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ANNUAL REPORT ON COMPETITION POLICY DEVELOPMENTS IN NEW ZEALAND

-- 2012 --

This report is submitted by New Zealand to the Competition Committee FOR DISCUSSION at its forthcoming meeting to be held on 30-31 June 2013.

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Executive Summary

1. This report presents the key competition law and policy developments in New Zealand for the year ended 30 June 2013.

2. The report is concerned primarily with two areas of New Zealand's competition law and policy that raise competition concerns under the Commerce Act 1986 (New Zealand's competition legislation): restrictive trade practices (that is, coordinated behaviour involving anti-competitive agreements and conduct involving the unilateral misuse of market power); and business acquisitions and mergers. As well as reporting on key activities and developments during the reporting period, the report includes information on the functions, organisational structure and resourcing of the New Zealand Commerce Commission (NZCC) – New Zealand's principal competition and regulatory authority – in relation to these two areas.

3. The report excludes developments in relation to other functions for which the NZCC is also the enforcement agency. These are various consumer laws and regulatory arrangements in relation to natural monopolies or other markets where competition either is not possible or is limited, with the exception that the report briefly comments on developments affecting the regulatory regimes for the dairy and telecommunications sectors.

4. Section 2 begins by commenting on amendments to New Zealand's competition laws following the passing of the Commerce Commission (International Co-operation, and Fees) Act. It then describes regulatory developments in the dairy and telecommunications sectors. This is followed by a discussion of new publications released by the NZCC in the form of guidelines and fact sheets aimed at making information available about the NZCC's work and educating the public about the provisions of the Commerce Act. Section 2 concludes with a discussion of a major legislative proposal to amend the Commerce Act: the Commerce (Cartels and Other Matters) Amendment Bill.

5. The next three sections of the report concentrate, for the reporting period, on: the NZCC's key activities (section 3); its role in the formulation of competition-related policies (section 4); and issues of the NZCC's organisational structure and resourcing (section 5).

6. To assess its effectiveness and ensure it is delivering value-for-money results, the NZCC carries out stakeholder surveys for the purpose of measuring its targeted advocacy work. It also undertakes *ex-post* reviews of its determinations in order to test the quality of its decision making and identify areas for improvement. Details of these for the reporting period are covered in the first part of section 6.

7. Finally, in the second part of section 6, the report discusses *Competition in New Zealand*. This is a major multi-year cross-departmental research project undertaken to examine competition across the New Zealand economy and determine the nature and extent of competition in New Zealand industries.

1. Introduction

1.1 Background

8. This report describes key competition law and policy developments in New Zealand during the period of 1 July 2012 to 30 June 2013. This period corresponds with the New Zealand government's fiscal year and the New Zealand Commerce Commission's (NZCC's) financial year.

9. The NZCC is New Zealand's primary competition enforcement and regulatory authority.¹ Its purpose is to achieve the best possible outcomes in competitive and regulated markets for the long-term benefit of New Zealanders.

10. The NZCC is responsible for enforcing laws relating to: competition, and economic regulation in markets where there is little or no competition and little or no likelihood of a substantial increase in competition (the Commerce Act 1986); fair trading (the Fair Trading Act 1986); and consumer credit contracts (the Credit Contracts and Consumer Finance (CCCF) Act 2003).

11. With respect to competition law, the purpose of the Commerce Act is to promote competition in markets for the long-term benefit of consumers within New Zealand. The Act prohibits conduct that restricts competition (restrictive trade practices). It also prohibits the acquisition of assets of a business or shares if the acquisition leads to a substantial lessening of competition in a market.

12. Restrictive trade practices include anti-competitive coordinated behaviour and unilateral conduct. Coordinated behaviour refers to agreements between competitors not to compete with each other. Such agreements may relate to price fixing, restricting outputs, allocating customers, suppliers or territories, and bid rigging. Unilateral conduct includes a person or business taking advantage of their substantial degree of power in a market for an anti-competitive purpose, or specifying a minimum price at which their goods or services can be sold by another (resale price maintenance). The NZCC is responsible for enforcing the provisions of the Commerce Act relating to restrictive trade practices.

13. In addition to its enforcement functions, the NZCC has some quasi-judicial functions under the Commerce Act. It can approve a business acquisition or merger that does not substantially lessen competition (known as a clearance). It can also approve a business acquisition that is anti-competitive or a restrictive trade practice that involves an agreement (except one relating to price fixing) but which would ultimately benefit New Zealand consumers (known as an authorisation). The effect of clearance and authorisation determinations by the NZCC is to offer businesses protection from legal action under the Commerce Act.

14. The aim of the two pieces of consumer legislation – the Fair Trading and CCCF Acts – is to promote fair competition and help ensure consumers can be confident of the accuracy of the information they receive when making purchase choices. The Fair Trading Act prohibits false and misleading behaviour by businesses. It also specifies when consumers must be given information about certain products and promotes product safety. The CCCF Act covers consumer lending, consumer leases and buy-back transactions. It requires lenders to disclose certain information to consumers when they enter into a credit contract and sets out rules about interest, payments and credit fees.

15. With respect to its economic regulation functions, the NZCC is responsible for implementing several pieces of legislation aimed at regulating natural monopoly businesses and other markets where competition either is not possible or is limited. Under Part 4 of the Commerce Act, the NZCC currently regulates: electricity lines and gas pipeline services supplied by electricity and gas distribution and transmission businesses; and specified airport services supplied at the three major international airports located in the cities of Auckland, Wellington and Christchurch. The Telecommunications Act 2001 regulates the supply of telecommunications services in New Zealand. The Telecommunications Act is administered by the NZCC under the stewardship of a Telecommunications Commissioner, a statutory position under the Act. Finally, the Dairy Industry Restructuring Act 2001 provides for the regulation of certain aspects of the dairy sector in New Zealand.

¹ The NZCC's website address is: <http://www.comcom.govt.nz>.

16. The NZCC is an independent government entity. Whilst it is primarily accountable to the Minister of Commerce for its performance and outputs, it is not subject to direction from the government in carrying out its enforcement, adjudication and regulatory control activities. The NZCC is, however, required to have regard to statements of government economic policy communicated by Ministers under the Commerce Act or the Telecommunications Act. The NZCC's independence requires it to be an impartial promoter and enforcer of the law.

17. The role of providing government with policy advice on competition matters belongs generally to the Ministry of Business, Innovation and Employment. The demarcation of roles between the NZCC and the Ministry ensures a clear separation and independence between the operational and policy functions within New Zealand's competition regime. That being said, whilst the primary role of the NZCC is an operational one, where relevant, the NZCC uses its experience to provide advice on policy developments and sectoral and legislative reviews, with particular focus on the operational aspects of a regime.

18. Internationally, the NZCC is actively involved with its counterpart agencies through forums such as the Organisation for Economic Co-operation and Development and the International Competition Network. In addition, the NZCC's relationship with the Australian Competition and Consumer Commission is strengthened through Commissioner cross-appointments.

1.2 *Scope of this report*

19. With the above background in mind, the purpose of this report is to describe developments in competition law and policy for the year ended 30 June 2013. The report addresses key competition developments concerning restrictive trade practices and business acquisitions and mergers. This includes comments on the relevant activities, organisational structure and resourcing of the NZCC. The report therefore excludes coverage of any developments related to the consumer laws which the NZCC enforces. It also ignores developments in the economic regulation of goods or services under Part 4 of the Commerce Act.

20. The report does, however, briefly look at changes in the regulatory arrangements affecting the dairy and telecommunications sectors. The reason for so doing is that the regulatory regimes for these two sectors are more in the nature of regulating access to vertically-integrated businesses to promote competition in downstream markets. These access regimes are also transitory in response to how the relevant markets evolve due to, for example, technological or market structure developments. The Competition Committee may be interested to learn how, for instance, structural changes in the telecommunications and dairy sectors affect competition in the relevant markets and the implications of this for economic regulation versus the application of general competition laws.

2. *Changes to competition laws and policies, proposed or adopted*

2.1 *Summary of new legal provisions of competition law and related legislation*

21. Section 2.1 begins by discussing the passing of legislation for the principal purpose of facilitating deeper co-operation between the NZCC and overseas regulators. It then considers recent competition-related developments in the dairy and telecommunications sectors.

2.1.1 *Commerce Commission (International Co-operation, and Fees) Act*

22. Legislation arising out of the Commerce Commission (International Co-operation, and Fees) Act was passed by the New Zealand Parliament on 16 October 2012 and came into force on 24 October 2012. The aim of the Act is to enhance co-operation between the NZCC and overseas competition, consumer and

telecommunications regulators (in particular, the Australian Competition and Consumer Commission),² while ensuring that appropriate safeguards are in place to address public interest concerns, including the maintenance of privacy interests, confidentiality and legal privilege.

23. To achieve this aim, the Commerce Commission (International Co-operation, and Fees) Act amended the Commerce Act, the Fair Trading Act, the Credit Contracts and Consumer Finance Act, and the Telecommunications Act to allow the NZCC to use its statutory powers to provide investigative assistance to overseas regulators and to provide, subject to conditions, compulsorily acquired information to them.

2.1.2 Dairy sector

24. The Dairy Industry Restructuring Act 2001 (DIRA) provided for an authorisation under the Commerce Act to allow for the formation of the dairy co-operative Fonterra. Upon its creation, Fonterra collected 96 per cent of New Zealand's milk production. In recognition of Fonterra's dominant market position, the DIRA set up a unique regulatory regime with the purpose of promoting the efficient operation of New Zealand dairy markets.

25. Fonterra was still subject to the provisions of the Commerce Act prohibiting restrictive trade practices. However, whereas the Commerce Act provides for *ex-post* examination of whether or not a company has taken advantage of market power, the DIRA is designed to act as an *ex-ante* incentive regime such that Fonterra does not have the incentive to act in an anti-competitive manner.

26. In particular, the DIRA promotes contestability in the market for farmers' milk through a requirement that Fonterra operate an "open entry and exit regime". This means that Fonterra must accept all milk supply offers from dairy farmers in New Zealand and allow relatively costless exit from the co-operative. These requirements ensure that Fonterra cannot "lock in" its farmer-suppliers and, as a consequence, Fonterra faces commercial incentives to pay efficient prices for farmers' milk and capital invested in Fonterra.

27. Amendments were made to the DIRA in July 2012 to further bolster the contestability of the market for farmers' milk. The amendments require greater transparency of how Fonterra sets the price it pays farmers for milk and introduce a new farm gate milk price monitoring regime to be undertaken by the NZCC.

28. Section 150A of DIRA specifies that the purpose of the milk price monitoring regime is to promote the setting of the base milk price³ by Fonterra that: (a) provides an incentive for Fonterra to operate efficiently, while (b) providing for contestability in the market for the purchase of milk from farmers.

29. Under the 2012 amendments to DIRA, the NZCC is required to carry out two statutory reviews of Fonterra's base milk price-setting for each milk season, beginning with the 2012/13 milk season. The first review requires the NZCC to report by 15 December each year on the extent to which Fonterra's Farm Gate Milk Price Manual is consistent with the purpose of the milk price monitoring regime.⁴ The second

² The Act contributes to the objectives of the *Single Economic Market Outcomes Framework* jointly announced on 20 August 2009 by the Australian and New Zealand Prime Ministers.

³ The base milk price is the price paid by Fonterra to dairy farmers for raw milk. It is also known as the 'farm gate' milk price.

⁴ The first statutory review report for the 2012/13 milk season was published on 14 December 2012. See Commerce Commission *The Dairy Industry Restructuring Act 2001: Review of Fonterra's 2012/13 Milk*

requires the NZCC to review Fonterra's calculation of the base milk price for each season and report by 15 September on the extent to which it is consistent with the purpose of the milk price monitoring regime.⁵

2.1.3 Telecommunications sector

30. The Telecommunications Act 2001 created an industry-specific regulatory regime for telecommunications, overseen by the Telecommunications Commissioner within the NZCC.

31. The NZCC can set comprehensive terms and conditions for regulated wholesale telecommunications services, such as interconnection, unbundled local loop services and mobile termination. The NZCC can also recommend that new wholesale telecommunications services be regulated, and if the recommendation is accepted by the Minister for Communications, then the service can be added to the schedule of regulated services under the Telecommunications Act. The NZCC produces regular reports on developments in competition in telecommunications markets under its general monitoring powers.

32. In February 2013 the Government announced a review of the Telecommunications Act. The review will take account of the market structure, technology developments and competitive conditions in the telecommunications industry, including the impact of fibre, copper, wireless, and other telecommunications network investment.

33. The first phase of the Telecommunications Act review will focus on how to improve the current copper price-setting process (for a transition period until 2020) to ensure consideration of current and future investments when setting prices. A discussion document was released in 2013, as part of this review.⁶

34. A review of local service Telecommunications Services Obligations arrangements is also underway and a report on the findings of the review is due to be completed in 2013 as required by the Telecommunications Act.

35. New Zealand and Australia agreed on a joint regulatory approach in late 2012 in response to historically high costs of trans-Tasman mobile roaming. In future, NZCC and the Australian Competition and Consumer Commission will collect data and report regularly on wholesale and retail trans-Tasman mobile roaming services. Both Commissions will also gain new powers to intervene in the market if necessary, and legislation to enable these changes is being prepared.

36. To make broadband offerings easier for consumers to understand and compare across different providers, a draft new industry code was developed by the New Zealand Telecommunications Forum in 2013.

Price Manual – Final Report. Available at: <http://www.comcom.govt.nz/regulated-industries/dairy-industry/>.

⁵ The second statutory review report for the 2012/13 season was published after the reporting period for this report, on 16 September 2013. See Commerce Commission *Dairy Industry Restructuring Act 2001: Review of Fonterra's 2012/13 base milk price calculation – Final Report.* Available at: <http://www.comcom.govt.nz/regulated-industries/dairy-industry/>.

⁶ The discussion document was published after the reporting period for this review, in August 2013. See Ministry of Business, Innovation and Employment *Review of the Telecommunications Act 2001 – Discussion Document.* Available at: <http://www.med.govt.nz/sectors-industries/technology-communication/communications>.

2.2 *Other relevant measures, including new guidelines*

37. The NZCC has a statutory role to provide guidance about the provisions of the Commerce Act. As part of this role, the NZCC publishes various written material to inform its stakeholders, such as guidelines and fact sheets.

2.2.1 *Guidelines*

38. NZCC guidelines set out its analytical approach to its enforcement and regulatory work and provide in-depth information and guidance to assist businesses and other stakeholders to understand the Commerce Act and how to comply with it.

Enforcement Response Guidelines

39. The NZCC published its Enforcement Response Guidelines in the period. The purpose of these guidelines is to describe the NZCC approach to enforcing breaches of Parts 2 (restrictive trade practices) and 3 (business acquisitions) of the Commerce Act, outline its enforcement response options, and explain the factors that the NZCC takes into account when deciding which response to use. (These guidelines also apply to the other legislation the NZCC enforces: the Fair Trading Act 1986 and the Credit Contracts and Consumer Finance Act 2003.)

Mergers and Acquisitions Guidelines

40. The NZCC has recently updated its Mergers and Acquisitions Guidelines and Authorisation Guidelines to reflect developments in case law, international experience, and the NZCC's Plain English standard. Following a public consultation period, the NZCC released both sets of revised guidelines in July 2013.

41. The Mergers and Acquisitions Guidelines, which outline the NZCC's approach and process when considering clearances, were last published in 2003. Since then, significant case-law developments have clarified how the merger test and the merger clearance regime apply. As new issues have emerged, the NZCC's thinking has evolved to assimilate to changing international scholarship, research and jurisprudence on antitrust issues.

42. The NZCC has sought to draft the guidelines in a user-friendly and straightforward way. The result is that much of the text from the 2003 guidelines has changed. However, for the most part, this does not signal substantive change. Rather, it simply reflects the wish to make the guidelines more user-friendly and understandable for businesses and their advisors.

43. That said, there are some substantive changes. A short summary of these appears below.

44. The NZCC has explained in detail how it assesses what is likely to occur without the merger (the counterfactual) and under what circumstances it will consider a substantial lessening of competition is likely, applying the approach of the New Zealand Court of Appeal in *The Warehouse case*⁷.

45. The NZCC has emphasised that its focus is on *conditions* of entry and expansion and their role in influencing the likelihood, extent and timeliness of entry and expansion by existing or new competitors.

⁷ Woolworths Ltd & Ors v Commerce Commission (2008) 8 NZBLC 102,128 (HC), and Commerce Commission v Woolworths Ltd & Ors (2008) 12 TCLR 194 (CA).

This change reflects the courts' own move away from the language of 'barriers' to entry and expansion to the term 'conditions'.

46. New Zealand courts have reiterated that market definition is a tool to aid in competition analysis, rather than an end in itself. In particular the NZCC has moved away from defining markets as a first step in the analysis and recognising that relevant markets need not always be defined precisely.

47. The NZCC has included a more detailed explanation of how it assesses mergers between competing buyers.

48. The Mergers and Acquisitions Guidelines clarify the NZCC's analytical approach to efficiencies, and its view that a merger which relies on efficiencies is better dealt with under the authorisation regime.

49. The guidelines also include the NZCC's divestment and failing firm guidelines.

Authorisation Guidelines

50. The Authorisation Guidelines outline the NZCC's approach and process when considering authorisations for anti-competitive mergers and agreements. They replace the Benefit and Detriment Guidelines published in 1997.

51. In particular, the guidelines clarify that the NZCC no longer presumes that an anti-competitive transaction will lead to a loss in productive and dynamic efficiency.

52. In the past, the NZCC moved quickly from finding that a transaction is anti-competitive to assessing the extent of any losses in productive and dynamic efficiency. In effect, there was a presumption that an anti-competitive transaction automatically leads to a loss in productive and dynamic efficiency.

53. However, the revised Authorisation Guidelines explain that the NZCC will assess whether an anti-competitive transaction will be likely to lead to any losses in productive and dynamic efficiency (and if so, their magnitude) on a case-by-case basis.

54. The NZCC's approach will continue to evolve. The revised guidelines will assist businesses to obtain a comprehensive view of the NZCC's approach to clearance and authorisation applications, and assist businesses in their decision making.

School uniforms and supplies – procurement guidelines for schools

55. The NZCC has updated its school uniforms and supplies procurement guidelines. The new guidelines reflect the fact that not only do school boards often have arrangements in place for the supply of school uniforms, but also for school supplies like stationery and, increasingly, electronic items such as tablets or laptops.

56. The guidelines provide guidance on how the Commerce Act applies to exclusive arrangements for school uniforms, stationery and other school supplies. They are intended to help schools maximise the benefits of competition, especially if schools opt for an exclusive arrangement with a supplier.

2.2.2 Fact sheets

57. Fact sheets published by the NZCC provide quick and easy to follow information about anti-competitive behaviour and/or NZCC policies or processes. They are designed to assist the general public,

media, and small businesses that perhaps do not have legal advisers. Relevant fact sheets are provided by the NZCC to people who make enquiries of the NZCC. All fact sheets are available on the NZCC's website.

58. The NZCC has published one new fact sheet during the reporting period. This is *Agreements that Substantially Lessen Competition* (July 2012). This fact sheet explains how and when an agreement may be illegal under section 27 of the Commerce Act. It is designed to give businesses an understanding of when agreements they have with competitors, suppliers or customers may substantially lessen competition in a market.

2.3 Government proposals for new legislation

59. The Government is currently working on a significant amendment to the Commerce Act: the Commerce (Cartels and Other Matters) Amendment Bill. This Bill is part of New Zealand's commitment to achieving the outcomes identified in the *Single Economic Market Outcomes Framework* endorsed by the Prime Ministers of Australia and New Zealand in August 2009.

2.3.1 Commerce (Cartels and Other Matters) Amendment Bill

60. The Commerce (Cartels and Other Matters) Amendment Bill, introduced into the New Zealand Parliament on 13 October 2011, proposes a new exemption regime for collaborative activities, an associated clearance regime, and the criminalisation of hard-core cartel activities.

61. A key feature of the Bill is that it clarifies the definition of cartel conduct to include the forms of cartel behaviour as defined by the OECD: price fixing, output restriction, and market allocation. Cartel conduct is currently prohibited under section 30 of the Commerce Act only to the extent that there is an effect on the price for goods or services. The definition of cartel conduct in the Bill makes it clear that contracts, arrangements and understandings that contain, or give effect to, any of the specified forms of cartel conduct are prohibited.

62. As a counterbalance to this more inclusive definition of cartel conduct, the Bill focuses on the substance of collaborative conduct (rather than on the form) by introducing a collaborative activity exemption. The purpose of the exemption is to ensure that legitimate pro-competitive collaborations are not prohibited. The exemption applies to all pro-competitive, efficiency-enhancing collaborations and not only to structural joint ventures, as currently provided under the Commerce Act.

63. The Bill also introduces a clearance regime to enable firms to approach the NZCC for a ruling on whether a proposed arrangement entered into by parties involved in a collaborative activity would raise competition concerns. In order to grant a clearance, the NZCC would need to be satisfied that the arrangement would not have, or would not be likely to have, the effect of substantially lessening competition in a market, and that if the relevant activity contains a cartel provision, that the provision is reasonably necessary for the purpose of the collaborative activity.

64. The part of the Bill that has attracted the most attention is the proposed imposition of criminal sanctions for hard-core cartel offences. The Bill, however, sets high thresholds for "intent" and "beyond reasonable doubt" criteria which must be satisfied in order for criminal behaviour to be proven.

65. The Commerce Select Committee has reported back on its consideration of the Bill, recommending that the Bill be passed with some amendments including repealing the out-dated competition regime for international shipping in the Shipping Act 1987. Under the Bill, competition in international shipping would be regulated under the Commerce Act. The Bill is awaiting its second reading in the New Zealand Parliament.

3. Enforcement of competition laws and policies

3.1 *Anti-competitive practices*

3.1.1 *Summary of activities*

66. In the year ended 30 June 2013, the NZCC has commenced and/or completed a number of investigations, and has seen the progression of some important litigation. This litigation has related to cartels which have had effects internationally as well as in New Zealand. Further details of these are set out below.

67. Given macro-economic conditions, the NZCC has sought to find the most effective ways to help businesses comply with competition laws. Choosing the right enforcement approach and tools is critical.

68. Throughout the year the NZCC has undertaken both targeted and general education and advocacy work. Through this work, combined with the publication of enforcement action taken, the NZCC hopes to see a lift in business and consumer awareness of competition law, particularly in the sectors targeted by the NZCC.

69. During this reporting period the NZCC continued its targeted advocacy campaign in the non-residential construction sector, the health sector, and in relation to the Christchurch region rebuild as a result of two major earthquakes. These advocacy campaigns continue, although the non-residential construction project has wound down.

70. Table 3.1.1 shows the number of restrictive trade practices enforcement cases investigated by the NZCC and authorisation determinations made in the two years ended 30 June 2012 and 2013.

Table 3.1.1: Restrictive trade practices enforcement and authorisation activity for the years ended 30 June 2012 and 2013

	2012/13	2011/12
Number of coordinated behaviour cases	10	9
Number of unilateral conduct cases	3	2
Number of authorisation applications processed	0	2

3.1.2 *Significant investigation cases*

71. While there has been significant publicity around investigations of an international nature, there has been an increased number of domestic cartel investigations during the last year. This is partly due to an increase in leniency applications through the NZCC's cartel leniency program. Many of the domestic cartels being investigated concern significant industries.

72. That said, the NZCC still has a strong focus on international cartels. A noteworthy investigation concerns allegations of cartel conduct in international shipping transportation. This cartel is the subject of investigation in other jurisdictions.

73. The NZCC has also commenced an investigation under section 47 of the Commerce Act (prohibited business acquisitions that have, or would be likely to have, the effect of substantially lessening competition in a market).⁸

⁸ This investigation is included in the figures in Table 3.2.1 below.

3.1.3 Significant court cases

74. The period since 1 July 2012 has seen some significant judgments regarding penalties for defendants who have admitted entering into various cartels against which the NZCC has commenced proceedings. Penalty hearings have resulted from settlements entered into by the NZCC and defendants in which an agreed penalty has been put to the Court.

75. Some of the judgments and their significance are discussed in turn below.

Kuehne+Nagel freight forwarding cartel proceedings

76. This case arose from the NZCC's proceedings against six freight forwarders. The NZCC had alleged that the defendants entered into and gave effect to price-fixing agreements.

77. All but one of the freight forwarding defendants have settled and paid fines totalling NZ\$8.5 million. Jurisdictional challenges have failed for Kuehne+Nagel International AG and the matter is now proceeding to trial.

Visy: conduct in New Zealand, "carrying on business in New Zealand", "effect on a market in New Zealand"

78. The *Visy*⁹ case relates to an alleged trans-Tasman cardboard packaging price-fixing cartel between Visy Board Pty Limited and its competitor Amcor. Visy admitted its part in the cartel in Australia, but denied that the cartel extended to New Zealand.

79. In these proceedings, Visy challenged on appeal the New Zealand High Court's jurisdiction to hear the case on the basis that:

- a) It had not undertaken conduct in New Zealand.
- b) It was neither resident nor carrying on business in New Zealand and so its overseas conduct was not caught by the Commerce Act.
- c) Even if it was carrying on business in New Zealand, its conduct had not affected a market in New Zealand and so fell outside the scope of the Commerce Act.

80. The New Zealand Court of Appeal unanimously dismissed Visy's protest. In doing so, the Court found on the facts that Visy had engaged in conduct both in and outside New Zealand. In relation to the conduct outside New Zealand the Court explained that:

- a) Whether or not a person is "carrying on business in New Zealand" is a question of fact in each case. A number of factors are relevant and the test must recognise the modern ways in which business is transacted, such as the internet. On the facts, Visy did carry on business in New Zealand.
- d) Conduct will affect a market in New Zealand where it "relates to" a market in New Zealand. Price-fixing conduct directed towards New Zealand consumers will inevitably affect a New Zealand market.

⁹ Commerce Commission v Visy Board Pty Limited [2012] NZCA 383.

81. Following the judgment the New Zealand Supreme Court declined Visy leave to appeal the Court of Appeal judgment. The judgment is significant because it establishes a set of factors relevant to when a person will be carrying on business in New Zealand. It also clarifies that offshore conduct directed towards New Zealand markets will “affect” a New Zealand market for the purposes of jurisdiction.

82. In August this year the NZCC and Visy went to a penalty hearing with an agreed settlement figure.

83. On 21 August 2013 His Honour Justice Venning released the judgment ordering Visy to pay a penalty of NZ\$3.6 million, and its former senior executive John Carroll NZ\$25,000, for breaching the Commerce Act by being involved in price fixing.

Air Cargo price-fixing proceedings

84. The conclusion of the Air New Zealand¹⁰ case in June 2013 brought to an end the long-running Air Cargo proceedings. Having settled with all airlines, penalties in the case totalled over NZ\$42.5 million – the highest ever for a cartel case in New Zealand – with awards of costs of nearly NZ\$3.4 million.¹¹

Table 3.1.2: Air Cargo – total penalties and costs from settlements

	Penalty NZ\$	Costs NZ\$
Qantas	6,500,000	100,000
British Airways	1,600,000	100,000
Cargolux	6,000,000	25,000
Japan	2,275,000	259,000
Korean	3,500,000	259,000
Emirates	1,500,000	659,000
Singapore Airlines Cargo	4,100,000	259,000
Cathay	4,300,000	259,000
MASkargo	2,600,000	659,000
Thai	2,700,000	259,000
Air New Zealand	7,500,000	559,000

85. The Air Cargo case arises from the NZCC proceedings against various international airlines in which the NZCC alleged that the airlines colluded to raise the price of freighting cargo by imposing fuel surcharges on cargo shipments into and out of New Zealand.

86. Throughout the Air Cargo case penalty judgments the Courts have been eager to endorse the public benefits of early resolution and as such limit their role to assessing whether the agreed penalty falls

¹⁰ Commerce Commission v Air New Zealand Ltd (2011) 9 NZBLC 103,318 (HC).

¹¹ All penalties are Crown revenue, and the NZCC forwards all penalty payments to Ministry of Business, Innovation and Employment within five working days of receipt. Costs are apportioned between the Crown and the NZCC.

within an appropriate range. In the Singapore Airlines¹² penalty judgment Justice Allen reinforced this approach. He discussed:

...the significant public interest in bringing about the prompt resolution of penalty proceedings and the role of the court in ensuring the efficacy of negotiated resolutions.

87. The Courts' willingness to adopt a proposed settlement penalty, where appropriate, is significant as it solidifies the NZCC's ability to effectively negotiate settlements with parties which avoids more protracted litigation.

3.2 Mergers and acquisitions

3.2.1 Summary of activities

88. The number of business acquisition and merger clearance applications continues to be lower than in previous years, which the NZCC believes is a result of the global financial downturn. However, the NZCC has noticed a small increase in the number of clearance applications received regarding global mergers.

89. Table 3.2.1 shows the number of merger clearance and authorisation applications received by the NZCC in the two years ended 30 June 2012 and 2013. It also shows any proposed or actual acquisitions or mergers for which clearances or authorisations were not sought but which were investigated by the NZCC to ascertain their effects on market structure and competition (market structure cases).

Table 3.2.1: Mergers and acquisitions activity for the years ended 30 June 2012 and 2013

	2012/13	2011/12
Number of clearance applications processed	9	9
Number of authorisation applications processed	0	1
Number of market structure cases investigated	2	1

90. Table 3.2.2 sets out details of clearances related to merger and acquisitions activity in the year ended 30 June 2013. There were no authorisation applications processed in that period.

¹² Commerce Commission v Singapore Airlines Cargo Pty Ltd [2012] NZHC 3583.

Table 3.2.2: Merger and acquisition clearances for the year ended 30 June 2013

Case	Description	Resolution
Universal Music Holdings Limited and EMI Group Global Limited	Application seeking clearance	Cleared
Fonterra and New Zealand Dairies Limited	Application seeking clearance	Cleared
Vodafone New Zealand Limited and Telstra Corporation Limited	Application seeking clearance	Cleared
Epay New Zealand Limited and Ezi-Pay Limited	Application seeking clearance	Declined
CSR Building Products (NZ) Limited and Brickworks Building Products (NZ) Limited	Application seeking clearance	Cleared
Bligh Finance Limited and Hire Equipment Group Limited	Application seeking clearance	Cleared
Vector Limited and Contact Energy Limited	Application seeking clearance	Cleared
Hamilton Radiology Limited and Medimaging Limited	Application seeking clearance	Declined
Bertelsmann SE & Co. and KGaG and Person plc	Application seeking clearance	Cleared
Perry Metal Protection Limited and CSP Coating Systems	Application seeking authorisation	Withdrawn

4. The role of competition authorities in formulating and implementing other policies

91. As discussed in section 1.1, the NZCC is an independent government entity responsible for enforcing various pieces of legislation. Although it may provide views on competition-related policy developments, this is usually restricted to commenting on operational matters. Fundamentally, to ensure an appropriate separation of policy and operational functions, the competition regime in New Zealand operates on the basis that responsibility for advising government on policy development issues falls upon the Ministry of Business, Innovation and Employment. However, the NZCC may provide advice on or information relevant to policy developments or legislative change when it has relevant expertise.

92. In the relevant period the NZCC has been involved in providing input to the Ministry of Business, Innovation and Employment on a market study examining the costs of residential housing in New Zealand. The New Zealand Productivity Commission released its report on housing affordability in April 2012. As part of the Government's response to this report, the Government asked the Ministry of Business, Innovation and Employment to conduct a market-level study into the residential construction sector to identify market-level barriers to improved housing affordability, with particular reference to the competitiveness and productivity of the sector. Improving the operation of the housing market overall has been identified as a Government priority and improved performance in the residential construction sector is seen as an important driver towards more affordable housing.

93. As the NZCC had been conducting an advocacy campaign in the non-residential construction sector in 2010/11 and 2011/12, it was well placed to provide input into the above market study.

5. Resources of the NZCC

5.1 Human resources

94. The NZCC recognises that one of its most important resources is its people. For this reason, in the year ended 30 June 2013 the NZCC maintained its *Better investment in people* as one of its five on-going strategic programmes aimed at business improvement.

95. The NZCC is led by a Board made up of NZCC Members who are appointed by the Governor-General on the recommendation of the Minister of Commerce (in the case of the Telecommunications Commissioner, on the recommendation of the Minister for Communications and Information Technology) and Associate Commissioners who are appointed by the Minister of Commerce. In addition, under the Commerce Act the Governor-General on the recommendation of the Minister of Commerce must appoint two Cease and Desist Commissioners for the sole purpose of hearing “cease and desist” applications.¹³

96. NZCC Members have both governance and decision-making roles in exercising the NZCC’s powers and functions. At least one NZCC Member must be a barrister or solicitor. The NZCC Board is headed by the Chair and Deputy Chair, who are both NZCC Members. As at 30 June 2013, the Board comprised six Members (including the Telecommunications Commissioner) and two Associate Commissioners.

97. The Chief Executive is responsible for managing the NZCC’s operations and is accountable to the NZCC Board. The Chief Executive is supported by a senior leadership team consisting of three General Managers responsible for the branches of the NZCC: Competition; Regulation; and Organisation Performance.

98. The NZCC’s personnel have a wide range of skills and experience to ensure the organisation’s effective functioning. This includes people with backgrounds in economics, finance, engineering, business and law, and with a mix of both private and public sector experience. As at 30 June 2013, the NZCC employed 79.6 full-time equivalent (FTE)¹⁴ staff in the Competition Branch. This compares with 77.25 FTE staff employed as at 30 June 2012.

99. The Competition Branch deals with both competition and consumer law issues. All staff employed in the Competition Branch can potentially work on either competition or consumer issues. However, personnel are generally divided into teams according to areas of specialisation. Table 5.1 shows numbers of FTE staff in the relevant teams.¹⁵

¹³ Under the Commerce Act, the NZCC has powers to obtain orders against anti-competitive behaviour. Cease and Desist Commissioners are able to make orders to restrain anti-competitive conduct or require a person to do something to restore competition or the potential for competition in a market.

¹⁴ An FTE employee is equivalent to one employee working full time for a full year. There is likely to be less FTEs than actual people employed since some employees are hired on a part-time basis.

¹⁵ Note that Table 5.1 shows the number of staff in the Competition Branch principally employed on competition issues (that is, on restrictive trade practices and business acquisitions and mergers work under the Commerce Act), with the exception of numbers of staff in the advocacy and development team, lawyers and economists, whose expertise is utilised across the Competition Branch (that is, on both competition and consumer law issues).

Table 5.1: Restrictive trade practices and business acquisitions and mergers – numbers of FTE employees as at 30 June 2013

	Restrictive Trade Practices	Business Acquisitions and Mergers	Advocacy and Development	Lawyers	Economists	Total
Technical Staff	12.66	4.79	6.59	13.2	4	41.24
Support Staff		1		3.9		4.9
Total	12.66	5.79	6.59	17.1	4	46.14

5.2 Annual budget

100. The NZCC's operating expenditure for its competitive markets function (that is, restrictive trade practices and business acquisitions and mergers activity) for the year ended 30 June 2013 was NZ\$10.403 million (US\$8.099 million)¹⁶. This compares with operating expenditure for the year ended 30 June 2012 of NZ\$11.763 million (US\$9.158 million).¹⁷ Table 5.2 provides a breakdown of this operating expenditure.¹⁸

Table 5.2: Annual operating expenditure for competitive markets (restrictive trade practices and business acquisitions and mergers) for the years ended 30 June 2012 and 30 June 2013

	Actual 2012/13 NZ\$000	Actual 2012/13 US\$000	Actual 2011/12 NZ\$000	Actual 2011/12 US\$000
Market structure cases	91	71	106	83
Coordinated behaviour cases	1,348	1,049	1,168	909
Unilateral conduct cases	412	321	327	255
Determinations	2,538	1,976	2,591	2,017
Advocacy and development	2,197	1,710	2,014	1,568
Reports to Ministers	0	0	158	123
Litigation	3,817	2,972	5,399	4,203
Total	10,403	8,099	11,763	9,158

¹⁶ All conversions in this report from New Zealand dollars to United States dollars are based on an exchange rate as at 28 June 2013 of NZ\$1 = US\$0.7785. This exchange rate was sourced from the Reserve Bank of New Zealand (available at <http://www.rbnz.govt.nz/>).

¹⁷ To put this expenditure in context, the NZCC's total operating expenditure across all its functions (as discussed in section 1 of this report) for the year ended 30 June 2013 was NZ\$34.077 million (US\$26.529 million). This compares with the NZCC's total operating expenditure for the year ended 30 June 2012 of NZ\$35.297 million (US\$27.479 million).

¹⁸ In Table 5.2, references to "cases" means to investigations undertaken by the NZCC in relation to business acquisitions and mergers for which prior clearances or authorisations were not sought from the NZCC but which the NZCC assesses may raise concerns about competition in the relevant markets (market structure cases), and to potentially anti-competitive coordinated and unilateral conduct. "Determinations" refers to clearances and authorisations considered by the NZCC in relation to notified business acquisitions and mergers, and to authorisations in relation to anti-competitive coordinated conduct.

6. New reports and studies on competition policy issues

6.1 NZCC reports and studies

101. The NZCC has carried out several stakeholder surveys, notably in the health sector, and one *ex-post* evaluation of its work.

6.1.1 Stakeholder surveys

102. One target sector for awareness and understanding of competition law is currently the health sector. In the year to 30 June 2013, the NZCC carried out stakeholder surveys of four professional groups within the health sector. The NZCC found that of respondents who have or have recently had a business role, 54 per cent were aware that the Commerce Act applies to them, but only 11 per cent knew how the Act applies to them. This survey was done in order to benchmark existing levels of awareness and understanding of competition, consumer, and credit law amongst a sample of health providers. The NZCC will then be in a position to measure the impact of targeted advocacy work it is planning to carry out over the next year in the sector.

103. The NZCC is also using the results of the survey to assist in drafting fact sheets tailored specifically for the health sector, to be released early in the new financial year. The fact sheets cover topics of relevance to the industry included setting fees, professional bodies and promoting your services. The NZCC will continue delivering its education initiative before surveying again at the end of the next financial year.

104. The NZCC again surveyed businesses with 100 or more employees to find out if the proportion of businesses that have an active compliance programme had increased from last year. There were increases: 44 per cent of businesses with 100 or more employees had a Commerce Act compliance programme, up from 38 per cent in 2012. This result may in part be due to NZCC's provision of information to industry groups and businesses subject to complaint. The NZCC will continue to work with industry groups and businesses to ensure the level of understanding lifts further.

6.1.2 Ex-post review of merger clearance decision

105. Merger reviews test the quality of NZCC's clearance decisions, and for authorisation decisions, consider whether its assessment of the likely benefits and detriments post-merger was correct.

106. In the year ended 30 June 2013, the NZCC conducted an *ex-post* review of its 2011 decision to grant an authorisation for the joint venture between Southern Cross Hospitals Limited and Aorangi Hospital Limited. The authorisation resulted in the merger of the only two operators of private hospitals in the city of Palmerston North.

107. The NZCC authorised the joint venture because it was satisfied that there was a positive net public benefit. It assessed the detriments arising from likely price increases and increased costs due to a lack of competition. The NZCC assessed benefits as arising from cost savings from rationalising staff, eliminating duplication of administration functions, and consolidating to one site. It also noted other non-quantifiable benefits, such as the potential for increased investment.

108. Because there was a delay in completing the final steps of the proposed joint venture (until August 2012), it is too early to fully assess the actual benefits and detriments against its 2011 estimates. That said, the evidence to date indicates that there have been no significant price increases as yet, and some of the estimated cost savings have occurred. The information the NZCC has collected also indicates that

events have occurred since the joint venture that were not known about at the time of the joint venture. These events may ultimately impact on the size of the cost savings benefits that will be realised.

109. As a result of the late completion of the joint venture, the NZCC will conduct a further review of the authorisation in two years' time when more information will be available.

6.2 *New Zealand study on competition*

110. The previous year's Annual Report discussed *Competition in New Zealand*, a multi-year research project involving the Ministry of Business, Innovation and Employment, the NZCC, the Ministry of Foreign Affairs and Trade, and the New Zealand Treasury.

111. Competition in New Zealand was undertaken to look at competition across the New Zealand economy and determine the nature and extent of competition in New Zealand industries. This recognises that there is currently little or no information of the degree of competition in the majority of industries in the New Zealand economy and how they compare with other economies. The aim of the project is to answer the following questions:

- a) How competitive are sectors in New Zealand?
- b) What is the link between the degree of competition and firm outcomes, such as innovation, productivity and management practices?
- c) How do these compare with other countries?
- d) What are the implications for competition policy and economic policy more generally?

112. The project uses firm level data from the prototype Longitudinal Business Database (LBD) held by Statistics New Zealand. The research team has drawn on international literature and engaged external experts to help develop frameworks and methodologies.

113. The project has considered competition *in* the market (the traditional view), as well as competition *for* the market. Consequently the analysis has looked at the dynamics of markets and the actions and performance of firms to understand competition in New Zealand.

114. The following are key findings from the project so far:¹⁹

- **Firm performance is very dispersed within New Zealand industries.** The significant heterogeneity observed in firm productivity, even within narrowly defined industries, appears to be larger in New Zealand than in other countries (for example, research suggests that the top 10

¹⁹ Some key papers to date are: Doan, T., Devine, H., Nunns, P. and Stevens, P. (2012). *Firm Entry and Exit in New Zealand Industries*. Wellington: Ministry of Economic Development, June. Available at: <http://www.nzae.org.nz/wp-content/uploads/2012/06/Stevens-et-al-NZAE-2012-Firm-Entry-Exit.pdf>; Devine, H., Doan, T. and Stevens, P. (2012). *Explaining Productivity Distribution in New Zealand Industries: The effects of input quality on firm productivity differences*. Paper presented to the New Zealand Association of Economists Annual Conference, Palmerston North 27–29 June. Available at: http://www.nzae.org.nz/wp-content/uploads/2012/07/Devine_Productivity-Distribution-NZAE-2012-14-June.pdf; Devine, H., Doan, T., Iyer., K., Mok, P. and Stevens, P. (2012). *Decomposition of New Zealand firm productivity, 2001–2008*. Wellington: The New Zealand Treasury and the Ministry of Economic Development. Available at: http://www.nzae.org.nz/wp-content/uploads/2012/07/Doan_NZAE-2012-submission_Tinh-Doan.pdf.

per cent of firms in New Zealand are 9.1 times more productive than firms in the bottom 10 per cent, whereas the difference in Denmark is between 1.6 and 3.5 times). Within markets the researchers expect firms to use the same or similar inputs therefore the differences in performance are stark. In New Zealand the researchers observe persistence in the distribution and firms tend to remain a top or bottom performer in the industry. This is interesting because in a competitive market poor performing firms would be expected to be weeded out of a market, allowing resource to be reallocated to a more productive use.

- **Heterogeneity in the market influences the effect of competition on both the firm and the market.** More efficient firms can gain greater market share, at the expense of less efficient firms who may be forced to shrink or leave the market. This must be taken into account when competition within markets is measured. Traditional measures of competition can incorrectly reflect changes in competition when profits are reallocated towards the more efficient firms and the least efficient firms become unviable and fail. The project uses a new measure of competition, the Profit Elasticity (PE) measure²⁰, which is robust to the reallocation of market share.
- **Levels of competition appear to be low in New Zealand.** Despite being close to best practice in terms of competition policy settings, the level of competition in New Zealand industries is lower than the Netherlands and the United Kingdom (for which the researchers have a comparison across measures of PE). This may be a function of the size and distance of the New Zealand economy. The research shows that the industries with the most intense competition – on average, as measured by PE – are manufacturing and construction. It also suggests that there may be room to improve competition in some industries; for example, within service-based industries.
- **High rates of firm entry and exit in New Zealand industries.** Firm entry, exit and competition are interrelated. Entering firms create greater competition and competition in the market influences whether new firms enter. The ease with which a business can be started in New Zealand reflects the high rate of entry. However, while the performance of new firms increases quickly in the first few years of operation, in relation to that of incumbents, their performance does not appear to catch up to the level of incumbents. This raises the question of how low performing entrants can compete with higher performing incumbent firms and remain in the market.
- **How much do new firms contribute to improvements in performance and how much is it due to incumbents?** Competition is a mechanism that drives firms to become more productive by becoming more efficient at what they do or being more creative to escape competition (for example, developing a new product). Productivity growth within an industry is caused by existing firms becoming more productive, more productive firms getting bigger and firms entering and exiting the industry. From decomposing productivity growth²¹ the researchers were able to show that the majority of contribution to productivity growth in New Zealand is from incumbents. There is a smaller positive net effect from more entering firms being more productive than the exiting firms they replace.

²⁰ Griffith, R., Boone, J. and Harrison, D. (2005). *Measuring Competition*. AIM Research Working Paper Series, No. 22. Advanced Institute of Management Research.

²¹ Melitz, M.J. and Polanec, S. (2009). *Dynamic Olley-Pakes Decomposition with Entry and Exit*. University of Ljubljana, Working Paper No. 03/09.