

## NEW ZEALAND

*(1 September 2001 – 31 August 2002)*

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### **1. Executive Summary**

1. This report summarises the major developments in New Zealand's competition law, the enforcement of that law, and in competition policy generally, over the period 1 September 2001 to 31 August 2002.

2. A minor technical amendment was made to the Commerce Act - New Zealand's key competition statute - in the report period. The Commerce (Clearance Validation) Amendment Act 2001 dealt with a transitional issue arising from the significant amendments in the last report period. It clarified the law with respect to applications for clearance of business acquisitions that spanned the date of the changes in legislation.

3. Last reporting period the Commerce Amendment Act 2001 strengthened the core provisions of the Act, lowering the thresholds for the abuse of market power and business acquisitions provisions, and increasing the enforcement powers and resources of New Zealand's competition enforcement agency, the Commerce Commission. Control provisions for electricity lines businesses were also introduced. Under its new responsibilities, the Commerce Commission is currently setting thresholds to identify electricity lines businesses for further control.

4. Sector-specific legislation in the telecommunications and dairy industries was enacted in the report period, and new legislation for the gas sector is being developed. In December 2001 the Telecommunications Act 2001 was passed to reform the regulatory arrangements for New Zealand's telecommunications industry. The new regime is designed to bring greater certainty, investment, competition and consumer benefits. The Dairy Industry Restructuring Act 2001 was enacted in October 2001. The Act authorised the creation of New Zealand's largest company, Fonterra. The Act also put in place a new regulatory regime designed to ensure that farmers have open entry to and exit from Fonterra, thereby minimising any competition problems that might result. Fonterra is now fully subject to the Commerce Act.

5. The Commerce Commission is revising its current leniency policy for whistleblowers and is in the final stages of reviewing its current enforcement criteria.

6. In the area of enforcement, the Commission opened 55 restrictive trade practice or Electricity Industry Reform Act enforcement cases for investigation, and four dairy industry behaviour investigations.

7. Finally, in the 2001/2002 year the Commerce Commission enforcement budget increased by \$1.5 million to \$6.8 million.

### **2. Changes to Competition Laws and Policies, Proposed or Adopted**

#### ***2.1 Changes to Competition Law***

8. The following summarises the major developments in New Zealand's competition law over the period 2001/2002.

### 2.1.1 *The Commerce Act 1986*

9. The Commerce Act 1986 regulates the process of competition in New Zealand. Its purpose is to promote competition in markets for the long-term benefit of consumers in New Zealand. The Act covers anti-competitive conduct in markets within New Zealand, and also overseas business activity insofar as New Zealand markets are affected.

10. A minor technical amendment was made to the Commerce Act - New Zealand's key competition statute - in the report period. The Commerce (Clearance Validation) Amendment Act 2001 dealt with a transitional issue arising from the significant amendments in the last report period. It clarified the law with respect to applications for clearance of business acquisitions that spanned the date of the changes in legislation. The need for this amendment was triggered by the Court of Appeal decision of *Foodstuffs v Progressive Enterprises Ltd* (referred to later in this paper).

11. Last year the Commerce Amendment Act 2001 and the Commerce Amendment Act (No.2) 2001 made significant amendments to the Commerce Act. The Commerce Amendment Act 2001 was enacted in May 2001. Amongst other things, this strengthened the Act's abuse of market power and business acquisition provisions, aligning these with the equivalent Australian competition law and other overseas jurisdictions. The prohibition against misuse of a dominant position (section 36) was amended to prohibit persons with a substantial degree of market power from taking advantage of that power for anti-competitive purposes. The prohibition against anti-competitive business acquisitions (section 47) was amended to prohibit acquisitions that substantially lessen competition. (The previous threshold was a market dominance test.) The new threshold allows the Commerce Commission to consider the prospect of co-ordinated market power, in addition to the more conventional restriction of mergers that result in unilateral market power.

12. The Amendment Act also modernised the provisions on price control, provided for cease and desist order powers, and increased the pecuniary penalties associated with anti-competitive behaviour. The cease and desist order provisions became operative on 1 April 2002 following the appointment of two Cease and Desist Commissioners to the Commerce Commission.

13. The Commerce Amendment Act (No. 2) 2001 came into force in August 2001. This introduced a special statutory scheme for the targeted control of large electricity lines businesses in markets directly related to electricity distribution and transmission. The Commerce Commission, as per its new responsibilities under the Act, is currently looking at the conceptual design of the regime, in particular the setting of thresholds used to identify lines businesses for further investigation by the Commerce Commission.

### 2.1.2 *New Telecommunications Act 2001*

14. Legislation was passed in December 2001 to reform the regulatory arrangements for New Zealand's telecommunications industry. The Telecommunications Act 1987 was repealed and replaced by the Telecommunications Act 2001. The new regime is designed to bring greater certainty, investment, competition and consumer benefits.

15. Central to the new legislation was the establishment of the Telecommunications Commissioner, a dedicated Commissioner residing within the Commerce Commission who is responsible for implementation of the regimes. The Commissioner will work with the industry to promote competition for the long-term benefit of New Zealand.

16. The Commission has three major functions under the Telecommunications Act. These are to:

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- resolve access disputes between carriers;
- oversee the telecommunications service obligations (TSO) regime and apportion the annual costs between carriers; and
- monitor the regulatory regime and recommend to the Minister changes (additions, modifications or amendment) to the list of regulated and specified services.

17. In addition, the telecommunications industry is subject to general market regulation under the Commerce and Fair Trading Acts. The Commission has available to it the full range of enforcement powers under those Acts.

### *2.1.3 Dairy Industry Restructuring Act 2001*

18. The Dairy Industry Restructuring Act 2001 was enacted in October 2001. This provides for the regulatory and structural reform of the dairy industry in New Zealand. The Act removes restrictions on exporting dairy products with a view to stimulating investment and innovation in the New Zealand dairy manufacturing and exporting sector.

19. The Act authorised the amalgamation of New Zealand's two largest dairy co-operatives - New Zealand Co-operative Dairy Company Ltd and Kiwi Co-operative Dairies Ltd - into New Zealand's largest company, Fonterra Co-operative Group Limited (Fonterra). This resulted in Fonterra owning all the shares in the New Zealand Dairy Board. Following the formation of Fonterra, the New Zealand Dairy Board was deregulated and ceased to have a statutory monopoly for the marketing of New Zealand dairy exports.

20. Fonterra is now fully subject to the Commerce Act, and the Fair Trading Act. The Dairy Industry Restructuring Act also put in place new regulatory regime designed to ensure that farmers have open entry to and exit from Fonterra, thereby minimising any competition problems that might result from the creation of such a large co-operative company in the New Zealand context. (The key market being addressed by the regulatory regime is the domestic market for farmers' raw milk.) The changes should provide for significantly improved competition in the processing and marketing of New Zealand dairy products. They should also provide new opportunities for involvement by foreign companies in the New Zealand dairy industry.

21. The Commerce Commission has been allocated a regulatory and enforcement role under the Dairy Industry Restructuring Act 2001. During the period the Commission did not receive any applications for a determination under this Act.

### *2.1.5 The Apple and Pear Industry Restructuring Act Repeal Act 2001*

22. The Apple and Pear Industry Restructuring Act Repeal Act 2001 was passed on 30 September 2001. This repealed the Apple and Pear Industry Restructuring Act 1999 providing for the liberalisation of export marketing of apples and pears.

## **2.2 Other Relevant Measures, Including New Guidelines**

### *2.2.1 New Leniency Policy*

23. The Commission is revising its current leniency policy for whistleblowers. The revised policy will describe how the Commission will exercise its discretion and be lenient if a party co-operates and provides information to the Commission in the course of its enforcement work.

### *2.2.2 Enforcement Criteria*

24. The Commission is in the final stages of reviewing its current enforcement criteria.

25. The Commission receives high volumes of information about possible breaches of the Fair Trading Act. In addition, investigations under the Commerce Act require significant time and resources. Both of these factors mean that the Commission must prioritise its enforcement activity in the areas where breaches of legislation and standards are the most serious and most common.

26. The Commission may initiate an investigation into an alleged breach of any of the Acts it enforces as a result of an initial assessment of information it receives from the public, and from its own market monitoring and surveillance activities.

27. In general terms, enforcement activity is focused on matters where:

- there is a significant detriment to consumers, other businesses or competition in the specific market or associated markets;
- the nature of the behaviour is in itself serious or raises serious issues in law; and
- the behaviour of the sector in which it occurs is an area of strategic priority for the Commission.

28. Strategic priority areas for the Commission are selected on the basis that behaviour within the sectors either currently presents a threat to healthy competition and informed choice or is likely to, given proposed changes in the sector.

29. The necessary prioritisation of issues means that many members of the public do not have their “complaints” investigated by the Commission. Wherever possible, these people are referred to other agencies for further assistance or are provided with information to assist them take their own cases to the Disputes Tribunal.

30. Every alleged breach will involve different circumstances, and the resolution option taken will be selected accordingly. In all cases, however, the Commission’s primary focus is to stop existing practices that are prohibited and deter businesses from starting or repeating prohibited practices.

## **2.3 Government Proposals for New Legislation**

31. There are no specific proposals for new generic competition legislation. However, there are a number of policy reviews underway which could have competition implications. In particular, the Government is currently undertaking a review of the gas sector. Key issues in this review include the

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overall efficiency of the gas sector and the efficacy of the current regulatory environment. On 6 November 2001, the Minister of Energy released a discussion paper that examined factors affecting consumer choice, such as pricing and fixed charges, and discussed issues relating to gas take-or-pay contracts – including their effect on efficiency of gas use. The report identified potential inefficiencies in the transmission and wholesale market for gas. The Ministry of Economic Development is advising the Minister of Energy on these issues.

### **3. Enforcement of Competition Laws and Policies**

#### **3.1 Summary of Activities of the Commerce Commission**

32. The Commerce Commission is the agency charged with enforcing a range of regulatory regimes, both general and industry specific. Its key competition enforcement activities during the year to 20 June 2002 are outlined below. More information can be obtained from the Commission's web site: <http://www.comcom.govt.nz>.

#### **3.2 Anti-competitive Practices**

33. The Commission undertakes market behaviour investigations within its responsibilities under the Commerce Act 1986, Dairy Industry Restructuring Act 2001, and the Electricity Industry Reform Act 1998.

##### **3.2.1 Market Behaviour Investigations**

34. The Commission opened 55 market behaviour (restrictive trade practice) investigations under the Commerce Act during 2001/02 and resolved 38. Market behaviour investigations include investigations of anti-competitive arrangements between competitors, the use of a substantial degree of market power in a market to hinder competition, and breaches of the Electricity Industry Reform (EIR) Act.

35. Of the 38 resolved, the Commission issued five warnings, began civil proceedings in two cases and closed 31 investigations after finding no apparent breach.

36. In addition, the Commission opened four dairy industry behaviour investigations, and resolved two after identifying no apparent breach of the legislation.

37. Where, as the result of an investigation into an alleged restrictive trade practice or an alleged breach of the EIR Act, a breach can be established, the Commission has the option of either administrative resolution or prosecution. The Commission employs two broad types of administrative resolution: warnings and settlements. The particulars of warnings and settlements are decided on a case-by-case basis. The emphasis is on rectifying the problems and restoring effective competition.

##### **3.2.2 Summary of Activities of Courts on Anti-competitive Practices**

38. During the period the Commission chose to take civil action against two restrictive trade practice cases. One involved alleged taking advantage of a substantial degree of power in a market and the other involved alleged price fixing.

### 3.2.3 *Market Behaviour Adjudications*

39. An application for authorisation of a restrictive trade practice requires the Commission to consider the benefit to the public of the acquisition or trade practice, and to weigh this against the resulting or likely detriment to competition.

40. There is no statutory time limit for an authorisation of a restrictive trade practice. However, the Commission will generally aim to complete these within 60 working days.

41. During the period the Commission received three applications for market behaviour authorisations, and no applications for determinations under the Dairy Industry Restructuring Act.

## 3.3 *Mergers and Acquisitions*

### 3.3.1 *Market Structure Investigations*

42. The Commission resolved 30 market structure investigations during the year. The market structure investigations are completed in 1-2 months, but a small number may take longer.

43. At the beginning of the year the Commission had one market structure proceeding before the courts. The Commission did not issue any new enforcement proceeding during the year.

### 3.3.2 *Market Structure Adjudications*

44. Under the Commerce Act, parties may lodge a notice with the Commission seeking a clearance or authorisation of a business acquisition.

45. In considering a clearance application, the Commission's role is to determine whether the merger has, or is likely to have, the effect of substantially lessening competition in any market. The clearance process has a statutory completion time of 10 working days. This time can be extended by agreement between the applicant and the Commission.

46. During the 2001/02 year the Commission received 24 clearance applications. The Commission resolved 25 applications, which included five applications received before the start of the year. Twenty-two applications were granted, two of which included undertakings by the parties that certain assets were to be divested. Of the remaining applications, in three cases the Commission was not satisfied that the acquisitions would not result in a substantial lessening of competition in a market. One clearance application was withdrawn and the Commission had three applications on hand at the end of the year.

47. The clearance process provides applicants with rights of appeal to the court. Interested parties can also issue administrative law challenges against the Commission. During 2001/02 there were three appeals against the Commission's decisions – all of which included administrative law challenges.

48. Market structure authorisations primarily involve business acquisitions where the parties consider that a proposed acquisition will result, or is likely to result, in a substantial lessening of competition in a market. The Commission must grant an authorisation if it is satisfied that the public benefit directly attributable to the acquisition outweighs any detriment. The Commission is required to provide a determination of an application for authorisation of a business acquisition within 60 working days.

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49. The Commission also considers applications for market structure authorisations under the Electricity Industry Reform Act. The Commission may grant exemptions if it is satisfied that the cross-ownership or involvement proposed would not inhibit competition in the industry or permit cross-subsidisation of generation assets or electricity retailing with electricity lines businesses. The Commission may also grant exemptions if it is satisfied that the involvement would result in relationships between lines and supply businesses that are at arms length.

50. During the period the Commission received three applications for market structure authorisations under the Electricity Industry Reform Act. Two applications were granted, with a decision not required on the third.

### *3.3.3 Case: Supermarkets*

51. A significant case over the period is that of Progressive Enterprises' application to purchase Woolworths New Zealand, a key competitor in the New Zealand supermarket market. Progressive lodged their application with the Commerce Commission in May 2001, just prior to the enactment of the Commerce Amendment Act 2001 which changed the merger threshold from one of dominance to that of substantially lessening competition (SLC). The Commission initially considered this transaction under the dominance test and, subject to divestments, determined it could proceed. Foodstuffs, the remaining competitor in this market, then won a Court of Appeal decision to have the application considered under the SLC test. Subsequently, when considering the application under the SLC test, the Commission determined that the transaction could not proceed.

52. The key reason for the change in decision was that under the SLC test the Commission was able to pay greater attention to the whole structure of a relevant market (rather than focussing on the resulting market share of the merged entity), and take into account the effect the acquisition would have on co-ordinated market conduct. The Commission was concerned that the reduction in the number of market players from three to two, in combination with other market characteristics identified as facilitating collusion and discipline, could lead to co-ordinated conduct substantially lessening competition in the New Zealand supermarket market.

53. Progressive subsequently took their case to the Privy Council and won, the Privy Council ruling that the old dominance test should have been applied. The merger has now gone ahead.

54. The Progressive decisions indicate a clear delineation between the old and new tests. However, experience under the new test does not indicate a major shift in the degree of restriction of acquisitions. The proportion of clearance applications that the Commission has approved, about 85 per cent, has not altered over the last two years. Two of the Commission's decisions to decline merger clearance applications under the new threshold have been appealed.

## **4. The Role of Competition Authorities in the Formulation and Implementation of Other Policies**

### *4.1 The Electricity Sector*

55. The electricity industry is subject to general market regulation under the Commerce and Fair Trading Acts, enforced by the Commerce Commission.

56. The Commerce Commission is currently assessing whether to authorise an industry-prepared proposal to establish an Electricity Governance Board under the Commerce Act. This proposal has been prepared in response to a Government policy statement issued in December 2000 (following a Ministerial Inquiry) which stated that a new Electricity Governance Board should be established to replace the three existing industry governance arrangements, as well as to take on some additional responsibilities. If the industry fails to do so, the Government has the power to impose a Crown Electricity Governance Board (Electricity Act 1992).

57. The Commerce Commission also enforces the Electricity Industry Reform Act 1998 as part of its market regulation activities. This legislation separates generation and retail businesses from transmission and distribution businesses. Companies are not permitted to be involved in both areas. The Commission considers applications for exemptions from the restriction. Exemptions are granted provided the Commission is satisfied there will be no adverse effects on competition. The Commission receives approximately two applications each year.

#### *4.1.1 Electricity Lines Businesses*

58. Electricity lines companies are additionally subject to the control provisions of Part 4A of the Commerce Act, introduced last year with the Commerce Amendment Act (No.2).

59. Part 4A of the Commerce Act provides for the Commission to impose regulatory control on large electricity lines businesses on its own initiative, rather than make a recommendation to the Minister of Commerce.

60. In particular, the Commission's responsibilities under Part 4A of the Act include:

- undertaking a comprehensive audit of Optimised Deprival Value (ODV) asset valuations of 29 electricity lines businesses plus Transpower (the national transmission grid). This audit has been completed;
- developing thresholds for the declaration of control of line services;
- investigating lines businesses to assess their performance against those thresholds;
- determining whether to declare regulatory control;
- controlling, if necessary, the line services of any businesses in breach of thresholds;
- authorising Transpower's pricing methodology, if required by Order in Council made on the recommendation of the Minister of Energy;
- developing and administering an information disclosure regime, under which lines businesses must publicly disclose financial and other performance information; and
- undertaking a review of asset valuation methodologies for lines business system fixed assets (currently optimised deprival value (ODV)).

61. The review of valuation methodologies, and the development of thresholds must be undertaken as soon as practicable. The Commission has commenced both projects.

#### **4.2      *Telecommunications***

62.      The Telecommunications Act 2001 provides for a dispute resolution regime for designated and specified telecommunications services to be administered by a Telecommunications Commissioner and the Commission. In addition, the Commission will be required to report on compliance with the Telecommunications Service obligations and allocate the cost of this obligation to all liable parties.

63.      Part of the Commission's preparatory work for making access determinations involved a benchmarking study to identify interconnection prices in comparable countries, and development of parameters for pricing methodologies. The Commission released its benchmarking report in August 2002.

64.      Towards the end of the period, the Commission received three applications for access determinations under the Act. Work on considering these applications is proceeding and will be completed in the first half of 2002/03.

#### **4.3      *Dairy Sector***

65.      The Commission has both enforcement and regulatory control roles under the Dairy Industry Restructuring Act.

66.      In the event that Fonterra does not set a discount rate for calculating its annualised share value for the 2001/02 season pursuant to regulation 9(2) of the Dairy Industry Restructuring (Raw Milk) Regulations 2001, the Commission must determine an appropriate rate. Work on setting the discount rate is in progress.

67.      There have been fewer investigations and adjudication matters for consideration under this Act than anticipated. It is envisaged this will change as industry participants become more familiar with the legislation and its impact on dairy markets.

#### **4.4      *Airports***

68.      The Commerce Commission completed its inquiry into airport services, as requested by the Minister of Commerce. The inquiry considered whether airfield activities provided by the three major international airport companies, Auckland, Wellington and Christchurch, should be controlled under Part 4 (*Controlled goods or services*) of the Commerce Act. Airfield activities are the activities undertaken (including the facilities and services provided) to enable the landing and take-off of aircraft.

69.      The Commission recommended to the Minister that control be imposed on Auckland International Airport and that it should not be imposed in Wellington and Christchurch. A full copy of the Commission's report to the Minister on its inquiry is available at <http://www.med.govt.nz/>.

### **5.      **Resources of the Commerce Commission****

70.      The following represents resources apportioned to the Commerce Commission responsibilities in competition law enforcement.

### 5.1 *Financial*

- Total Annual Budget 2001-02: \$(NZ) 17.7 million \$(US) 8.2 million
- Annual Enforcement Budget 2001-02: \$(NZ) 6.8 million \$(US) 3.1 million (conversion rate @ 0.46 cents)

### 5.2 *Number of Employees*

Category <sup>1</sup>	Numbers	FTE
Economists	6	6
Lawyers	4	4
Other professionals	20	20
Support staff	7.50	7
All staff combined	37.5	37

### 5.3 *Allocation of Human Resources*

Category	Numbers	FTE
Enforcement against anti-competitive practices	24	23.5
Merger review and enforcement	10	10
Advocacy efforts	4	4

## 6. Reference on Competition Policy Issues

### 6.1 *The Commerce Commission*

71. During the report period the Commerce Commission withdrew its publication, *The Commerce Act: A General Guide* (February 1999) following legislative amendments. The Commission has completed a review of the publication, and will release a revised publication relating to anti-competitive practices under the Commerce Act in September 2002.

72. In addition, the Commission has published a series of free brochures on the provisions of the Commerce Act. These are available at the Commission's offices and can be ordered from their website at <http://www.comcom.govt.nz/publications/publist.cfm>.

<sup>1</sup> Economists represents the Economic Services Branch, Lawyers represents the Legal Services Branch, Other professionals represents the Market Structure and Market Behaviour groups in the Business Competition Branch.

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73. Recent publications include:

- Practice Note: 4, The Commission's Approach to Adjudicating on Business Acquisitions under the changed threshold in section 47 – A test of substantially lessening competition (Commerce Commission, 28 May 2001). This is also available on the Commerce Commission's website from <http://www.comcom.govt.nz/adjudication/bag.cfm>.
- Practice Note: 3, Electricity Industry Reform Act 1998 Commission's Role and Processes (Commerce Commission, revised in August 1999). This is also available on the Commerce Commission's website from:  
[http://www.comcom.govt.nz/publications/publications.cfm?year=1999&pub\\_ID=6](http://www.comcom.govt.nz/publications/publications.cfm?year=1999&pub_ID=6)
- Commerce Commission Airports Inquiry Final Report (Commerce Commission, 6 August 2002). This report was written in response to a request from the Minister of Commerce for a study on whether airfield activities provided by the three major international airport companies should be controlled under Part 4 of the Commerce Act. See the airports inquiry website at: [http://www.med.govt.nz/buslt/bus\\_pol/airports/index.html](http://www.med.govt.nz/buslt/bus_pol/airports/index.html)

### 6.2 *Consultant's Reports*

74. *Port Companies and Market Power - A Qualitative Analysis*, Submitted to the Ministry of Transport and the Ministry of Economic Development (Charles River Associates (Asia Pacific) Ltd, 29 April 2002). The purpose of the study is to provide the Government with an overview of competition issues for seaports and the information necessary to make an informed decision about the merits of a Commerce Commission inquiry or other possible courses of action. See the ports review website at: [http://www.med.govt.nz/buslt/bus\\_pol/portsreview/index.html](http://www.med.govt.nz/buslt/bus_pol/portsreview/index.html)