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**ROUNDTABLE ON CHANGES IN INSTITUTIONAL DESIGN OF COMPETITION AUTHORITIES**

-- Note by New Zealand --

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## NEW ZEALAND

### 1. Introduction

1. As one of the smallest economies in the OECD, New Zealand faces some unique challenges in the design of its competition institutions. These challenges have been revisited on a regular basis as New Zealand's competition policy has evolved in line with international best practice for a small open economy. This submission seeks to draw out the key design principles and practical considerations to which decision makers have had regard.

### 2. New Zealand's competition authority institutional settings

2. New Zealand has a multi-function competition authority with the New Zealand Commerce Commission (the NZCC) being responsible for generic competition law enforcement, economic regulation, and consumer law enforcement. It is responsible for enforcing laws relating to competition, fair trading, and consumer credit contracts, and has regulatory responsibilities in the electricity lines, gas pipelines, telecommunications, dairy and airport sectors. Its publicly stated mission is to achieve the best possible outcomes in workably competitive and regulated markets for the long-term benefit of New Zealanders. The NZCC has a staff of 184 full time equivalent employees and a total budget of approximately NZ\$41 million (US\$32M).<sup>1</sup>

3. The issue of institutional design has arisen frequently through various reforms of competition law. This paper will focus on two of these: i) independence and accountability; and ii) multifunction versus single function competition authorities, with an emphasis on drawing out insights for small open economies.

### 3. Independence and Accountability

#### 3.1 Entity form and independence

4. Like most OECD countries, New Zealand's competition and regulatory agency is at arm's length from Executive Government. The NZCC is an Independent Crown Entity under the Crown Entities Act 2004. This organisational form is often employed for entities that have quasi-judicial functions, where directions from Executive Government would be inappropriate. The legislation establishing the NZCC (the Commerce Act 1986) provides that the NZCC must act independently in performing its statutory functions and duties and exercising its powers.

5. However, the nature of the functions, duties, and powers delegated to it by Parliament differs across competition/consumer law and economic regulation. In competition and consumer law, the NZCC independently enforces a set of prohibitions and administrative procedures that have the ultimate aim of enhancing long-term consumer welfare. It is free to determine its own enforcement and advocacy priorities, and freely chooses the cases it investigates and prosecutes. While the NZCC has the power to

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<sup>1</sup> Commerce Commission, *Annual report 2013/14*, <http://www.comcom.govt.nz/the-commission/about-us/accountability/>.

issue infringement fees in some areas of consumer law, more serious breaches of competition and consumer law are adjudicated by the court system i.e. the NZCC is the plaintiff in the generic court process rather than the final decision maker/adjudicator.

6. In economic regulation, the NZCC has both an advisory and an implementation role reflecting the highly technical nature of this function. Decisions on whether economic regulation should be extended to goods or services where it has not previously applied, or where a different type of regulation is proposed to be applied, can only be made following investigation and analysis by the NZCC. Recognising that these decisions usually involve complex judgements about the weights that should be given to producer and consumer welfare, the final decision on whether to regulate or change the form of regulation rests with the relevant Minister.<sup>2</sup> Once a decision by the relevant Minister has been made to regulate or change the form of regulation, the NZCC has full independence to implement regulation within the framework set out in the empowering legislation.

### **3.2 Accountability arrangements**

7. Accountability for regulatory decision making is provided through a multifaceted approach. New Zealand's public sector management framework<sup>3</sup> provides for the specification of ex ante output and outcome measures together with evaluation and review ex-post. The performance of the NZCC is monitored by the Ministry of Business, Innovation and Employment (MBIE) which also has responsibility for policy advice on the competition, consumer and regulatory frameworks.<sup>4</sup> In addition to this generic accountability framework, there are also a range of judicial and merits appeals that are applicable to different types of NZCC decisions. In general, the type of appeal right that is provided is governed by the nature of the required decision and who the initial decision maker is.

### **3.3 Governance**

8. The NZCC is governed by a board of between four and six members (the Commissioners) who have executive decision making powers on certain competition, consumer and economic regulation issues delegated to them by Parliament.<sup>5</sup> The board is also responsible for the overall governance of the NZCC. Appointments to the board are made by the Governor General<sup>6</sup> on the recommendation of the relevant Minister. Appointments are generally for a term of five years, although shorter term appointments are sometimes made to reflect the nature of the work before the NZCC or to observe the constitutional conventions that apply in the 'period of restraint' before General Elections. In making appointments, the Minister of Commerce will consult other Ministers who have an interest in the work of the NZCC, particularly the Minister of Communications (for telecommunications regulation) and the Minister of Primary Industries (for dairy regulation). The Minister for Communications is responsible for appointing

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<sup>2</sup> Under Part 4 of the Commerce Act 1986, the Minister of Commerce can either accept or reject the Commission's recommendation following a Part 4 inquiry. If the Minister rejects the Commission's recommendations, the Minister must publicly release the reasons for the rejection. Under the Telecommunications Act 2001, the Minister of Communications can accept, reject, or require the Commission to reconsider its recommendations to alter regulated services.

<sup>3</sup> The three pillars of New Zealand's public sector management framework are the State Sector Act 1988, the Public Finance Act 1989, and the Crown Entities Act 2004.

<sup>4</sup> The Ministry of Primary Industries is the lead policy agency in relation to dairy regulation.

<sup>5</sup> The Commerce Act also provides for the appointment of Associate Commissioners in relation to a matter or a class of matters to be specified in the notice of appointment.

<sup>6</sup> The Governor General is New Zealand's effective head of state, being Queen Elizabeth II's representative in New Zealand.

the statutory position of Telecommunications Commissioner. Cross-appointments between the NZCC and the Australian Competition and Consumer Commission (ACCC) are also made to promote the development of a single economic market between New Zealand and Australia, and to help co-ordinate of the enforcement of anti-competitive or unfair conduct laws or the review of mergers that impact on both jurisdictions. While appointments can be an important accountability tool, the Executive has very limited ability to replace Commissioners before the end of their term in the absence of some form of gross misconduct. The board appoints the NZCC's Chief Executive following consultation with the State Services Commission on the terms and conditions of employment.<sup>7</sup>

### **3.4 Funding**

9. Funding for the NZCC's activities is appropriated by the New Zealand Parliament, although decisions on the level and structure of funding are effectively decided by the Executive. New Zealand has a strong history of bipartisan support for ensuring that the NZCC is a well-funded and credible competition, consumer, and regulatory authority. The adequacy of the NZCC's funding is monitored by the MBIE. Funding is increased or decreased from time to time depending on the volume and nature of work that is before the Commission. In general, funding for generic competition and consumer activities is separated from economic regulation, and in some cases is the responsibility of different Ministers.<sup>8</sup> Regulatory activities tend to be funded by industry levies whereas competition and consumer law enforcement and advocacy activities are largely Crown-funded. Major litigation is funded through a dedicated Crown appropriation and the NZCC is able to draw on significant financial reserves in the advent of unforeseen circumstances or an adverse cost award in its enforcement activities. The NZCC is regularly called before Parliamentary Select Committees that oversee the expenditure of Government funds.

10. The combined impact of these institutional settings is a competition, consumer and regulatory authority that is independent from Government in its day to day operations. However, this independence is balanced by a set of accountability arrangements that monitor the NZCC's delivery on its statutory objectives.

## **4. Multi-function competition authorities**

11. New Zealand has seen periodic debate about whether a multi-function competition authority or a more narrowly focussed authority is the best institutional approach. This has been part of a wider debate about the merits of regulatory institutions having multiple functions given New Zealand's limited fiscal and human resources.<sup>9</sup> As in most OECD countries, the concept of a joint competition and consumer protection authority is generally accepted in New Zealand. While the nature of competition and consumer functions is not identical, the inherent similarities in the outcomes sought and enforcement approaches means there is little academic or practitioner debate on them being combined in a single entity. However, there is far less consensus about whether the implementation of economic regulation should sit alongside

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<sup>7</sup> The State Services Commission is the public sector department responsible for appointing and managing the performance of public service Chief Executives. Its role in relation to Crown Entity Chief Executives is explained at: <http://www.ssc.govt.nz/cegmls4>

<sup>8</sup> In particular, funding for telecommunications regulation is the responsibility of the Minister for Communications. Funding and accountability arrangements for the regulation of dairy, airports, electricity lines, and gas pipelines are the responsibility of the Minister of Commerce and Consumer Affairs. However, the portfolio ministers for Primary Industries, Energy, and Transport are regularly consulted on funding and accountability issues.

<sup>9</sup> For example, the Reserve Bank of New Zealand includes both prudential regulation (including insurance) and monetary policy.

the enforcement of competition and consumer law. Discussion in this section will therefore focus on this dimension of the multi-function competition authority debate.

12. Whether or not to institutionally combine economic regulation functions with the enforcement of competition and consumer law has been considered a number of times in New Zealand, most notably in 2007/08 when the generic approach to economic regulation in Part 4 of the Commerce Act 1986 was significantly reformed. Given the high degree of economic integration and similarities in competition law between New Zealand and Australia, the draft proposal of the Australian Competition Policy review to separate out the economic regulation functions of the ACCC into a new regulatory authority is likely to spark another round of debate in New Zealand. Looking around the world, numerous jurisdictions have made changes to their institutional arrangements in recent times. However, it is difficult to discern a clear direction of change with some jurisdictions moving towards multifunction institutions (e.g. Spain and the Netherlands), while others appear to be moving in the opposite direction (e.g. Australia). It is worth noting that compared to many other OECD countries, New Zealand applies economic regulation to a narrower range of goods and services, recognising the different structure and institutional settings around many New Zealand markets.

13. Debate on the pros and cons of a multifunction competition authority for New Zealand has tended to focus on two competing arguments: (i) regulatory culture and capture; and (ii) economies of scale and scope. Opponents of multifunction competition authorities in New Zealand emphasise the different regulatory culture and approaches required between competition/consumer law and economic regulation. They contend that the implementation of ex-ante economic regulation requires a forward looking focus on positive behavioural obligations consistent with a long-term regulatory partnership/contract, whereas the enforcement of competition/consumer law involves the enforcement of ex-post or backward looking negative duties. In their view, combining these functions results in the authority putting too much emphasis in its regulatory functions on short term wealth transfers to consumers that undermine the incentives for investment that promote the longer term interests of consumers. These arguments have been mirrored in the recent debate in Australia.<sup>10</sup>

14. Proponents of multifunction authorities tend to focus on the potential for significant economies of scale and scope. Because of the small size of the New Zealand economy, New Zealand institutions tend to be much smaller than comparable institutions in other jurisdictions. For example, the NZCC's full time equivalent staff complement is a quarter of that in the comparable Australian institutions.<sup>11</sup> Questions regularly arise in New Zealand about the 'minimum efficient scale' or 'critical mass' for public service departments and regulatory agencies. Separating out the NZCC's regulatory functions into a standalone agency would be likely to result in an agency of around 60 to 70 staff. Ministers and officials have historically thought that a regulatory agency of this size is unlikely to be sustainable in the medium term, particularly given the difficulties in securing suitably qualified Commissioners for multiple agencies from a small talent pool.<sup>12</sup>

15. On economies of scope, proponents of multifunction authorities argue that there are significant spill-over benefits from combining functions given the similar outcomes sought, and that the underlying

<sup>10</sup> Australian Competition Policy Review, Draft Report, September 2014 available at <http://competitionpolicyreview.gov.au/draft-report/>.

<sup>11</sup> The New Zealand Commerce Commission has a complement of 184 full time equivalent staff: <http://www.comcom.govt.nz/dmsdocument/12697>. The Australian Competition and Consumer Commission (ACCC) and the Australian Energy Regulator (AER) have a combined staff of 736: [https://www.accc.gov.au/system/files/866\\_Annual%20Report\\_2013-14\\_COMPLETE\\_FA\\_WEB.pdf](https://www.accc.gov.au/system/files/866_Annual%20Report_2013-14_COMPLETE_FA_WEB.pdf).

<sup>12</sup> For similar reasons, the separation of regulatory rule making and implementation into separate regulatory agencies has not been pursued in New Zealand.

skill sets of most Commissioners and staff are grounded in law and economics. It is often argued that having both competition/consumer law and economic regulation functions allows a variety of work for staff that promotes recruitment and retention. The international trend towards the promotion of greater competition in regulated sector supply chains is also cited as an argument in favour of multifunction agencies given the synergies and knowledge spill-overs that can arise from having both competition and regulatory functions under one roof. In a New Zealand context, these spill-overs can flow in both directions as a competition analysis is a pre-requisite to the imposition of economic regulation, and merger analysis often occurs in sectors like telecommunications where economic regulation staff have detailed and valuable industry knowledge. Finally, proponents of multifunction agencies point to the concept of regulatory capture. They argue that the possibility of capture of regulatory decision makers by the industries they regulate is reduced in an agency that regulates multiple sectors or also has competition and consumer law functions.

16. In dealing with these opposing arguments, New Zealand has resorted to innovative solutions that reflect its status as a small, open economy in its design of regulatory agencies across many sectors of the economy. Administrative solutions have generally been favoured to deal with issues that larger countries have resolved through structural solutions. For example, in 2009/10 the NZCC underwent a restructure that separated competition and consumer law work into a separate branch from the NZCC's economic regulation work. The ability of the NZCC board to divide into sub-committees has also allowed Commissioners to specialise in the competition, consumer, or economic regulation work of the NZCC. In addition, the Telecommunications Act 2001 requires the appointment of a Telecommunications Commissioner who is empowered to discharge some regulatory functions independently of the rest of the board. It can be argued that the combined effect of these administrative arrangements is that the key benefits of a structurally separated economic regulator can be achieved concurrently with the key benefits cited for a multifunction competition agency. That said, some flexibility in this approach is likely to be desirable given the relatively small number of Commissioners and the difficulties that can be experienced in finding a sufficient number of appropriately qualified Commissioners to fill separate pools. This issue can be particularly acute during times of transition between existing and new Commissioners.

#### **4.1 *Overlap between generic and sectoral regulators***

17. One final aspect of multifunction agencies that has been raised from time to time is the potential for regulatory gaps or overlaps to arise between generic regulators (e.g. the NZCC) and sectoral regulators (e.g. Electricity Authority, Financial Markets Authority, Reserve Bank of New Zealand).<sup>13</sup> These issues arise in all OECD jurisdictions given the different outcomes, approaches, and skill sets of generic and sectoral regulators. However, they can be more problematic in a small open economy like New Zealand where the resources devoted to regulatory activities can be a fraction of those in larger jurisdictions. Rather than throw more resources at these issues, New Zealand has tended to manage the potential for gaps and overlaps through communication and co-ordination between regulators.<sup>14</sup> Specific tools used include memoranda of understanding, cross-appointments, and regular cross-agency staff meetings, between the

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<sup>13</sup> For example, see New Zealand Productivity Commission, *Regulatory Institutions and Practice Final Inquiry Report*, 2014: <http://www.productivity.govt.nz/sites/default/files/regulatory-institutions-and-practices-final-report.pdf>.

<sup>14</sup> For example, consideration has recently been given to whether consumer credit regulation should sit with the NZCC or the NZ Financial Markets Authority (NZFMA).

generic competition agency and sectoral agencies.<sup>15</sup> The NZCC also shares some back office functions with the Electricity Authority.

## **5. Concluding remarks**

18. Designing competition authorities is a complex and controversial issue around the world. The significant variance across in international practice suggests there is no single correct design or template that can be applied across multiple jurisdictions. Instead, jurisdictions must consider a range of factors in the design of their institutions. These include the nature of competition issues in their economy, the available financial and human resources, and the public sector management and constitutional conventions of the jurisdiction. In New Zealand, the small scale of the New Zealand economy and accompanying limited financial and human resources has necessitated innovative approaches to institutional design. Where larger countries have used structural and resourcing solutions to address institutional design issues, New Zealand has tended to use administrative solutions. The efficacy of these solutions is likely to come under increasing scrutiny in the near future in light of recommended changes to institutional arrangements in Australia.

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<sup>15</sup> For fair trading in financial products, the NZCC and the NZFMA signed a memorandum of understanding to provide stakeholders with clarity on the respective roles of the two organisations – see <http://www.comcom.govt.nz/dmsdocument/11723>.