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AN ANALYSIS OF THE "RELEVANT MARKET"
CONCEPT IN THE CONTEXT OF THE
COMMERCE ACT 1986 AND THE
TRADE PRACTICES ACT 1974

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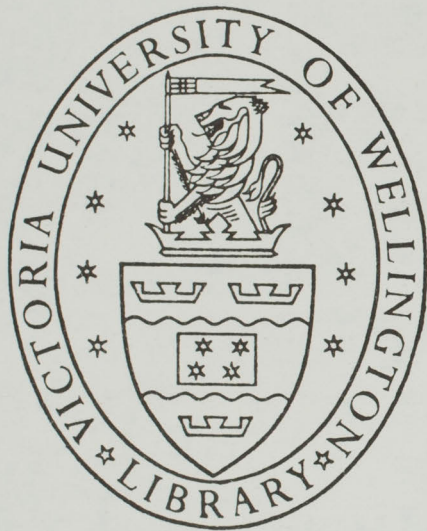
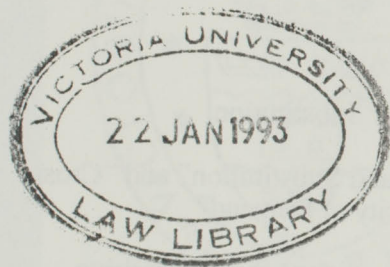


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Word Length

The text of this paper (excluding names, dates, footnotes, bibliography and answers) comprises approximately 17,500 words.

ABSTRACT

This paper will examine the process of defining a relevant market within both the New Zealand Commerce Act 1986 and the Australian Trade Practices Act 1974 (Cth) in light of cases and writings in the major overseas antitrust systems, such as the European Common Market and the United States. This discussion will commence with an examination of the statutory definition of "market" within both the Trade Practices Act and the Commerce Act. The next step in the enquiry will be to analyse the product, geographic space, function and time dimensions of the relevant market concept that have frequently been employed by New Zealand and Australian authorities as an aid to the determination of the relevant market. Consideration will also be given to the concept of a sub-market and its utility within New Zealand and Australian trade practices litigation. This discussion will demonstrate that the approach to market definition adopted by New Zealand and Australian authorities requires a large amount of subjective assessment on the part of the relevant court or tribunal. Therefore, by way of conclusion this paper will suggest that such flexibility within this market definition methodology should be moderated against an increased emphasis upon the commercial realities of the particular factual situation involved in any such proceedings.

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PART I

1. INTRODUCTION

Under competition laws the market concept is an indispensable analytical tool. It assists in the ascertainment of material facts, provides a framework for determinations, and allows judicial authorities to make succinct and informed assessments of particular practices. Although some concept of a "market" is inherent in all systems of competition law, a striking feature which is common to both the New Zealand Commerce Act 1986 and the Australian Trade Practices Act 1974 (Cth), is that many of their principal provisions relating to mergers and takeovers¹, and restrictive trade practices depend² in one way or another on the identification of a market or markets in which competition has been injured by the impugned conduct. This is largely a result of the fact that at the time when the Australian and New Zealand legislation came to be drafted the concepts of market definition and market control had evolved to a highly developed state in other jurisdictions, particularly in the United States.³

Now, however, after six years' experience with market definition under the Commerce Act 1986 and 18 years' under the Trade Practices Act 1974, the Australian and New Zealand doctrines should have their own contribution to make towards the concept of a "market" in antitrust analysis. It would be rewarding, therefore, to describe and analyse within this paper the principles that have so far emerged under the New Zealand and Australian legislative schemes, in light also of cases and writings in the major overseas antitrust systems, such as those of the European Common Market and the United States. As the process of market definition will often prove to be determinative in regard to suits or applications brought under the Commerce Act 1986 and the Trade Practices Act 1974, an examination of those principles which underly the identification of a relevant market will have practical as well as conceptual importance.

It must, however, be pointed out that in contrast to the Commerce Act and the Trade Practices Act, there is no statutory definition of the term "market" within antitrust legislation in the United States or the European Common Market. The task of delineating a

¹ See, Commerce Act 1986 ss.47, 66, and 67; Trade Practices Act 1974 ss. 50, and 94.

² See, Commerce Act 1986 ss. 27, 28, 36 and 36A; Trade Practices Act 1974 ss.45, 46, 46A, 47, 49 and 50.

³ See for example, *United States v E.I. du Pont de Nemours & Co.* 351 US 377 (1956), in which the Supreme Court of the United States employed sophisticated theoretical concepts such as demand substitution and cross-elasticity of demand to determine whether different products should be included in the same market.

relevant market is, however, routinely undertaken by courts within these jurisdictions in order to provide a medium within which market power can be assessed.⁴

The following discussion of the relevant market concept must logically commence with an examination of the statutory definition of a market within the Commerce Act and the Trade Practices Act. Once the requirements and implications of those statutory provisions have been taken upon board, the next step in the enquiry will be to analyse the product, geographic space, function and time dimensions of the market concept that have been employed within New Zealand and Australian authorities as an aid for the determination of the relevant market. Consideration will also be given to the notion of a sub-market and its value under the Commerce Act and the Trade Practices Act in light of certain criticisms of the sub-market concept emanating from the United States. The discussion contained within this paper will serve to demonstrate the fact that the process of market delineation employed by New Zealand and Australian authorities is a somewhat impressionistic exercise which involves a large amount of subjective assessment on the part of the relevant court or tribunal. Therefore, by way of conclusion it will be suggested that the task of market definition should be approached in a pragmatic manner which necessarily takes account of such flexibility within the market definition process and tempers it against an increased emphasis upon the commercial realities of the particular factual situation involved in any such proceedings.

The Economic Concept of a "Market"

A classically defined economic market is "that area and set of products within which prices are linked to one another by supply or demand side arbitrage and in which those prices can be treated independently of goods not in the market."⁵ The economist Alfred Marshall explained this concept of a market in terms of, a collection of buyers and sellers who are "in such free intercourse with one another that the prices of the same goods tend to equality easily and quickly".⁶

⁴ See, L.A. Sullivan, *Antitrust* (West Publishing Co., St Paul [Minnesota], 1977) 41; *Europemballage and Continental Can Co. Inc. v E. C. Commission* [1973] 12 CMLR 199, 226.

⁵ D.T. Scheffman & P.T. Spiller, "Geographic Market Definition under the U.S. Department of Justice Guidelines", 30 *J. Law & Econ.* 123, 125 (1987).

⁶ A. Marshall, *Principles of Economics* (9 ed., MacMillan & Co Ltd, London, 1961) 324.

Originally a market was a public place in a town or village where merchandise was exposed for sale, however, Marshall points out that such a distinction based on locality is no longer necessary:⁷

“The traders may be spread over a whole town, or region of country, and yet make a market, if they are, by means of fairs, meetings, published price lists, the post office or otherwise, in close communication with each other.”

The element of communication is crucial, for a competitive market is essentially an information system. It transmits data that enables producers to adjust their operations to changes in consumer tastes, technology or in the availability of materials (indeed, if these factors were not continually changing there would be no need for economic decision-making at all). Through the market, a firm's suppliers tell it how much of their raw materials they are prepared to supply at different prices, and buyers tell the firm each time they make a purchasing decision what products they want and what quantities they are prepared to take at various prices. The market gives all producers an incentive to emulate those who best adapt to, and make use of, change. The contest among suppliers to respond most effectively to changes in demand and supply conditions is the process called competition.

All competition therefore presupposes the existence of a market, and all competition law is designed to keep the market mechanism free to do its job of informing and rewarding without its effectiveness being impaired by sellers who form cartels or exploit dominant positions which enable them to ignore these signals from the market.⁸

Alfred Marshall's definition⁹ relates to the geographic aspects of the market. This definition also assumes that a market consists of homogeneous products, as shown by the use of the words, “the same goods”.¹⁰ However, for the purposes of applying competition law one must consider not only the geographic dimensions of the market, but also the product market (which includes a range of non-identical goods or services which are substitutable for those supplied by the parties under scrutiny), the temporal dimension (the time period over which the degree of substitutability is to be assessed), and the functional level in question (such as manufacturing or importing, wholesaling, or retailing).

⁷ A. Marshall, *Principles of Economics*, above n.6, 325.

⁸ See, M. Friedman and R. Friedman, *Free to Choose: A Personal Statement* (Harcourt Brace & Jovanovich, New York, 1980) 15-18.

⁹ A. Marshall, *Principles of Economics*, above n.6.

¹⁰ Above n.6.

When a market is defined in these terms, one is in effect saying that if prices were appreciably raised for the product within a given area, supply from outside could not be expected to enter quickly enough and in sufficiently large amounts to restore the old price. Defining the market therefore identifies those sellers who, if they all chose to act in concert would have effective monopoly power, at least in the short run.¹¹ Conversely, it identifies the sellers who currently are (or should be) competing among themselves and whose actions will thus limit one another's market power. Thus the market may be described as an arena for the primary demand and supply forces that determine the price of the particular product to which the impugned conduct under legal scrutiny relates.¹²

The Legal Concept of a "Market"

For most persons in business there is nothing extraordinary about the process of analysing markets. Firms make decisions each day in the context of their appraisal of the markets in which they operate or propose to operate. That appraisal will more than likely be based upon the firm's experience and knowledge of its own pattern of trade and that of its competitors and also upon special investigations, perhaps involving market research. One could predict that business operators would be dismayed to discover that the process of market analysis under the Commerce Act 1986 and the Trade Practices Act 1974 may in fact result in the relevant market being delineated in a manner which is incompatible with the views of the business person.

The broad policy aim of the Commerce Act and Part IV of the Trade Practices Act is the preservation and promotion of "competition."¹³ However, the existence of competition in any given situation is itself delineated by reference to market definition, persons being regarded as competitors when they operate in the same market. Thus, the term "market" should be looked upon as a construct designed to assist in the analysis of processes of competition, as competition does not take place in a vacuum, but in a context dubbed "the

11 As over a period of time, a position of market power will tend to be eroded as customers turn to other products as substitutes for the monopolised one ('cross-elasticity of demand'), and as other suppliers, seeing that the cartel or dominant concern is able to reap monopoly profits, enter the market in order to share in some of those profits and, by increasing the supply, ultimately increase competition and drive the price down ('cross-elasticity of supply'). See, below n.184.

12 See, G. deQ. Walker, "Product Market Definition In Competition Law", 11 Fed.L.R. 387, 388 (1980).

13 In delivering the judgement of the Court of Appeal in *True Tone Ltd v Festival Records Retail Marketing Ltd* [1988] 2 NZLR 352, Richardson J. at 358 found that this policy of promoting and preserving competition which underpins the Act is "based on the premise that society's resources are best allocated in a competitive market where rivalry between firms ensures maximum efficiency in the use of resources."

relevant market”¹⁴. For this reason the process by which the relevant market is to be delineated will obviously have a considerable impact upon antitrust proceedings. In 1976 the Trade Practices Act Review Committee (Swanson Committee) observed:¹⁵

“... market definition is always of considerable importance. If the market is too widely defined it may be that the requisite effect upon competition cannot ever be shown, to the detriment of those seeking relief from a restrictive agreement or practice. Alternatively, if the market is too narrowly defined it may result in hardship to and unnecessary limitations upon business actions, such as inhibitions upon exploiting novelty”.

Therefore, delineation of the relevant market is not to be viewed as an end in itself. Its significance lies rather in the fact that it specifies the relevant universe within which a complete antitrust analysis should be focused.¹⁶ Thus, the market delineation process provides the first in a set of stepping-stones which enable the courts to discharge this task of assessing the degree of market power possessed by the impugned party in the principled and certain manner required by the doctrine of the rule of law. The procedures within it enable the court (or other trier of fact) to organise complex fact situations and classify them in such a way as to enable competition policy (as embodied in the Commerce Act and the Trade Practices Act) to be intelligently applied.

It follows from this line of reasoning that, where a provision within the Commerce Act or the Trade Practices Act requires the impugned conduct of a party to be assessed in the context of a market, it would be logically appropriate to define the boundaries of the relevant market from the outset. A similar line of thought was expressed by Mr Justice Richardson in the New Zealand Court of Appeal’s decision in *Tru Tone Ltd v Festival Records Retail Market Ltd* (hereinafter referred to as *Tru Tone*), where his Honour observed that:¹⁷

14 R. J. Ahdar (ed), *Competition Law and Policy in New Zealand* (Law Book Co., Sydney, 1991) 155-160.

15 Trade Practices Act Review Committee, “Report to the Minister for Business and Consumer Affairs” (Canberra, 1976), 4.19. See also, N. R. Norman and P. Cornwell, “Market Competition and Dominance: A Note on Economic Concepts Imported from Economic Analysis”, in CCH Trade Practices Editors, *Australian Trade Practices Reporter* (CCH (Australia) Ltd, Sydney, 1990) ¶2-500.

16 F.M. Fisher, “Diagnosing Monopoly,” 19 Q. Rev. Econ. & Bus. 7 (1979).

17 [1988] 2 NZLR 352, 358. See also, *Telecom Corporation of New Zealand Ltd v Commerce Commission* (1991) 3 NZBLC ¶99-239, 102,364: “Market definition is but a first step, albeit an important step, in the analysis of dominance detriment and public benefit.”

"... the identification of the relevant market is the first step towards the assessment of the current state of competition and of the nature and extent of any inhibition of competition."

DEFINITION OF "MARKET"

The substantive provisions of the Commerce Act 1986 closely follow those of Part IV of the Australian Trade Practices Act 1974 (Cth), allowing for variations in form and procedure attributable to constitutional differences between these two nations. This is part of the policy connected with the ANZCERTA treaty¹⁸ to harmonise New Zealand and Australian commercial legislation. The achievement of harmonisation has also been assisted by the attitude of the New Zealand judiciary in their interpretation of the Commerce Act 1986. The leading cases have shown an acceptance of the idea that the form and substance of the Commerce Act requires them to have regard to Australian authorities where relevant.¹⁹ In the *New Zealand Apple and Pear Marketing Board v Apple Fields* decision the President of the New Zealand Court of Appeal observed:²⁰

"... Australasian uniformity and reciprocity in commercial law are goals to be pursued by the courts as well as the legislature."

Therefore, in view of this it is submitted that an examination of the Australian approach to the definition of "market" in section 45 of the Trade Practices Act will be of great assistance in shedding light upon the corresponding New Zealand provision.

¹⁸ The Australian-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) came into effect on 1 January 1983. The ANZCERTA treaty was subsequently revised between November 1987 and August 1988. As a result of this review, New Zealand and Australia entered into the "Memorandum of Understanding Between the Government of New Zealand and the Government of Australia on Harmonisation of Business Law". This Memorandum provided that New Zealand and Australia should develop a program for moving towards further harmonisation of a range of business laws by 30 June 1992. See, T. Dallow and J. P. B. "Competition Law and Trade-Related Trade", in R. Abde (ed), *Competition Law and Policy in New Zealand*, above n 14, 24-31.

¹⁹ See, for example, *Archibald Regional Authority v Mutual Bond Corp (Archibald Report) Ltd* (1988) 2 NZBLC 103,041, 103,082.

²⁰ (1989) 2 NZBLC 103,741, Cases 7, 103,757. See also, the foreword of R. E. Alder (ed), *Competition Law and Policy in New Zealand*, above n 14, where the Right Honourable Sir Ivor Richardson comments as follows: "One theme running through many of the chapters is that the courts and tribunals of the two countries should be prepared in far as possible to recognise the progress that has been made towards a common market, the goal of increasing harmonisation of commercial regimes reflected in ANZCERTA and a shared interpretation of certain statutory areas. That willingness to understand and apply - but not slavishly - the words of Federal or national material has been a positive feature of the approach taken by the Commission and the courts in competition areas in recent years."

PART II

2. THE STATUTORY DEFINITION OF "MARKET"

The substantive provisions of the Commerce Act 1986 closely follow those of Part IV of the Australian Trade Practices Act 1974 (Cth), allowing for variations in form and procedure attributable to constitutional differences between these two nations. This is part of the policy connected with the ANZCERTA treaty¹⁸ to harmonise New Zealand and Australian commercial legislation. The achievement of harmonisation has also been assisted by the attitude of the New Zealand judiciary in their interpretation of the Commerce Act 1986. The leading cases have shown an acceptance of the idea that the form and substance of the Commerce Act requires them to have regard to Australian authorities where relevant.¹⁹ In the *New Zealand Apple and Pear Marketing Board v Apple Fields* decision the President of the New Zealand Court of Appeal observed:²⁰

"... Australasian uniformity and reciprocity in commercial law are goals to be pursued by the courts as well as the legislature."

Therefore, in view of this it is submitted that an examination of the Australian approach to the definition of "market" in section 4E of the Trade Practices Act will be of great assistance in shedding light upon the corresponding New Zealand provision.

18 The Australian-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) came into force on 1 January 1983. The ANZCERTA treaty was subsequently reviewed between November 1987 and August 1988. As a result of this review, New Zealand and Australia entered into the "Memorandum of Understanding Between the Government of New Zealand and the Government of Australia on Harmonisation of Business Law". This Memorandum provided that New Zealand and Australia should develop a program for moving towards further harmonisation of a range of business laws by 30 June 1990. See, T. Dellow and J. Feil, "Competition Law and Trans-Tasman Trade"; in R. Ahdar (ed), *Competition Law and Policy in New Zealand*, above n.14, 24-30.

19 See, for example, *Auckland Regional Authority v Mutual Rental Cars (Auckland Airport) Ltd* (1988) 2 NZBLC 103,041, 103,062.

20 (1989) 2 NZBLC 103,741, Cooke P., 103,747. See also, the foreword to R. J. Ahdar (ed), *Competition Law and Policy in New Zealand*, above n. 14, where the Right Honourable Sir Ivor Richardson comments at v: "One theme running through many of the chapters is that the courts and tribunals of the two countries should be prepared as far as possible to recognise the progress that has been made towards a common market, the goal of increasing harmonisation of commercial statutes reflected in ANZCERTA and a shared interpretation of common statutory areas. That willingness to understand and apply - but not slavishly - the wealth of Australian material has been a positive feature of the approach taken by the Commission and the courts in competition areas in recent years".

(1) The Australian Definition of "Market"

Section 4E²¹ of the Trade Practices Act provides:

"For the purpose of this Act, "market" means a market in Australia and, when used in relation to any goods or services, includes a market for those goods or services and other goods or services that are substitutable for, or otherwise competitive with; the first mentioned goods or services."

This statutory definition embodies the concept of a market which was enunciated by the Australian Trade Practices Tribunal in *Re Queensland Co-operative Milling Association Ltd and Defiance Holdings Ltd* (hereinafter referred to as *QCMA*)²²:

"We take the concept of market to be a basically simple idea. A market is the area of close competition between firms or, putting it a little differently, the field of rivalry between them ... Within the bounds of a market there is substitution - substitution between one product and another, in response to changing prices. So a market is the field of actual and potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given a sufficient price incentive ... Whether such substitution is feasible or likely depends ultimately on customer attitudes, technology, distance, and cost and price incentives.

It is the possibilities of such substitution which sets the limits upon a firm's ability 'to give less and charge more'. Accordingly, in determining the outer boundaries of the market we ask a quite simple but fundamental question: If the firm were to 'give less and charge more' would there be, to put the matter colloquially, much of a reaction?"

In the subsequent decision of *Re Tooth & Co Ltd: Re Tooheys Ltd*, the Trade Practices Tribunal had occasion to explain in greater detail the principles which had been enunciated in the *QCMA* case:²³

21 Section 4E was inserted by the Trade Practices Amendment Act 1977.

22 (1976) ATPR ¶40-012, 17,247.

23 (1979) ATPR ¶40-013, 18,196.

“[C]ompetition may proceed not just through the substitution of one product for another in use (substitution in demand) but also through the substitution of one source of supply for another in production or distribution (substitution in supply). The market should comprehend the maximum range of business activities and the widest geographic area within which, if given a sufficient economic incentive, buyers can switch to a substantial extent from one source of supply to another and sellers can switch to a substantial extent from one production plan to another. In an economist’s language, both cross-elasticity of demand and cross-elasticity of supply are relevant.”

It has been made plainly obvious by the numerous Australian authorities²⁴ which have adopted the *QCMA* approach in interpreting the subsequently enacted definition of “market” in section 4E, that the requirement of substitutability is to be treated as a central consideration in any delineation of a relevant market.

(2) The Original Definition of “Market” in New Zealand

Although the term “market” was originally defined in section 3(1) of the Commerce Act 1986 (prior to 1 July 1990), New Zealand courts²⁵ quickly adopted as the source of that statutory definition the following passage from the former Commerce Commission’s decision in *Edmonds Food Industries Ltd/W. F. Tucker & Co. Ltd* (under the since repealed Commerce Act 1975)²⁶:

“A market has been defined as a field of actual or potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run if given a sufficient price incentive. In delineating the particular market in any particular case there is a value judgement which must be made which involves, for example, an assessment of pertinent

²⁴ See in particular, *Re Tooth & Co. Ltd*; *Re Tooheys Ltd* (1989) ¶40-113, 18,196; *TPC v Nicholas Enterprises Pty Ltd* (1979) ATPR ¶40-126, 18,356; *Outboard Marine Australia Pty Ltd v Hecar Investments (No 6) Pty Ltd* (1982) ATPR ¶40-327, 43,983; *TPC v TNT Management Pty Ltd* (1985) ATPR ¶40-512, 46,142-46,144; *Mark Lyons Pty Ltd v Bursill Sportsgear Pty Ltd* (1987) ATPR ¶40-809, 48,797-48,798; *TPC v Australia Meat Holdings Pty Ltd* (1989) ATPR ¶40-932, 51,783. The *QCMA* approach was also approved (either expressly or impliedly) by Mason C.J., Wilson, Dawson and Toohey J.J., in the High Court of Australia’s decision in *Queensland Wire Industries Pty Ltd v The Broken Hill Pty Co. Ltd* (1989) ATPR ¶40-925, (Mason C.J. and Wilson J.) 50,008; (Dawson J.) 50,015; and (Toohey J.) 50,021.

²⁵ See, *Auckland Regional Authority v Mutual Rental Cars (Auckland Airport) Ltd* [1987] 2 NZLR 647, 669; *True Tone Ltd v Festival Records Retail Marketing Ltd* [1988] 2 NZLR 352, 358-359.

²⁶ Commerce Commission Decision No.84 (21 June 1984), para. 7.

market realities such as technology, distance, cost and price incentives; an assessment of the degree of substitutability of products; an appreciation of the fact that a market is dynamic and that potential competition is relevant; and an evaluation of industry viewpoints and public tastes and attitudes. Particularly important in this process is industry recognition (both by supplier and purchaser) and recognition by the consumer. Ultimately the judgement as to the appropriate market and its delineation by function, product and area - *is a question of fact which must be made on the basis of commercial common sense in the circumstances of each case.*" (Emphasis added)

The pragmatic nature of the *Edmonds/Tucker* definition appears to have impressed those responsible for drafting the Commerce Act 1986 for they incorporated the "fact" and "commercial common sense" components into the statutory definition of market contained in s.3(1) of the 1986 Act as originally enacted. That provision read:

"'Market', means a market for goods and services within New Zealand that may be distinguished as a matter of fact and commercial common sense."

The reference to "fact and commercial common sense" within this definition associated with the lack of any requirement of substitutability has led to some rather confusing judicial pronouncements regarding this provision. Initially it appeared that the requirements of "commercial common sense" within section 3(1) and the notion of substitutability included within the Australian provision²⁷ would be compatible concepts. In the New Zealand High Court decision of *Auckland Regional Authority v Mutual Rental Cars (Auckland Airport) Ltd* (hereinafter referred to as *ARA*) Mr Justice Barker commented:²⁸

"Counsel submitted that the reference to 'fact and commercial common sense' in the New Zealand definition meant that, in New Zealand, the Court should give more weight to the views of businessmen in the market place when defining the relevant boundaries of the market. In my view that submission is simplistic; the reference in the Act to commercial common sense (as distinct from any other kind of common sense) as the yardstick by which to determine a market is another and more straight forward way of articulating the Australian definition.

27 Trade Practices Act 1974, s.4E.

28 [1987] 2 NZLR 647, 669.

The matters in the Australian definition must enter the Court's assessment of 'fact and commercial common sense'. The assessment must be made from a consideration of the composition of and forces in the market. The perceptions of the participants can only be part of the necessary information available.

I should have been sorry to have reached an opposite conclusion and to have held the Australian definition inappropriate."

A somewhat different approach is evident in the New Zealand Court of Appeal's judgement in *Tru Tone*. In delivering the judgement of the Court, Richardson J. commented:²⁹

"In focusing in the definition in s.3(1) on distinguishability as a matter of fact and commercial common sense the legislation has carefully avoided giving prominence to any particular criterion. In particular, the test is not substitutability as such, although that will ordinarily be an important consideration."

However, in two subsequent decisions of the New Zealand High Court the differences between the Australian and New Zealand statutory formulation were accorded greater emphasis. In *New Zealand Apple and Pear Marketing Board v Apple Fields*, Holland J. (after citing Richardson J.'s comments in *Tru Tone*) observed:³⁰

"The definition of 'market' is not the same as that in the Trade Practices Act in Australia and this renders some of the observations in Australian cases to be of little assistance."

While Tipping J. in the *New Zealand Magic Millions Ltd v Wrightson Bloodstock Ltd* decision also noted the differences between the two definitions and cautioned against giving too much weight to substitutability:³¹

"While I acknowledge that questions of substitutability are certainly relevant in delineating a market in New Zealand, they are by no means the be all and

29 [1988] 2 NZLR 352, 359.

30 (1989) 2 NZBLC ¶99-154, 103, 577.

31 [1990] 1 NZLR 731, 746.

end all of the exercise and care must be taken not to give too much weight to that or any other aspect. It is a matter of weighing all the relevant considerations and then, against our statutory definition, distinguishing the relevant market as a matter of fact and commercial common sense. Matters pertaining to economics and economic theory are relevant but must be kept in perspective in the light of the direction to the Courts inherent in the definition."

Thus, section 3(1) of the Commerce Act could be seen as providing a somewhat unsatisfactory definition of "market" as it created a degree of uncertainty as to whether this formulation was intended to displace the economic approach contained within s.4E of the Trade Practices Act. This state of affairs was a hindrance to the move towards harmonisation of New Zealand and Australian business law.

(3) The Current Definition of "Market" in New Zealand

In 1988 and 1989 the New Zealand government conducted a review of the Commerce Act 1986³² to examine the substantive differences between the Australian and New Zealand legislation. As a result of this review it was decided that the definition of market contained in s.3(1) should be amended to incorporate the concept of "substitutability" and thus more closely resemble the Australian formulation.³³ The new definition of "market" was introduced by section 3(1A) of the Commerce Amendment Act 1990, which reads:

"Every reference in this Act ... to the term 'market' is a reference to a market in New Zealand for goods or services as well as other goods or services that, as a matter of fact and commercial common sense, are substitutable for them."

³² Department of Trade and Industry, "Review of the Commerce Act 1986: A Discussion Paper" (Wellington, 1988). See also, Ministry of Commerce, "Review of the Commerce Act 1986: Reports and Decisions" (Wellington, 1989).

³³ See, Ministry of Commerce, "Review of the Commerce Act 1986: Reports and Decisions," above n.32, where it was observed at para 3.2: "In a number of cases under the Commerce Act substantial references to the leading Australian cases concerned with market definition have been included. However, in a more recent judgement the judge noted the differences between New Zealand and Australia and commented that this rendered the Australian observations 'of little value.' We are concerned that following this case the means of defining a market under the Commerce Act and the Trade Practices Act might diverge. For this reason we propose that a new definition more closely resembling that in the Trade Practices Act be adopted."

The first occasion³⁴ on which the New Zealand High Court has discussed the implications of this amendment, was in the decision of *Telecom Corporation of New Zealand Ltd v Commerce Commission* (hereinafter referred to as *Telecom*)³⁵. The High Court, (comprising of Greig, J., Mr W. G. Shaw and Professor M. Brunt) found that s.3(1A) did not give rise to any new change in focus for the process of market definition under the Commerce Act. On this point, the Court commented:³⁶

“The practical effect of the revised wording appears to be no more than to make the relevance of economic substitutability explicit. It thus resolves some doubts that had previously been expressed, and confirms the relevance of the main line of New Zealand decisions (such as *Auckland Regional Authority* and *Tru Tone* at first instance and on appeal) and of Australian authorities (such as *QCMA*, *Tooth and Tooheys*, *Queensland Wire*). The retention of the reference to “commercial common sense”, a term that first appeared in *Edmonds Food Industries Ltd/W.F. Tucker & Co. Ltd* ... affirms the traditional New Zealand emphasis upon the need for a commercially realistic factual base. We see no source of conflict or tension in the juxtaposition of the two elements, substitutability and commercial common sense, in this formulation. Compare Barker, J. in *Auckland Regional Authority* at NZBLC p. 103, 061; NZLR 669-670.”

The Court then noted that in both the Australian and New Zealand jurisdictions it has been said, in effect, that a mechanical reliance upon substitution criteria in a contextual vacuum is not sufficient. In endorsing the view that “market” is an instrumental concept, the Court observed:³⁷

“Hence the boundaries should be drawn by reference to the conduct at issue, the terms of the relevant section or sections, and the policy of the statute. Some judgement is required, bearing in mind that ‘market’ is an instrumental concept designed to clarify the sources and potential effects of market power that may be possessed by an enterprise. In the words of

34 As on earlier occasions the New Zealand High Court had not discussed this matter fully. See, *McDonald Motors Ltd v Christchurch International Airport Ltd*, Unreported, 6 December 1991, High Court, Christchurch Registry, CP 413/91, 12; *Hoyts Corporation Holdings Operations (NZ) Ltd v Commerce Commission*, Unreported, 17 December 1991, High Court, Auckland Registry, CL 44/91, 11.

35 (1991) 3 NZBLC ¶99-239.

36 (1991) 3 NZBLC ¶99-239, 102,360.

37 (1991) 3 NZBLC ¶99-239, 102,360.

Mason C.J. and Wilson J. in *Queensland Wire* at ATPR p.50,008; CLR p.187: 'Defining the market and evaluating the degree of power in that market are part of the same process'..."

Therefore, it appears that the Australian and New Zealand definitions of "market" are compatible formulations although differing in emphasis due to the retention of the "fact and commercial common sense" element within the amended New Zealand provision. The decision of the New Zealand legislature to retain this element of the statutory definition may perhaps be an implied recognition of the notion that, important as they are, the concepts of substitutability of supply and demand will not provide a complete solution to the task of defining the relevant market. It is impossible to state the precise level of cross-elasticity of supply and cross-elasticity of demand required to include a product or service in a particular market or exclude it.³⁸ The adjudicator is thereby given a certain degree of flexibility in determining the boundaries of the market. It seems, therefore, quite possible that the New Zealand Legislature in enacting s.3(1A) may have intended that any such flexibility provided by the notion of "substitutability" should be tempered against the requirement of "commercial common sense". Thus, it is submitted that the boundaries of the relevant market should reflect the commercial realities of the particular industry in question as well as the theoretical substitution possibilities.³⁹ It may be safely assumed that those parties involved in any particular case would wish the matters in dispute to be judged on the particular facts as they present them, rather than theoretical rules of economics that are designed to achieve, what has been suggested is an illusory certainty.⁴⁰

38 See, *Queensland Wire Industries Pty Ltd v Broken Hill Proprietary Co. Ltd* (1989) ATPR ¶40-925, Dawson J., 50,015: "Important as they are, elasticities and the notion of substitution provide no complete solution to the definition of a market. A question of degree is involved - at what point do different goods become closely enough linked in supply or demand to be included in the one market - which precludes any dogmatic answer. See, *Times-Picayune v United States* 345 US 594 (1953) at p. 612, n. 31. The process is an inexact one as may be illustrated by reference to the concept of a sub-market which has been employed from time to time."

39 See, e.g., *True Tone Ltd. v Festival Records Retail Marketing Ltd.* [1988] 2 NZLR 352, 360; where the New Zealand High Court rejected the plaintiffs submission that each album on the charts constituted a separate and unique market, on the grounds that "as a matter of fact and commercial common sense" no distributor or retailer could run a business on the basis that the market is confined to just one unique album.

40 See, Trade Practices Act Review Committee, "Report to the Minister for Business and Consumer Affairs", above n.15, 4.21.

PART III

3. DIMENSIONS OF THE "MARKET"

As an aid for the determination of the relevant market, the courts and tribunals in Australia and New Zealand have traditionally adopted the approach of considering three different dimensions of the market concept separately - the product dimension, the functional level and the geographic dimension.⁴¹ However, if a thorough analysis of the relevant market is to be achieved then the appropriate time period for assessing the degree of substitutability must also be considered. For as Professor Maureen Brunt explains:⁴²

"A market has product, space, function and time dimensions. Between what set of *products* can customers and suppliers switch? Within what geographic *space*? Is the focus to be on the selling *function*, and how many levels or stages of production and distribution is it appropriate to distinguish in order to assess the scope for substitution through trade? Finally, how much *time* is needed for customers and suppliers to make their adjustments in response to economic incentives?"

These four dimensions to the market construct which have been identified by Professor Brunt merit individual analysis within this paper.

(1) THE PRODUCT MARKET

The first specific set of questions the analyst must ask when delineating the relevant market relate to the range of different 'products' (i.e., goods or services⁴³) which should properly be included within the same market as the product in issue. Like their overseas counterparts, courts and tribunals in Australia have recognised substitutability as a central criterion for determining the width of the relevant market. As we have seen, the introduction of the revised definition of market in s. 3(1A) of the Commerce Amendment

41 Y. van Roy, *Guidebook to New Zealand Competition Laws* (2 ed., CCH (NZ) Ltd, Auckland, 1991) 61. See also, *True Tone Ltd v Festival Records Retail Marketing Ltd* [1988] 2 NZLR 352; *In re Tooth & Co. Ltd; In re Tooheys Ltd* (1979) ATPR ¶40-113.

42 Professor M. Brunt, "'Market Definition' Issues in Australian and New Zealand Trade Practices Litigation"; in R. J. Ahdar (ed), *Competition Law and Policy in New Zealand*, above n.14, 130.

43 Commerce Act 1986 s.3(1A): "Every reference in this Act ... to the 'market' is a reference to a market in New Zealand for *goods or services* ..." (Emphasis added)

Act 1990 has resolved any doubts as to the appropriateness of this approach in the New Zealand context.⁴⁴

The product market is probably the most important dimension, for the outcome of a case will often depend on how willing the particular court or tribunal is to accept a wider range of goods or services as credible substitutes for the product in question.⁴⁵ The wider the range accepted as substitutes, the larger the relevant market, and the less likely the persons responsible for the conduct at issue will be considered to "substantially lessen competition"⁴⁶ or be in a "dominant position".⁴⁷

(a) The Concept of Substitution

Although a detailed economic analysis is outside the scope of this paper, some understanding of the economic concept of 'substitution' is essential since it is expressly referred to in the statutory definition of market in s.3(1A) of the Commerce Act and s.4E of the Trade Practices Act. The notion of substitutability leads to a consideration of the economic principles of 'cross-elasticity of demand' and 'cross-elasticity of supply'. In the *ARA* decision *Barker, J.* observed:⁴⁸

"The *Tooth* case makes it clear that one must take the goods or services relevant to the enquiry and identify the area of close rivalry or competition, seeking the boundaries by examination of the ready availability or interchangeability of substitute services in response to economic incentives [in] demand or supply; in other words to use 'economists speak' one must identify cross-elasticity of demand and cross-elasticity of supply."

(i) "Demand Substitution" and "Cross-Elasticity of Demand"

An important consideration in determining the product market is the notion of 'demand substitution', that is the extent to which buyers can switch their demand from one product

44 Above n.33 and n.36.

45 See, Y. van Roy, above n.41, 61.

46 Commerce Act 1986 ss. 27, 28 and 30.

47 Commerce Act 1986 ss. 36 and 36A.

48 [1987] 2 NZLR 647, 670-671. See also, *Queensland Wire Industries Pty Ltd v Broken Hill Pty Co. Ltd* (1989) ATPR ¶40-925, Dawson, J., 50,014: "The substitution test involves the ascertainment of cross-elasticity of supply and cross-elasticity of demand, that is to say, the extent to which the supply or demand for a product responds to a change in the price of another product. Cross-elasticities of supply and demand reveal the degree to which one product may be substituted for another, an important consideration in any definition of market."

to another in order to satisfy their needs.⁴⁹ 'Cross-elasticity of demand is a concept which is used to evaluate the degree of demand substitutability between two products. This concept measures the extent to which the relative demand for two products is sensitive to changes in the price of each, relative to the other. In the New Zealand High Court's decision in the *Telecom* case this construct was phrased in terms of one fundamental question, which is referred to as "the price evaluation test":⁵⁰

When a particular product undergoes a notional small increase in price, will the potential purchasers of that product switch their demand to an alternative product?

Example; If the manufacturer of 'Surf' laundry powder increases the price of its product, would consumers switch their demand to 'Dynamo' laundry liquid?

If a rise in the price of one product is followed by an increase in the demand for another product (the price of which is held constant), there may be positive cross-elasticity of demand between the two products. If the degree of positive cross-elasticity is sufficiently high, the two products may be considered as competing in the same market. Conversely, a low degree of cross-elasticity of demand indicates that the products are independent of each other and are not to be included in the same market.

However, in many situations pricing levels will not be the sole determinant of 'demand substitution'. In considering whether products have a sufficiently high degree of substitutability other factors such as physical characteristics of the products and consumer preferences may also be relevant in determining whether potential purchasers of a product will switch their demand to an alternative product in response to a price increase.⁵¹

⁴⁹ See, *In re Tooth & Co Ltd; In re Tooheys Ltd* (1979) ATPR ¶40-113, 18,196.

⁵⁰ In *Telecom Corporation of New Zealand Ltd v Commerce Commission* (1991) 3 NZBLC ¶99-239, it was observed by Greig J., Mr W.G. Shaw and Professor M. Brunt at 102,362 that "[t]he mental test that prompts a summary evaluation of the evidence is to ask how buyers and sellers would likely react to a notional small percentage increase in price of the products of interest ... (the 'price evaluation test')."

⁵¹ See, S. G. Corones, *Competition Law and Policy in Australia* (Law Book Co., Sydney, 1990) 44. This is also supported by the New Zealand High Court's findings in *True Tone Ltd v Festival Records Retail Marketing Ltd* [1988] 2 NZLR 352, 360 that when a recorded album is performing well in the 'charts' a sizeable percentage of popular purchasers will want that particular album and will not be prepared to substitute it for another.

(ii) The Requisite Level of Positive "Cross-Elasticity of Demand"

The dictionary definition of the verb 'substitute' is to put one thing in the place of another.⁵² However, the inclusion of the phrase "as a matter of fact and commercial common sense" within s.3(1A) of the Commerce Act, and the words "or otherwise competitive with" in s.4E of the Trade Practices Act indicate that it was not the intention of the New Zealand or Australian legislature that the term 'substitutable' should require the alternative product to be virtually identical (e.g., two different brands of long grain rice) to the product in issue.

Nevertheless, a certain degree or level of positive 'cross-elasticity of demand' between the two products will be required before they can be said to be substitutable and included within the same market.⁵³ Otherwise, the resulting delineation of the relevant market may be so wide as to greatly understate the market power of a firm, because in one sense all products are substitutes for one another. For as Edward Chamberlin explains:⁵⁴

"... the only perfect monopoly conceivable would be one embracing the supply of everything, since all things are more or less imperfect substitutes for each other."

It is interesting to note that in Australia the Swanson Committee's Report of 1976 it was recommended at para. 4.22, "that the Act should require that, in the determination of a 'market' for particular purposes, regard shall be had to substitute products being products which have a reasonable interchangeability of use and which have a high cross-elasticity of demand, i.e. where a small decrease in the price of a particular product would cause a significant quantum of demand for a similar product to switch to the product in question."⁵⁵ However, it is apparent from the subsequent insertion of section 4E by the

⁵² *The Shorter Oxford English Dictionary* (3 ed., Oxford University Press, London, 1950) vol. II, 2064.

⁵³ A perfect substitute would have infinite cross-elasticity of demand (i.e. an increase in the price of one item would result in the other item substituting itself totally for the first). On the other hand, zero cross-elasticity of demand suggests that the items are independent of each other (i.e. the price of one has no bearing on the quantity sold of the other).

⁵⁴ E. H. Chamberlin, *The Theory of Monopolistic Competition: A Re-Oriented Theory of Value* (8 ed., Harvard University Press, Cambridge [Massachusetts], 1962) 65.

⁵⁵ Trade Practices Act Review Committee, above n.15, 4.22: "There is however, one aspect of the definition of 'market' about which we consider the Act should give useful legislative guidance; namely, in relation to product substitution. The Committee therefore recommends that the Act should require that, in the determination of a 'market' for particular purposes, regard shall be had to substitute products, being products which have a reasonable interchangeability of use and which have *high cross-elasticity of demand*, i.e., where a small decrease in the price of a particular product would cause a significant quantum of demand for a similar product to switch to the product in

Trade Practices Amendment Act 1977 that this suggestion was not accepted by the Australian Federal Parliament. The reason for this may lie in the notion that such a statutory requirement poses a danger as courts may become unduly channelled into this one line of enquiry, at the expense of other considerations which may be equally illuminating for market delineation purposes (e.g., cross-elasticity of supply).

It is submitted that under s.3(1A) of the Commerce Act and s.4E of the Trade Practices Act the degree of substitutability required before a competing product or service is included in the market under investigation is ultimately a matter for the courts to decide on the facts of each case. It is a matter concerning which the evidence of those operating in the market will be highly relevant. The court should be presented with expert testimony from marketing personnel on the question of demand substitutability, and then make its own subjective assessment as to the boundaries of the product market on the basis of this evidence. Economic theory is useful to explain how markets work but is less useful on market definition. It can not prescribe the exact degree or level of substitutability required to include a product in a market for the purposes of giving practical content to sections 3(1A) and 4E. It is not possible to state the precise level of cross-elasticity of demand or cross-elasticity of supply that is required to include a product in a particular market or to exclude it. This is a matter for the court's subjective assessment.

“Reasonable Interchangeability”

The classic case concerning demand side substitutability is *United States v. E. I. du Pont de Nemours & Co*⁵⁶ (commonly referred to by commentators as the *Cellophane* case) in which the United States Supreme Court adopted ‘cross-elasticity of demand’ and ‘reasonable interchangeability’ of use as product market definition tests. At issue in this case was the question of whether the relevant product market was cellophane (in which 75 percent of all sales in the United States were from the defendant's production (i.e. du Pont)) or flexible packaging materials (in which cellophane constituted less than 20 percent of the sales). To make this determination the Supreme Court looked to the existence of substitutability in demand between cellophane and other flexible packaging materials. The Court reasoned that a high level of cross-elasticity of demand would indicate that the products are to be included in the same product market.⁵⁷ In determining what was to be

question.” (Emphasis added) See also, *Queensland Wire Industries Ltd v. Broken Hill Pty Co. Ltd* (1989) ATPR ¶40-925, where Toohey J. mentions at p. 50,021 this recommendation by the Swanson Committee.

⁵⁶ 351 U.S. 377 (1956).

⁵⁷ 351 U.S. 377, 400 (1956): “If a slight decrease in the price of cellophane causes a considerable number of customers of other flexible wrappings to switch to cellophane, it would be an indication

considered as a high level of cross-elasticity of demand the Court formulated the following test:⁵⁸

“[a] market is composed of products that have *reasonable interchangeability* for the purposes for which they are produced - price, use and qualities considered.” (Emphasis added)

In applying this test to the facts of the case, the majority of the court found that a very considerable degree of functional interchangeability existed between cellophane and other flexible wrapping materials. On this point the majority emphasised that sales of cellophane (for several different uses) were price sensitive, i.e., in response to price and quality changes, many customers switched from cellophane to other flexible wrapping materials.⁵⁹ The Court therefore concluded that the product market in question was not the market for cellophane only but for all flexible wrapping materials.⁶⁰

However, Chief Justice Warren, writing for the minority, argued that the relevant product market in this case was cellophane. His Honour pointed to the different physical components of the products and, more importantly, to the higher price of cellophane. Warren C. J. noted cellophane’s “unique combination of qualities lacking among less expensive materials in varying degrees”⁶¹ and continued⁶²:

“If the conduct of buyers indicated that glassine, waxed and sulphite papers and aluminium foil were actually ‘the selfsame products’ as cellophane, the qualitative differences demonstrated by the comparison of physical properties ... would not be conclusive. But the record provides convincing proof that businessmen did not so regard these products ... We cannot believe that buyers, practical businessmen, would have brought cellophane in increasing amounts over a quarter of a century if close substitutes were available at from one-seventh to one half cellophane’s price. That they did so is testimony to cellophane’s distinctiveness.”

that a high cross-elasticity of demand exists between them; that the products compete in the same market.

58 351 U.S. 377, 404 (1956).

59 351 U.S. 377, 400 (1956).

60 351 U.S. 377, 400 (1956).

61 351 U.S. 377, 415 (1956).

62 351 U.S. 377, 416-417 (1956).

The Chief Justice also challenged the majority's conclusion that there was great price sensitivity to sales of cellophane, by criticising their failure to take account of the conduct of other suppliers. Warren C. J. noted at 417:⁶³

"Finding 587 states that Sylvania, the only other cellophane producer, absolutely and immediately followed every du Pont price change, even dating back its price list to the effective date of du Pont's change. Producers of glassine and waxed paper, on the other hand, displayed apparent indifference to du Pont's repeated and substantial price cuts ... [F]rom 1924 to 1932 du Pont dropped the price of plain cellophane 84%, while the price of glassine remained constant ... If 'shifts of business' due to 'price sensitivity' had been substantial, glassine and waxed paper producers would have been compelled by market forces to meet du Pont's price challenge just as Sylvania was."

Many other commentators⁶⁴ have subsequently agreed with the minority's view that cellophane should have been grouped into a separate product market from other flexible wrapping products, so that du Pont could be said to have wielded monopoly power in the cellophane product market. However, despite such criticism of the manner in which the majority applied this product market definition test ("reasonable interchangeability" based on 'cross-elasticity of demand') to the facts of the *Cellophane* case, it still remains the basic test for market delineation purposes in the United States⁶⁵ and the European Economic Community.⁶⁶

Legal commentators have subsequently pointed out that the majority of the Court made a logical error in applying the reasonable interchangeability test. This has become known as the "*Cellophane* trap." The following criticism of the majority's reasoning by Professors Posner and Easterbrook exposes the nature of this error:⁶⁷

⁶³ 351 U.S. 377, 417 (1956).

⁶⁴ See, e.g., R. Pitofsky, "New Definitions of Relevant Market and the Assault on Antitrust", 90 Colum. L. R. 1805, 1814 (1990); K.G. Elzinga, "Defining Geographic Market Boundaries", 26 Antitrust Bull. 739, 744 (1981); D.F. Turner, "Antitrust Policy and the Cellophane case", 70 Harv. L. Rev. 281, 308-310 (1956); G.C. Schaerr, "The *Cellophane* Fallacy and the Justice Department's Guidelines for Horizontal Mergers", 94 Yale L. J. 670, 676-677 (1985).

⁶⁵ See, *Brown Shoe Co v United States* 370 U.S. 294, 325 (1962); *Telex Corp. v IBM Corp.*, 510 F 2d 894, 917-918 (10th Cir. 1975).

⁶⁶ See, *L'Oreal v De Nieuwe AMCK* (1980) 8 ECR 3775, 3793.

⁶⁷ R.A. Posner and F.H. Easterbrook, *Antitrust: Cases, Economic Notes and Other Materials* (2 ed., West Publishing Co., St Paul [Minnesota] ,1981) 362.

"To include products that were good substitutes for cellophane *at the price at which cellophane was being sold by its sole producer* begged the question whether the producer had a monopoly. If he had a monopoly and was charging the monopoly price, that would make substitutes attractive which at a competitive price would be considered grossly inferior substitutes. In fact it seems almost certain that the cross-elasticity of demand between cellophane and other flexible packaging materials for many important uses would have been very low had cellophane been sold at a price substantially nearer its cost."

Thus, in order to avoid the "*Cellophane* trap," the court or tribunal should ideally examine substitution by reference to competitive prices rather than the prevailing price⁶⁸, although admittedly this may not always be administratively practical. Awareness of this trap, however, should alert the relevant adjudicators to an analytical snare they might otherwise overlook.

"Closely Substitutable"

Australian commentators⁶⁹ have argued that the term "substitutable" in section 4E of the Trade Practices Act must be taken to mean 'closely substitutable' in terms of both demand and supply. In practice the Trade Practices Tribunal has explicitly and consistently defined the product market in terms of "close substitutes," rather than using the "reasonable interchangeability" test from the *Cellophane* case.⁷⁰ The question of close substitutability as against reasonable interchangeability has yet to be argued before the Federal Court of Australia, however, the approach so far taken by the Federal Court would suggest that it has implicitly adopted the Tribunal's position.⁷¹ As a matter of speculation it may be suggested that the requirement of "reasonable interchangeability" is a wider test than that of "close substitutability," as on its face the word 'close' would appear to imply a higher level of cross-elasticity of demand than the word 'reasonable'.⁷²

68 J.H. Farrar and A. Borrowdale, *Butterworths Commercial Law in New Zealand* (2 ed., Butterworths, Wellington, 1992) 668.

69 S. G. Corones, above n.51, 54; G. deQ. Walker, above n. 12, 399-400.

70 *In re Tooth & Co Ltd*; *In re Tooheys Ltd* (1979) ATPR ¶40-013, 18,196; *Re Howard Smith Industries Pty Ltd* (1977) ATPR ¶ 40-023, 17,336; *Q.C.M.A.* (1976) ATPR ¶40-012, 17,247.

71 J.D. Heydon, *Trade Practices Law* (Law Book Co.(Australia) Ltd., Sydney, 1992) vol.I, 1603-1604.

72 Assuming of course that it would be correct to treat the words 'substitutability' and 'interchangeability' as being synonymous.

The New Zealand courts have followed this same approach, of delineating the relevant product market by focusing upon 'close substitutes' in terms of both demand and supply.⁷³ This is illustrated in the following obiter statement by Henry J. and R. G. Blunt Esq., regarding the supply of products that are substitutable for cinema viewing, in the recent New Zealand High Court decision of *Hoyts Corporation Holdings Ltd v Commerce Commission*⁷⁴:

"The error in interpreting the impact of such activities as indicating the parameters of the market arises from a failure to pay sufficient regard to the need for the substitute product, if it is to form part of the relevant market, to be one which in terms of commercial reality is used in place of the other rather than simply being an alternative. The term "close substitute" was used by the Commission and by both counsel in their submissions, and although that qualification is not expressed in the statutory formulation it would seem to capture its intent."

(iii) "Supply Substitution" and "Cross-Elasticity of Supply"

In setting the limits of the product market the emphasis has historically been placed upon 'demand side' considerations, but more recently the 'supply side' has come to be regarded as significant.⁷⁵ Courts and antitrust authorities in a number of jurisdictions are increasingly acknowledging the role of supply substitution in the market definition process. The notion of supply substitutability describes the ability of alternative suppliers to provide a substitutable product within the relevant market so as to limit the market power of the impugned firm.

In most cases an evaluation of the boundaries of the product market will focus primarily on firms that currently produce and sell a relevant substitute. However, in certain circumstances it may be necessary to include additional firms within that market due to the fact that the same production and distribution facilities can sometimes be used to produce and sell two or more different types of goods and services. "Production substitution" refers to the shift by a firm in the use of its machinery or facilities from producing and

⁷³ See, *Auckland Regional Authority v Mutual Rental Cars (Auckland Airport) Ltd* [1987] 2 NZLR 647, 669; *True Tone Ltd v Festival Records Marketing Ltd* [1988] 2 NZLR 352, 358-359; *Telecom Corporation of New Zealand Ltd v Commerce Commission* (1991) 3 NZBLC ¶99-239, 102,360-102,361.

⁷⁴ Above n. 34, 14.

⁷⁵ *Queensland Wire Industries Pty Ltd v Broken Hill Pty Co. Ltd* (1989) ATPR ¶40-925, Dawson J., 50,014.

selling one product to producing and selling another. Thus, a supplier of product (A), may be included in an examination of the relevant market for product (B) if that supplier can use its production facilities to make a product that is substitutable for product (B) (e.g., product (B2)). This may be so despite the fact that the consumer would not consider product (A) and product (B) to be substitutable. If therefore, suppliers of fencing wire can, with only minor adjustments to their machinery or facilities, turn out the light steel rod which is used in making concrete reinforcing mesh, then those suppliers of fencing wire may be considered as potential new entrants to the reinforcing mesh product market.⁷⁶ Thus, where for example, a 5 per cent rise in the price of a particular product would cause a number of potential competitors to switch to the production and supply of a substitutable product, then this high level of cross-elasticity of supply would indicate that one must take into account not only current competitors but also these potential competitors when determining the relevant market. The basic rationale behind this approach of considering potential competitors in the process of market delineation is explained by Professor F. M. Scherer⁷⁷:

“Groups of firms making completely non-substitutable products may nevertheless be meaningful competitors if they employ essentially similar skills and equipment and if they can quickly move into each other’s product lines should the profit lure beckon.”

The concept of ‘cross-elasticity of supply’ therefore measures the response of incumbent competitors and potential competitors to the conduct of an impugned firm which raises the price of its product.

Example; If the manufacturer of ‘Surf’ laundry powder increases the price of its product, would the manufacturers of ‘Dynamo’ laundry liquid respond by increasing their supply? Would the manufacturers of ‘Sunlight’ dishwashing detergent switch to the production of laundry power or liquid?

It is likely that the most significant source of cross-elasticity of supply will be from incumbent suppliers who desire a larger market share and possess the capacity to increase their level of supply within a short period of time. Whereas potential competitors are likely

⁷⁶ See, G. deQ Walker, above n. 12, 405.

⁷⁷ F.M. Scherer, *Industrial Market Structure and Economic Performance* (2 ed, Rand McNally College Publishing Co., Chicago, 1980) 60.

to provide a lower degree of cross-elasticity of supply because of the financial cost and time delays which are usually involved in switching-over production facilities.

The Australian Trade Practices Tribunal has consistently acknowledged the relevance of cross-elasticity of supply in the process of evaluating the relevant market. In *Re Howard Smith Industries Pty Ltd* the Tribunal observed:⁷⁸

“[A]n important consideration in identifying a market is the ease of substitution by suppliers as well as by buyers. In other words, can suppliers readily substitute one type or quality of product or service for another or can they vary the quantities supplied at different locations if there are differences in the prices which they obtain at those locations?”

The High Court of Australia confirmed the importance of both demand and supply substitutability in the *Queensland Wine Industries Pty Ltd v Broken Hill Pty Co Ltd* decision.⁷⁹ This is demonstrated within the judgement of Toohey, J., who after referring to s.4E and the test of interchangeability of products on the demand side (i.e., the *Cellophane* test⁸⁰), commented at p. 50,021:⁸¹

“[I]n delineating the scope of the product market demand substitutability has often been emphasised at the expense of supply substitutability. But this does not mean that supply substitutability is irrelevant to the task of market definition: see *Europemballage and Continental Can Co Inc v E. C. Commission* [1973] 12 CMLR 199. Rather, the definition of the relevant market requires a consideration of substitutability both on the demand and on the supply side.”

The relevance of supply side substitution under the statutory definition of market in s.3(1A) of the Commerce Act has recently been reaffirmed by the New Zealand High Court in the

78 (1977) ATPR ¶40-023, 17,336.

79 (1989) ATPR ¶40-925.

80 Above n. 57.

81 A similar observation was made by Dawson J. in the *Queensland Wire* case at (1989) ATPR ¶40-925, 50,014: “In setting the limits of a market the ... basic test involves the ascertainment of both supply and demand, that is to say, the extent to which the supply of or the demand for a particular product responds to change in the price of another product. Cross-elasticities of supply and demand reveal the degree to which one product may be substituted for another, an important consideration in any definition of a market.”

Telecom decision.⁸² Greig, J., Mr W. G. Shaw and Professor M. Brunt observed at p. 102,362 of the judgement:

“... competition may proceed both through substitution in demand and substitution in supply in response to changing prices or, more comprehensively, the changing price-product-service packages offered, as was first recognised in this Court by Barker, J., in *Auckland Regional Authority* ... The mental test that prompts a summary evaluation of the evidence is to ask how buyers and sellers would likely react to a notional small percentage increase in price of the products of interest, e.g. the standard telephone service, the cellular service (the ‘price evaluation test’).”

(iv) **“Supply Substitution” as Distinct from “New Entry”**

The notion of supply substitution by a potential competitor is closely related to the concept of ‘new entry’ by a firm wishing to compete in a particular market as both constructs involve a switch-over of production facilities so as to enable entry into the market. The main distinction between these two concepts would appear to lie in the firm’s relative ease of entry into a market in terms of time and adjustment of production facilities.⁸³ Professor Scherer addresses the problem as follows:⁸⁴

“How quickly must firms be able to shift over between products to be classified in the same industry? Given a long enough period and sufficient investment, shifts in production activity more accurately described as ‘new entry’ than as ‘substitution’ can take place. A distinction between substitutability in production and ease of entry (i.e., where barriers to entry are minimal) must be drawn. At the risk of being somewhat arbitrary we should probably draw the line to include as substitutes on the production side only existing capacity that can be shifted in the short run, i.e., without significant new investment in plant, equipment and worker training.”

This issue discussed by Scherer has also been commented upon by the New Zealand High Court in the *Telecom* decision.⁸⁵ On 17 October 1990, the Commerce Commission⁸⁶

82 (1991) 3 NZBLC ¶99-239.

83 See, F. M. Scherer, above n.77, 60-61.

84 F. M. Scherer, above n.77, 60-61.

85 (1991) 3 NZBLC ¶99-239.

86 Decision No. 254 of the Commerce Commission, 17 October 1990.

declined to give a clearance or grant an authorisation for, Telecom's acquisition of the management rights for the radio frequency spectrum AMPS-A.⁸⁷ The Commission found that Telecom's ownership and control of the Public Switched Telephone Network (PSTN) gave it a dominant position in both the voice telephony (*fixed*) market and the voice telephone (*mobile*) market. It was considered that the acquisition of AMPS-A by Telecom would strengthen its position in the mobile market. On appeal to the New Zealand High Court, counsel for Telecom submitted, inter alia, that the Commission failed to take a long-run approach, leading it to focus only on mobile telephone technology actually operating in the New Zealand commercial market at the time of the decision rather than including the numerous alternative technologies which were either currently available or are on a development path. Counsel submitted that if the purpose of the exercise was to assess the market power of an incumbent, one should extend the market boundaries on the supply side to include both substitution in production and entirely new entry in order that all relevant constraints be considered. The High Court, however, rejected the validity of this approach on the basis that:⁸⁸

“[I]n accordance with standard procedure in litigation of this type, the time-frame for market definition is not identical with the time-frame for assessing market constraints when account is taken of the potential for new entry. The phrase in common use ‘to enter a market’ contemplates that market boundaries are placed about buyers and sellers already in existence. We include within the market those sources of supply that come about from deploying existing production and distribution capacity but stop short of including supplies arising from entirely new entry. Thus ‘the long run’ in market definition does not refer to any particular length of calendar time but to the operational time required for organising and implementing a redeployment of existing capacity in response to profit incentives.”

However, the High Court did accept that the Commerce Commission in its general orientation and its approach to market definition adopted too short a time perspective.⁸⁹ Hence while endorsing the Commission's treatment of the mobile telephone service as a product market distinct from the fixed telephone service, (the high price of the cellular service was decisive in making this distinction)⁹⁰, the Court was critical of the Commission

87 AMP is an abbreviation of the phrase ‘Advanced Mobile Phone System.’

88 (1991) 3 NZBLC ¶99-239, 102,363.

89 (1991) 3 NZBLC ¶99-239, 102,363.

90 (1991) 3 NZBLC ¶99-239, 102,364.

for not explicitly canvassing new technology in the form of wireless-based products and services for inclusion in the relevant markets.⁹¹

The geographic dimension of the market relates to the examination and delineation of a particular geographic area within which suppliers of a product operate and in which purchasers of such goods or services are willing to "shop around" to find the best deal.⁹² As with the determination of the relevant product market, elasticities of demand and supply are important in determining the scope of the relevant geographic market.⁹³ In the *Tooth* decision the Australian Trade Practices Tribunal observed:⁹⁴

"The market should comprehend the maximum range of business activities and the widest geographic area within which, if given sufficient economic incentives, buyers can switch to a substantial extent from one source of supply to another and sellers can switch to a substantial extent from one production plant to another."

Professors Areeda and Turner in their widely-used treatise on antitrust law state that the dimensions of the geographic market turn on the "ability of firms to sell beyond their immediate locations."⁹⁵ However, this statement, while true as far as it goes, is potentially misleading for it tends to emphasize the supply side of the observed transactions at the expense of the demand side. Since the market is the arena for the interplay of primary supply and demand forces, emphasizing one side at the expense of the other can, and not infrequently does, lead to error. Thus, although the supply of rare books might be concentrated in Auckland and Wellington, the relevant market would not be confined to those two cities because the demand for this product is probably nation-wide. The buyers would be resident anywhere in New Zealand and their purchases would usually be forwarded to them. On the other hand, the fact that buyers from all over New Zealand may come to Wellington to buy a particular product is not enough to make the market a national one if the supply is local.

The Federal Court of Australia erred in this respect in the *Pacific U.F.F. Pty. Ltd. v Seven P.M. Pty. Ltd.* decision,⁹⁶ when considering a joint raise-opts issued by two Sydney PM radio stations for advertisers on those stations. "The relevant market", Lockhart J. stated,

⁹² *Y. van Roy, Guidelines on New Zealand Competition Law*, para 2.41, 63.

⁹³ See, for example, *Re New Zealand Airport Authority v British Airways Corp (the second Airport Lit)* (1987) 2 NZLR 667, 676.

⁹⁴ *Re Tooth & Colgate, Re Colgate Ltd* (1979) ATPR 380-381, 380-381.

⁹⁵ *Areeda & Turner, Antitrust Law* (1975) 139-140, 139.

⁹⁶ (1991) 3 NZBLC ¶99-239, 102,363.

(2) THE GEOGRAPHIC MARKET

The geographic dimension of the market relates to the examination and delineation of a particular geographic area within which suppliers of a product operate and in which purchasers of such goods or services are willing to "shop around" to find the best deal.⁹² As with the determination of the relevant product market, elasticities of demand and supply are important in determining the scope of the relevant geographic market.⁹³ In the *Tooth* decision the Australian Trade Practices Tribunal observed:⁹⁴

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The Federal Court of Australia erred in this respect in the *Radio 2 U E Pty. Ltd. v Stereo F.M. Pty. Ltd.* decision,⁹⁶ when considering a joint rate-card issued by two Sydney FM radio stations for advertisers on those stations. "The relevant market", Lockhart J. stated,

⁹² Y. van Roy, *Guidebook to New Zealand Competition Laws*, above n.41, 63.

⁹³ See, for example, *Auckland Regional Authority v Mutual Rental Cars (Auckland Airport) Ltd* (1987) 2 NZLR 647, 676.

⁹⁴ *Re Tooth & Co Ltd; Re Tooheys Ltd* (1979) ATPR ¶40-113, 18,196.

⁹⁵ P.E. Areeda & D.F. Turner, *Antitrust Law* (Little Brown & Co, Boston, 1978) vol. II, 355.

⁹⁶ (1982) ATPR ¶ 40-318.

“is not the radio listening audience, but the advertisers, including advertising agencies, for whose business radio stations compete. The market comprises advertisers throughout Australia.”⁹⁷ In reaching the conclusion that the market was national in scope, Lockhart J. gave weight to the fact that “[m]any of the advertised products are sold throughout Australia.”⁹⁸ Hence it is clear that Lockhart J. looked solely at the demand-side considerations to the exclusion of the characteristics of the supply-side, and may even have been misled into studying the market in which some of the advertisers, rather than the defendant radio stations, were trading. Unlike rare books, radio advertising time in various locations is not substitutable. An advertiser who wants to reach a Sydney audience will not regard air-time on a Perth radio station as an acceptable substitute.

The factors that will be relevant in defining a geographic market include: the location of buyers; the sales patterns of the relevant firms; the excess capacity of firms outside the immediate geographic area that are capable of shifting production; and market barriers that might limit the ability of firms to sell in particular areas (including transportation and distribution costs, customer convenience, physical location of resources⁹⁹, and customer preferences for the products of particular suppliers).¹⁰⁰ Thus, geographic market definition is not an abstract exercise, rather it is dependant upon the nature of the product and the competitive conditions facing the particular firm or group of firms in question.

The geographic element of the relevant market is concerned with the appropriate area within which the court or tribunal is to assess the level of market power possessed by the impugned firm. Economic theory would suggest that firms are to be grouped into the same geographic market if they are so located that they are able to exert a restraining influence on each other's exercise of market power. This concept is explained by Professor Hovenkamp as follows:¹⁰¹

97 (1982) ATPR ¶ 40-318, 43,916.

98 (1982) ATPR ¶ 40-318, 43,916.

99 The costs and nature of certain products may make it uneconomic to transport them very great distances. From the consumer's perspective a retail market is generally limited because consumers do not travel any great distance to differentiate retail products. The geographic market may well be determined by the physical location of resources. See, B.M. Hill and M.R. Jones, *Competitive Trading in New Zealand: The Commerce Act 1986* (Butterworths, Wellington, 1986) 14. In the Trade Practice Appeal Authority's decision of *Registered Hairdressers* [1961] NZLR 161, Dalglis J. noted at 172: "It is however, of little assistance to a prospective customer in Dunedin to know that he may have his haircut at a cheaper rate at Balclutha, or on the other side of Dunedin."

100 J. H. Farrar and A. Borrowdale, *Butterworths Commercial Law in New Zealand*, above n.68, 671.

101 H. Hovenkamp, *Economics and Federal Antitrust Law* (West Publishing Co., St Paul [Minnesota], 1985) 70.

"The relevant geographic market for antitrust purposes is some 'section of the country' in which a firm can increase its price without (1) large numbers of its customers immediately turning to alternative supply sources outside the area; or (2) producers outside the area quickly flooding the area with substitute products. If either of these things happen when the firm attempts to charge a supracompetitive price then the estimated geographic market has been drawn too narrowly and a larger market must be drawn to include these outside suppliers."

Therefore, in delineating the geographic market we are really seeking to identify an area which includes a sufficient number of sellers of the product for them to have, if they chose to act in collusion, enough monopoly power to raise prices to a significant degree, and hold them there in the short to medium term, without attracting a sufficient flow of supply from outside to restore prices to earlier levels.¹⁰²

(a) Imports and Market Definition

In line with the general lowering of tariff barriers¹⁰³ and the liberalisation of trade between New Zealand and Australia under the Closer Economic Relations Agreement (ANZCERTA), there has been a widespread trend for competition within the domestic markets of these two countries to be increasingly international in scope so that the range of existing and potential suppliers of goods and services to New Zealand and Australian consumers increasingly includes suppliers who do not produce or are not primarily headquartered within the nations they are supplying products too.¹⁰⁴ The issue of whether the geographic scope of the relevant market should transcend national boundaries in order to incorporate competition from suppliers located offshore may have considerable impact upon antitrust proceedings as existing or potential competition from foreign sources may obviously represent a significant restraint on the exercise of market power¹⁰⁵ by domestic firms within Australia and New Zealand.

¹⁰² This notion received recognition within the 1982 *Merger Guidelines* issued by the United States Department of Justice and Federal Trade Commission: Trade Reg. Rep.(CCH) No.546, 15 (1982).

¹⁰³ Tariffs may be viewed as particular market barriers which limit the ability of firms to sell in particular geographic areas. See, P.E.Areeda & D.F.Turner, *Antitrust Law*, above n.95, vol. II, 362-363.

¹⁰⁴ The evidence supporting this claim of internationalisation of the Australian and New Zealand domestic markets is, perhaps unavoidably, largely anecdotal.

¹⁰⁵ See, G. Hay, J.C. Hilke & P.B. Nelson, "Geographic Market Definition in an International Context," 64 *Chicago Kent L. Rev* 711, 717 (1988).

(i) **The Scope of the Geographic Market**

As s.3(1A) of the Commerce Act defines a "market" as being "a market in New Zealand for goods or services" the courts and the Commerce Commission are unable to extend the geographic scope of the relevant market beyond New Zealand (except in relation to s.36A).¹⁰⁶ A similar restriction exists under the Trade Practices Act as s.4E of that Act defines the term "market" as meaning "a market in Australia". Thus, while it is obvious that the wording of s.3(1A) will prevent those goods or services that are not actually supplied within New Zealand from being included within the relevant market, there has been some recent debate as to whether or not goods or services supplied outside New Zealand could be taken into account when determining the effect on competition in a relevant market within New Zealand. This confusion has arisen from the wording of s.3(3) of the Commerce Act which provides:

"For the purposes of this Act, the effect on competition in a market shall be determined by reference to all factors that affect competition in that market including competition from goods or services supplied or likely to be supplied by persons not resident or not carrying on business in New Zealand."

The New Zealand High Court had the opportunity to interpret the ambit of s.3(3) in the *New Zealand Magic Millions Ltd v Wrightson Bloodstock Ltd* decision.¹⁰⁷ In this case it

¹⁰⁶ See, below n.132.

¹⁰⁷ [1990] 1 NZLR 731. This case concerned the actions of Wrightson Bloodstock in causing its yearling thoroughbred auction near Auckland to coincide with that of Magic Millions, who had organised competing sales to take place at Trentham during the Wellington Spring Carnival. Wrightsons, who before the advent of Magic Millions had been the sole player in the market, had conducted sales for 60 years at Trentham on this weekend. It had, however, recently moved its sales location nearer to Auckland vacating the Trentham site. Before Magic Millions entered the market, Wrightsons had deferred to the wishes of the Wellington Racing Club and organised its sales around Auckland Anniversary Weekend so as not to conflict with the Wellington Spring Carnival. However, when Magic Millions emerged in 1989, Wrightsons (stating in evidence), saw a need to maintain a "competitive position," and thereby changed its sales dates back to clash with those of Magic Millions, making it impossible for buyers and sellers to attend both auctions. Wrightsons not only changed its sales date, but it allocated the sales dates between what became known as the K1 sale of premier yearlings, and K2 which covered less valuable horses, tying buyers in the K1 and K2 sub-markets together.

In 1989 negotiations between these two competitors resulted in Wrightsons changing its sale date so as not to coincide with the Wellington Spring Carnival. However for 1990 Wrightsons again set its dates to clash with the Magic Millions sale, insisting that the Commonwealth Games had made this necessary. Negotiations between the competitors failed, therefore Magic Millions brought an action against Wrightsons under section 36 of the Commerce Act 1986. In the New Zealand High Court Tipping J found Wrightsons was in breach of s.36. His Honour noted that Magic Millions sales date was inflexible due to the requirements of its sponsor, and therefore

was argued by Wrightsons in its submission that it was not dominant in the market for auction sales of thoroughbred horses, that the court should take into account competing or potentially competing auction sales for thoroughbred horses on the east coast of Australia. From the point of view of economic theory it may perhaps be correct that auction sales in Queensland, Sydney and possibly elsewhere in Australia should be included within the same geographic market as New Zealand auction sales¹⁰⁸ on the basis that these services are substitutable in terms of both supply and demand.¹⁰⁹ Doing so would of course greatly expand the range of suppliers who could be considered within the relevant market and thus greatly reduce the apparent market power of a domestic supplier. However, Tipping J. concluded that the statutory definition of market was not extended by s.3(3) to include services supplied outside of New Zealand. His Honour expressed the opinion that:¹¹⁰

“However desirable it may be economically to take that wider view I do not consider that the Act permits it. In my judgment s.3(3) should be construed as if it read:

‘... including competition from goods or services supplied or likely to be supplied [in New Zealand] by persons not resident or not carrying on business in New Zealand.’

It seems to me that it is necessary to make that implication so as to harmonise s.3(3) within the definition of market as being a market within New Zealand. In my judgment services supplied outside New Zealand by persons not resident or not carrying on business in New Zealand are irrelevant when defining the market within New Zealand or assessing dominance within it.”

Tipping J. supported this construction of s.3(3) by reference to the treatment of residence in section 4 of the Commerce Act, which states that the “Act extends to the engaging in conduct outside New Zealand by any person resident or carrying on business in New

granted an injunction until 31 January 1993 preventing Wrightsons from auctioning commercial thoroughbred yearlings at Karaka on dates to be used by Magic Millions at Trentham.

108 [1990] 1 NZLR 731, 759.

109 [1990] 1 NZLR 731, 758. See also, M. Brunt, “‘Market Definition’ Issues in Australian and New Zealand Trade Practices Litigation”, above n.42, 142.

110 [1990] 1 NZLR 731, 759.

Zealand to the extent that such conduct affects a market in New Zealand.”¹¹¹. Tipping J. then stated:¹¹²

“Put shortly, overseas conduct by New Zealand organisations is relevant to the extent that it affects the market in New Zealand. Overseas conduct by non New Zealand organisations should not be regarded as providing effective competition in a New Zealand market unless the goods or services are supplied within New Zealand.”

Such an interpretation of s.3(3) is subject to criticism on the basis that it undermines the economic concept of a market being delineated in terms of both actual competition and potential competition flowing from offshore sources, at a time when trans-Tasman economic interaction is assumed to be increasing. Such an argument is advanced by Hill who points out that:¹¹³

“[t]here is no economic reason for limiting the influence of situations and firms outside New Zealand because economically and commercially there are no national boundaries to competitive influences, if there is actual or potential trade between national jurisdictions.”

However, Tipping J. appears to have given consideration to such matters in his judgment as is demonstrated by his Honour’s reference to counsel’s acknowledgment that the consequence of such an interpretation “might be unfortunate from the economic point of view and from the point of view of competition law generally, but that is something for Parliament and not for me.”¹¹⁴

¹¹¹ [1990] 1 NZLR 731, 759. In, B.M. Hill, “A Review of Developments under Section 36 of the Commerce Act 1986”, A paper presented to the August 1990 Workshop of the Competition Law and Policy Institute of New Zealand (Inc.); Hill expresses the opinion at p.37 that: “Tipping J’s view that the words ‘a market within New Zealand’ impose a residency requirement on the goods or services traded in the market is wrong as a matter of law because the geographic parameters of markets are inherently incapable of being based only on statutory jurisdiction considerations. Residency within New Zealand and extra territorial statutory effect are relevant to the *enforcement* of the section 36 prohibition against persons and conduct offshore. But there is no converse legal or practical barrier against admitting the influence of offshore situations, in determining a New Zealand resident’s liability under New Zealand law.”

¹¹² [1990] 1 NZLR 731,759-760.

¹¹³ B.M. Hill, “A Review of Developments under Section 36 of the Commerce Act 1986”, above n.111, 36-37.

¹¹⁴ [1990] 1 NZLR 731, 759.

Professor Maureen Brunt also casts some doubt over the correctness of the interpretation accorded to s.3(3) in the *Magic Millions* case by expressing the view that:¹¹⁵

“It is not clear why his Honour chose to exclude the phrase ‘all factors that affect competition in that market’ that prefaces the quoted passage. What is clear is that particular difficulty was occasioned by the very notion of competition in services (as distinct from goods). The problem discerned was that services supplied outside New Zealand inherently lack the capacity to be transported to New Zealand.

But this is to introduce an unnecessary complication to the logic. While the service of conducting auction sales in Australia is performed wholly outside New Zealand, the auction house could be employed by both Australian and New Zealand breeders to sell their horses. The New Zealand breeders import the services of Australian auctioneers in precisely the same way as a New Zealand patient who desires specialised surgery from an Australian surgeon operating in an Australian hospital imports medical services to New Zealand. No distinction between imports of goods and imports of services is drawn on National Accounts. More to the point, in the present context, if enough imports are undertaken or there is sufficient fear of import competition (whether from auction houses or Australian surgeons), the very content of domestic transactions will be affected: the substitution relationships will be affected: competition in New Zealand will be different.”

While Professor Brunt’s analysis is sound from an economic perspective, it must be remembered that the statutory definition of market in 3(1A)¹¹⁶ of the Commerce Act is concerned with “markets in New Zealand” (except with respect to s.36A).¹¹⁷ Whereas s.3(3) enables the court or the Commission, when considering the effect on competition in

¹¹⁵ M. Brunt, “‘Market Definition’ Issues in Australian and New Zealand Trade Practices Litigation”, above n.42, 143-144.

¹¹⁶ The change of wording in the statutory definition of market, from “within New Zealand” under s.3(1) of the Commerce Act 1986 to “in New Zealand” under s.3(1A) of the Commerce Amendment Act 1990 may have perhaps been seen as necessary to rebut the connection drawn by Tipping J in the *Magic Millions* case between market definition and the assessment of competition. Alternatively, it may represent a decision to deprive those interpreting the section the opportunity to attribute special meaning to the word “within”. However, when the definitions are compared the difference in terminology is relatively insignificant, which is perhaps an indication that the alteration is a result of an arbitrary drafting preference.

¹¹⁷ See, above n. 33.

a market (in New Zealand, s.3(1A)), to take into consideration "all factors that affect competition in that [New Zealand] market including competition from ... persons not resident or not carrying on business in New Zealand." Thus it is clear that s.3(3) does not extend the definition of market in s.3(1A) to include the possibility of a single market for goods or services between New Zealand and Australia.

Hence, it is submitted that the most compelling analysis to this puzzle is provided by Yvonne van Roy in the text, *Guidebook to New Zealand Competition Laws* ¹¹⁸ at p. 65:

"If the provision of services in Australia is to be taken into account under the *Commerce Act* ... then these services would have to be considered as *imports* into the New Zealand market. The New Zealand courts have never had to consider whether *goods* purchased by New Zealanders in Australia are imports into the New Zealand market, for these transactions are clearly part of the Australian market, and involve quite different costs and decisions (to those with respect to the importation of goods into New Zealand). The question is whether *services* are different, and whether the importation of services into the New Zealand market should include not only those services which Australians provide in *New Zealand*, but also services provided by New Zealanders in *Australia*. This question is really one of policy rather than strict interpretation of sec.3(3). The view expressed by *Tipping, J.* is probably that which is most consistent with the policy and scope of the *Commerce Act*."

It is submitted that the enactment of s.36A within the Commerce Amendment Act 1990 lends further support to the interpretation of s.3(3) adopted by Tipping J, as while this subsequent provision extended the geographic scope of the market in which a dominant position was to be assessed, it is made clear by s.36A(1), (d), (e) and (f) that the geographic scope of the relevant market for assessing the impact or effect of this market dominance on competition is limited to "any market in New Zealand."¹¹⁹ This subsequent amendment thereby reflects the reasoning of Tipping J., in restricting the geographic scope of those substitutable goods and services which may be taken into account when determining the effect on competition in the relevant market under s.3(3), to those that are supplied or likely to be supplied within New Zealand. This would serve to reinforce the view of van Roy that the interpretation adopted by Tipping J is "that which is most

118 Above n.41.

119 See, below,n.132.

consistent with the policy and scope of the Commerce Act.”¹²⁰ However, there is obviously a wide divergence of opinion as to the correct interpretation of s.3(3), such diversity serves to highlight the difficulties encountered when incorporating economic concepts within a statutory formulation of antitrust policy.

It is interesting to note that a similar aberration in geographic market delineation appears within the Australian Trade Practices Tribunal’s decision in *Re Broken Hill Proprietary Co Ltd* (hereinafter referred to as *BHP-Koppers case*)¹²¹. In this case the Tribunal described the market for steelworks tar and the processed products made from it as being “quasi-international” and went on to add that “[w]e do not find it helpful to confine our attention too narrowly upon the domestic scene”¹²². Elsewhere the Tribunal referred to the relevant geographic market being partly national and partly international¹²³. This would appear to mean that certain other countries, or parts of other countries, were regarded as forming part of the geographic market. However, it will be recalled that section 4E of the Trade Practices Act defines a market as a “market in Australia.”¹²⁴ Now it is true that section 102(4) of the Trade Practices Act, which contains the test to be applied by the Tribunal in determining appeals from the Trade Practices Commission’s decisions, does not mention the word “market”, and it could therefore be argued that the Tribunal in the performance of its function was not bound by the statutory definition of market in s.4E. On the other hand, s.102(4) does require the Tribunal to consider whether any benefit to the public would outweigh the detriment to the public constituted by any “lessening of competition,” and obviously such an appeal could not be pursued without first delineating the relevant market in which competition may have been reduced. Hence there are arguments both ways. However, the Tribunal did not even address itself to the problem. Indeed, there is, inexplicably, no mention of s.4E anywhere in the judgement at all. The approach taken in *BHP-Koppers* would, therefore, appear to be at odds with the Australian statutory definition of market.

120 See, Y. van Roy, above n.116, 65.

121 (1981) ATPR ¶40-203. At issue in this case was a twenty years-plus exclusive dealing agreement under which Koppers was to buy all the steelworks coal tar produced by BHP and its subsidiary. BHP was the sole producer of steelworks tar, although gasworks tar could be used as a substitute for some purposes. Koppers used the tar to produce electrode-pitch, naphthalene, carbon black feedstock, creosote, enamel and road tars. International trade in steelworks tar was rare, and BHP, as the Australian monopolist benefitted from a high degree of natural protection together with a 13 per cent import duty. International trade in gasworks tar was apparently non-existent. However, the processed products made from both steelworks tar and gasworks tar were frequently traded internationally. The Tribunal in delineating the relevant product market lumped together in the same product market both steelworks tar and the processed products made from it despite the fact that they are not substitutable and are not produced on the same equipment.

122 (1981) ATPR ¶ 40-203, 42,828.

123 (1981) ATPR ¶ 40-203, 42,825.

124 See, above n.21.

(ii) The New Trans-Tasman Market Provisions

As part of the ANZCERTA treaty review conducted in 1988 the New Zealand and Australian governments agreed to remove the application of anti-dumping¹²⁵ laws to trans-Tasman trade in goods originating in either country and to rely instead on competition law.¹²⁶ The first step in implementing this agreement in New Zealand was to exclude legislation relating to dumping investigations and to remove the imposition of anti-dumping duties, in respect of goods originating in Australia.¹²⁷ With the elimination of New Zealand's anti-dumping laws in relation to Australia, reliance has now been placed on the application of the Commerce Act 1986 to safeguard trans-Tasman trade from conduct involving the exploitation of market power. However, it was never suggested that competition laws would be modified to replace anti-dumping provisions. Rather, it was intended that the application of domestic competition laws should be extended to have trans-Tasman application.

The principal provision which is relevant in this context is s.36 of the Commerce Act. Section 36 prohibits the use of a dominant position in a market for the purposes of restricting the entry of any person into a market, preventing or deterring any person from engaging in competitive conduct in a market, or eliminating any person from a market. This provision is intended to prevent the misuse of market power and with minor amendments to the Act it could be used to prevent such misuse in the context of a trans-Tasman market between New Zealand and Australia. If s.36 was to operate effectively in the trans-Tasman context it must necessarily apply to those parties which possess the relevant degree of market power within the Australian domestic market, in circumstances where those parties have exploited this market power for one of the proscribed purposes in respect of a market in New Zealand.

125 Under the General Agreement on Tariffs and Trade (GATT), dumping is referred to as the introduction of a product into the commerce of another country if the price of the product is lower than the price at which the same goods are sold in the ordinary course of business in the domestic market of the country from which they are exported. See, T. Dellow and J. Feil, "Competition Law and trans-Tasman trade," above n.18, 39.

126 Article 4 of the protocol to ANZCERTA provides that :
"The member states agree that anti-dumping measures in respect of goods originating in the territory of the other member state are not appropriate from the time of achievement of both free trade in goods between member states on July 1 1990 and the application of their competitive laws to relevant anticompetitive conduct affecting trans-Tasman trade in goods."

127 In New Zealand, the Dumping and Countervailing Duties Act 1988 was amended by the Dumping and Countervailing Duties Amendment Act 1990, passed on 29 June 1990. The Amendment Act came into force on 1 July 1990.

Hence, the Commerce Amendment Act 1990¹²⁸ introduced a new s.36A together with certain amendments to the statutory definition of market.¹²⁹ When these associated amendments are incorporated into s.36A it reads as follows:

- “(1) No person who has -
- (a) A dominant position in a market in *New Zealand*; or
 - (b) A dominant position in a market in *Australia*; or
 - (c) A dominant position in a market in *New Zealand and Australia* -
shall use that person’s dominant position for the purpose of-
 - (d) Restricting the entry of any person into any market in *New Zealand*, not being a market exclusively for services; or
 - (e) Preventing or deterring any person from engaging in competitive conduct in any market in *New Zealand* not being a market exclusively for services; or
 - (f) Eliminating any person from any market in *New Zealand* not being a market exclusively for services.” (Emphasis added)

This provision is mirrored by s.46A of the Australian Trade Practices Act headed “Misuse of Market Power - Corporation with Substantial Degree of Power in trans-Tasman Market” which also came into effect on 1 July 1990.¹³⁰ When the associated definitions of “impact market” and “trans-Tasman market” set out within s.46A(1)¹³¹ are incorporated into s.46A(2), it will read:

- “(2) A corporation that has a substantial degree of market power in a [market in *Australia*, *New Zealand* or *Australia and New Zealand*] must not take advantage of that power for the purpose of-
- (a) eliminating or substantially damaging a competitor of the corporation ... in any [market in *Australia* that is not a market exclusively for services]; or

128 The Commerce Amendment Act 1990, s.1(1) states that the Commerce Amendment Act 1990 shall be read together with and deemed part of the Commerce Act 1986.

129 See, Commerce Amendment Act 1990 ss.3(1A), 3(1B) and 3(1C).

130 Section 46A was incorporated into the Trade Practices 1974 by the Trade Practices (Misuse of trans-Tasman Market Power) Act 1990.

131 Trade Practices Act 1974, s.46A(1);

“‘impact market’ means a market in Australia that is not a market exclusively for services;”

“‘trans-Tasman market’ means a market in Australia, New Zealand or Australia and New Zealand for goods and services;”

- (b) preventing the entry of a person into [a market in *Australia* that is not a market exclusively for services]; or
- (c) deterring or preventing a person from engaging in competitive conduct in [a market in *Australia* that is not a market exclusively for services].” (Emphasis added)

Both the Australian and New Zealand amendments distinguish between the relevant market in which the level of market power¹³² held by the defendant is to be assessed (the “trans-Tasman market”¹³³), and the relevant market in which the defendant must be shown to have taken advantage of such market power for a proscribed purpose (the “impact market”¹³⁴). The geographic scope of the relevant (“trans-Tasman”) market in which the degree of market power is to be assessed may be:

- within New Zealand;
- within Australia;
- within both New Zealand and Australia.

Whereas the geographic scope of the relevant market for assessing the *impact* of this market power is restricted to:

- s.36A, “any market in New Zealand”.
- s.46A, “a market in Australia”.

Therefore, the legislative objective which underlies the drafting of these provisions, is obviously “to widen the geographic definition of market for the purpose of defining the location of dominance.”¹³⁵

(iii) The Chicago School Theory on the Relevance of Imports in Geographic Market Definition

It is important to recall that while there is no statutory definition of the term ‘market’ within United States antitrust legislation, the process of delineating the relevant market is

¹³² The threshold level of market power is described in s.36A(1) of the Commerce Act as being “...A dominant position in a market...”; Whereas, under s.46A(2) of the Trade Practices Act it is described as “...a substantial degree of market power...”.

¹³³ See, Trade Practices Act 1974, s.46A(1).

¹³⁴ See, Trade Practices Act 1974, s.46A(1).

¹³⁵ Ministry of Commerce, “Review of the Commerce Act 1986: Reports and Decisions,” above n.32, 4.

undertaken by the courts when applying such legislation in order to provide a medium within which market power can be assessed.¹³⁶ The question of whether or not foreign production should be counted in measuring the market power held by domestic firms operating within the United States is complicated and rather controversial, however, because frequently the issue revolves around foreign imports to the United States.

In recent years there has been much academic debate as to the extent to which potential imports from foreign sources should be taken into consideration when determining the effect upon competition within a relevant market located in the United States.¹³⁷ This debate was initially triggered by two proponents of "Chicago School Thinking"¹³⁸, Professor Landes and Judge Posner, in their influential article "Market Power in Antitrust".¹³⁹ Under the so-called "Landes-Posner Assessment of Foreign Competition"¹⁴⁰ it is claimed that the traditional approach to market definition in the United States results in an exaggeration of the domestic suppliers level of market power as insufficient consideration is accorded to foreign imports as a source of potential competition within the domestic market. Hence, they argue that, where a foreign seller has some sales in a local market, all of its sales, wherever made, should be considered as part of that relevant market for the purposes of computing the local sellers market share.¹⁴¹ Their argument in favour of including the total production of a foreign competitor within the relevant geographic market is based upon the "diversion approach", by which it is reasoned that "because the distant seller has proved its ability to sell in the market and could increase its sales there, should the local price rise, simply by diverting sales from other markets,"¹⁴² such sales by the foreign competitor in offshore markets should be treated as a substitutable source of supply within the local market. They reason that if foreign sellers can make some sales in the local market then domestic producers do not have the ability to exclude them entirely. Thus if the foreign firms are able to make some sales "they ought to be able to sell many units there at no appreciably higher costs, since they have only to divert output

136 See, above n.4.

137 For a useful summary of the current literature, see T. Calvini, "The Uncertainties of International Geographic Markets," 32 *World Competition Law & Econ. Rev.* 93 (1988).

138 The term "Chicago School Thinking" refers to the unmistakable influence of the Chicago School of Economics on antitrust policy in the United States. Its influence is a result of the Antitrust Division of the Department of Justice and the Federal Trade Commission having been dominated by appointees who subscribe to Chicago School views. This coincided in part with the Reagan governments of 1981 and 1985.

139 W. M. Landes and R. A. Posner, "Market Power in Antitrust Cases," 94 *Harv. L. Rev.* 937, 963 (1981).

140 See, G. Hay, J.C. Hilke & P.B. Nelson, "Geographic Market Definition in an International Context," above n.105, 724.

141 W. M. Landes and R. A. Posner, "Market Power in Antitrust Cases," above n.139, 963.

142 W. M. Landes and R. A. Posner, "Market Power in Antitrust Cases," above n.139, 963.

from other markets. It follows that if the domestic producer cannot keep foreign production out, then the distant seller represents a limitation on the domestic firms market power as they are unable to raise prices without being inundated by increased competition from exports".¹⁴³

In effect Landes and Posner would argue that if two domestic producers of motor vehicles in the United States, Chrysler and Ford, were to merge, all foreign sales of Toyota vehicles (even cars scheduled for sale in Japan) should be included in the local market (as Toyota has some sales in the United States) for the purpose of assessing the market power possessed by the merging companies in the United States domestic market.¹⁴⁴ The application of such an approach would clearly dilute the impugned market power of the domestic producers to a point where the relevant statutory competition test may not apply.

However, the Landes-Posner approach is not without its critics.¹⁴⁵ Professor Hawk, for example, points out that there are a number of limitations on the ability of foreign producers to shift sales into the local market.¹⁴⁶ His objections to including geographically remote production or output include the following:¹⁴⁷

- (a) The ability of foreign producers to direct sales into the local market in response to a local price rise may be limited by foreign demand. Greater exports may cause prices to rise in foreign markets so that foreign producers will no longer have an incentive to divert sales.
- (b) Transportation facilities may not be able to cope with increased imports in the short run¹⁴⁸.

¹⁴³ W. M. Landes and R. A. Posner, "Market Power in Antitrust Cases," above n.139, 964-965.

¹⁴⁴ See, R. Pitofsky, "New Definitions of Relevant Market and the Assault on Antitrust" above n.64, 1854-1855.

¹⁴⁵ For criticisms of the Landes and Posner approach, see T.J. Brennan, "Mistaken Elasticities and Misleading Rules," 95 Harv. L. Rev. 1849 (1982); L. Kaplow, "The Accuracy of Traditional Market Power Analysis and a Direct Adjustment Alternative" 95 Harv. L. Rev. 1817 (1982).

¹⁴⁶ B. Hawk, *United States, Common Market and International Antitrust: A Comparative Guide* (Law & Business Inc./Harcourt Brace Jovanovich, New York, 1987) at 324-332 and 463-478.

¹⁴⁷ B. Hawk, *United States, Common Market and International Antitrust: A Comparative Guide*, above n.146, at 324-332 and 463-478.

¹⁴⁸ T.J. Brennan, "Mistaken Elasticities and Misleading Rules," above n.145, points out at 1849 that Landes and Posner's "diversion analysis" is most obviously wrong when capacity to import a product into the local region A from the distant region B is fixed. In that case, no matter what price increase there may be in region A, the seller in region B cannot increase its exports into region A. A specific example illustrates the problem. Suppose the product in question is oil, and the sole means of moving oil from B to A is a pipeline that can transport only 100,000 barrels per day and cannot be expanded except at great expense. Thus it is obvious that sellers in region B

- (c) There may be quotas or tariffs restricting the ability of imports to provide effective competition.¹⁴⁹
- (d) Foreign imports may be sufficiently differentiated from the domestic product, so that imports may only satisfy a small segment of the local market, such that foreign sellers cannot readily sell in response to a local price increase.
- (e) Foreign sellers may have long term commitments to consumers and distributors in their own domestic markets.¹⁵⁰
- (f) If the local price increase is a result of a lack of domestic capacity, imports may only be a temporary phenomenon if domestic capacity increases.
- (g) Whether foreign sellers would be prepared to divert sales “involves numerous imponderables, including home market politics and the depth of [their] export commitments to other countries.”¹⁵¹

The Supreme Court of the United States has not directly addressed the problem of defining a relevant geographic market for situations where an impugned party is operating on a worldwide basis, but in defining relevant geographic markets for wholly domestic mergers and acquisitions under section 7 of the Clayton Act, the Supreme Court has stressed that commercial realities and economic considerations must dominate the analyses.¹⁵² The foundation for any market definition analysis under section 7 was established by the Supreme Court in *Brown Shoe Co. v United States* (hereinafter to be referred to as *Brown Shoe*)¹⁵³ in which it was stated that “the boundaries of the relevant markets must be drawn with sufficient breadth to include the competing products of each of the merging companies

will be unable to divert a higher ratio of their output into region A in the short run in response to an increase in the price of oil in region A.

149 The realities of world trade would suggest that if any such diversion began to develop, the importing country would modify tariffs or quotas to insure that its domestic industry is not overwhelmed.

150 The idea that Toyota would abandon its distributors and customers in Japan to take advantage of a price increase in the United States may make sense theoretically but in practice it is inconceivable, as a diversion of total production by Toyota to a distant market would have long-term strategic consequences with respect to their distributors and customers in the Japanese domestic market.

151 B. Hawk, *United States, Common Market and International Antitrust: A Comparative Guide*, above n.146, 467-468.

152 *United States v Philadelphia National Bank*, 374 US 321, 359 (1963); *Brown Shoe Co. v United States*, 370 US 294, 336-337 (1962); *United States v Pabst Brewing Co.*, 384 US 546, 549 (1966).

153 370 US 294 (1962).

and to recognise competition where, in fact, competition exists.”¹⁵⁴ In *Brown Shoe*, the Court also emphasised that under the terms of s.7, “[t]he geographic market selected must ... both ‘correspond to the commercial realities’ of the industry and be economically significant.”¹⁵⁵

In *United States v Philadelphia National Bank*,¹⁵⁶ the Supreme Court defined the geographic market in a bank merger action as that area “ ‘in which the seller operates, and to which the purchaser can practicably turn for supplies ’.”¹⁵⁷ In brief, the threatened foreclosure of competition in any merger action under s.7 must be in relation to the market affected.¹⁵⁸ Thus, the Supreme Court’s traditional approach to market analysis for alleged violations of s.7 suggests the propriety of using market dimensions which are sufficiently broad so as to recognise competition in an industry outside the national borders of the United States, if such a source of competition in fact exists and has a measureable impact upon competition within the United States.

Although the legislative history is silent on the permissibility of world markets, courts and enforcement agencies have in the past discerned a Congressional intent in the phrase “in any section of the country” included within s.7,¹⁵⁹ that market analysis should be conducted with regard to particular geographic segments of the United States.¹⁶⁰ The crux of the legal dispute over defining a geographical market in global terms, therefore, arises from the apparent domestic focus of the provision itself. A literal interpretation of the phrase, “in any section of the country,” appears to support the conclusion that the effects of a merger must only be examined in the context of a market area within the United States. Consequently, courts in the United States have been reluctant to test the geographic parameters of the Clayton Act by using market definitions which transcend the national territorial boundary.¹⁶¹

154 370 US 294, 326 (1962).

155 370 US 294, 336 (1962).

156 374 US 321 (1963).

157 374 US 321, 359 (1963)

158 *Tampa Electric Co. v Nashville Coal Co.*, 365 US 329, 337 (1961).

159 Section 7 of the Clayton Act reads: “No corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital, and no corporation subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another corporation engaged also in commerce, where in any line of commerce *in any section of the country*, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly.” (Emphasis added)

160 See, e.g., *United States v Tracinda Investment Corp.*, 477 F. Supp. 1093, 1105 n.11 (C.D. Cal. 1979).

161 E.W. Kitner, *Federal Antitrust Law* (Anderson Publishing Co., Cincinnati [Ohio], 1984) vol.IV, 497.

One exception to this general rejection of world geographic markets is the California District Court's ruling in *United States v Tracinda Investments Corp.* (hereinafter referred to as *Tracinda*),¹⁶² an action concerning the acquisition of a controlling stock interest by an American shareholder in a domestic corporation involved in the business of producing motion pictures. The foreign element of this action arose from evidence indicating that there existed a world market in which motion picture producers operated and to which the distributors could practicably turn for supplies of motion pictures.¹⁶³ Therefore, a worldwide geographic market was supported by both production and consumption patterns in the affected motion picture industry, making it a commercially realistic geographic dimension within which to determine the effects of the proposed stock acquisition.

The evidence in *Tracinda* showed that foreign-produced pictures directly compete in the United States with American produced films, and that American production companies derived much of their income from foreign distribution.¹⁶⁴ Therefore, Hauk J. found that "the most relevant geographic market for motion pictures is the entire world."¹⁶⁵ However, in a footnote to the opinion, Hauk J. added that this did not mean that the Court would look to the worldwide effects of a merger for all purposes, in light of the phrase "in any section of the country" included within section 7 of the Clayton Act.¹⁶⁶ Thus, the Court's conclusion "with respect to the geographic market rest[ed] in a recognition of the extent to which the worldwide nature of this industry affects competition here in the United States."¹⁶⁷

Thus, the *Tracinda* case may perhaps indicate a greater willingness on the part of the courts in the United States (in line with the increasing influence of "Chicago School thinking" on American antitrust policy¹⁶⁸) to go beyond the traditional definition of the relevant geographic market under section 7 of the Clayton Act, as only including those imports which are actually present within the domestic market, to the inclusion of potential output of foreign suppliers which may be diverted into the local market if the economic incentive is sufficient. Such an observation may also be supported by reference to the 1984 Merger

162 477 F. Supp. 1093 (C.D. Cal. 1979).

163 477 F. Supp. 1093, 1105 (C.D. Cal. 1979).

164 477 F. Supp. 1093, 1105 (C.D. Cal. 1979).

165 477 F. Supp. 1093, 1105 (C.D. Cal. 1979).

166 477 F. Supp. 1093, 1105 n.11 (C.D. Cal. 1979).

167 477 F. Supp. 1093, 1105 n.11 (C.D. Cal. 1979).

168 Above n.138.

Guidelines subsequently issued by the United States Department of Justice,¹⁶⁹ which states that if production, either foreign or domestic, outside of a particular geographic market within the United States, would be diverted into that market in the event of a substantial increase in price, then that outside production should be counted to some extent in measuring the market power held by firms operating within that geographic area.

(3) THE FUNCTIONAL MARKET

The relevant functional market refers to the 'horizontal level' of production or distribution at which a firm operates in the life cycle of a product, e.g., manufacturing, wholesaling or retailing.¹⁷⁰ Markets exist *between* functional levels as goods move from a person at one level to a person at another. In this sense the functional aspect is the hinge upon which the definition of a market turns because it determines which particular buyers and sellers meet each other with the same competitive interest. For while parties to a trade practice or a merger or takeover proposal may deal in the same goods or services, the functional dimension of the market gives recognition to the fact that these firms may be operating at different stages or levels,¹⁷¹ so that firms within the same industry¹⁷² will not necessarily be viewed as competitors in the same market.¹⁷³

However, the decision of both the New Zealand High Court and the Court of Appeal in *Tru Tone*¹⁷⁴ provides an example of two separate functional levels of the market being fused into one broad functional market. The facts of the *Tru Tone* case were complicated, but basically concerned the use by Festival RML Ltd of a system of maximum retail pricing of Top 50 albums and the enforcement of this price by means of refusals to supply key

169 Department of Justice Guidelines, 4 Trade Reg.Rep.(CCH) ¶13,103 (June 14, 1984) [hereinafter referred to as the 1984 Merger Guidelines] §3.23. See, R. Pitofsky, "New Definitions of Relevant Market and the Assault on Antitrust" above n.64, 1854-1855.

170 Y. van Roy, *Guidebook to New Zealand Competition Laws*, above n.41, 62.

171 Y. van Roy, *Guidebook to New Zealand Competition Laws*, above n.41, 62.

172 A market is not the same as an industry. An industry is a grouping of firms making related products. A market is the structure through which products are moved to purchasers. An industry may serve many separate markets. For instance, the steel industry produces a vast range of products from steel sheet through to girders and wire which may all properly be grouped into different markets. Conversely, a market may be served by many different industries. The market for housing construction materials, for instance, is served by the brick industry, the timber industry, the glass industry and many more. Similarly, buyers for a number of industries may be purchasing products in the same market. The steel industry, for example, serves the steel sheet market in which manufacturers of white goods, automobiles and aircraft are all purchasers. See, M. Brunt, "Market Definition' Issues in Australian and New Zealand Trade Practices Litigation", above n.42, 130.

173 On the question of whether conduct at one functional level can affect competition at others, see *Pluteus (No.8) Pty Ltd v G.J. Coles & Co Ltd* (1983) ATPR ¶40-391, 44,584.

174 (1988) 2 NZBLC 103,081 (HC); [1988] 2 NZLR 352 (CA)

retailers who chose to charge prices in excess of the stipulated maximum price. In the recording industry, the first functional level involves recording artists, as sellers, negotiating with recording companies as buyers, for recording contracts. The next functional level is where recording companies manufacture, and distribute as wholesalers, albums to retailers. The third functional level is where the retailers then sell albums directly to the public. The buyers and sellers will be different at each functional level, and therefore one could expect different patterns of competition to exist at each functional level. However, the High court fused the last two functional levels just mentioned into a single functional market because "the promotion which propels an album to a top place in the chart and therefore creates its demand is generated by the distributor who, at that initial stage, conducts his campaign over the head of the retailer as it were, seeking to create demand directly through television, radio and other publicity among the customers."¹⁷⁵ This analysis helped the Court to view each album as a clear substitute for albums previously released, for "when an album is enjoying popularity, promotion of another is gathering momentum."¹⁷⁶

The important role which the functional dimensions of the market may play in overall market analysis can be seen in the *Telecom* decision.¹⁷⁷ In this case the High Court outlined the following principles governing functional identification and their application to the particular factual situation presented to the Court:¹⁷⁸

"If we ask what functional divisions are appropriate in any market definition exercise the answer, plainly enough, must be whatever will best expose the play of market forces, actual and potential, upon buyers and sellers. Whenever successive stages of production and distribution can be co-ordinated by market transactions, there is no difficulty: there will be a series of markets linking actual and potential buyers and sellers at each stage. And again, when pronounced efficiencies of vertical integration dictate that successive stages of production and distribution must be co-ordinated by internal managerial processes, there can be no market. But a feature of this application is the presence of the integrated PSTN [Public Switched Telephone Network] linking all members of the community in innumerable two-party and multi-party communications; and there is also the possibility of some market transactions along the way, i.e., in interconnections with

175 (1988) 2 NZBLC 103,081, 103,089 (HC); [1988] 2 NZLR 352, 360 (CA).

176 (1988) 2 NZBLC 103,081, 103,089 (HC); [1988] 2 NZLR 352, 360 (CA).

177 (1991) 3 NZBLC ¶99-239.

178 (1991) 3 NZBLC ¶99-239, 102,363.

duplicate or by-pass networks and in leased circuits as permitted by the incidence of economies of scale and scope.

In this case (and with no artificial regulatory requirements limiting the freedom of entry to particular segments of the network, as in the United States) we think it best to regard the functional delineation of the standard telephone services as the whole PSTN, comprising the largely fixed facilities for the supply of local, national and international service to households, firms and interconnected suppliers (such as Clear). The PSTN comprises both the trunking network and the local loop.”

For the mobile telephone service, however, the Court distinguished three functional levels.¹⁷⁹ Firstly, network operation and service supply such as that conducted by Telecom Cellular Ltd, providing service, including air-time, on a wholesale basis for Telecom Approved Service Providers (TASP's). Secondly, distribution of connections, continuing access and usage, such as that provided by the four “service providers”, the TASP's. Finally, the retailing of mobile service contracts and hand sets such as that conducted by over 150 Telecom dealers.

The Court found that the Commerce Commission's market delineation was inadequate in its treatment of the functional dimension of the market.¹⁸⁰ In particular, it was critical of the Commission for its failure to identify the PSTN as the fundamental ingredient of the standard telephone service and, also, for making no reference to the various functional levels in the provision of the mobile services. The Court indicated that its own findings led it to give the PSTN greater prominence in its decision than did the Commerce Commission. The Court also found that wholesale distribution and retailing functional level was of some relevance in its assessment of dominance in the mobile telephone market.¹⁸¹

However, it is important to keep in mind that due to the relatively small size of the domestic economy there is a significant level of “vertical integration” within New Zealand,¹⁸² so that many firms will perform more than one distinct function within the distribution chain (e.g., a firm may be involved in both manufacturing and retailing a particular product). Thus,

179 (1991) 3 NZBLC ¶99-239, 102,364.

180 (1991) 3 NZBLC ¶99-239, 102,365.

181 (1991) 3 NZBLC ¶99-239, 102,365.

182 See, B. M. Hill and M. R. Jones, *Competitive Trading in New Zealand: The Commerce Act 1986*, above n.99, 14-15.

there may be times when the distinctions between the "horizontal levels" of an industry are blurred and the functional market is, therefore, difficult to determine.¹⁸³

(4) THE TEMPORAL DIMENSION

All market parameters change over time as participants enter and exit from markets, or as barriers to entry become relevant.¹⁸⁴ Some products have a short "shelf" life and others are subject to rapid technological evolution or changes in fashion. In one sense it is the time lag between changes in consumer preference and producer response which is the very heart of competition law policy. In a perfectly competitive market the response would be immediate, but in many markets restrictive trade practices inhibit this process of transition to the detriment of consumers and effective resource allocation.¹⁸⁵ The reality of potential competition and the timing of its impact will therefore often be the decisive factor in determining the level of workable and effective competition in any particular market. Hence in determining the relevant market it will be necessary to consider the time period over which the degree of substitutability is to be assessed.

Over a period of time, a position of market power will tend to be eroded as customers turn to other products as substitutes for the monopolised one ('cross-elasticity of demand'), and as other suppliers, seeing that the cartel or dominant concern is able to reap monopoly profits, enter the market in order to share in some of those profits and, by increasing the

183 The first Chairman of the Commerce Commission discussed this problem in relation to the *Cement Industry Inquiry* (Commerce Commission, "Report of the Commerce Commission Following an Inquiry into the Question of Removal of Cement from the Positive List of Controlled Goods and Services 1981 and an Inquiry into Certain Matters Relating to Price Control and Pricing Practices in the Manufacturing and Distribution of Cement" (Wellington, 1986)) and gave the following guidance as to how the Commission might determine the matter:

"For example, the market for wholesale distribution of cement (i.e., the resale of cement by merchants to user and reseller) would be likely to be considered separately from the sale of cement by manufacturers to wholesalers. Should the market for primary distribution (i.e., from cement works to bulk storage depots) be considered separately? This will depend particularly upon whether it would be unrealistic for primary distribution to be separated from manufacture. If the distribution process is interlinked with that of production or if there are few options for transport facilities other than those used by the cement companies or if customers look to buy cement locally rather than ex-factory, then the Commission may be reluctant to consider primary distribution as a separate market. However, there may well be industries in which the function of transport from ex-works to selling depots can be regarded as a separate market or trade."

184 See, *Watties Industries Ltd/Taylor Freezer Holdings Ltd*, Commerce Commission Decision No. 127 (16 May 1985), 7: "Although no barriers are totally insurmountable for all time, and although governmental barriers as to imports, tariffs and investments in this industry may be lifted further we think there are sufficient practical barriers in this industry (contributed to by this proposal) to have a considerable dampening effect - so as to make the possibility of effective competition remote."

185 See, B. M. Hill and M. R. Jones, *Competitive Trading in New Zealand: The Commerce Act 1986*, above n.99, 15.

supply, ultimately increase competition and drive the price down ('cross-elasticity of supply'). Thus, in the 1920's, when both the supply of and the demand for coal in the United States was thought to be inelastic, a coal monopoly or cartel would have been regarded as having great market power. Over time, however, coal users have turned to other sources of energy such as hydro-electricity, oil and gas, while the discovery of new coalfields has shown that the supply of coal itself is elastic.¹⁸⁶ However, this process of substitution took many years. What time lag in substitution should be regarded as being too long to qualify the alternative product or alternative producer as being within the relevant market?¹⁸⁷

The reaction time that one would tend to regard as too long will obviously vary with the nature of the particular product in question. A delay of 12 months might be considered too lengthy a period in the clothing industry, but not in the coal mining industry, where lead-times for expansion are much longer. If a time factor which is too short is assumed, the market will be defined too narrowly, thereby overstating the power of the parties to disregard competition. Conversely, market power would be understated if too long a time factor is assumed. Therefore, the time parameter must be a matter of judgement, although common sense would dictate that it should be based on an analysis of evidence about the "commercial realities" of a particular industry and not on inferences at large.¹⁸⁸

The Trade Practices Tribunal declared in the *re Tooth & Co Ltd* decision that it was concerned with longer run, rather than short-run, substitution possibilities:¹⁸⁹

"It is plain that the longer the period allowed for likely customer and supplier adjustments to economic incentives, the wider the market delineated. In our judgement, given the policy objectives of the legislation,

186 See, K. Elzinga and T. Hogarty, "The Problem of Geographic Market Delineation Revisited: The Case of Coal," 23 Antitrust Bull. 1 (1978); P. Griffin and J. Kusher, "Geographic Submarkets in Bituminous Coal," 21 Antitrust Bull. 67 (1976); T. Schwartzman, "The Cross-Elasticity of Demand and Industry Boundaries: Coal, Oil, Gas and Uranium," 18 Antitrust Bull. 483 (1973); R.E. Shrieves, "Geographic Market Areas and Market Structure in the Bituminous Coal Industry," 23 Antitrust Bull. 589 (1978).

187 This question usually arises in the context of the product market; as supplies of most commodities can be brought in from other geographic areas relatively quickly, whereas developing substitutes or expanding competitive productive capacity normally takes much longer. See, G.de Q. Walker, above n.12, 391.

188 See, *True Tone Ltd v Festival Records Retail Marketing Ltd* [1988] 2 NZLR 352, per Richardson J. at 360: "Viewed in relation to product and time the single album definition of market ignores commercial realities. It focuses on short run phenomenon. It represents a snapshot rather than a moving picture of continuing commercial activity ... [T]he movement of albums in and out of the charts, and their constantly shifting positions are clear evidence of the manner in which, and the extent to which substitution takes place."

189 (1979) ATPR ¶40-113, 18,196.

it serves no useful purpose to focus attention upon a short-run, transitory situation. We consider we should be basically concerned with substitution possibilities in the longer run. This does not mean we seek to prophesy the shape of the future - to speculate upon how community tastes, or institutions, or technology might change. Rather, we ask of the evidence what is likely to happen to patterns of consumption and production were existing suppliers to raise price or, more generally, offer a poorer deal. For the market is the field of actual or potential rivalry between firms.”

The New Zealand Court of Appeal has also emphasised the desirability of considering substitution possibilities in “the long run,” within the *True Tone* decision.¹⁹⁰

As we have already noted,¹⁹¹ the New Zealand High Court in *Telecom* was concerned with the temporal dimension of the relevant market. In considering whether technology that is still being developed should be considered as substitutable for existing services (and therefore as affording potential competition in the same market), the Court accepted Telecom’s argument that the Commission adopted too short a time perspective.¹⁹² It should have expressly canvassed new technology in the form of wireless-based products and systems.¹⁹³ However, this omission was not fatal and the Court concluded that the Commission gave adequate recognition to the overall *dynamic forces* in the industry.¹⁹⁴ The basic lesson is that market boundaries should be described in terms that do not unwittingly preclude consideration of prospects for new entry, as would, for example, a description of the market as the cellular telephone services market, rather than the mobile telephone services market.¹⁹⁵ Therefore, in considering the constraints upon market incumbents, the court or tribunal should pay adequate and appropriate regard to dynamic forces within that relevant market.¹⁹⁶

In short, the Court’s criticism of the Commission’s failure to address the dynamism of the market was aimed at the short term perspective taken by the Commission.¹⁹⁷ In particular, it was concluded that the Commission had failed to adequately consider the ability of other

190 *True Tone Ltd v Festival Records Retail Marketing Ltd* [1988] 2 NZLR 352, 360.

191 See, above n.87.

192 (1991) 3 NZBLC ¶¶99-239, 102,363 and 102,365.

193 (1991) 3 NZBLC ¶¶99-239, 102,363.

194 (1991) 3 NZBLC ¶¶99-239, 102,364.

195 (1991) 3 NZBLC ¶¶99-239, 102,364.

196 (1991) 3 NZBLC ¶¶99-239, 102,364.

197 (1991) 3 NZBLC ¶¶99-239, 102,365.

firms to redeploy existing capacity,¹⁹⁸ and the extent to which technological change (a fundamental characteristic of telecommunications markets) could be accommodated within the parameters of those relevant markets described by the Commission.¹⁹⁹

Despite the fact that the primary focus of courts and tribunals in proceedings under the Commerce Act and the Trade Practices Act will be on longer run substitution possibilities considerations relating to substitution possibilities in a short-run sense may not be altogether irrelevant, as shown by the following discussion of the concept of sub-markets.²⁰⁰

The notion of a sub-market has proved to be a source of great confusion for antitrust jurisprudence in the United States.²⁰¹ However, if used properly the concept of a sub-market can be a useful aid to competition analysis within the Trade Practices Act and the Commerce Act. Few problems should arise with this concept if courts and tribunals in Australia and New Zealand keep in mind the qualifications expressed by the Trade Practices Tribunal in *QOMA*²⁰²:

"The distinction between markets and sub-markets can be merely one of degree. Sub-markets are the main market defined, explicitly or implicitly, by some discontinuity in substitution possibilities. Where the defining feature of a market is the existence of close substitutes (whether in demand or supply), the defining feature of a sub-market is the existence of still closer and more immediate substitutes. Sub-markets may be especially useful in registering the short-run effects of change, but they may be misleading if used indiscriminately to assess long-run competitive effects". (Emphasis added)

198 (1991) 3 NZBLC ¶¶99-239, 102,364 and 102,365.

199 (1991) 3 NZBLC ¶¶99-239, 102,365.

200 See, below n.202.

PART IV

4. THE CONCEPT OF SUB-MARKETS

As an aid to the determination of the relevant market the concept of a 'sub-market' may in certain circumstances be useful where there exists substitution possibilities that are important in a short-run sense, in terms of both supply and demand. For instance mens and womens shoes might well be placed in different markets on purely demand side substitution criteria, for it is unlikely that an increase in the price of mens or womens shoes relative to the other will induce a significant swing in consumption to the other type. From the supply viewpoint, however, the technological similarities in the production of mens and womens shoes, using given materials, are more likely to suggest that mens and womens shoes should be considered as coming within the one market, because production substitution could be achieved within a short period of time. Yet, to penetrate the characteristics and interests of buyers, it may be useful to delineate individual sub-markets (e.g., mens shoes, womens shoes, and childrens shoes) within the broader footwear market.

The notion of a sub-market has proved to be a source of great confusion for antitrust jurisprudence in the United States.²⁰¹ However, if used properly the concept of a sub-market can be a useful aid to competition analysis within the Trade Practices Act and the Commerce Act. Few problems should arise with this concept if courts and tribunals in Australia and New Zealand keep in mind the qualifications expressed by the Trade Practices Tribunal in *QCMA*²⁰²:

"The distinction between markets and sub-markets can be merely one of degree. Sub-markets are the more narrowly defined, typically registering some discontinuity in substitution possibilities. Where the defining feature of a market is the existence of close substitutes (whether in demand or supply), the defining feature of a sub-market is the existence of still closer and more immediate substitutes. Sub-markets may be especially useful in registering the short-run effects of change; *but they may be misleading if used uncritically to assess long run competitive effects*". (Emphasis added)

201 See, below n.212.

202 (1976) ATPR ¶40-012, 17,247. See also, *Re Howard Smith Industries Pty Ltd* (1977) ATPR ¶40-023, 17,337.

In that case the relevant product markets were found to be flour and bread, however, baker's flour was held to be an important sub-market of the flour market.²⁰³ The Tribunal then proceeded to study the play of competitive forces in that sub-market as indicative of the likely effects of the proposed merger in the overall market for flour.

The Tribunal has subsequently presented a more carefully developed analysis of the sub-market concept in the *re Tooth & Co Ltd* decision:²⁰⁴

“... within the bounds of the market, substitution possibilities may be more or less intense and more or less immediate: the field of substitution is not necessarily homogeneous but may contain within it sub-markets wherein competition is especially close or especially immediate. There may be, too, certain key sub-markets such that their competitive relationships have a wider effect upon the functioning of the market as a whole. In these matters we have found that the identification of relevant sub-markets may be rather helpful in clarifying how competition works.”

One of the issues which arose in this case was the extent to which Tooth's exclusive dealing restrictions effectively lessened competition in a market. As these exclusive dealing restrictions applied only to bulk beer, not packaged beer, it was argued that the relevant product market should be confined to the production and distribution of bulk beer. However, the evidence of substitutability on both the demand and supply sides persuaded the Tribunal that bulk and packaged beer properly belonged within the same relevant market. The Tribunal did, however, state that bulk beer was a significant sub-market which would repay close study.²⁰⁵

There are at least two distinct ways by which the sub-market concept may be utilised, one of which is helpful and one of which, it is submitted, will merely cause confusion and inconsistency within the process of market analysis. Firstly, under what is generally referred to as the “American approach”²⁰⁶, the notion of a sub-market may be equated with the relevant market itself. Thus, in United States antitrust litigation, “liability can attach as a result of dominance or market power in a sub-market”.²⁰⁷ This line of reasoning had its

203 (1976) ATPR ¶40-012, 17,248.

204 (1979) ATPR ¶40-113, 18,197.

205 (1979) ATPR ¶40-113, 18,198.

206 See, M. Brunt, “ ‘Market Definition’ Issues in Australian and New Zealand Trade Practices Litigation,” above n.42, 144. See also, *New Zealand Magic Millions Ltd v Wrightson Bloodstock Ltd* [1990] 1 NZLR 731, 752.

207 *New Zealand Magic Millions Ltd v Wrightson Bloodstock Ltd* [1990] 1 NZLR 731, 752.

genesis in the *United States v Bethlehem Steel Corp* decision,²⁰⁸ but was first enunciated by the United States Supreme Court in *Brown Shoe Co v United States*.²⁰⁹ This approach is clearly spelt out in the recent decision of *Aspen Highlands Skiing Corp v Aspen Skiing Co*,²¹⁰ where Aspen Skiing Co was found to have monopolised the market for downhill skiing services at Aspen in violation of section 2 of the Sherman Act. Holloway J.'s instruction to the jury in that case contained the following statement:²¹¹

“There can be both a relevant market and a relevant sub-market or just a relevant market without any relevant sub-market. Thus, if you decided that the relevant product market is downhill skiing at destination ski resorts, you must still determine whether downhill skiing services, including multi-area, multi-day lift tickets is a submarket within a larger market.”

This use of the sub-market concept has been rightly criticised on the ground that it is self-contradictory to hold that both a broad area is a market and that smaller parts of that same area are also markets.²¹² As Professor Posner points out, in this sense “a sub-market would be a group of sellers from which sellers of good substitutes in consumption or production had been excluded, and these exclusions would deprive any market-share statistics of their economic significance.”²¹³ Such an approach may also be criticised on the basis that, where the relevant market is to be narrowed down to what might have been referred to as a sub-market, then the term ‘sub-market’ should logically lapse, for as Donald and Heydon contend “[t]here are just more markets, not sub-markets”.²¹⁴

In light of such criticism it is important to note that in the New Zealand context a similar line of reasoning (to the “American approach”) appears to have been incorporated within

208 168 F. Supp. 576 (S.D.N.Y. 1958). See, P. Areeda and D.F. Turner, *Antitrust Law*, above n.95, vol II, 409-411.

209 370 US 294 (1962). In this case the Supreme Court commented at 325 that: “The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it. However, within this broad market, well-defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes ... Because §7 of the Clayton Act prohibits any merger which may substantially lessen competition ‘in any line of commerce’ (emphasis supplied), it is necessary to examine the effects of a merger in each such economically significant submarket to determine if there is a reasonable probability that the merger will substantially lessen competition. If such a probability is found to exist, the merger is proscribed.”

210 738 F.2d 1509 (10th Cir. 1984).

211 738 F.2d 1509, 1528-1529 (10th Cir. 1984).

212 P. Areeda and D.F. Turner, *Antitrust Law*, above n.95, 411.

213 R. Posner, *Antitrust Law* (Harvard University Press, Cambridge [Massachusetts], 1976) 126.

214 B. Donald and J.D. Heydon, *Trade Practices Law* (Law Book Co., Sydney, 1978) 98.

the New Zealand High Court's decision in the *ARA* case.²¹⁵ In delivering the judgement in this case, Barker, J. held that the relevant market was that of providing rental car services to airline passengers at Auckland airport.²¹⁶ However, his Honour also described this relevant market as a sub-market of the national geographic market for rental car services in New Zealand.²¹⁷ Thus, Barker, J. appears to have fallen into the trap of equating the notion of a sub-market with that of the relevant market itself.

Secondly, identifying sub-markets can be used as a way of clarifying how competition works within the broader market, rather than employing it as the field in which competition is conducted. This is the sense in which the concept has been used by the Trade Practices Tribunal²¹⁸ in such cases as *QCMA*²¹⁹ and *re Tooth & Co Ltd*²²⁰. The distinction between this approach and the "American approach" is brought to the fore in the Australian Federal Court's decision in *TPC v TNT Management Pty Ltd*, where Franki J. concluded²²¹:

"I think it is correct to say that the word 'market' in sec.45(3) should be read as referring to a relevant market rather than a relevant sub-market although it may be very helpful to examine the degree of competition in a particular sub-market and then apply the conclusion to a consideration of the position in the whole market."

While, in the context of New Zealand's Commerce Act 1986, Tipping, J. has made a similar distinction between the two concepts of 'relevant market' and sub-market' in the *New Zealand Magic Millions Ltd v Wrightson Bloodstock Ltd* decision²²²:

"It appears that in America in antitrust cases, liability can attach as a result of dominance or market power in a sub-market ... But that is not the position in New Zealand and it is not, as I understand it, the position in Australia either. There is no doubt however that the concept of a sub-market may be used as a convenient tool of analysis of the dynamics of a market."

215 [1987] 2 NZLR 647.

216 [1987] 2 NZLR 647, 677.

217 [1987] 2 NZLR 647, 671.

218 The Trade Practices Commission has done likewise in a number of cases such as *CRA Services Ltd*, Unreported, 4 November 1976, Trade Practices Commission, Sydney, C22435; where a broad market was identified as resources and energy with a specific sub-market being stipulated as 'coal'.

219 (1976) ATPR ¶40-012.

220 (1979) ATPR ¶40-113.

221 (1985) ATPR ¶40-512, 64,143.

222 (1990) 1 NZLR 731, 752 (HC).

Therefore, in regard to the Commerce Act 1986 and the Trade Practices Act 1974, the fundamental utility of the sub-market concept, both to applicants and the determining authorities, is that it conveys the sense of varying degrees of substitutability without attempting to catalogue the whole complexity of the market place. Furthermore, this notion may help to bridge the gap between short-run considerations or conceptions of a 'market' and those notions that are relevant to the long-run competitive issues to which the Commerce Act and the Trade Practices Act are fundamentally addressed.²²³ Therefore, it is to be concluded that it would be most unfortunate if criticisms generated by the "American approach" were to lead New Zealand and Australian courts and tribunals to abandon their own distinctive concept of a sub-market.

223 See, above n.189 and n.190.

PART V

5. CONCLUSION

The Commerce Act 1986 and the Trade Practices Act 1974 contain statutory definitions of the term 'market' that are to be interpreted with the aid of the economic concept of substitutability. Hence, the market delineation process in New Zealand and Australian competition law is necessarily a task of mixed legal-economic analysis. However, such an approach to market definition, involving lengthy argument by counsel and the tendering of expert economic evidence on actual and potential demand and supply substitution, has arguably further increased the cost of litigation²²⁴ without necessarily shedding much light upon the real focus of such proceedings, which is the degree of 'market power' possessed by the defendant in the relevant market. For as Pincus, J. observed in the *Australia Meat Holdings Pty Ltd v TPC* decision:²²⁵

"... the process of identification of the relevant market must be carried out keeping in mind the object of doing so; in the instant case that is to determine whether the appellant was at the relevant time in a position to dominate the market, or was by the acquisition placed in such position.

The linking together of the process of definition of the market and its object implies some flexibility in the former."

Thus, if market definition is to be an aid to competition analysis it must serve to concentrate attention upon the defendant's market power, as too great a focus upon market delineation *per se* will inevitably cause this fundamental fact to be overlooked. To this end, Australian and New Zealand courts and tribunals should keep in mind the following comment by Franklin Fisher²²⁶:

²²⁴ See, the observation by Wilcox, J. in *Australia Meat Holdings Pty Ltd v TPC* (1988) ATPR ¶40-876, 49,479-49,480: "Economists are able to assist the court in relation to economic principles. But once, the relevant principles are expounded, their application to the facts of the case is a matter for the court. The proper definition of a market is entirely a matter of fact, the determination of which ought not to be made more protracted and expensive by the adduction of unnecessary economic evidence."

²²⁵ (1989) ATPR ¶40-932, 50,104. See also, *Queensland Wire Industries Pty Ltd v Broken Hill Pty Co Ltd* (1989) ATPR ¶40-925, 50,008; *Telecom Corporation of New Zealand Ltd v Commerce Commission* (1991) 3 NZBLC ¶99-239, 102,361.

²²⁶ F.M. Fisher, "Diagnosing Monopoly", above n.16, 13. Similar sentiments have also been expressed by the New Zealand High Court in *Telecom Corporation of New Zealand Ltd v Commerce Commission* (1991) 3 NZBLC ¶99-239, 102,360-102,361: "In both the Australian and New Zealand jurisdictions it has been said, in effect, that a mechanical reliance upon substitution criteria in a contextual vacuum is not sufficient...". Hence the boundaries should be drawn by

"... the primary question in defining a relevant market ought to be that of constraints on the alleged monopolist. The principal constraints can be of two types, those relating to demand and those relating to supply. The courts have paid appropriate attention to demand and supply substitutability - appropriate because these are criteria by which to judge the constraints on the alleged monopolist. It should not be forgotten, however, that it is the constraints which are the object of analysis and not the properties of substitutability themselves."

Economic theory often suggests that there is no one "right" market, but a collection of interlinked markets, so that all sellers face competitive impacts of ever reducing significance from other firms ranged further and further away from them.²²⁷ As Deane, J. pointed out in the *Queensland Wire Industries* case²²⁸:

"The economy is not divided into an identifiable number of discrete markets into one or other of which all trading activities can be neatly fitted. One overall market may overlap other markets and contain more narrowly defined markets which may, in their turn, overlap, the one with one or more others. The outer limits (including geographic confines) of a particular market are likely to be blurred: their definition will commonly involve an assessment of the relative weight to be given to competing considerations in relation to questions such as the extent of product substitutability and the significance of competition between traders at different stages of distribution."

The preceding discussion on the various dimensions of the market concept serves to demonstrate that, important as they are, the notions of demand and supply substitutability will not provide a complete solution to the task of market definition as a question of degree is involved (i.e., at what point do different goods or services become closely enough linked in terms of supply or demand so as to be included in the one market?)²²⁹. Hence, it would

reference to the conduct at issue, the terms of the relevant section or sections, and the policy of the statute. Some judgement is required, bearing in mind that 'market' is an instrumental concept designed to clarify the sources and potential effects of market power that may be possessed by an enterprise."

227 L.A. Sullivan, *Antitrust*, above n.4, 64.

228 (1989) ATPR ¶40-925, 50,013.

229 See, *Queensland Wire Industries Pty Ltd v Broken Hill Pty Co. Ltd* (1989) ATPR ¶40-925, 50,015; See also, M. Brunt, "Market Definition' Issues in Australian and New Zealand Trade Practices Litigation," above n.42, 149-152.

be fallacious to assume that a relevant market may be delineated solely by reference to the concept of substitutability within the different dimensions of the market, as a court or tribunal will still be required to perform an act of judgement as to the appropriate level of substitutability that is required to include different products in the same market. Since that judgement is necessarily subjective in nature, the resulting delineation of the relevant market may not always be seen as consistent or predictable. Therefore, it is submitted that the inherent flexibility which is provided by the concept of substitutability within the statutory definition of "market" in s.3(1A) of the Commerce Act and s.4E of the Trade Practices Act should be tempered against an increased emphasis upon the commercial realities of the particular factual situation involved in any such proceedings. In the words of the United States Supreme Court, a "pragmatic, factual approach to the definition of the relevant market" is required, rather than a purely "formal legalistic one."²³⁰

Such an approach would perhaps be achieved where the parties to proceedings are required to present evidence as to the commercial facts of that particular industry rather than theoretical possibilities.²³¹ Then, as a starting point the market could be narrowly defined as the goods or services which are the subject of the dispute between the parties. It must be emphasised, however, that this is only a starting point in the market delineation process, for in the past certain Australian courts and tribunals have fallen into the trap of linking the relevant product market with those particular goods or services supplied by the defendant without conducting a proper inquiry as to whether such a market is really self-contained or whether it might be part of a larger market.²³²

The next step would be to ascertain from those who supply the goods or services in question and those who consume such goods or services, the identity of existing competitors. It should then be possible to ascertain from those existing competitors the

230 *Brown Shoe Co. Inc v United States* 370 US 294, 336 (1962). This passage was cited with approval by Pincus J. in *Australia Meat Holdings Pty Ltd v TPC* (1989) ATPR ¶40-932, 50,105.

231 See, M. Brunt, "Market Definition' Issues in Australian and New Zealand Trade Practices Litigation," above n.42, 153-154; J.D. Heydon, *Trade Practices Law*, above n.71, vol I, 1571-1572; G. deQ. Walker, "Geographical Market Definition in Competition Law", 13 Fed.L.R. 299, 322 (1983).

232 See, e.g., *Top Performance Motors Pty Ltd v Ira Berk (Qld) Pty Ltd* (1975) ATPR ¶40-004 (where the relevant product market was found to be the brand name market for Datsun vehicles); *McLean v Shell Chemical (Aust) Pty Ltd* (1984) ATPR ¶40-462 (where the relevant product market was found to be that for the raw material Cypermethrin used in the production of an insect killing chemical for use on sheep); *Warman International v Envirotech Australia Pty Ltd* (1986) ATPR ¶40-714 (where the relevant product market was found to be that for slurry pumps and their replacement parts); and *Williams v Papersave Pty Ltd* (1987) ATPR ¶40-871 (where the relevant product market was found to be the collection and treatment of waste computer paper in the inner Sydney metropolitan area.) See also, G. deQ. Walker, "Product Market Definition In Competition Law," above n. 12, 389-390.

identity of likely potential competitors. The identity of those potential competitors would of course be dependent upon the existence and height of barriers to entry. However, before the market boundary is extended to include those potential entrants, it should be demonstrated that the threat of new entry is more than ephemeral; it must act as a real constraint on the conduct of existing competitors.²³³

This pragmatic and factual approach to market definition would not necessarily result in clearly defined markets in every case, but it would result in a relevant market being defined in such a way as to only include near substitutes rather than remote substitutes for the products supplied by the defendant. It is submitted, therefore, that such an approach would reflect the commercial realities of that particular industry as it is only near substitutes that will constrain the conduct of the defendant in the market place.

Such a flexible approach to market definition may perhaps be subject to criticism on the basis that it would create uncertainty and inconsistency within Australian and New Zealand competition law. However, the force of any such criticism is greatly diminished when it is realised that the subjective nature of the present market delineation process does not in truth guarantee results which are any more certain or predictable.²³⁴

Lawyers for their part should ensure that claims of substitutability which are presented during such proceedings are based on "commercial common sense"²³⁵ and the realities of commercial behaviour in that industry. They need to simplify the issue for the court rather than engage in theoretical speculation as to substitution possibilities. In this regard, the following observations of a United States practitioner prove to be most enlightening²³⁶:

"Testimony by economic witnesses is expert opinion testimony, which means that in almost every case your expert and the other side's expert will be drawing competing inferences from the same basic set of facts. The more complex the issues, the more likely that the judge or jury or commission or tribunal will react ... by basically disregarding the conflicting economic testimony. This is why the cardinal rule for litigators and economists in antitrust cases should be to simplify - not to

233 See, above n.83. See also, R. Pitofsky, "New Definitions of Relevant Market and the Assault on Antitrust", above n.64, 1861-1862; P.E. Areeda & D.F. Turner, *Antitrust Law*, above n.95, vol II, 349-350.

234 See, above n.229.

235 See, Commerce Amendment Act 1990, s.3(1A).

236 J.S. Kingdon, "Economic Argument in Antitrust Cases: An American Litigator's Perspective" [1987] *European Competition Law Review* 371, 381.

oversimplify, but to simplify - the economic issues as much as possible, and to present them in plain, *common sense* terms." (Emphasis added)

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