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Competition and Consumer Policy
Ministry of Business, Innovation & Employment
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Review of section 36 of the Commerce Act and other matters

Electric Kiwi and Haast Energy welcome review of section 36 of the Commerce Act.

It is important suppliers with substantial market power are deterred and prevented from misusing or abusing ("taking advantage of") their market power for anti-competitive purpose.

Based on our experience with establishment of Electric Kiwi and entry into the electricity retail market there are substantial market power and competition issues which are holding back the electricity sector, and harming consumers.[1] Many of these have been articulated in submissions to the Electricity Price Review.

We were not surprised one of the large vertically-integrated gentailers previously opposed the reform of section 36, or that another of the large vertically-integrated gentailers sought to limit the Commerce Commission's jurisdication.

We support the proposed amendment of section 36

We support the proposed amendment of section 36. We consider the change is well over-due, having been considered by the previous Government.

In supporting the MBIE proposals to amend section 36, we are guided by the competition law expertise of the Commerce Commission and the ACCC. Both have raised similar concerns to that of MBIE about section 36.

The Commerce Commission has commented that the support reform of section 36 and a move to a substantially lessening competition test, and has detailed its concerns about the competitive market counterfactual test.[2] The ACCC[3] has also noted that the section 36 provisions (and the previous equivalent section 46 in Australia) are "not fit for purpose (that is, to prohibit misuse of market power)", including because:

> The current section 46 [NZ section 36 equivalent] fails to capture a range of anti-competitive conduct by firms with substantial market power. The Australian Courts have found that conduct by a firm with a substantial degree of market power does not involve a taking advantage of that power if a firm without substantial market power could engage in the same conduct. This ignores the very different consequences that can flow from the same conduct undertaken by a large firm versus a small firm in same the market.

and

> The current purpose test in section 46 [NZ section 36 equivalent] of the CCA is focussed on the impact of the conduct on individual competitors, not on the impact to the competitive process generally. This is inconsistent with the other sections of the CCA and the rationale for having competition laws, which is to protect the competitive process, not individual competitors.

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[1] By way of example, Entrust has recently called on the Commerce Commission to investigate potential restrictive trade practices and collusion by electricity generators Meridian, Genesis Energy, Mercury and Contact Energy's in their arrangements to supply Tiwai Aluminium Smelter with artificially low-cost electricity at the expense of consumers across the country: https://www.entrustnz.co.nz/news/media-releases/entrust-calls-on-commerce-commission-to-investigate-potential-restrictive-trade-practices-and-collusion-by-electricity-generators/

[2] Commerce Commission, Commerce Commission submission to Targeted Commerce Act Review Issues Paper, 10 February 2016.

[3] ACCC, Targeted Review of the Commerce Act 1986, February 2016.

We also consider MBIE's observation that "to our knowledge New Zealand is the only country requiring a strict causal connection between market power and the conduct in question" and "New Zealand is also the only jurisdiction without any consideration of the effects of the conduct" is telling.

Opponents of the status quo need to be able to explain how it is that current New Zealand legislation alone is correct, and all other relevant jurisdictions have erred in setting the thresholds for determining anti-competitive conduct. Opponents would also need to be able to demonstrate why the examples of anti-competitive conduct, MBIE outlined in the consultation paper, that may not breach section 36 should be considered acceptable (and to the long-term benefit of consumers).

Reliance of section 36 and Part 2 of the Commerce Act is a slow process which allows continued and ongoing abuse of market power

Amending section 36 to make it easier to demonstrate that anti-competitive behaviour has occurred, as MBIE propose, should be helpful, but however section 36 is amended demonstrating anti-competitive behaviour is complex and there can be significant information asymmetries to get around to successful demonstrate there has been anti-competitive conduct.

Experience with Part 2 of the Commerce Act shows that addressing anti-competitive conduct issues is a lengthy and expensive process, which means it is a long time before anti-competitive conduct and the resulting consumer detriments are addressed.

For example, the successful 'data tails' case against Telecom related to breaches of section 36 between 2001 and 2004. The case wasn't resolved until 2012 when the Court of Appeal upheld that Telecom breached section 36. In some cases, such as with 0867 and 'data tails' the activity may no longer be a relevant issue by the time the case has been determined.

Changes to section 36 will not change the issues with how long it takes to resolve section 36 cases.

Electric Kiwi and Haast Energy consider MBIE should broaden the focus of the Commerce Act review to consider other remedies which could also help deter and prevent suppliers with substantial market power engaging in anti-competitive conduct.

Penalties for breach of Part 2 of the Commerce Act should be increased

We consider the review of section 36 should include the level of penalties. We support the Commerce (Criminalisation of Cartels) Amendment Bill 2018 but consider that Part 2 Commerce Act penalties should be reviewed more broadly. The last amendment to the penalties was in the Commerce Amendment Act 2001.[4]

The cost-benefit to suppliers with substantial market power from engaging in anti-competitive conduct is impacted by the likelihood of being found in breach of the Commerce Act and the level of penalty (discounted by the amount of time the breach takes to determine). By way of analogy, the higher the level of fines for speeding the less police (and speed cameras) are needed to defer drivers from speeding, and vice versa. Any penalty would also be less effective if it wasn't issued until 10 years after the breach of the speed restrictions.

To this end, the OECD report into Pecuniary Penalties for Competition Law Infringements in Australia 2018 is instructive. The penalties in New Zealand and Australia for breaches of section 36 are essentially the same (the difference is the difference between the value of the New Zealand and Australian currencies). The OECD report noted that "in most regimes pecuniary penalties are set by reference to a detailed and publicly available methodology that focuses largely on the size of the infringing company" and "the maximum penalties that are imposed in Australia for competition law infringements are lower than in comparable jurisdictions".

[4] To keep up with inflation the penalties would need to be increased by 50% in nominal terms.

Industry-specific regulation is more effective than reliance on generic Commerce Act provisions

In the case of the 'data tails' case, the anti-competitive conduct was addressed (prevented) by network access regulation by the Telecommunications Commissioner under the Telecommunications Act before it was resolved by the Courts in the section 36 case.

Unless MBIE is able to find ways to address the amount of time it takes for section 36 cases, and Part 2 Commerce Act cases generally, to be resolved, industry-specific regulation, if operated well, is likely to be more effective than reliance on generic Commerce Act provisions.

If incentives to engage in anti-competitive behaviour are based on market structure the first best solution is also likely to be structural. For example, submissions to the Electricity Price Review made by Electric Kiwi and Haast Energy, other independent retailers, and other stakeholders concerned about competition in the electricity industry, have highlighted the competitive harm caused by vertically-integrated incumbent gentailers. These submissions have recommended structural change, including vertical-separation of generation and retail activities, and horizontal separation (particularly of Meridian) of generation assets to reduce the level of market power, particularly the level of market power during dry-years (when Meridian can essentially operate as a monopoly).

Electric Kiwi has also experienced exactly this abuse in trying to establish metering arrangements as a new entrant electricity retailer. In order to gain access to the market, a mandatory requirement is to also have access to smart metering data for billing and reconciliation purposes. There are only two significant players, one of whom is owned by a vertically integrated generator-retailer. The pricing and terms offered were materially restrictive and costlier than their own subsidiary enjoys, a clear example of high access pricing designed to limit competition.

Eliminating substantial market power (ability to engage in anti-competitive conduct) and/or incentives to engage in anti-competitive conduct (e.g. due to generation-retail-metering vertical-integration) should be seen as a first best solution, and more effective than any reform of Part 2 of the Commerce Act is likely to be.

Concluding remarks

Electric Kiwi and Haast Energy support review of section 36 of the Commerce Act and MBIE's proposed amendments to section 36.

We would like to see the review expand to consider the role of penalties (including raising the levels of penalties) in deterring and reducing the incentives to engage in anti-competitive conduct.

We also consider that it would be worthwhile to consider the extent to which structural remedies and industry-specific regulation have been effective at addressing anti-competitive conduct and competition issues more generally. Submissions to the Electricity Price Review (including Flick and Vocus) have noted the benefits of separation of wholesale (Chorus) and retail (Spark) in telecommunications, while wholesale and retail are largely vertically-integrated in electricity. The limitations of Part 2 of the Commerce Act should be considered when the Electricity Price Review evaluates options for reform of the electricity sector, particularly structural reform of retail and generation.

Yours sincerely,

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