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WINDOW DRESSING: THE COMMERCE  
AMENDMENT ACT 2001 AND POLICING THE  
MISUSE OF MARKET POWER IN NEW ZEALAND

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## 1 INTRODUCTION

### *Abstract*

This paper examines the reforms to New Zealand's misuse of market power provision brought about by the Commerce Amendment Act 2001. The issues that led to the reform are explored including the dissatisfaction with the courts' prior application of section 36 of the Commerce Act 1986, the public outcry triggered by the difficulties in establishing competition in the electricity and telecommunications industries, and the competition policies of the Labour-Alliance Coalition Government. The amendments themselves are then examined before the reasons why the Government opted for the reforms it did are discussed. The paper concludes that little significant change to section 36 has resulted, and that the reforms have failed to bring about the certainty and strengthening of the laws against the misuse of market power intended and promised. The primary reason put forward for this is the inability or unwillingness of the Coalition Government to take a clear position on the fundamental purpose of our competition laws.

### *Statement on word length*

The text of this paper (excluding contents page and footnotes) comprises approximately 15,800 words.

## *I INTRODUCTION*

In 2001 the Labour-Alliance Coalition Government passed the Commerce Amendment Act in a move designed to strengthen New Zealand's competition laws. One of the key reforms made was to the misuse of market power prohibition embodied in section 36 of the Act. This paper outlines the context and substance of the changes and asserts that there has in fact been no significant reform. It also examines the aspirations of the Government in passing the amending legislation and the beliefs underpinning those aspirations, in an attempt to understand how and why a golden opportunity to revitalise an ailing section of our competition law was seemingly passed up.

Before doing so, it is helpful to establish some basic principles regarding the prohibition of the misuse of market power, and the reasons why a provision such as section 36 is considered necessary in the regulation of our markets.

## *II THE DOMINANT POSITION PARADIGM*

Monopolists and dominant firms that face little or no competition are typically considered to indulge in such practices as inefficient or limited production, lack of innovation and the extortion of monopolistic prices from consumers. Such firms have every incentive to ensure the continuation of that state of affairs by deterring or restricting the development of meaningful competition in the markets in which they operate. Their dominance in the market often means that without some form of intervention, they will be successful in preserving their privileged position.

While the need to regulate the behaviour of firms that dominate their market sector is a fundamental concern of competition law, there are divergent beliefs as to why such control is needed. Two principal schools of thought behind the prohibition of misuse of market power are evident: those that see the primary reason for the prohibition as based on principles of social policy and fairness, and those that ground competition law and the control of dominant firms' behaviour in the promotion of economic efficiency.

## A *Social Principles of Competition Law*

Social concerns associated with the regulation of dominant firm's behaviour and the promotion of the competitive process have typically been associated with the 'Traditional', 'Populist' and Harvard schools of competition law. These schools display a policy preference for diversity and opportunity for the unestablished, founded upon political principles reflecting a vision of society, and a vision of the individual's participation in the economic enterprise.<sup>1</sup> Typically these schools evince an underlying distrust of big business and "concern for consumers; concern for the 'little man'; interest in access, diversity and pluralism; and condemnation of coercion and exploitation."<sup>2</sup>

While noting that increased competition leads to increased economic efficiencies, these schools draw a link between high concentrations of market power, diminished competition, and negative impacts on consumer wellbeing. Fewer competitors and low competitive pressures in a market are believed to result in less choice and higher prices for consumers. Key to the promotion of competition is the protection of small business, illustrated by Judge Learned Hand in *United States v. Aluminum Co. of America*:<sup>3</sup>

Throughout the history of the antitrust laws it has been constantly assumed that one of their purposes was to perpetuate and preserve for its own sake and in spite of possible cost, an organization of industry in small units. . . .

For these reasons, based more on notions of equity than efficiency, firms dominant in a market should be constrained to act in a manner that does not hinder the ability of smaller firms to compete in that or another market. To this end dominant firms have a special responsibility not borne by smaller firms. In the words of Scalia J in *Eastman Kodak Co v Image Technical Services Inc (Eastman Kodak)*:<sup>4</sup>

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<sup>1</sup> Eleanor M Fox and Lawrence A Sullivan, "Antitrust - Retrospective and Prospective: Where Are We Coming From? Where Are We Going?" (1987) 72 NYUL Rev 936, 942; see also Lawrence A Sullivan "The Viability of the Current Law on Horizontal Restraints" (1987) Cal L Rev 835, 841 pronouncing a positive relationship between an economy in which many have a personal stake and degree of control and democratic and liberal polity.

<sup>2</sup> Eleanor M Fox "The Battle For The Soul of Antitrust" (1987) Cal L Rev 917.

<sup>3</sup> *United States v. Aluminum Co. of America* (1945) 148 F 2d 416, 429 (2d Cir).

<sup>4</sup> *Eastman Kodak Co v Image Technical Services Inc* (1992) 504 US 451, 488.

Where a defendant maintains substantial market power, his activities are examined through a special lens: Behaviour that might otherwise not be of concern to antitrust laws – or that might even be viewed as procompetitive – can take on exclusionary connotations when practiced by a monopolist

In the United States, the values of the Harvard School of competition law were largely discredited during the rise of the Chicago School, however these values have resurfaced in the thinking of the 'New Coalition'<sup>5</sup> and also find expression in the competition laws of the European Union.<sup>6</sup> The preamble to the Treaty of Rome itself expresses values of social policy, fair competition and the protection of small and medium sized firms.<sup>7</sup>

### ***B Economic Principles: The Promotion of Efficiency***

While the promotion of efficiency had generally been associated with competition law, it became its almost singular focus in the United States following the rise to prominence of the Chicago school of competition law. The Chicago school views the primary objective of competition law as maximising consumer welfare<sup>8</sup> through efficiency in the use and allocation of resources. Asserting that the competitive forces of the market punish inefficiency faster and better than the machinery of law<sup>9</sup> the Chicago School argues for minimal legislative control over markets. The law it is argued should only intervene in the market to reprehend inefficient behaviour.<sup>10</sup>

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<sup>5</sup> See generally Fox, above.

<sup>6</sup> See *Michelin NV v EC Commission* [1985] CMLR 282, 326: “[a firm in a dominant position] has a special responsibility not to allow its conduct to impair genuine undistorted competition...”

<sup>7</sup> Valentine Korah *An Introductory Guide to EC Competition Law and Practice* (6ed, Hart Publishing, Oxford, 1997) 76.

<sup>8</sup> See generally Robert Bork *The Antitrust Paradox: A Policy At War With Itself* (Basic Books, New York, 1978) 90-117: consumer welfare is defined as the increase of aggregate wealth or the sum of producer and consumer welfare, on the premise that if producers make more money, consumers benefit because producers will invest in things that consumers want. Thus if consumers lose, but producers benefit more than consumers lose, consumer welfare has been increased.

<sup>9</sup> Frank H Easterbrook “The Limits of Antitrust” (1984) 63 *Tex L Rev* 1, 24.

<sup>10</sup> Easterbrook, above, 23.

While the Chicago school of competition law has attracted its share of criticism in recent times,<sup>11</sup> its emphasis on economic analysis and the promotion of efficiency, with a greater emphasis on innovative or dynamic efficiency,<sup>12</sup> remain popular principles of competition law.<sup>13</sup>

Those who view efficiency as the core concern of competition law claim that dominant or monopolistic firms that do not face competition from other efficient firms should only be subject to regulatory intervention if they operate inefficiently or suppress innovation.<sup>14</sup> The market is considered able in most instances to discipline such inefficient behaviour through the responses of efficient competitors, both actual and potential. Competitors using new technologies or more efficient production methods can compete on product quality and price with the incumbent dominant firm, thereby forcing the incumbent to operate more efficiently themselves, or face a reduction in their market share and profits. Consumers then benefit through improved product, greater product choice and lower prices. It is only in situations where for various reasons competition cannot be expected to develop in a particular market that a monopolist's attempts to protect their inefficient operation should become subject to the sanction of law.

Notions of the protection of less efficient small businesses are rejected by the Chicago School and its subsequent variants. The classic judicial expression of this principle is found in the words of Posner J in *Olympia Equipment Leasing v Western Union Telegraph Co (Olympia)*:<sup>15</sup>

...the lawful monopolist should be free to compete like everyone else; otherwise the antitrust laws would be holding an umbrella over inefficient competitors. "A Monopolist, no less than any other competitor, is permitted and indeed encouraged to compete aggressively on the merits..."

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<sup>11</sup> See generally H Hovenkamp "Antitrust Policy After Chicago" (1985) 84 Mich L Rev, 213.

<sup>12</sup> See Joseph F Brodley "The Economic Goals of Antitrust: Efficiency, Consumer Welfare and Technological Progress" (1987) 7 NYUL Rev 1027, 1028.

<sup>13</sup> See Phillip Areeda and Donald F Turner *Antitrust Law: An Analysis of Antitrust Principles and Their Application* (Little Brown and Co, Boston, 1978) vol 1, 7-20.

<sup>14</sup> See Bork, above, 193.

<sup>15</sup> *Olympia Equipment Leasing v Western Union Telegraph Co.* (1988) 797 F 2d 370, 375.



### III POLICING THE MISUSE OF MARKET POWER UNDER THE COMMERCE ACT 1986

In the years since the Commerce Act was enacted in 1986, firms dominant in New Zealand markets have been subject to minimal government intervention in their markets, a regime commonly referred to as 'light-handed regulation'. Government intervention was limited to the generic prohibitions of the Commerce Act and the threat of further regulation should it be required. This regime was predicated on the belief that competition, not government, is the best market regulator, but that in circumstances where it is demonstrated that competition in a market is unable to correct undesirable behaviour, government intervention may be necessary.

Under the light-handed regime, section 36 of the Commerce Act was relied upon to prevent firms from abusing their dominant market position to prevent the development of competition. As originally enacted the provision stated:

No person who has a dominant position in a market shall use that position for the purpose of:

- (a) restricting the entry of any person into that or any other market; or
- (b) preventing or deterring any person from engaging in competitive conduct in that or in any other market; or
- (c) eliminating any person from that or any other market.

The prohibition was based on that contained in Article 86 of the Treaty of Rome and took its definition of dominance as the ability to operate largely independently of one's competitors from the seminal *Re Continental Can Co Inc and Europemballage Inc (Continental Can)*<sup>16</sup> decision. However to many observers, the protection afforded by section 36 was eroded by two high profile cases during the 1990s. These cases together were widely regarded as removing

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<sup>16</sup> *Re Continental Can Co Inc and Europemballage Inc* [1972] CMLR, D11, para 11.3.

the application of the prohibition to all but a handful of firms and giving even those firms the ability to act in a manner that seemed anti-competitive.<sup>17</sup>

#### *A The First Signs of Discontent: the Telecom Cases*

The first case was that of *Telecom Corporation of New Zealand Ltd v Commerce Commission (AMPS-A)*<sup>18</sup> in which the Court of Appeal determined the meaning of dominance under the section 36 prohibition. Instead of basing its definition on the economic principles envisaged, the court instead relied on a dictionary definition and equated dominance with notions of “a prevailing, commanding, ascendant, governing, primary, principal or leading influence.”<sup>19</sup> This appeared to necessitate the ability to singularly control the market, an ability that few firms other than monopolies possessed. In the words of Ross Paterson, the Court of Appeal decision “rejected the fundamental principles upon which the New Zealand jurisprudence had been based, and discredited the economic framework upon which the test for dominance had been built.”<sup>20</sup>

The second case, that of *Telecom Corporation of New Zealand Ltd v Clear Communications (Telecom v Clear)*<sup>21</sup> saw the Privy Council cite with approval the quote of Posner J in *Olympia*<sup>22</sup> and pronounce the test for whether a firm had used its dominant position in the following terms:<sup>23</sup>

It cannot be said that a person in a dominant market position ‘uses’ that position for the purposes of section 36 [if] he acts in a way which a person not in a dominant position but otherwise in the same circumstances would have acted.

<sup>17</sup> See Ross H Patterson “How the Chicago School Hijacked New Zealand Competition Law and Policy” (1996) 17 NZULR 160 for a discussion of how judicial interpretation of section 36 turned from its EU-derivations to adopt the efficiency-oriented values of the Chicago school.

<sup>18</sup> *Telecom Corporation of New Zealand Ltd v Commerce Commission* (1992) 3 NZLR 429 (CA).

<sup>19</sup> *Telecom v Commerce Commission*, above, 434 per Cooke P; see also 442 per Richardson J.

<sup>20</sup> Ross H Patterson “The Rise and Fall of a Dominant Position in New Zealand Competition Law: From Economic Concept to Latin Derivation” (1993) 15 NZULR 265.

<sup>21</sup> *Telecom Corporation of New Zealand Ltd v Clear Communications* [1995] 1 NZLR 385 (PC).

<sup>22</sup> *Telecom v Clear*, above, 402.

<sup>23</sup> *Telecom v Clear*, above, 403.

In its application of this counterfactual test, the Privy Council overruled the Court of Appeal and stated that by adopting a pricing policy for network interconnection that included opportunity costs, Telecom was not using its dominant position for the purposes of section 36.<sup>24</sup> These opportunity costs could include the monopoly rents that Telecom was assumed to be earning in the current provision of its services, although Clear had not actually established the existence of these monopoly rents. The decision seemingly allowed Telecom, the dominant firm, to act in a manner that was contrary to the promotion of competition, and held to an assumption that a monopolist should be allowed to compete as aggressively as firms that do not have that degree of economic strength,<sup>25</sup> rather than take a special responsibility for its actions.

### ***B Impetus for Reform Grows: The Problem of Electricity and Telecommunications***

The longstanding calls for a revamp of New Zealand's competition laws gained impetus as the behaviour of the formerly State-owned public utilities started to impact on the purse strings of the New Zealand public. Telecommunications and electricity provide two of the country's most obvious examples of industries in which the market power is concentrated in the hands of one or two big players. They both involve natural monopoly elements, in the form of networks, established and developed by the State, which are uneconomic for any new market entrants to duplicate. The incumbent network owner is consequently in a position of dominance in the market. For competition to develop in these industries, new entrants need access to the network to compete in an upstream or downstream market. Where the incumbent network owner also competes in those markets, they have an incentive to delay access to the network, or make access available on unreasonable terms and conditions, and thereby deter or restrict the development of competition.

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<sup>24</sup> Arguably this finding was simply one of appropriate statutory interpretation, however the merits of the case are not the subject of this paper, what is important is the perception that arose as a result.

<sup>25</sup> Ross H Patterson "How the Chicago School Hijacked New Zealand Competition Law and Policy" above, 187.

In the lead up to the 1999 general election, the seeming inability of New Zealand's light-handed regulatory regime to modify the behaviour of monopoly or dominant firms was highlighted by the troubled 1998 electricity reforms of the National-led Government and the seemingly unassailable position of Telecom in the New Zealand telecommunications market.

### *C The Electricity Crisis*

In 1998, the then National Government instituted reforms of New Zealand's electricity sector through Hon M Bradford's Electricity Industry Reform Bill. The Bill was an attempt to introduce competition into electricity generation and overcome the anti-competitive energy trading of the monopoly electricity lines business. The Bill sought to achieve this by structural means through splitting the State generator Electricity Corporation of New Zealand (ECNZ) into three generators who it was envisaged would compete with each other, Contact Energy and smaller private generators. The Bill would also force local power companies to split into separate lines and energy businesses and divest themselves of one of these operating arms.

On the enactment of his Bill on 3 July 1998, Hon M Bradford promised that his reforms would ensure "genuine sustainable competition"<sup>26</sup> throughout the electricity sector, meaning that lower prices were just around the corner for both households and business. The Electricity Industry Reform Act 1998 was supported through the House by the centre-left Labour party while in opposition, although they reserved the right to review the situation and reassemble ECNZ should it prove warranted. The champion of the political left, the Alliance party, fearful of the future privatisation and likely foreign ownership of another of New Zealand's essential services, opposed the reforms and advocated that ECNZ be kept together and retained in State ownership.<sup>27</sup>

The split of ECNZ under the Electricity Industry Reform Act took place on April 1 1999. As early as April 20, significant price increases were felt in and

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<sup>26</sup> "Electricity change Bill passed" (4 July 1998) *The Dominion* Wellington 1.

<sup>27</sup> "Alliance Plans to Reverse Split" (9 November 1999) *The Dominion* Wellington 5.

around the New Zealand's main centres.<sup>28</sup> Humbled by the failure of his reforms to bring lower prices to the New Zealand public, Hon M Bradford promised intervention in the form of price and profit controls on the electricity lines businesses. Legislation in the shape of the Commerce Amendment (Controlled Goods) Bill was hurriedly drafted to allow the Commerce Commission to impose price and revenue control on the lines businesses. However, in an election year and with a tenuous hold on government,<sup>29</sup> Hon M Bradford and National faced a difficult road to supplement his original reforms and bring the lower prices promised. National's usual political ally, the Association of Consumers and Taxpayers (ACT), refused to support Hon M Bradford's latest electricity reforms due to their fundamental opposition to government regulation of industry. To gain passage of his Bill, Hon M Bradford curried the favour of Labour and New Zealand First, and gained their support through the first and second readings in the House. However both parties withdrew their support before the Bill's final reading on the grounds that it was hastily drafted and did not impose any control on electricity retailers, who were suspected of shared responsibility for the increased electricity prices.

Labour's decision to withdraw its support for the Bill was purely political move. By delaying potentially immediate consumer relief the National Government's electricity crisis deepened as the general election loomed. After flexing its political muscle in stalling the Government's attempted reforms, a confident Labour promised that as the incoming government it would appoint an inquiry into the industry and introduce regulation only after its findings had been considered. Labour also sought guarantees from the electricity industry that no further price increases would occur prior to the impending election. In so doing, Labour were able to justify its opposition to seemingly needed reforms, while ensuring that public dissatisfaction with National's regulation of the monopolistic powers of the electricity generators carried through to the election.

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<sup>28</sup> Marta Steeman "Transalta Prices Go Up Today Despite Reforms" (20 April 1999) *The Dominion* Wellington 3. The average household price for electricity rose by 10 percent in Wellington, 10.5 per cent in Auckland and 13 per cent in Christchurch.

<sup>29</sup> The National-led Government's slender Parliamentary majority was secured by virtue of a collection of disaffected former New Zealand First and Alliance MPs.

#### *D Telecommunications and the Unassailable Position of Telecom*

Following its privatisation in 1989, Telecom had continued to enjoy a near monopoly over local residential and business services through its ownership of the Public Service Telecommunications Network (PSTN). The Telecommunications Users Association of New Zealand joined with new market entrants in decrying the difficulties in setting up meaningful competition as a curb to Telecom's continued dominance.<sup>30</sup> New Zealand's light-handed regulatory regime seemingly allowed Telecom to make it more difficult for challengers to assail its envious position. Clear Communications, the first meaningful market entrant had been confronted with years of highly publicised litigation over its negotiations with Telecom for access to the PSTN. This culminated in the Privy Council decision in 1994 which allowed Telecom to charge its rival an access fee that incorporated the monopoly rents it would necessarily forego by allowing Clear access to its network.<sup>31</sup> Yet despite this the then Minister of Communications unsympathetically dismissed the complaints as a 'policy of shared misery', on the basis that the new entrants had "whinged every day since they first got here",<sup>32</sup> a view not widely held by either the public or officials.

Public perception worsened, though with less foundation, when in 1998 Telecom offered a rebate to its Hutt Valley customers in response to the lower rental prices charged by another new entrant, Saturn. The move drew wide public outcry but no official censure. The Ministry of Commerce stated publicly that there was no policy requiring a dominant firm to reduce prices to all customers when facing competition in a limited portion of the market.<sup>33</sup> The Commerce Commission, New Zealand's competition watchdog, took no action in response to Telecom's actions, finding that the prices charged by Telecom

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<sup>30</sup> "Minnows Still Trailing in Telecom's Mighty Wake" (8 January 1998) *The New Zealand Herald* Auckland 9.

<sup>31</sup> Although in the face of government pressure, the Baumol-Willig pricing model approved by the Privy Council was never actually imposed by Telecom for interconnection to the PSTN.

<sup>32</sup> "Williamson Counter-attacks Telecommunications Critics" (4 August 1997) *New Zealand Infotech Weekly* Wellington 2.

<sup>33</sup> "Telecom's Hutt Pricing Not Unorthodox" (13 July 1998) *The Dominion* Wellington 5.

were not below the incremental cost of providing local access services to its Hutt Valley customers.

The lack of meaningful competition, complemented by a readiness to push the letter of its public service obligations embodied in the government's kiwi share, fed the perception that Telecom had abused its position to deter competition so as to continue achieving high profits at the expense of the consumer. In the years since its privatisation, Telecom had achieved super-profits while domestic rental prices had been increased by the rate of inflation, the maximum permissible level. This situation the leader of the Alliance referred to as a "licence to print money for nearly 10 years."<sup>34</sup>

#### *IV EARLY ATTEMPTS AT REFORM*

##### *A The Commerce Amendment (Control of A Dominant Position) Bill 1999*

Early in 1999 the Alliance had sought to redress the imbalance of New Zealand's competition laws towards dominant players with the introduction of the Commerce Amendment (Control of a Dominant Position) Bill. The Bill, introduced by L Harre, MP proposed the addition to section 36 of the phrase "in a manner that has, or is likely to have the effect of substantially lessening, competition in a market" to the existing prohibition of a firm taking advantage of its dominant position in a market for a proscribed purpose. This would give the consequences of a firm's conduct on the level of competition in the market the same relevance as the firm's purpose, when determining whether the conduct was anti-competitive.

In introducing the Bill's second reading L Harre, MP railed against the ineffectiveness of the current statute and in particular the need for the anti-competitive purpose of the dominant firm to be proved.<sup>35</sup>

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<sup>34</sup> Hon J Anderton, MP (1 June 1999) 578 NZPD 17231.

<sup>35</sup> Hon L Harre, MP (31 March 1999) 576 NZPD 15813.

Why should motive need to be proved? If a reduction in competition is incidental to the use of a dominant position for some other purpose, then should the behaviour be allowed to continue? We say not.

Proof of purpose was also considered difficult for those alleging a breach of section 36 to establish, as any subjective evidence of the intended purpose was in the hands of the alleged contravenor and could be easily concealed or destroyed. Although the proposed amendment retained the element of purpose, the Bill also proposed that the courts be able to infer a dominant firm's purpose from the facts and circumstances of the case. A similar provision had been provided for under section 46 of the Australian Trade Practices Act 1976 to overcome the apparently onerous evidential burden of establishing a dominant firm's purpose.

While the Bill had the support of the Labour Party, the National-led Government dismissed the legislation as piecemeal as it addressed only one aspect of the Act, and the Bill was discharged by a two-vote majority.

### ***B National's Commerce Amendment Bill***

Soon after the public rancour that accompanied his electricity reforms, and in conjunction with his attempts to bring price control to the lines businesses, Hon M Bradford had on 1 June 1999 introduced his own Commerce Amendment Bill. This Bill purported to address some of the stated weaknesses of the existing statute by strengthening its enforcement regime and increasing the penalties available for a breach of the act so that "large businesses could no longer consider these simply as a cost of doing business."<sup>36</sup> The current penalties were supplemented by an alternative maximum penalty of up to three times the value of the illegal gain achieved, or ten per cent of the annual turnover of the transgressing firm.

The Bill was initially silent on the provision in relation to misuses of market power by dominant firms. Possibly in the face of Opposition criticism on precisely that point and the growing public outrage regarding the actions of the



dominant electricity and telecommunications players, Hon M Bradford added three amendments to section 36 into the Supplementary Order Paper (no. 203) passed to the Select Committee. The first amendment proposed a further definition to the term 'dominant position' by explaining it as the position to exercise a 'high degree of market power.'<sup>37</sup> This was hailed as a return to the level of power previously understood to attract section 36 attention "where there is a large discretion to depart from competitive behaviour" as stated by the High Court in its consideration of the *AMPS-A* case.<sup>38</sup>

The next amendment expressly provided that 'use' in relation to a person's dominant position in a market be treated only as the causal connection between the dominant position and the stated proscribed purposes.<sup>39</sup> Interestingly the last amendment to section 36 proposed by Hon M Bradford adopted the inference of evidence with regard to purpose provision employed in Australia and earlier advocated by the Alliance's proposed reforms.

Time, however, had run out for Hon M Bradford's reforms. With the election looming ever closer, his proposed amendments were stranded at the select committee stage, to be carried over to the new government's term. As it so turned out, the new government would be that of the Labour-Alliance Coalition, two parties that had as cornerstones of their respective commercial policies, the revamp of the country's competition laws.

## **V THE COMPETITION POLICIES OF THE COALITION PARTNERS**

### **A The Alliance**

The Alliance's competition policy was very much founded upon the belief that New Zealand's light-handed regulation simply did not work. The present laws were not enough to modify the behaviour of firms dominant in their market

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<sup>36</sup> Hon D Carter (1 June 1999) 578 NZPD 17229.

<sup>37</sup> Commerce Amendment Bill 1999, SO203, cl 2A(1).

<sup>38</sup> *Telecom Corporation of New Zealand v Commerce Commission* (1991) 4 TCLR 473, 509 (HC).

<sup>39</sup> Commerce Amendment Bill 1999, SO203 cl 4A (1A)(a).

sectors. This was evidenced by the fact that the “excess profits of Telecom and its monopoly control were at least as strong as the day it was sold.”<sup>40</sup> Fair competition was essential if New Zealand’s economy was to be successful both domestically and internationally. This notion of fair competition was stated to be a situation in which there were “no wide disparities of power between parties to commercial transactions and all parties come to transactions with the desire to achieve mutually beneficial outcomes.”<sup>41</sup> This idealistic expression of competition reflected not only the idea of competition law as providing a level playing field, but as a means to actually level the market power of the players.

The Alliance saw the primary impediment to fair competition to be the anti-competitive behaviour of large companies that dominated their market sector and made it difficult for competitors to compete in that market. These large corporations, unconstrained by competition or potent regulation were thus able to plunder the pockets of New Zealand consumers. Increased competition combined with tighter regulation would ensure a more even distribution of market power across the market participants. This thinly veiled threat to the actions of Telecom was made more obvious in headlines that accompanied their policy in the run in to the election such as “Alliance leash for Spot” and “Alliance Guns for Telecom” and the promise that “Telecom would have one Y2K problem after the election – fair competition.”<sup>42</sup>

The Alliance sought to eradicate anti-competitive behaviour through a variety of measures.

First, section 36 of the Commerce Act would be redrafted “to ensure that the intent of the Act is adhered to and not bogged down in endless litigation as at present.”<sup>43</sup> The fundamental driver behind this was the need to make the statutory prohibition more easily enforceable and remove lengthy litigation as another weapon in the arsenal of dominant firms when responding to challenges

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<sup>40</sup> The Alliance Party “Competition Policy” <<http://www.alliance.org.nz/info.php3?Type=Policy&ID=989>> (last accessed 29 June 2002).

<sup>41</sup> The Alliance Party, above.

<sup>42</sup> Peter Luke “Alliance Leash for Spot” (24 November 1999) *The Press* Christchurch 2.

<sup>43</sup> The Alliance Party, above.

from their competitors. This would be achieved through clarification of the definitions of dominant position and use of that position, and by the introduction of an 'effects test' to focus attention on the consequences of the firm's conduct on competition in the market.

Further to the stated need to redraft section 36, the Alliance's policy envisaged a need for specific regulation for industries in which competition could not be expected to regulate dominant firms in the foreseeable future. Wide-ranging regulation of the telecommunications sector was proposed.<sup>44</sup>

As a final tonic, increased penalties for breaches of the Commerce Act were also advocated, such that the commercial gains of anti-competitive behaviour were outweighed by the sanctions able to be enforced for such a breach.

At the forefront of the Alliance's policy was the idea of competition law as a tool of social policy, a means by which protection of the vulnerable could be achieved and imbalances of power could be addressed. The market, and particularly big business, could not be trusted to give any significant weight to the consideration of the interests of the general public where profit was at stake. Telecom had supposedly proved this time and again. The Alliance policy also hinted at a belief in a wider function of competition law as it talked of empowering the Commerce Commission to 'take account of a wider range of social and environmental factors in establishing whether or not the public good is being served when it comes to identifying anti-competitive behaviour.'<sup>45</sup> This sought to move the determination of 'public benefit' away from the efficiency-dominated measurement applied by the Commerce Commission under the current legislation,<sup>46</sup> and acknowledge explicitly that other interests are also represented by 'public benefit'. Their policy seemed largely to ignore economic considerations, despite their assertion that fair competition was essential to the success of the New Zealand economy. Their desire to address imbalances in

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<sup>44</sup> This included establishment of statutory principles governing interconnection to the PSTN and pricing of monopoly services, comprehensive disclosure regime, price ceilings and reduction targets along with a possible revision of the kiwi share obligation.

<sup>45</sup> The Alliance Party, above.

market power to create a more equitable market place is questionable from an economic perspective. In many cases corporations grow in stature through efficiencies gained through economies of scale. To punish rather than reward those firms is counter-productive from the viewpoint of economic advancement.

### ***B A Clear Policy Plank: Labour's Competition Policy***

Labour's competition policy was more equivocal in relation to the current light-handed regulatory approach, acknowledging both its benefits and shortcomings in advancing the interests of New Zealanders through the promotion of competition. Competition, it was reiterated, was directly beneficial to consumers by encouraging productivity, innovation and lower prices. Competition was also pivotal to Labour's export-led growth strategy as a dynamic, competitive and efficiently operating domestic market would also enhance the country's ability to compete internationally and export successfully. But Labour's primary focus in the promotion of competition was as a means to enhance consumer welfare and it proposed first and foremost that appropriate words be added to the long title of the Act, and a relevant purpose clause incorporated to reflect this focus.

In seeking reform of the Commerce Act, Labour's policy noted the changing nature of New Zealand economy and an increase in large corporations dominating their market sector through foreign investment and the corporatisation and privatisation of formerly State-owned operations. Competition law, it was stated, had not kept pace with these changes meaning that the power of these large corporations could be used against the interests of consumers and to stymie the benefits of competition:<sup>47</sup>

Labour believes that firms which have significant market power should not be able to misuse that power. Only when the misuse of power has been addressed can the potential advantage of competition be realised. It is therefore the focus of this policy to promote competition where appropriate by cracking down on unfair and anti-competitive behaviour.

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<sup>46</sup> See generally Commerce Act 1986, s 3A and Commerce Commission *Guidelines to the Analysis of Public Benefits and Detriments* (Wellington, 1994).

<sup>47</sup> Labour Party "Improving Competition Policy" (10 August 1999) <<http://www.labour.org.nz/Frame-Search.html>> (last accessed 29 June 2002).

Labour planned to ensure that firms would not be able to take unfair advantage of dominant positions, and that the effects of their actions on consumers be given weight in law. This focus on the effects of firms' actions on consumers, suggested a mirroring of the Alliance's position in relation to the introduction of an effects test into section 36. Labour had earlier supported the Commerce Amendment (Control of a Dominant Position) Bill which sought to introduce such a test, and in a 1998 discussion paper Labour had explicitly promoted the replacement of the purpose limb of section 36 with an effects test.

Labour's competition policy in 1999 however relied heavily on the Ministry of Commerce discussion paper *Review of the Competition Thresholds in the Commerce Act 1986 and Related Issues*<sup>48</sup> and the submissions made in response to that paper. The paper considered the issue of anti-competitive effects but deemed an effects test to be inappropriate. The reasons given were the risk that legitimate competitive activity would be deterred by the expanded scope of activity brought within the reach of section 36, and because of the uncertainty involved in postulating hypothetical scenarios to compare the effect of the conduct against what might have happened without the particular conduct.<sup>49</sup>

Labour were taken with the preferred option of the Ministry of Commerce's paper, that of revamping New Zealand's competition laws by aligning them with those of our closest neighbour and trading partner, Australia. Anti-competitive behaviour by dominant firms would be addressed through the alignment of the prohibition in section 36 of the Commerce Act with its Australian counterpart, section 46 of the Trade Practices Act 1974. This would be achieved by the replacing dominant position with the term 'substantial degree of market power', replacing 'use' with 'take advantage of' and by adding a clause, equivalent to that of section 46(4) of the Australian legislation to clarify the interpretation of purpose. Despite dropping its call for an effects test, Labour still considered that:<sup>50</sup>

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<sup>48</sup> Ministry of Commerce *Review of the Competition Thresholds in the Commerce Act 1986 and Related Issues* (Wellington, 1999).

<sup>49</sup> Ministry of Commerce, above, 24.

...the effect of anti-competitive behaviour should be taken into consideration in determining whether the behaviour is acceptable or not. Some analysis of the Australian legislation suggests that their interpretation of 'purpose' allows this to happen. Labour will expect the select committee considering the Commerce Act amendments, to fully consider this issue and if necessary recommend further amendments to ensure that the effects are able to be considered.

The analysis of the Australian legislation is not expanded upon in Labour's competition policy, and indeed appears suspect given that there have been repeated calls across the Tasman for an effects test to be given express recognition in the Trade Practices Act. Further, it appears strange that an opposition party would rely so heavily on a departmental paper for a policy that ignored a fundamental aspect of its previous policy position. A likely motive for this was the desire to gain credibility with the business community and dispel their fears of a highly interventionist and socialist-leaning government. Labour could be seen to be addressing a problematic area of law without adopting a measure considered abhorrent by big business. By stating that the matter would be given further consideration at the select committee stage, Labour were effectively fence-sitting on the issue, and avoiding criticism from either those that pursued an effects test, or those who were diametrically opposed to it. Indeed Labour's entire competition policy appeared slightly double-edged, the rhetoric suggesting a shift in direction for New Zealand's competition laws but the substance of their proposals appearing to lack the same commitment to change.

Several benefits in harmonising New Zealand's competition laws with those of Australia were touted in Labour's competition policy. It was in the spirit of the our Closer Economic Relations agreement in which uniformity of competition laws was seen as advantageous to the ultimate goal of free trade between the two countries.<sup>51</sup> It would reduce transaction costs for firms dealing in the trans-Tasman market and spread the cost of testing the limits of competition policy across market participants in both countries. It would also increase the level of certainty as to the court's interpretation of the legislation as they could apply precedent Australian case law to New Zealand's markets.

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<sup>50</sup> Labour Party, above.

Like the Alliance party, and for that matter National before them, Labour also proposed that penalties for breaches of the Act be increased to eliminate the possibility that a firm could consider prosecution to be an acceptable cost of doing business. Labour also anticipated the necessity of specific regulation of some industries, 'particularly those with a natural monopoly element'.

Having announced its intention to commission a review of the electricity lines business, Labour would also initiate a review of the telecommunications industry and indeed stated that it would review all existing industry specific regulations to ensure their continued effectiveness. The possibility of generic network utilities legislation was suggested. Labour signaled too that should an industry be faced with monopolistic practices, as government it would be prepared to invoke the price control provisions of the Commerce Act to protect the interests of consumers, something previous governments had been extremely reluctant to do.

#### ***VI THE COMMERCE AMENDMENT ACT 2001***

Upon attaining power, the Labour-Alliance Coalition Government initiated their promised reviews of the telecommunications and electricity industries. They also set about the long and convoluted process of enacting their reforms to the Commerce Act.

The Supplementary Order Paper of the National Government (No. 203) lapsed and was replaced in August of 2000 by a second Supplementary Order Paper (No. 37) that proposed the reforms embodied in the Labour's pre-election policy. A Commerce Amendment Bill, which omitted the proposed amendments to section 36, was then introduced to the House. This was then reformulated and returned to the Commerce Committee.

The Commerce Amendment Bill (No.2) was eventually presented to the House and became law on 31 July 2001. The Act introduced amendments to the key

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<sup>51</sup> Australia New Zealand Closer Economic Relations Agreement 1984, art 1.

provisions of section 36, and of section 47 that deals with business acquisitions. The price control provisions, enforcement and penalties regimes were amended, while a consumer welfare-focused purpose statement was also added to the Act. Interestingly, specific price control provisions applicable to the electricity lines businesses were also introduced as part of the amendment to the Act. These provisions mimicked the provisions that Hon M Bradford had earlier tried and failed to introduce prior to the election.

In relation to section 36, the context of the amendments, in both the speeches before the House and in the Select Committee report on the proposed amendments, was very much one of the failure of the judiciary to give the intended effect to the language of the provision as it previously stood. The courts, it was said, had raised the bar for establishing anticompetitive behaviour too high, making the success of actions against those using their market power for anticompetitive purposes unlikely.<sup>52</sup> Clear signals would now be sent to the courts as to how the provision was to be interpreted, by aligning our legislation with that of Australia and adopting her jurisprudence. Importantly for the promotion of competition, the amended provisions would bring certainty to its application for business so that legitimate competitive behaviour would not be deterred; “the point is that business wants certainty, and wants good quality, tidy law, and that is what we will give it.”<sup>53</sup>

The Commerce Amendment Act (No.2) 2001 brought the following changes to section 36:

- The threshold of the dominant position was replaced with one of a ‘substantial degree of power’;
- The prohibition on the ‘use’ of that power for a proscribed purpose became a prohibition on taking advantage of that power;
- The proscribed purposes specified could be ‘inferred from the conduct of any relevant person or from any other relevant circumstances’.

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<sup>52</sup> Hon P Swain, MP (4 April 2001) 591 NZPD 8734.

<sup>53</sup> D Cunliffe, MP (4 April 2001) 591 NZPD 8741.



New Zealand's rules for governing anti-competitive behaviour by a firm with market power now mirrored almost exactly those of section 46 of the Australian Trade Practices Act 1974.

On the face of it, then, it appeared that the objectives of both Labour and the Alliance found satisfaction in the amending legislation. The amendments to section 36 specifically proposed by Labour were enacted. The limited application of the section had been corrected through the lowering of the dominance threshold. The hypothetical 'use' test that had allowed Telecom to claim monopoly profits, was replaced by a phrase that ostensibly had been interpreted as simply a causal connection by the authoritative Australian case on the point, the High Court decision of *Queensland Wire Industries Pty Ltd v Broken Hill Proprietary Co Ltd (Queensland Wire)*.<sup>54</sup> The ability to infer a proscribed purpose from conduct and circumstances meant that a potentially onerous evidential burden on a party wishing to establish anti-competitive conduct was expressly removed. Seemingly the effects of conduct would now be given consideration when determining anti-competitive behaviour. All of this pointed to a provision with wider scope of application and fewer barriers to successful enforcement.

## VII THE SUBSTANCE OF THE CHANGES

A number of commentators have asserted that section 36 in its new guise has brought little, if any, significant change.<sup>55</sup> Have then the amendments introduced by the Labour-Alliance coalition brought any tangible change to New Zealand's laws governing the misuse of market power?

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<sup>54</sup> *Queensland Wire Industries Pty Ltd v Broken Hill Proprietary Co Ltd* (1989) 167 CLR 177 (HCA).

<sup>55</sup> see generally Stephen Land and Tim Clarke "The Commerce Amendment Act 2001" (2001) 7 NZBLQ 217, 222; M R Dean and Tom Weston *Competition Law Update* (New Zealand Law Society, Wellington 2001) 39.

*A From Dominance to Substantial Degree of Power in a Market*

The change to the threshold of market power required to bring about liability under section 36 did not change any of the questions asked in determining the relevant market, or to the level of power held by the firm alleged to have engaged in anti-competitive conduct. The parameters of the market are defined in section 3(1A) of the Commerce Act as being a market in New Zealand for goods and services as well as other goods and services that, as a matter of fact and commercial common sense, are substitutable for them. Factors to be considered in determining the relevant market include: the product in question; the geographical area within which the competition operates; the functional levels of the competitors and how much time is needed for customers and suppliers to respond to the acts of the competitors.

Prior to the 2001 reforms, the elements to be considered in determining whether a firm had the requisite degree of market power were listed in section 3(8) of the Act. These were the firm's share of the market, technical knowledge, access to materials or capital, the extent to which the firm was constrained by the conduct of competitors, actual and potential, and by the conduct of suppliers or acquirers of goods or services in that market. These same elements will still be considered despite the repeal of that section, as these same factors are referred to in Australian case law,<sup>56</sup> and specifically provided for in section 46(3) of the Trade Practices Act. Primary importance is given to the barriers to entry in the relevant market.<sup>57</sup>

The replacement of 'dominant power in a market' with 'substantial degree of market power', as pointed out by then Minister of Commerce Hon P Swain, means that section 36 will now apply to a greater number of firms and markets and "signal to the courts that the test to be considered is whether a firm has sufficient power to harm the process of competition, rather than the test of what each of the words means."<sup>58</sup> The objectives in the replacement of this threshold

<sup>56</sup> See *Eastern Express Pty Ltd v General Newspapers Pty Ltd* (1992) 35 FCR 43, 62 (FC).

<sup>57</sup> *Re Queensland Cooperative Milling Association Ltd* (1976) 25 FLR 169, 188 (FC).

<sup>58</sup> Hon P Swain, MP (4 April 2001) 591 NZPD 8734.

were obvious, that of circumventing the dictionary definition of dominance applied by the Court of Appeal in the *AMPS-A* case, so that all firms with power to harm the process of competition would be captured by the prohibition. In practice it is difficult to determine whether the definition provided by the Court of Appeal had any significant impact on cases brought under section 36 as there is no measure of firms that have been deterred from bringing actions believing themselves to be unable to establish the dominance of the alleged wrongdoer. Of the section 36 cases that have reached the High Court since the *AMPS-A* decision however, none have failed for want of establishing dominance. Indeed the Court of Appeal itself had sought to soften the impact of the *AMPS-A* decision in *Port Nelson Ltd v Commerce Commission (Port Nelson)* in which Gault J stated that the earlier definition of the court had not shifted the concept of dominance from where it had been derived; the idea that a dominant firm being one that could act to all intents and purposes independently of its competitors.<sup>59</sup> What needed to be borne in mind, it was stated, was the distinction between the concept of dominance and the test for its existence, which incorporated an economic analysis of the elements of market power. The threshold contained in section 36 was deemed to contemplate "a dominant position in which there still is a perceived need to act aggressively. A dominant position is not one that is so controlling that it is impenetrable."<sup>60</sup>

But to how many firms and to what level of market power will the 'substantial degree' threshold apply? The definition of 'substantial' within the Act does not apply to section 36<sup>61</sup> and there is no other guidance on this point within the Act itself. If the courts are to give effect to Parliamentary intention, the answer to this must be informed by the relevant Australian jurisprudence.

The Australian jurisprudence on this point itself is rather vague. In the explanatory memorandum to the Trade Practices Revision Bill 1986, in which the Australian legislature itself introduced the notion of a substantial degree of market power, it was stated this provided a lower threshold than that of

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<sup>59</sup> see *Continental Can*, above.

<sup>60</sup> *Port Nelson Ltd v Commerce Commission* [1996] 3 NZLR 554, 574 (CA).

<sup>61</sup> Commerce Act 1986, s 2(1)(A).

dominance or the ability to substantially control a market. Judicial interpretation of the threshold has held the term to signify 'large or weighty', 'considerable, solid or big.'<sup>62</sup> Indeed the Australian judiciary has noted that the threshold is quantifiably imprecise and calculated to conceal a lack of precision.<sup>63</sup> What is apparent is that it is possible for more than one firm to have a substantial degree of power in a market at any one time.<sup>64</sup> From this it would seem that the new threshold sits somewhere between the notions of dominance and the section 2(1A) definition of 'real or of substance,' a rather broad definition that will no doubt turn on the facts of each particular case.

When the Commerce Act was first enacted, dominance was considered appropriate to the New Zealand business environment in which many sectors of the economy comprised few players.<sup>65</sup> By adopting the equivalent Australian position, New Zealand has in essence taken on a threshold considered suitable in an economy significantly larger than our own.<sup>66</sup> Certainly in a number of industries it is questionable whether New Zealand is able to sustain even two competitors. In telecommunications, domestic air services and free to air television, to name but a few industries, the non-incumbent competitors have struggled to be profitable. The likelihood that a firm capable of exerting its power for anti-competitive purposes in a New Zealand market would not be captured by a threshold of dominance appears small.

Indeed the greater risk appears to be that firms lacking the degree of market power to truly justify section 36 attention may in fact now be captured by this adopted and lower threshold. Many of the submissions on the proposed amendment<sup>67</sup> registered the concern that by lowering the threshold, a greater number of firms would be deterred from legitimate competitive behaviour

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<sup>62</sup> *Dowling v Dalgety* (1992) 34 FCR 109 (FCA); *Tillmans Butcheries v Australian Meat Industry Employees Union* (1979) 42 FLR 331 (FCA).

<sup>63</sup> *Tillmans Butcheries v Australian Meat Industry Employees Union*, above, 338 Bowen CJ.

<sup>64</sup> see *O'Keefe Nominees Pty Ltd v BP Australia* (1990) ATPR 41-057 (FCA). In this case BP Australia, which was one of six competitors in the market, was seen to possess the requisite market power for the purposes of s 46.

<sup>65</sup> See also Department of Trade and Industry *Review of the Commerce Act 1986* (August 1998).

<sup>66</sup> Craig Howie "Aussie Flavour Might Not Work in NZ Competition Law – Expert" (5 August 2000) *The Dominion* Wellington 16.

<sup>67</sup> Including those from Telecom, Tranz Rail, Microsoft, Fletcher Challenge, Vodafone, Chapman Tripp and NZ Forest Industries Council.

contrary to the Labour party's stated goal of promoting competition. To counter this, the Minister stated that "the actual application of that test will need to take into account what makes economic sense in New Zealand conditions."<sup>68</sup>

This point appears to be a concession to the difference in scale between the economies of New Zealand and Australia, and recognition that the test for substantial degree of power will need to be handled differently in our smaller economy. If, as the Minister exhorted them to do, the courts are to pay heed to what makes sense in New Zealand conditions, then comparison with Australian findings of fact should be of little assistance to them. But as has been noted however, it is hard to see how the same words used in the Commerce Act can be interpreted any differently from how they have been interpreted in Australia. There is nothing in the Commerce Act itself that suggests that a different approach could or should be taken.<sup>69</sup>

How then would the courts assess whether or not the market power of a firm is substantial enough to warrant the attention of section 36? After identifying the relevant market and considering the various factors to be taken into account in an assessment of market power, the courts are then required to determine whether the market power established on the facts is substantial or 'large and weighty'. This requires a value judgement on the part of the court and will turn largely on the definition of the market preferred by the court. With little further guidance other than that the threshold is lower than that of dominance, and the stated Parliamentary intention that it should be a test of whether a firm has sufficient market power to harm the process of competition,<sup>70</sup> there is ample scope for the net to be cast too wide. Guidance will inevitably be gained as our case law on the point builds, however the courts have come up with an undesirable interpretation before and the new threshold provides scope for it to happen again.

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<sup>68</sup> Hon P Swain, MP (4 April 2001) 591 NZPD 8734.

<sup>69</sup> See Stephen Land and Tim Clarke "The Commerce Amendment Act 2001" (2001) 7 NZBLQ 217, 218.

<sup>70</sup> Hon P Swain, MP (4 April 2001) 591 NZPD 8735.

Given then that the intentions of the Government were to strengthen section 36 to ensure the prohibition of anticompetitive acts by, in the words of the Alliance, 'large companies that dominate their market sector', and those of Labour, 'large corporations dominating their market sector through foreign investment and the corporatisation and privatisation of formerly State-owned operations', it is questionable whether the threshold of substantial degree of market power satisfies this intention accurately. The lower threshold appears likely to capture more firms than is appropriate in the New Zealand economy. While the Alliance may have been pleased with the very wide application of the prohibition, it seems that the more economy-focused Labour may in fact have got more than it bargained for. The wider than intended reach of section 36 has increased the number of firms that need to be wary of its application, potentially resulting in a far greater deterrence of competitive behaviour than was previously the case. These businesses also face the added uncertainty of further inconsistent or undesirable interpretation by the courts, the same concerns that initiated the drive for reform in the first place.

### ***B Taking Advantage Not Using***

Under the amended Commerce Act, a firm found to possess a substantial degree of market power must not 'take advantage' of that power for one of the purposes proscribed in subsections 36(2)(a), (b) or (c). At the time of the amendment, the Australian authority on taking advantage came from High Court of Australia decision in *Queensland Wire*. In the context of refusing to supply a product to a downstream competitor, the court examined the issue of whether taking advantage incorporated notions of unfair, predatory or morally blameworthy behaviour. The court was unanimous in its classification of the phrase in a non-pejorative sense, essentially rendering this limb of the provision to be a causal connection between the market power of the firm and its anticompetitive purpose. To take advantage of one's market power was simply to use it. The majority of the court found the respondent to have taken advantage of its market power by virtue of the fact that its refusal to supply the plaintiff with a product was made possible by its position in the market and absence of competing

suppliers.<sup>71</sup> In so doing it introduced the counterfactual test for taking advantage; that a firm would be taking advantage of its market power if it acted otherwise than it would be expected to behave in a competitive market.

This causal connection was further elucidated in the case of *Natwest Australia Bank v Boral Gerrard Strapping Systems Ltd*<sup>72</sup> in which it was stated that connection could be demonstrated by showing “a reliance by the contravener upon its market power to insulate it from the sanctions that competition would normally visit upon its conduct.”<sup>73</sup>

As stated previously the requirement to use this counterfactual test, and its inappropriate application in *Telecom v Clear* were precisely the points that the reforms of the Labour-Alliance coalition sought to obviate. The New Zealand Court of Appeal, although unable to expressly overturn the decision of their Lordships, had subsequently expressed dissatisfaction that the ‘use’ test they pronounced must be applied to determine use of market power in every case.<sup>74</sup>

Less than one month following the introduction to the New Zealand legislation of the term ‘take advantage’, the High Court of Australia reconsidered the issue of taking advantage of market power in *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd (Melway)*.<sup>75</sup> Another case involving essentially a refusal to supply, the court leveled a number of criticisms at the reasoning behind the decision reached in *Queensland Wire*. Echoing the sentiments expressed by Gault J in *Port Nelson* the majority of the court stated that instead of the counterfactual test, “direct observation may lead to the correct conclusion.”<sup>76</sup>

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<sup>71</sup> *Queensland Wire*, above, 192 Mason CJ and Wilson J; 198 Deane J; 203 Dawson J; 216 Toohey J.

<sup>72</sup> *Natwest Australia Bank v Boral Gerrard Strapping Systems Ltd* (1992) ATPR 41-196 (FCA).

<sup>73</sup> *Natwest*, above, 40-644, French J.

<sup>74</sup> *Port Nelson*, above, 577 Gault J: “while it is not easy to see why the use of a dominant position should not be determined simply as a question of fact without the need to postulate artificial scenarios, we are content in this case to adopt that approach.”

<sup>75</sup> *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd* (2001) 205 CLR 1 (HCA).

<sup>76</sup> *Melway*, above, 24.

While acknowledging that the counterfactual test was useful in determining whether advantage of market power had been taken, the assumptions on which this analysis was based needed to be grounded in fact:<sup>77</sup>

It is one thing to compare what [the firm] has done with what it might be thought to do if it lacked that power. It is a different thing to compare what it has done with what it would do in circumstances that are completely divorced from the reality of the market.

By grounding the test in the reality of the market, the majority in *Melway* allayed concerns that the test could be corrupted by hypothetical scenarios that bore no resemblance to the market in which the firms actually operated. On the facts of that case *Melway*, whom it was established had a substantial degree of power in the relevant market, and had refused the supply of their street directories to prevent the respondent from competing with their existing wholesale distributors, were held not to have taken advantage of their position because they were in effect maintaining a distribution system that they had in place prior to gaining substantial power in the market. *Melway*'s behaviour was classed as a termination of a distributorship and their action one of protecting a business practice, that they found beneficial.

Ironically the *Melway* decision could be construed as placing Australian case law on taking advantage in very much the same position as had previously existed in New Zealand under the Privy Council decision in *Telecom v Clear*. By allowing *Melway* to refuse the supply of its product on the grounds that it would do so in a competitive market, the High Court of Australia endorsed the principle that a dominant firm can be justified in the exercise of what appears to be an anticompetitive act; that of refusing access of a competitor to a market. The decision has arguably ushered into our competition law the legitimate business justification defence,<sup>78</sup> and thereby increased the arsenal of the dominant firm when countering section 36 actions. In the post-*Melway* decision of *Carter Holt Harvey Building Products Ltd v Commerce Commission*,<sup>79</sup> the New Zealand Court of Appeal considered justifications advanced by the

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<sup>77</sup> *Melway*, above, 25.

<sup>78</sup> See generally Mark N Berry "The Uncertainty of Monopolistic Conduct: A Comparative Review of Three Jurisdictions" (2001) 32 *Law & Pol Int Bus* 263, 302-303.

<sup>79</sup> *Carter Holt Harvey Building Products Ltd v Commerce Commission* (5 November 2001) Court of Appeal, Wellington CA 180/00.



dominant firm that the predatory pricing of which they were accused was for the purposes of maintaining market share while developing a new product, and meeting pressure exerted by their distributors. While the court rejected these arguments on the facts, they were not rejected on principle, pointing to their availability as a means to escape section 36 liability.

As a result there appears to be little substantive difference in the application of the test that New Zealand courts are to apply in the determination of taking advantage, as they were required to do under the previous test for use. While the Court of Appeal has since acknowledged that the counterfactual test need not be applied in every case, they have in at least one case following the decision in *Melway* remained content to apply it.<sup>80</sup> The counterfactual test while no longer mandatory, is still the generally accepted test for, or at least a basis for establishing, the taking advantage of market power. The fact that New Zealand had dropped the term 'use' for a term that the High Court of Australia had deemed to mean simply 'use' suggested that there would be no change to this limb of the prohibition. The reality is that the subsequent decision in *Melway* has once again rendered this limb of the prohibition to constitute more than a mere causal connection. Contrary to the express wishes of the Alliance it has also provided another area of legal vagary potentially exploitable by a dominant player to escape section 36 sanction, or at least ensure that the ensuing legal proceedings are protracted.

### *C The Inference of Purpose*

The final limb to be established to constitute a breach of section 36 is that the substantial degree of market power has been taken advantage of for one of the proscribed purposes in subsections 36(2)(a), (b) or (c). Under subsection 2(5)(b) of the Act, that purpose need only be one of the purposes of the conduct provided that it was a substantial purpose of the firm in engaging in that conduct.

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<sup>80</sup> *Telecom Corporation of New Zealand Ltd v Commerce Commission* (2001) 10 TCLR 182 (CA).

The addition of section 36B to the Act allows the court to infer purpose of the alleged contravener from the conduct of any relevant person or from any other relevant circumstances. The manner in which purpose can be inferred was demonstrated in *Queensland Wire* where the court was able to infer a proscribed purpose from the evidence that BHP had not offered any business justification for its refusal to supply Y-bar and that this refusal was inconsistent with its normal selling policy in relation to its other products in which it faced competition for the supply thereof.<sup>81</sup>

New Zealand courts are then able to infer the purpose from the evidence presented to it, in so far as they show the likely intended consequences of the dominant firm's conduct. This certainly appears to go some way to reducing the evidential burden on the party alleging a breach of section 36, in that they do not need to furnish evidence of the subjective intent of the dominant firm. It is questionable however whether there was ever a need to do this prior to the amendment. In *Port Nelson* Gault J summed up the situation thus:<sup>82</sup>

Much has been written on this distinction which generally is unimportant in practice. There will be very little difference in most cases between ascertaining subjective purpose by inference from what was said and done and ascribing objectively a purpose from evidence of what was said and done.

In practical terms a plaintiff would attempt to establish anti-competitive purpose through the objective inference of the natural and probable consequences of the defendant's conduct, while the defendant would seek to establish that they did not possess an anti-competitive purpose.

Indeed the select committee report acknowledged that the introduction of section 36B made no difference to the approach already adopted by the courts, however it felt the amendment necessary for two reasons.<sup>83</sup>

Firstly, it will make transparent what has been good practice. Secondly, it reinforces the move by the Court of Appeal to play down the significance of the debate on whether purpose is a subjective or objective test.

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<sup>81</sup> *Queensland Wire*, above, 50,011 Mason CJ and Wilson J.

<sup>82</sup> *Port Nelson*, above, 564.

<sup>83</sup> Commerce Amendment Bill 2001, no 296-2, (the commentary), xiv.

It may be that Labour felt that the section 36B provision to infer purpose from 'any other relevant circumstances' would allow anti-competitive effects to be considered. However the absence of any Australian precedent on this point, and the very fact that numerous unsuccessful attempts have been made to introduce an effects test into section 46 of the Trade Practices Act would suggest otherwise. The provision itself still focuses on the purpose of the alleged wrongdoer, so while a resulting anti-competitive effect may assist in the establishment of an anti-competitive purpose, it is not the effect that is the measure of whether the conduct is anti-competitive or not. The prohibition remains grounded in the intent of the firm rather than whether competition is in fact hindered by their behaviour. Given their awareness that the introduction of section 36B would make no substantive difference to the existing evidential burden of establishing a section 36 breach, and the concern that both Labour and the Alliance had expressed at the difficulty of establishing purpose, it is surprising that greater change was not made at least in this limb of the provision.

The question of establishing purpose may in any case be trivial. The bulk of jurisprudence on the point notes that purpose and the use (or take advantage) limb of the prohibition are very much interconnected, and that the distinction between pro-competitive and anti-competitive behaviour is at best a very fine one. In *Telecom v Clear* the Privy Council noted that if "a person has used his dominant position it is hard to imagine a case in which he would have done so otherwise than for the purpose of producing an anti-competitive effect."<sup>84</sup> Indeed all firms could be characterised as behaving anti-competitively in that they advance their own interests at the expense of the competition as part of the normal competitive process. It would appear then that an anti-competitive purpose could be read into almost any act by a firm in the normal process of competition. The danger stems from the fact that some firms pose a greater threat to competition in pursuing a purpose that is characterised as anti-competitive, because their market power means that they are in a position of advantage in doing so and therefore much more likely to succeed because of the

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<sup>84</sup> *Telecom v Clear*, above, 402.

relative lack of competitive constraints upon them. Hence the substance of the prohibition is in the degree of market power and the use thereof. This accords with the view expressed by Scalia J in *Eastman Kodak*<sup>85</sup> and cited by the majority in *Melway*.<sup>86</sup>

The filter then that distinguishes pro- and anti-competitive behaviour is the use or take advantage limb of the prohibition. If market power has been employed in certain conduct as evidenced by the fact it can't be considered an act that would have been carried out regardless of that power, then it is anti-competitive. The Commerce Committee<sup>87</sup> and officials from the Ministry of Economic Development<sup>88</sup> endorse this view. The purpose limb of the prohibition therefore seems to serve very little practical function in the establishment of a section 36 case.

#### **VIII THE PURPOSE STATEMENT: LONG TERM CONSUMER BENEFIT**

The signals of the Australian jurisprudence on anti-competitive conduct have been revealed as less than clear. Scope remains for the courts to colour their decisions with their own belief of the prohibition's function. The other interpretive signal provided by the amendment, it would seem, could be found in the new purpose statement in section 1A of the Act. This reads 'The purpose of this Act is to promote competition in markets for the long term benefit of consumers within New Zealand.'

While at least superficially this statement accords well with the Alliance's concentration on consumer protection and Labour's focus on advancing consumer welfare through the promotion of competition, it is debatable what, if anything, the statement will do to assist the courts in their application of the Act. Under section 5 (1) of the Interpretation Act 1999, courts are required to give meaning to legislation from its text and in light of its purpose. Having been

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<sup>85</sup> *Eastman Kodak*, above, 488.

<sup>86</sup> *Melway*, above, 18.

<sup>87</sup> Commerce Amendment Bill 2001, no 296-2, above, xiii.

<sup>88</sup> Ministry of Economic Development *The 'Use' Test in Section 36 of the Commerce Act* (CAB/MED/9, Wellington, 2000) 3.

provided with such a purpose, the courts will no doubt feel compelled to try and give effect to it. The purpose statement, however, suffers from an ambiguity that reduces its effectiveness as a tool for guiding the courts in applying the provisions of the Commerce Act and section 36 in particular. Indeed even the intention of Parliament with regard to the purpose statement is ambiguous. When the Commerce Amendment (No. 1) Bill first came before the House, the Chair of the Commerce Committee declared that the purpose statement:<sup>89</sup>

...makes it clear that the New Zealand Parliament supports a welfare-based, Harvard School approach that puts the interests of consumers first. However, we have taken due account of the arguments that we have to take a long-term perspective and see dynamic efficiency play in the market, and for that reason it is the long-term interests of consumers that appear in the new purpose statement.

The very mention of dynamic efficiency gives Labour's concept of consumer welfare efficiency-driven connotations of aggregate wealth, as espoused by the Chicago School.<sup>90</sup> The reference to 'long-term' benefit in the purpose certainly suggests a focus on dynamic efficiency,<sup>91</sup> but equally there may be no focus on efficiency at all, given that a reference to efficiency in the purpose statement initially proposed, was expressly removed at the Select Committee stage. Efficiency was not to be looked at by the courts. It was deemed to be a consideration only for the Commerce Commission when authorising restrictive trade practices.<sup>92</sup>

The select committee report itself downplays the significance of the purpose statement: "We consider that the addition of the purpose statement will not fundamentally change the interpretation of the Act."<sup>93</sup> Officials from the Ministry of Economic Development certainly felt this way too, seeing the main impact of the statement as being in the measurement of public benefit by the Commerce Commission during the authorisation process. In their view the scheme of the Act was such that:<sup>94</sup>

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<sup>89</sup> Hon D Cunliffe NZPD

<sup>90</sup> See Bork, above, 193

<sup>91</sup> See James Mellsoy "What is the Objective of the Commerce Act" (April 2002) *Competition and Regulation Times* 4.

<sup>92</sup> Commerce Amendment Bill 2001, no 296-2, above, vii.

<sup>93</sup> Commerce Amendment Bill 2001, no 296-2, above, vii.

<sup>94</sup> Ministry of Economic Development *The Purpose Statement in the Commerce Act* (CAB/MED/6, Wellington, 2000) 9.

...there is a presumption that the goal of long term benefits to consumers will be achieved through the promotion of competition. However it seems consistent with the purpose statement that this presumption may be rebutted if the long term benefits to consumers may be achieved through efficiency gains that outweigh any anti-competitive detriment.

This suggests that the promotion of efficiency could be considered a greater means of securing consumer welfare than competition, the very means envisaged in the words of the purpose statement itself. Section 36 contraventions, however, cannot in themselves receive Commerce Commission authorisation under the Act, which suggests that efficiency-seeking conduct is no defence to misuses of market power.

A further confusing element is evident in the fact that the purpose statement for Part 4A of the Commerce Act, which deals with the regulation of the electricity lines businesses, expressly aims to promote the efficient operation of that market.<sup>95</sup> The absence of a similar phrase from the section 1A purpose statement tends to support the argument that efficiency is not to be considered in the pursuit of consumer welfare through competition.

It all serves to demonstrate the level of confusion that exists as to what the purpose of our competition laws really is. Given that there are conceivably a myriad of different factors that could be considered as contributing to consumer benefit, the new purpose statement can really mean anything to anyone. It is debatable whether the politicians themselves knew exactly what was meant by the purpose statement and its reference to consumer benefit.

The socially conscious thrust of the Alliance's policies would seem to imbue the purpose statement with notions of allowing competitors access to markets to give consumers freedom of choice, and redistributing income between producers and consumers of anti-competitively priced goods thereby driving prices down. To this extent the courts would be able to read into the statute a

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<sup>95</sup> Commerce Act 1986, s 57E.

function such as the elimination of monopoly profits, as attempted by the Court of Appeal,<sup>96</sup> but shelved by the Privy Council in *Telecom v Clear*.

Labour's concept of promoting competition for consumer benefit instead appears consistent with that expressed by the Ministry of Economic Development and founded upon the promotion of consumer welfare through efficiencies derived from competition. Their assumption being that competitive markets deliver optimal outcomes for both producers and consumers alike. Issues of consumer protection were seen as more appropriately undertaken on an industry basis through such means as the Telecommunications Service Obligation and the Electricity Complaints Commission.

Just how this purpose statement will affect the courts' interpretation of section 36 and in particular the consideration of legitimate business justifications under the take advantage limb, is an open question.

It would seem likely that the courts will interpret the provision as a tool for promoting consumer benefits, such as lower prices and greater choice of product and supplier, through the efficient operation of competitive markets. However the reference to 'long-term' brings a speculative element into play and makes it even more questionable whether the purpose statement can be given a practical effect by the courts. In trying to give effect to this element of the purpose statement, the courts may be less inclined to look at the immediate effects of a firm's anti-competitive actions on the assumption that future competition will erode any monopolistic practices. Conversely they may decide that any act that has a short term adverse impact on competition will necessarily limit long term competition and not lead to long term consumer benefit, or even that smaller competitors who are inefficient in the short term should be protected so that consumer benefits might be achieved in future.

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<sup>96</sup> See *Clear Communications v Telecom Corporation of New Zealand Ltd* (1993) 5 TCLR 413, 436 (CA) per Gault J: "I cannot accept that the objects of the Commerce Act are served by a method of pricing that secures the profits of a firm in a dominant position."

If the select committee are to be believed, then the courts should not diverge from their existing interpretation of section 36, but is this the idea of allowing new competitors to achieve equal footing with incumbent participants as originally endorsed in *ARA v Mutual Rental Cars (Auckland Airport) Ltd*<sup>97</sup> or the Privy Council's agreement that a monopolist shouldn't be required to hold an umbrella over inefficient competitors in *Telecom v Clear*? While the general dissatisfaction with the Privy Council's decision might suggest the former, it seems again that Parliament has handed the courts a less than clear and potentially dangerous signal.

### **IX THE EFFECT OF THE AMENDMENTS**

To summarise then, the intention of the Labour-Alliance coalition in amending the Commerce Act was to promote competition in the interests of consumers by providing simple legislation prohibiting the anticompetitive acts of firms dominant in their market sector, to provide clear signals to the courts about how the legislation was to be interpreted, and to give consideration to the anti-competitive effects of those firms' conduct in determining whether the conduct was acceptable or not.

The amended section 36 instead appears at the very least uncertain in its application. It arguably constrains the legitimate competitive behaviour of firms who really should be outside the scope of the prohibition, provides less than clear interpretive signals to the courts thereby enabling them to give unintended meanings to its terms, and it seemingly gives no further consideration to the effects of a dominant firm's behaviour than was available under the provision prior to its amendment. The addition of a purpose statement has served only to add another potential ambiguity to the interpretation of the statute.

What other options might have been considered to strengthen section 36 and ensure an effective prohibition on the misuse of market power and the curbing

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<sup>97</sup> *ARA v Mutual Rental Cars (Auckland Airport) Ltd* [1987] 2 NZLR 647, 671 (HC).



of anti-competitive behaviour by large firms that was deemed so necessary in the lead up to the election.

#### *A The Failure of Certainty*

A fundamental concern with any regulatory reform is over the issue of certainty. This is particularly true when dealing with market behaviour as no government wants to stymie business and thereby reduce the overall productivity of the economy. Economic performance is the driver of modern government as social welfare intrinsically tied up in the ability to pay for it. A stagnant economy will not lead to the improvement of the overall welfare of its consumers. The Coalition Government was strong in its commitment to providing tidy and certain legislation so that business would know the parameters of prohibited conduct and could get on with operating efficiently and competing fairly. In adopting the Australian approach to the policing of unilateral market power, the Government felt this certainty would be provided by 14 years of Australian jurisprudence, yet in doing so they effectively devalued any certainty provided by prior New Zealand jurisprudence on the point. As stated previously, however, the courts have been handed few clearer signals in the interpretation of section 36 than they had prior to the 2001 reforms.

The pivotal certainty issue surrounds the question of which firms come within the ambit of the section 36 prohibition. Given that competitive and anti-competitive conduct often appear very similar, the very reason that the prohibition contains a threshold is so that the behaviour of only a certain number of firms, those with sufficient market power to actually harm the process of competition, is constrained. The uncertainty of the adopted substantial degree of power threshold means that a greater number of firms are likely to hesitate before pursuing legitimate competitive actions in the fear that they will be captured by the prohibition.

In his supplementary order paper, Hon M Bradford sought not to change the actual threshold of market dominance but to amend the definition of dominance within section 3(8) of the Act by substituting 'high degree of market power' for

'dominant influence'. While this was ridiculed by the Coalition Government: "well, no-one knew what that was... it would have caused great confusion,"<sup>98</sup> it did at least have the benefit of retaining the existing language of the section. Also, Hon M Bradford purportedly sought a return to the threshold to a level previously understood by the business community from the cases of *Re Magnum Corporation v Dominion Breweries Ltd*<sup>99</sup> and the High Court decision in the *AMPS-A* case<sup>100</sup> in which dominance had been characterised as constituting sufficient market power or economic strength to enable the firm to behave to an appreciable extent in a discretionary manner without suffering detrimental effects in the relevant markets.

While Hon M Bradford's reform may not have brought any greater degree of certainty than that achieved by the change to a substantial degree of market power, value might be found in his attempt to amend the definition of dominance rather than the threshold itself. Could certainty not be achieved by a quantifiable definition of dominance? There is precedent for this in at least one overseas jurisdiction. Section 19(2) of the German Act Against Restraints of Competition contains a refutable presumption that a firm is dominant in a market if it possesses one-third of the share of that market. Firms that come within this definition then have the possibility of establishing that for other reasons such as low entry barriers to that particular market, they cannot be considered to be in a position of dominance. Merit can certainly be found in the suggestion. The setting of a presumption too would have the advantage of taking into account the particular characteristics of the New Zealand economy, unlike the adoption of an Australian threshold. By introducing a quantifiable market share presumption, an expectation would be set in the business community as to which firms would need to be wary of section 36 liability, also it would remove the degree of speculation involved over the courts' interpretation of the threshold. Concerns over the level not being appropriate in certain circumstances would be mollified by allowing a firm to argue that

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<sup>98</sup> Hon P Swain (8 May 2001) 592 NZPD 9072.

<sup>99</sup> *Re Magnum Corporation Ltd v Dominion Breweries Ltd* (1986) 2 TCLR 177 (HC).

<sup>100</sup> *Telecom Corporation of New Zealand v Commerce Commission* (1991) 4 TCLR 509 (HC).

despite their existing market share, they do not possess the requisite market power.

Given the existing scheme of the Commerce Act and the lack of quantifiable thresholds in other parts of the Act, it seems unlikely that such a measure would be introduced. Precedent for a refutable presumption does exist outside the Act however, as evidenced by the 'safe harbours' prescribed by the Commerce Commission<sup>101</sup> in its consideration of mergers and acquisitions and whether they are likely to lessen competition in a particular market. A similar guideline could have been published regarding the question of dominance for section 36 purposes and indeed could still be done under the new threshold of substantial degree of market power. Firms that come within the presumption would then be required to consider the impact of their conduct lest it be characterised as anti-competitive and face action from the Commerce Commission. Other smaller firms could be left to compete, subject only to the sanctions of the market.

Another method of affording certainty not given explicit consideration during the reforms, is a procedure whereby clearance could be given for conduct by the Commerce Commission. A firm uncertain as to whether their conduct might be in violation of section 36 could apply to the Commerce Commission for a determination of whether their conduct would be likely to raise a section 36 action from the Commission, prior to undertaking that conduct. While such an approach may raise issues of timeliness and response to market conditions, it too has merit, and is worthy of further consideration.

Having set a level of market power a firm must possess in order to attract section 36 liability, the prohibition then needs to characterise the type of behaviour that those firms must be restrained from carrying out. If the Commerce Committee is to be believed, it is the take advantage limb of section 36 that provides the filter between acceptable and unacceptable conduct. As stated previously, there has been little, if any, change effected to this component

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<sup>101</sup> See Commerce Commission *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* (Wellington, 2001) 28-9.

of section 36 by the 2001 reforms. Nor, it is asserted did there need to be. Removal of this limb would result in either a shackling of all conduct by large firms if anti-competitive purposes were readily inferred, or place too great a reliance on subjective evidence of purpose, the problems of which have been discussed earlier. The counterfactual test as espoused by the Privy Council in *Telecom v Clear* is an essentially sound filter of competitive and anti-competitive behaviour, provided that the object of the section is clear and the warnings from *Melway* are borne in mind. The test must be grounded in reality and should not become a substitute for the actual question of whether advantage of market power has been taken. As such this limb provides the causal connection between the market power and the proscribed conduct; that the firm was able to carry out the conduct by reason of its market power.

#### ***B The Case for an Effects Test***

It is, then, by defining the proscribed conduct that the next big issue with section 36 should have been considered. Given that it was a stated aim of both coalition parties that anti-competitive effects be given consideration, a closer examination of the effects test is appropriate.

The main reasoning behind the introduction of an effects test, is that by determining acceptability or otherwise of a firm's conduct through the consideration of its effect on competition, the requirement to establish an anticompetitive purpose on the part of the firm possessing market power would be replaced. This would remove a potentially onerous evidential burden on a party alleging a breach of section 36 and therefore encourage greater use of the provision in policing anti-competitive behaviour. It also has the advantage of basing the prohibition in its very essence, the restriction of competition in a market. If competition in a market has been reduced because a firm with market power has acted in a manner available to it by virtue of that market power, is there really a need to discover whether it was the firm's purpose to do so?

Another reason advanced for the adoption of an effects test is that it addresses the public concern of the increasing concentration of big industry players and

natural monopolies stifling competition, by focusing on the effect of their actions on the rest of the competition. The effects test has as a result typically been associated with the socially-motivated competition policy and the political left.

As mentioned earlier, Labour had shifted away from the introduction of an effects test despite backing the Alliance's attempt to introduce such a test in 1999. While Labour had been dissuaded from such a test following the Ministry of Commerce's discussion paper, the Alliance had not. Failing to advance the effects test any further, the Alliance sought instead to strengthen the prohibition by instead reversing the onus of proof of purpose. This would deem a firm to be taking advantage of their substantial market power in breach of section 36 unless it could prove otherwise. This option was put to the Commerce Committee as an option alongside the inference of purpose proposal, but was dropped from Supplementary Order Paper (No. 37) following representations from business leaders that it would lead to vexatious or frivolous actions being undertaken by a firm's competitors.<sup>102</sup> To ameliorate this it was proposed that the reverse onus apply only in actions brought by the Commerce Commission. This, however, raised a further concern that private enforcement of the provision would be undermined and instead too much reliance would be placed on public enforcement. As well as this, concern around the novelty of the proposal,<sup>103</sup> namely the fact that it did not appear in the competition laws of other countries, and the uncertainty it may cause in the business world, meant that it too was dropped.

The introduction of an effects test as either a replacement of or complement to the existing purpose test in section 46 of the Trade Practices Act has come under consideration on numerous occasions across the Tasman.<sup>104</sup> On each occasion it has been rejected.

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<sup>102</sup> "Government Rethinking Changes to Competition Law" 27 December 2000) *The New Zealand Herald* Auckland A11.

<sup>103</sup> Cabinet Minute "Commerce Act: Strengthening the Prohibition Against a Misuse of a Dominant Position" (28 March 2000) FIN (00) 54, 38c.

<sup>104</sup> An effects test has been put forward for consideration by the Blunt Committee in 1979, the Griffiths Committee in 1989, the Cooney Committee in 1991, the Hilmer Committee in 1993, Reid Committee in 1997, Baird Committee in 1999, the House of Representatives

Crucial to its repeated rejection by the various committees, the effects test has been criticised for giving the prohibition too wide an application and bringing too much legitimate business conduct within its ambit. Inadvertent or efficiency-driven conduct could be at risk because the test doesn't distinguish between socially beneficial and socially detrimental behaviour. Companies would be forced to evaluate the potential effects of their every action on competitors both actual and potential. The process of effective competition involves engaging in conduct which will potentially produce the very ends proscribed by section 46. Prohibiting conduct by reference to its effect may therefore challenge the competitive process itself. A purpose based test has been seen to have the advantage of an appropriate interpretation and greater level of certainty for business.<sup>105</sup>

Other criticisms of the effects test are that there is an issue of causation to be considered, and a question over how long a period the effect needs to arise. The effects of conduct on competition in a market may not be felt for quite some time. By contrast an immediate effect may later be countered by the actions of existing or new competitors.

There is certainly credence in the arguments that an effects test increases the scope for more legitimate conduct to be considered within the provision and given the drive to align this country's competition laws with those of Australia, it is not surprising that the New Zealand Government has shied from adopting a test rejected consistently across the Tasman. However it is noticeable that the Australian discussion on the relative merits of the purpose and effects test has been far more comprehensive than that on our shores. The Australian Competition and Consumer Commission (ACCC) has been at the forefront of calls for the introduction of an effects test<sup>106</sup> and has been supported in its calls

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Standing Committee on Economics, Finance and Public Administration in 2001 and is currently before the Dawson Committee.

<sup>105</sup> See Mitchell Landrigan, Anne Peters and Jason Soon "An effects test under s46 of the Trade Practices Act: Identifying the Real Effects" (2002) 9 CCLJ 2 for a discussion of the reasons outlined by the various committees for and against the adoption of an effects test.

<sup>106</sup> Ross Jones "The Path to Competitive Discipline" (11 July 2002) *Australian Financial Review* Sydney 63.

by small business.<sup>107</sup> Big business on the other hand has waged a public campaign against both the ACCC and the effects test, mistrustful of the powers that the ACCC already wields and no doubt fearful of the potential impact such a test would have on their ability to compete.<sup>108</sup> Big business has been supported in its stance by the Productivity Commission, a government think tank charged with continuously looking for ways to improve the efficiency of the Australian economy.<sup>109</sup>

Concerns about a resulting deterrence of competitive behaviour can be allayed however, particularly if one believes the indications that the taking advantage limb is also key to the determination of whether conduct is legitimate or not. It is not every act by a firm with market power that produces an anti-competitive effect that is condemned by section 36. That market power must have been employed in the act. Also, by restricting the scope of the prohibition to firms that are in a position to control their particular markets, i.e. those that are in the greatest position to affect competition, the number of firms required to consider the effects of their conduct is limited. On such an approach, a threshold of dominance even to the level proposed by the Court of Appeal in the *AMPS-A* case might not be inappropriate.

Given the stated needs of strengthening the Commerce Act to curb the behaviour of large corporations through simple legislation that gives consideration to the anti-competitive effects of those firms' conduct, it is surprising that such an approach was not given more consideration. Indeed the balance struck by a prohibition aimed at a higher level of market power, with an objective filter, in which anti-competitive behaviour is determined by its effect on competition, appears more suitable to the aspirations of the Coalition Government than that of the lower threshold, objective filter and purpose based prohibition settled for.

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<sup>107</sup> Michael Delaney "Trade Safeguards Need Balance" (9 July 2002) *Australian Financial Review* Sydney 63.

<sup>108</sup> Steven Kates "Rabid Watchdog Needs a Shorter Leash" (26 April 2002) *The Australian* Sydney 9.

## X REASONS FOR THE REFORMS

Why then did the Government settle for such lightweight reform. It goes without saying that strong public statements whilst seeking election are likely to be subject to compromise upon the attainment of power. In the words of Herbert Hovenkamp:<sup>110</sup>

Few elements of statutory interpretation are more frustrating than the study of legislative history to determine a statute's meanings. The debates and compromises leading to a statute's passage often contain conflicting statements, made by persons who were elected by disparate interest groups, who had different motives and different perceptions about what a statute would do. Sometimes legislative committees achieve compromises by making statutory language intentionally ambiguous, leaving to the courts to decide later which interpretation should prevail.

Certainly these words ring true when the reforms finally embodied in the Commerce Amendment Act are examined. As mentioned previously, the passage of the Act was not straightforward. It was characterised by a series of delays, amendments and the inability of the Select Committee considering the Bill to agree on some of the fundamental amendments. The Commerce Committee was split evenly on the two key reforms to section 36, namely the threshold of substantial degree of market power and the substitution of 'use' with 'take advantage', hence the omission of these from the first Commerce Amendment Bill. Indeed agreement had still not been reached on those limbs of section 36 before the Commerce Amendment (No.2) Bill was tabled in the House.

### A Honouring Pledges

Despite the numerous amendments that were made to the amendments and the raft of submissions received in response to the two supplementary order papers, the reforms of the Commerce Amendment Act remained largely those of Labour's pre-election policy or rather those proposed by the Ministry of Commerce in its discussion document of 1999.

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<sup>109</sup> Stephen Bartholomeusz "Productivity Commission No Friend to an ACCC Seeking More Powers" (25 July 2002) *The Age* Melbourne 3.



Importantly from Labour's perspective, the enactment of their proposed reforms was seen to be in keeping with their pre-election promise, a virtue that they took pride in, and trumpeted as a key achievement during their term in government.<sup>111</sup> But in doing so, it appears that they either lost focus of the intent behind their reforms, or assumed too greatly that the wording they chose in enacting those reforms would give effect to those intentions. Certainly the advice received from their officials in the Ministry of Commerce and its successor the Ministry of Economic Development did not deviate from that of their 1999 discussion paper, that the preferred option for reform lay in the adoption of the Australian approach.

### **B The Influence of Officials**

That paper laid out the Ministry's perspective on the driving force behind the Commerce Act, that it was a means to facilitate gains in economic efficiency across the economy,<sup>112</sup> a view of competition law not unlike that espoused by the Australian Productivity Commission. To that end the role of the thresholds contained in the Commerce Act were threefold, to capture for scrutiny those activities likely to result in economic harm (i.e. exercises of market power that would result in efficiency losses), to not deter or prevent efficiency enhancing behaviour and to minimise uncertainty and costs of administration, compliance and enforcement. Importantly, these thresholds were only seen to be of benefit in so far as the harm prevented was greater than the costs incurred through scrutiny and prohibition.<sup>113</sup>

In terms of the substantial degree of market power threshold, the Ministry's support was unwavering. The threshold from Australia would apply to some more firms, but only those to whom it should have applied but didn't because the economic approach to dominance had been supplanted by a dictionary definition. There was no evidence that a reduction of competitive and efficient

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<sup>110</sup> H Hovenkamp *Federal Antitrust Policy: The Law of Competition and its Practice* (2ed, West Group, St Paul, Minnesota, 1999) 47.

<sup>111</sup> "Confident Clark Looks to Future" (December 27 2000) *The Dominion* Wellington 2.

<sup>112</sup> Ministry of Commerce, above, 3.

<sup>113</sup> Ministry of Commerce, above, 12.

behaviour had occurred as a result of this threshold in Australia. Any increase in compliance costs from the greater number of firms coming within the purview of the provision, would be outweighed by the overall benefits of stronger competition.<sup>114</sup>

By substituting 'take advantage' for 'use' the New Zealand courts would be availed of an approach less rigid than the counterfactual test previously laid down by the Privy Council. The courts would have the freedom to move away from the Privy Council formulation when appropriate, without adopting a subjective purpose driven approach.<sup>115</sup> The inference of purpose would codify the courts' existing good practice.

The Ministry's comments are replicated consistently through the Government rhetoric on the 2001 amendments. Having not received any official advice contrary to its stated position, it is hardly surprising that Labour, a government devoted to keeping its pledges, saw its reforms carried through in their original form.

### **C Harmonisation**

A constant theme running through the 2001 reforms was the benefits of bringing New Zealand's competition laws into line with those of Australia. In the documented consideration of the amendments to each limb of section 36, whatever advantage the change itself brought was always reinforced by the fact that consistency with our closest trading partner brought benefits of its own. However in light of the substantive changes that these reforms have, or haven't, brought to our laws on the misuse of market power, it is not unreasonable to think that the Government placed too much value in harmonising for harmonising's sake.

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<sup>114</sup> Ministry of Economic Development *Official's Report on the Commerce Amendment Bill* (CAB/ MED/18, Wellington, 2000) 5.

<sup>115</sup> Ministry of Economic Development *The 'Use' Test in Section 36 of the Commerce Act* (CAB/ MED/9, Wellington, 2000) 9.

Harmonisation it was stated would improve transparency and the ease with which businesses could operate across borders. For New Zealand producers it would ease access to a market consisting of approximately 20 million consumers. Differences between regulatory environments would require a firm wanting to operate in both New Zealand and Australia to comply with two different sets of rules and increase their costs therein, which could deter competition in both markets. A more closely aligned trans-Tasman commercial environment would also allow a common outward focus in commercial activities within the greater global market.<sup>116</sup> Overseas firms looking to move into or invest in the sizeable Australian market would be more inclined to move into New Zealand as well should they not face a different regulatory regime.

But are these real benefits? In the words of Kerrin Vautier:<sup>117</sup>

The rationale for harmonisation has always been shaky, especially from an economics perspective. Essentially it has relied upon assertions of business certainty, reduced transaction/compliance costs and trade enhancement in the context of a 'single market'. But ex post verification of a positive correlation between harmonisation and, in particular, lower impediments to trade, has been lacking and such assertions have become more muted.

Given that the three amendments to section 36 brought about by this harmonisation could be characterised as inappropriate or inconsequential, and given too that the relevant provisions of the two countries as they previously stood were so similar as to be for all intents and purposes harmonised already, it seems that this aspiration and the resulting benefits peddled were overstated. Certainly without tangible evidence of those benefits, of which none was presented in the passage of the Act, the costs associated with the amendment of section 36 may turn out to be greater than any benefits foregone by retaining the previous provision.

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<sup>116</sup> Hon P Swain, Minister of Commerce (Speech to Institute for International Research Ltd, Auckland, 13 March 2002).

<sup>117</sup> Kerrin Vautier "Competition Law and CER" (March 2001) *Competition and Regulatory Times*, 8.

## *D Industry Specific Regulation*

Electricity and telecommunications lifted the public profile of competition law in New Zealand. The failure of the previous Government to address the shortcomings of light-handed regulation in policing those industries had made competition a hot election issue in 1999. Both Labour and the Alliance had advocated regulatory regimes specific to those industries, and following the respective ministerial inquiries, new legislative controls were introduced.

The amendments embodied in Part 4A of the Commerce Act give the Commerce Commission powers to impose price control on the electricity lines businesses, while also subjecting those businesses to tighter information disclosure requirements. The Telecommunications Act 2001 appointed a specific regulator, the Telecommunications Commissioner, to oversee issues arising in the industry. Rules for the provision of network access were set out, as were universal service obligations replacing the existing 'kiwi share' obligations. The public demands for tighter controls on these two utilities could be seen to have been addressed by the increased regulation manifested in these reforms, but again it is questionable whether they in fact have brought about any significant change. Control over the prices charged for utilities was always available to government under Part 4 of the Commerce Act. Previous governments had simply been unwilling to invoke them lest the image of light-handed regulation be tainted.

### *1 The Regulation of Electricity Lines Businesses*

The new provisions for electricity lines businesses serve to shortcut the process so that an Order in Council on the recommendation of the Minister is not required to declare that goods or services provided by them are 'controlled' for the purposes of the Act. Instead such a declaration may be made by the Commerce Commission. These declarations are subject to a raft of procedural requirements including the establishment of thresholds for the declaration of control. Industry and consumer consultation is required and must be given

regard to,<sup>118</sup> and it is questionable therefore whether there are any real streamlining gains over the old process. Section 57O of the Act states that the pricing methodologies of Transpower, who own and operate New Zealand's national grid for electricity transmission, may need Commerce Commission authorisation. This will, however, only occur in the event that it is required by Order in Council, so again little real change from the previous price control provisions is evident.

## 2 *The Telecommunications Act 2001*

The new telecommunications regime heralded by the Telecommunications Act 2001 could also be criticised for bringing little significant change. While a Telecommunications Commissioner has been appointed to oversee the industry and make determinations on such issues as the contribution to universal service obligations and network access and the terms thereof, the Act still gives primacy to commercial negotiations in access disputes. The commissioner may make a determination on a dispute where the negotiations fail. The potential for protracted access disputes still exists, what appears to have changed is that an arbiter more qualified in the industry than the courts will now make the determinations. Schedule 2 of the Act also provides for self regulation by a forum comprised of representatives from firms in the industry. This forum is able to prepare telecommunication access codes in relation to designated and specified services. The wisdom of having the telecommunications industry regulate itself is questionable and given the difficulties already faced in agreeing the composition of the forum itself,<sup>119</sup> it appears that the problems of the light-handed regime have simply been supplanted by new time-consuming problems.

## 3 *Diluting the Commerce Act?*

The reliance on specific regulation to deal with problematic industries provides a concerning precedent however. In so doing government has given a signal that

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<sup>118</sup> see Commerce Act ss 57G(1), 57I(1) regarding thresholds for declaration of control and process before declaration made respectively.

<sup>119</sup> "Telecomms Forum Stymied" (18 February 2002) *NZ Infotech Weekly* Wellington 1.

should similar problems in other industries arise under a provision that is essentially the same as that which failed telecommunications and electricity, these may be dealt with by further industry-specific regulation.

The imposition of industry-specific regulation on telecommunications and electricity lines may well have taken some of the wind out of the Government's sails in relation to the generic prohibition on the misuse of market power. Whatever the merits of the regulation itself, Labour could be seen by voters to have delivered on its promises. The Alliance, though unsuccessful in obtaining the return of ECNZ to full State ownership, could be satisfied that the regulation of Telecom it had demanded had been achieved. Having introduced new rules for governing telecommunications in particular, there may have been a belief that there would now be few industries in which the misuse of market power provisions would raise issues of great concern to the economy and the public. Aware that telecommunications and electricity lines were going to be separately regulated, it is questionable then whether the Government needed to bring about any changes to section 36 at all. It might also be argued that the reforms were calculated not to bring about any substantive change, and were simply a tool to display the Government's intent to harmonise our business laws with those of Australia and show itself to be honouring its pledges.

## *XI WHO DARES WIN?*

Given the lack of significant change brought about by the Commerce Amendment Act 2001, it is difficult to say whether anybody can feel truly satisfied with the state of New Zealand's prohibition on the misuse of market power following the amendments.

While big business will no doubt be pleased that an effects test that would have placed larger constraints on their activities was not introduced, the very fact that other changes have been made to section 36 means that larger businesses in general face increased compliance costs. The lack of certainty afforded by the amendments also suggests that larger firms will be more risk averse in their competitive strategies for fear of breaching section 36 and attracting a much

larger penalty than the previous legislation provided for. The stated desire for efficiency to be given express recognition in the purpose statement of the Act<sup>120</sup> was also unfulfilled.

Small businesses on the other hand have even less to be grateful for. The prohibition is still rooted in the purpose of the firm holding market power rather than the effect of their conduct on competition. While the pre-eminence of the Privy Council's use test has been undermined somewhat, the *Melway* and *Carter Holt* decisions suggest that dominant firms will still be availed of excuses for acts that impact negatively on the ability of smaller firms to compete. Without explicit recognition in the Act, in either the purpose statement or in section 36, the interests of small business have been largely ignored.

Consumers may feel that following the amendments they are better off as the Act is now intended to promote competition for their long term benefit. But the scheme and purpose of the Commerce Act has not changed in any significant way. The consumer benefit referred to in the purpose statement seems intrinsically tied up benefits derived from dynamic efficiency, and does not take in other notions such as choice of suppliers, income redistribution, and other populist notions such as the support of local and independent producers.

## *XII CONCLUSION*

It appears then that an almost blind devotion to harmonisation, a penchant for keeping pledges, the ambush of the High Court of Australia's decision in *Melway*, the introduction of specific legislation for the electricity and telecommunications industries, and a seeming unwillingness to address specifically the function of our generic competition laws and introduce legislation unique to New Zealand, have conspired to render the reforms to section 36 a costly exercise in window dressing at best. The strengthening of the Commerce Act so audibly heralded has simply not happened, indeed with the

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<sup>120</sup> See New Zealand Business Roundtable "Submission to the Commerce Committee on the Commerce Amendment Bill 1999" 2.

increasing reliance upon sector-specific regulation a strong case can be made that the Act has diminished in importance.

Balancing the social and economic aspirations of competition law is a difficult task for a government, and one that the Labour-Alliance Government may have found too difficult to stick their neck out either way on. The conflict between promoting economic growth and delivery on social policy outcomes must have weighed heavy on a centre-left government eager to curry economic credibility. However these aspects of the 2001 reforms passed with barely a mention in our newspapers and certainly without any in-depth analysis of the options for reform that the differing perspectives might bring. The non-economic goals of the protection and preservation of the independence of smaller, locally owned business were largely ignored. The Alliance, the minority partner, were the only political party that appeared truly concerned with the interests of small business in their pre-election rhetoric, and with the Alliance's recent fall from power, it is questionable whether there is in fact anybody left in their corner. Consumer welfare was given lip service, but in the form of an ill-defined purpose statement which seems to measure benefits in purely economic terms. Economic considerations, particularly those of efficiency, remain unchallenged as the prime drivers of our competition laws.

The Commerce Amendment Act marked an opportunity for an incoming government to revisit New Zealand's laws on the misuse of market power at a time of heightened frustration with the current regime. Instead the 2001 reforms ushered into place a prohibition with little distinguish it from its oft-criticised predecessor, or that proposed by the previous National Government, and basing it on an Australian provision that itself has faced regular calls for review. The reluctance to tackle directly the issues surrounding the policing of misuses of market power in the New Zealand economy suggests that the Government may have put this whole area of competition law in the too-hard basket, or rather, placed problematic industries in the hands of regulators and given the unenviable task of determining the fundamental purpose of our misuse of market prohibition to the courts, as and when section 36 cases arise.



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