

To the extent that MBIE wants to more closely align the prohibition with s 27 (the prohibition on anti-competitive agreements), it should at least remove the *actual effect* part of the test. The prohibition could be limited to conduct that has the "*purpose"* or *"likely effect"* of substantially lessening competition in a market. If that approach is taken it would also need to be clear that "likely effect" for the purposes of s 36 means a "probable" outcome that is "reasonably foreseeable" at the time the conduct is undertaken by the firm with market power, and is not merely a "real risk", as "likely" has been interpreted in the merger control context. (Note here, that New Zealand is an outlier, even as compared to

Australia, in setting such a low threshold of probability for "likely" in the merger control context).

Management could conceivably seek some sort of ‘referee’ indication or authorisation from the Commerce Commission for pricing, promotional and branding decisions prior to making any such decisions.

Numerous decisions are made every year by businesses with a substantial degree of power in a market about pricing, discounting, branding and offerings under loyalty programs. Seeking prior guidance or authorisation of these would insert the Commerce Commission into the day-to-day or at least the weekly decisions of company management.

Apart from the question of whether a regulator such as the Commerce Commission should be so involved in such decision making, delays in responding would be inevitable. Rather than promoting competition, the inclusion of such an effects test could easily stifle competition, causing consumer prices to be higher than necessary, as management and boards sought to comply with the law.

It is claimed that purpose is difficult to prove, and that New Zealand (& Australia) is unique in adopting a competition law, but proscribed purposes have been found by the courts in a number of cases.

It is MetalsNZ’s view that where cases have failed, it has rarely been on the element of purpose.

Further, although the primary competition instruments of some other jurisdictions do not refer explicitly to purpose, an element of purpose, intent or wilfulness has frequently been applied by courts and regulators in these jurisdictions.

Much has been written on this subject and MetalsNZ found the best summaries out of Australian text including Sir Daryl Dawson and his colleagues in the Dawson Report (April 2003) and the more recent analysis by Dr Alexandra Merrett and her colleagues on their web-based The State of Competition Report (issue 14, November 13). Both recommend against inserting an effects test into Section 46 of the Act.

History of the effects test In 1976, the Trade Practices Act Review Committee (the Swanson Committee) recommended that the section should only prohibit abuses by a monopolist that involve a proscribed purpose. In 1979, the Trade Practices Consultative Committee (the Blunt Review) rejected an effects test because it would give the section too wide an application, bringing within its ambit much legitimate business conduct.

The 1984 Green Paper, The Trade Practices Act Proposals for Change, recommended the introduction of an effects test because of difficulty in establishing purpose. In 1989, the House of Representatives Standing Committee on Legal and Constitutional Affairs (the Griffiths Committee) concluded that there was insufficient evidence to justify the introduction of an effects test into section 46. In 1991, the Senate Standing Committee on Legal and Constitutional Affairs (the Cooney Committee) concluded that an effects test

might unduly broaden the scope of conduct captured by section 46 and challenge the competitive process itself.

In 1993, the Independent Committee of Inquiry into Competition Policy in Australia (the Hilmer Committee) rejected an effects test because it would not adequately distinguish between socially detrimental and socially beneficial conduct. In 1997, the House of Representatives Standing Committee on Industry, Science and Technology (the Reid Committee) noted the effects test and the views of the Hilmer Committee, but did not recommend its introduction. In 1999, the Joint Select Committee on the Retailing Sector (the Baird Committee) rejected an effects test on the basis that such a far reaching change to the law may create much uncertainty in issues dealing with misuse of market power. In 2001, the House of Representatives Standing Committee on Economics, Finance and Public Administration (the Hawker Committee) noted significant opposition to an effects test and that five inquiries since 1989 had not recommended its introduction including currently.

Dr Merrett and her colleagues have made the point: To date, no-one has come forward with a real-life example of conduct which should be caught -examples where competitors or even competition are adversely affected, but where there has been no use of market power.

The State of Competition Report issue 14, November 2013, p. 8) Under an effects test, Section 46 of the Competition and Consumer Act 2010 relating to the misuse of market power would be amended so that a corporation with a substantial degree of power in a market must not take advantage of that power not only with the purpose of but with the effect or likely effect of eliminating or substantially damaging a rival, preventing the entry of a rival into a market or preventing a rival from engaging in competitive conduct in that market or any other market.

Primary Recommendation: That as s36 of the Commerce Act already assures consumers' best interest, an options paper on this issue is deemed not necessary.

Alternative enforcement Mechanisms

MBIE's preliminary conclusion is that the current Commerce Act mechanisms are not operating satisfactorily and therefore reform is required.

From MetalsNZ's perspective, of the Issues Paper's proposals for change those in the chapters dealing with alternative enforcement mechanisms are the least concerning of the three key issues.

Table 5 on page 48 does a good job of summarising possible future options.

MetalsNZ believes the matter of alternative enforcement mechanisms should be considered ' in full view' of what other changes are finally decided in chapters 2 & 4.

Recommendation: On the basis that MetalsNZ position is one of supporting the current wording of s36, an options study into procedural application & refinement for alternative mechanisms would be supported.

Market Studies

Market studies 4.5 Is there a gap? Do the approaches to market studies described in the Issues Paper align with a gap in New Zealand's institutional settings for promoting competition? 45 What procedural settings for a market studies power would best fit the identified gap, in terms of: a) Who may initiate a market study; b) Who should conduct market studies; c) Whether mandatory information-gathering powers would apply; d) The nature of recommendations the market studies body could make; and e) Whether the government should be required to respond. 46 11

Research does indicate an increasing international trend in the use of market studies by competition agencies; used more as an instrument for promoting competition.

MetalsNZ opposes any further market studies decision power being given unilaterally to a central government department. The concern being the potential to create a never ending series of investigations that will in most instances simply lead to more regulations that businesses have to comply with.

The case 'as is' where ad hoc Ministerial decision making may instigate a Market Study, (as evidenced in the more recent Plasterboard study), is deemed sufficient with the Commerce Commission then leading any investigation.

An options study involving an independent party to the Commerce Commission would be supported by MetalsNZ. Currently resourcing at the Commerce Commision is challenged by their current workload and so any cost/benefit study would need to be considered very carefully.

Market studies should be focused on market or industry-wide conditions or practices and on advocating the benefits of competition to regulators.

Market studies and industry studies are not meant to address the anti-competitive activities of specific firms or individuals, which are still best addressed by the enforcement provisions of the Commerce Act.

It is MetalsNZ understanding that the Commerce Commission does not have formal powers to initiate market studies or in fact compel companies to provide the necessary full scope of information, it envisions that such powers could be highly beneficial but only with an alternative independent party.

For example, in cases where parties are reluctant to provide information voluntarily for fear of reprisals or key information is known to be available but is not being provided voluntarily. Therefore, in cases where key information is confidential and difficult to access, the impact assessment becomes more theoretical.

International commentary reports these studies are a very useful tool for competition advocacy. They have been an important instrument that has helped influence the policy making process and, in some cases, has been decisive in pushing for reform. In addition, the accompanying communication strategy triggered by publishing of the market study serves to position competition principles at the centre of public discussion.

Furthermore, market studies have served as a complement of enforcement activities, with the aim of solving competition problems by modifying public policies and the regulatory framework, in order to achieve market structures more favourable to competition

The negative side of the criticism expressed by entrepreneurs' complaints are usually connected with, in their opinion, the too large scope of data requested by any competition authority. Enterprises complain about the additional unpaid work that their employees must perform while collecting the data, they also fear disclosing their company secrets.

There were also situations, when the problems created by enterprises during the study were aimed at making it impossible for the authority to gather information on the irregularities existing in the market. Additional difficulties with which the competition authority must deal during the study and after finishing it is providing a proper protection for company secrets included in the collected source material. This is particularly problematic when the decisions to publish the study reports is made.

The answer lies in the balance.

Recommendation: Metals NZ is clearly of the view that at this time there is no clear gap in any of the current provisions relating to market studies and the current mechanisms and powers are deemed adequate.

Any cost/benefit based option study around an independent Market Study body to the Commerce Commission would be supported holding information gathering powers.

The option study recommendation should not be misconstrued to believe in suggesting this MetalsNZ supports it. Its a recommendation in recognition of the gap perceived in NZ's regulatory framework.

This view seems to be the commonly held position in Australia also.

Trans-Tasman harmonization is an important policy issue in a time of increasing legal and economic integration of the two countries. If legislative change occurs in Australia, New Zealand is likely to want to align, otherwise the current alignment best serves the market and consumers at this time.

.....END OF SUBMISSION

APPENDIX

The Issues Paper;

In 2015 Business Growth Agenda progress report announced that the Government would "review the misuse of market power prohibition and related matters" in the Commerce Act 1986.

Anti-competitive exclusionary conduct New Zealand's rule against anti-competitive exclusionary conduct is set out in section 36 of the Commerce Act. The persons subject to the rule are those with a substantial degree of market power. The way the rule is framed is to prohibit the "taking advantage" of market power with the purpose of excluding competitors from the market. There is no defence to a case under section 36 other than to disprove one of the elements of the claim, and the authorisation regime is not available in respect of conduct that will or is likely to breach section 36.

The Issues Paper released seeks to assess the functioning of section 36 of the Commerce Act, as applied by the courts. In this regard, it seeks feedback on what the appropriate criteria for assessment are.

Those that it has chosen on a preliminary basis are:

- whether section 36 is assuring the long-term benefit of consumers;
- whether the application of section 36 is sufficiently simple;
- other potential criteria: alignment with other prohibitions in the Commerce Act, and equivalent prohibitions in overseas jurisdictions; and the small size and remoteness of the New Zealand economy.

Using these criteria, the Ministry's preliminary view is that the operation of section 36 has not been satisfactory. This is because section 36 appears:

- to be failing to maximise the long-term benefit of consumers, by failing to punish anticompetitive conduct by powerful firms;
- to be too complex to allow for cost-effective and timely application; and
- to be misaligned with other prohibitions in the Commerce Act (sections 27 and 47 both include an 'effects test' while section 36 relies on a 'purpose test') and with equivalent provisions in a number of foreign jurisdictions (the US, the EU and Canada do not require that a powerful firm 'take advantage' of its market power).

Alternative enforcement mechanisms. A problem facing jurisdictions around the world is the high cost and delay associated with standard competition law enforcement processes. In this context, competition regimes throughout the world have developed alternative enforcement mechanisms that are designed to resolve competition issues in an efficient manner – essentially, by avoiding a full substantive process. The two main alternative enforcement mechanisms in New Zealand are administrative settlements and the cease and desist regime.

The Issues Paper has adopted, and seeks feedback on, the following criteria for assessing New Zealand's alternative enforcement mechanisms regime:

- whether these mechanisms are assuring the long-term benefit of consumers;
- whether these mechanisms are sufficiently simple;
- respect for natural justice;
- the current need for alternative enforcement mechanisms; and
- potentially, alignment with, but not duplication of, other relevant enforcement mechanisms.

Applying these criteria, the Ministry's preliminary view is that the alternative enforcement mechanisms, taken as a whole, are not operating satisfactorily.

This is because:

- the settlements regime: is weak because it is based on contractual arrangements, for example: financial penalties for the alleged breach of the Commerce Act can only be included with the approval of the High Court; the parties may fail to make all provisions public; and if the settlement terms were breached, the Commerce Commission would have to take a civil claim in the High Court (a long and costly process), and before the court could order that the firm perform its obligations under the settlement, it would have to be convinced that monetary damages were an insufficient remedy. o is misaligned with recent changes to the Fair Trading Act 1986 and the Telecommunications Act 2001, where enforceable undertaking regimes were introduced,

and

- the cease and desist regime: is less needed following changes to the High Court's Commercial List, the introduction of ex ante regulatory regimes in certain sectors, and the fact that the Commerce Commission no longer needs to make an undertaking as to damages when seeking an interim injunction; o has proven ineffective in assuring the long-term benefits of consumers, because it has been used only once in 14 years; o if it were used, would be unlikely to be cost-effective and timely, due to its cumbersome procedural requirements; and o is misaligned

with other relevant legislation (none of the other Acts that the Commerce Commission enforces have a cease and desist regime) and may unduly duplicate the (interim) injunction process. Market studies Recent international developments have shown a growing trend for the use of market studies by competition agencies. While only a handful of states had market studies powers 20 years ago, a 2009 study by the International Competition Network found that at least 40 competition agencies now have the ability to conduct market studies. Different public bodies in New Zealand — such as the Commerce Commission, the Productivity Commission and the Electricity Authority — have varying powers to undertake research that may be described as market studies. However, unlike comparable jurisdictions, there is no formal power specifically directed at analysing competition across any market, for the purpose of improving market performance. This has been identified by the OECD as a significant gap in New Zealand's competition framework.

This Issues Paper canvasses various aspects of the market studies power as it is exists in different jurisdictions. Three interconnected approaches to market studies, as seen in the international experience, are identified: 7

- diagnosing market problems;
- removing regulatory barriers to competition; and
- building an evidence base as a precursor to enforcement.

The Ministry considers that the question of whether New Zealand needs a formal market studies power is dependent on whether there is a definable gap in its competition framework that aligns with one or more of these approaches