# Targeted Review of the Commerce Act 1986: Issues Paper

**Two Degrees Mobile Limited response to the Ministry of Business, Innovation & Employment**

**commerceact@mbie.govt.nz**

9 February 2015

# Contents

# 1 Introduction

2degrees welcomes the opportunity to provide comment on the Ministry of Business, Innovation and Employment Issues Paper, *Targeted Review of the Commerce Act 1986* (the Issues Paper).

The importance of competition as a key driver of efficiencies and economic growth is well-recognised internationally, yet New Zealand's competition law, the Commerce Act, has been the subject of long-standing concerns regarding its inability to effectively address anti-competitive conduct and the effectiveness of the enforcement regime.

As a small, remote economy 2degrees considers it is especially important to ensure an effective competition regulatory framework is in place, which recognises the challenges of a smaller market and the importance of ensuring sustained competitive discipline on operators over time. This view is further reinforced by the recent findings of the Productivity Commission, which concluded as part of its work on the services sector inquiry that low intensity of competition is an important contributor to New Zealand's sub-par productivity performance, particularly in the services sector.

In light of these factors, 2degrees strongly supports this review and considers that further improvements to the Commerce Act and wider competition regulatory framework of New Zealand have the potential to deliver significantly improved competitive outcomes across New Zealand sectors, in the long term benefit of consumers.[1]

Our initial views on the specific matters addressed in the Issues Paper are set out below. In summary:

- We support the Ministry's preliminary view that the operation of section 36 has not been satisfactory and that alternatives, including the potential to shift to an effects test, merit further consideration.
- We support a review of alternative enforcement mechanisms in the Act, including consideration of an enforceable undertakings regime, but do not consider a modified settlements and/or enforceable undertakings regime can be considered a substitute for a cease and desist regime (or interim injunction mechanism) given the time such a process is likely to take. The latter should be considered separately and include input from the Commerce Commission on the workability of each of the current cease and desist and injunction regimes.
- We support the Commerce Commission, as the independent competition regulator, being provided powers to undertake market studies as to the state of competition in different markets.

# 2 Anti-competitive exclusionary conduct

2degrees supports the Ministry's preliminary view that the operation of section 36 has not been satisfactory and that alternatives warrant further consideration.

Section 36 is the principal prohibition of New Zealand's general competition law that deals with anticompetitive unilateral conduct. It covers all sectors including telecommunications, and is

[1] As set out in 2degrees' submissions on the current Telecommunications Act and Radiocommunications Act reviews, there are a range of competition issues that are not adequately dealt with in either the sector-specific regimes or the Commerce Act.

particularly relevant to those aspects of telecommunications that are not covered under the Telecommunications Act wholesale access regime, which includes retail anticompetitive conduct issues and issues regarding services/terms that are not regulated under Schedule 1 of the Act.

An effective section 36 should deter and prevent dominant firms from misusing market power to damage the competitive process (rather than competitors per se) and thus drive efficiencies over time to the long term benefit of end users.

However, experience in the telecommunications sector (including the Telecom/TelstraClear interconnection and 0867 decisions) shows that addressing anticompetitive conduct issues under this prohibition is a long and costly process, which can result in substantial delays and uncertainty in addressing anticompetitive issues and significant long term consumer detriment.[2] Ultimately in the case of telecommunications this was addressed through the introduction of the sector specific wholesale access regime.

Further, the Commerce Commission itself has made clear that it does not consider that the current section 36 enables it to successfully challenge what they consider anticompetitive behaviours, unless such behaviour is egregious, and that the interpretation of the courts (in particular the strict application of the "counterfactual test", as opposed to a range of potentially relevant tests or an effects-based approach)[3] imposes too high threshold, biased towards the dominant operator. Industry, including potential new entrants, cannot have confidence that anticompetitive behaviour that arises can or will be effectively addressed when the competition regulator, experts in competition law and enforcement, has stated the current law is unworkable and has the potential for significant economic harm. The result is a lower degree of risk/competitive discipline on dominant firms and increased costs and risks of investment in entry and expansion placed on smaller firms and new entrants.

We consider the regulator should be confident that its toolkit enables it to address anticompetitive concerns when they arise. This is especially the case given Government decisions not to intervene in other areas can rely on the ability of the Commerce Act to address any competition issues that arise.[4]

While we acknowledge capturing efficiencies is a relevant consideration, it is important to recognise that the impact of a dominant firm versus a smaller firm or new entrant is different (with actions by the latter less likely to be harmful as they attempt to get a foothold in market) and thus sole reliance on a counterfactual test is likely to be inappropriate.[5] Further, it should be recognised that harm to the competitive process over time (including harm to market entry and the ability of firms to expand and provide competitive discipline in the long term) can outweigh shorter term efficiency benefits.

---

[2] For example the 0867 dispute extended over 10 years. Even "successful" cases brought under section 36, such as the data tails case, take an extensive period of time to settle. In the data tails case it wasn't until 2012 when the Court of Appeal upheld that Telecom had breached section 36 over the period from 2001 to 2004 and a $12m penalty was finally payable.

[3] For example in Australia 'direct observation' and 'materially facilitated' tests can also be used. In Europe, the US and Canada the anticompetitive *effect* of the conduct is considered. Under the counterfactual approach as interpreted in the New Zealand court system, a firm can only be in breach if it can be proved that the firm would behave differently in a competitive market. This test does not consider whether any anticompetitive effects from the conduct of the dominant firm outweigh any realised efficiencies.

[4] In this respect we note an effective generic competition law framework could reduce the need for future *ex ante* regulation.

[5] The Commerce Act does recognise that section 36 should only apply to a person with a substantial degree of power in a market, however the interpretation by the Court requires that the dominant firm's behaviour differs from how it would behave in a competitive market. Sector specific competition regulation in New Zealand and internationally also recognises that it is behaviour of firms with market power that is a concern.

This is especially important for a small country like New Zealand where a smaller target market/higher entry barriers can more easily lead to long term market capture by one or two firms and why we consider the key criteria for assessment should be the *long term* benefit of consumers, which takes into account the impact on the competitive process over time.

Having given these issues consideration both the Commerce Commission and the Productivity Commission have concluded that addressing the current issues with section 36 is likely to require legislative amendment of the Commerce Act. 2degrees also support further consideration of the possible improvements identified in the Issues Paper, including consideration of an effects test approach.

While we acknowledge this may reduce the level of certainty for dominant firms acting in potentially anticompetitive manners, some reduction in certainty is likely to be justified given the current position where only egregious cases are likely to be challenged.[6] This uncertainty could be mitigated against, for example with clear guidance on any new interpretation and/or the introduction of an authorisations/public benefits process available for dominant firms that are concerned their actions may breach section 36. A key benefit of a separate authorisation mechanism is that it enables a robust (undiluted) competition law test that addresses anticompetitive conduct concerns, but a process for recognising and enabling efficiency enhancing developments in specific cases where the long term consumer benefits from the conduct are likely to outweigh the competitive harm.

# 3 Alternative enforcement mechanisms

2degrees support a review of the alternative enforcement mechanisms currently set out in the Act.

Anticompetitive behaviour has the potential to cause rapid damage to competition and it is important that the competition regulator is equipped to promptly address such behaviour when it is occurring. Given the time and costs associated with Commerce Act cases it is essential that alternative enforcement mechanisms are provided for alongside the standard enforcement approach.

We recognise the challenges associated with the enforcement of the current settlements regime and as such, consider there is merit in further consideration of an enforceable undertakings regime. Should such a regime be put in place it will require appropriate checks and balances to address natural justice considerations. We also consider that in any undertakings regime the Commission should have the flexibility to accept both structural and/or behavioural undertakings to address potential competition issues that may arise. Divesting of assets will not address all competition issues and in some cases is likely to be disproportionate, for example where remedies such as wholesale access could address the competition concern.

Notably, while we support consideration of amendments to the settlements regime/the potential introduction of an undertakings regime, these should not be considered a substitute for a stop order type mechanism. The settlement/undertaking processes could still take some time and therefore would not address the issue the stop order mechanism seeks to address, which is intended to put a quick stop to likely anticompetitive behaviour before it does significant and/or irreversible harm to market competition. We regard the issue as to whether cease and desist issues are adequately

[6] This is the Commerce Commission's position but challenges with the Act provisions also extend to third parties. The cost and length of time of such cases against a well-resourced dominant firm reinforces this position.

addressed by an interim injunction mechanism as a separate question within the scope of this review.

As set out in the Issues Paper, the cease and desist regime has not been used nearly as often as expected. However we still see value in the capability of the Commission to intervene on an urgent basis where it considers there are breaches of competition law. We are not clear as to the reasons that the Commission had not used this tool more and whether its sees value in keeping it (potentially with amendments to improve usability). Nor are we clear of the Commission's view on whether the interim injunction process is satisfactory.

In making a decision it will be important to understand the Commission's view (for example does the Commission view the procedure as too cumbersome to enable the urgent action that is required/not fit for purpose, does it consider the interim injunction mechanism is sufficient to address the issue or is the lack of use related to challenges with the substantive tests of the Act). Depending on these answers and the Commission's view regarding interim injunctions there may be merit in exploring modifications to improve the cease and desist regime, for example adopting less cumbersome procedures such as the stop order regime under the Financial Markets Conduct Act.[7]

The key issue from our perspective is the ability of the Commission to take timely action where it considers there is a likely Commerce Act breach occurring. In this regard we note that the *ex ante* access regime of the Telecommunications Act is not a substitute for an alternative enforcement mechanism of the Commerce Act. The Telecommunications Act regime is specific to certain regulated services under the Act and does not cover retail anticompetitive behaviour or behaviour regarding new or unregulated services. To have a new service regulated under this Act requires an extensive and costly regulatory process. It is thus not a substitute for the ability for the Commission to intervene on an urgent basis. While there are also enforceable undertakings regimes in lieu of *ex ante* regulation under the Telecommunications Act, we note that in practice these have also involved extensive processes.[8]

In Australia, the Australian Competition and Consumer Commission (ACCC) has a specific stop-go power that applies in telecommunications markets. The Telecommunications Competition Notice regime recognises that anticompetitive conduct can have fast-acting results/long term damage on competition and potential new entrants. Under this regime, the ACCC can issue a competition notice in respect of conduct which it believes has the effect of substantially lessening competition. Substantial fines can apply until the party against whom the competition notice has been issued ceases the anticompetitive conduct.[9] The Telecommunications Commissioner does not have a similar power in New Zealand.

[7] We note that in terms of misalignment between Acts it could be considered that the Financial Markets Conduct Act 2013 and Fair Trading Act 1986 are misaligned in that they both deal with misleading conduct, but in contrast to the Financial Markets Authority under the Financial Markets Conduct Act 1983 under the Fair Trading Act the Commission is unable to issue a cease and desist order. If a modified cease and desist order regime is adopted there may be a case to impose a time limit on these powers in the interest of natural justice considerations.

[8] For example consideration of undertakings as part of the Commission's Mobile Termination Access Service process.

[9] See the ACCC's recently updated guidelines: Telecommunications Competition Notice Guidelines, Issued pursuant to section 151AP(2) of the Competition and Consumer Act, 2010, September 2015.

# 4 Market Studies

2degrees supports the Commerce Commission, as the independent competition regulator, being provided powers to undertake market studies as to the state of competition in different markets.

Market studies can play an important role in assisting the regulator in identifying market problems and regulatory barriers (if any) and build greater understanding of the market and dynamics. We consider this appropriate use of Commission expertise which can help inform Commission, Government and wider industry decision making.

The ability of the regulator to carry out such studies is relatively common overseas. 2degrees considers similar powers under section 9A of the Telecommunications Act to conduct inquiries in relation to telecommunications markets to be a useful addition to the regulatory toolkit.

Any such studies should be at the discretion of the Commerce Commission, as an independent agency. Notably, such studies will require resources to carry out that will need to be balanced against other Commerce Commission priorities.