

Oceania

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By Alicia Murray



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In New Zealand, the prohibition on unilateral conduct (Section 36 of the Commerce Act 1986 (“Commerce Act”)) requires the taking advantage of market power for an anti-competitive purpose. For well over a decade, the Commerce Commission (the “Commission”) has been vocal in its views that Section 36 is difficult to enforce and not fit for purpose. The government has now accepted that Section 36 should be amended to include an effects test, and legislation was introduced into parliament on March 11, 2021.²

However, it is fair to say that the proposed reform is not being welcomed uniformly with open arms. Those opposed are concerned that it will lower the threshold for breach, prohibit conduct which is otherwise pro-competitive, and introduce uncertainty and ambiguity into everyday business decisions.

This article looks at the current position and proposed reform. I argue that in light of the real and perceived issues with enforcement of the current provision, the inclusion of an effects test within Section 36 of the Commerce Act is a welcome reform. It is also important for New Zealand to have a degree of consistency with Australia and other OECD countries in the application and enforcement of competition law, and the proposed reform makes the same amendments to Section 36 as were made in Australia in 2017 to equivalent position

(Section 46 of the Competition and Consumer Act 2010).

Current Law

In New Zealand, the prohibition on unilateral conduct is set out in Section 36 of the Commerce Act. Section 36 prohibits firms with a substantial degree of market power from taking advantage of that market power for a proscribed anti-competitive purpose (including restricting the entry of a competitor in the market, preventing a person from engaging in competitive conduct or eliminating a competitor from the market).

The key elements in proving a breach of Section 36 are to show that a person:

1. Has substantial market power;
2. Takes advantage of that market power; and
3. Does so for one of the proscribed purposes

Determining whether a firm has a substantial degree of market power was set out clearly by the Supreme Court in *Commerce Commission v. Telecom Corporation of New Zealand*.

However, there has been a number of high-profile cases to determine the test for assessing whether a firm took advantage of that market power. Court decisions in New

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² Commerce Amendment Bill 2021.

Zealand had resulted in a very high threshold being applied.

In 1994 the Privy Council held that “it cannot be said that a person in a dominant market position ‘uses’ that position for the purposes of s 36 [if] he acts in a way which a person not in a dominant position but otherwise in the same circumstances would have acted.”³

This has been described as the “counterfactual test.” Despite a change in the wording of Section 36, in 2010 the Supreme Court decided that the connection issue in Section 36 of the Commerce Act should remain a counterfactual (or “comparative”) exercise.⁴ The Supreme Court stated:⁵

Anyone asserting a breach of section 36 must establish there has been the necessary actual use (taking advantage) of market power. To do so, it must be shown, on the balance of probabilities, that the firm in question would not have acted as it did in a workably competitive market, that is, if it had not been dominant.

The test is underpinned by four policy propositions:⁶

1. mere possession of market power is no cause for concern,
2. large firms can compete,

3. competition law protects a competitive process, and

4. clear rules are important.

Issues with the Current Law

There has been a significant amount of criticism of the current law, including from the Commission itself and from the Productivity Commission.⁷

In 2013, the Commission noted in a statement about the year ahead:⁸

We are also hoping for legislative reform to clarify uncertainty in how to practically apply section 36 of the Commerce Act, which deals with monopolistic conduct. The uncertainty has arisen following a decision by the New Zealand Supreme Court involving the Commission’s case against Telecom for alleged misuse of market power in the internet dial-up industry. As a result, we have completed only two unilateral conduct cases in the last year. Given the complexity and cost of these types of cases we are choosing to investigate only those involving clear harm.

³ *Telecom Corp of New Zealand Ltd v. Clear Communications Ltd* [1995] 1 NZLR 385 (PC) at 403.

⁴ *Commerce Commission v. Telecom Corp of New Zealand Ltd* [2010] NZSC 111, [2011] 1 NZLR 577, (2010) 12 TCLR 843.

⁵ *Commerce Commission v. Telecom* (2010) 12 TCLR 843 at [34] per Blanchard and Tipping JJ.

⁶ Matt Sumpter (ed) *NZ Competition Law and Policy* (online loose-leaf ed, Wolters Kluwer) at [100-030].

⁷ See for example New Zealand Productivity Commission *Boosting productivity in the services sector* May 2014 at page 6 <https://www.productivity.govt.nz/assets/Documents/cf6ed35675/Final-report-Boosting-productivity-in-the-services-sector.pdf>.

⁸ Commerce Commission statement, *Looking ahead to 2013*, January 28, 2013, <https://comcom.govt.nz/news-and-media/bulletin/looking-ahead-to-2013>.

The Ministry for Business, Innovation and Employment (“MBIE”) raise three primary concerns with the test:⁹

1. It has the potential to fail to deter or penalize some forms of anti-competitive conduct, because some conduct which would be undertaken in the absence of market power may still have harmful or anticompetitive effects when undertaken by firms with market power.
2. It is costly and complex to enforce, which reduces the incentive for businesses to comply with the law. This is because there is uncertainty in developing and applying the hypothetical counter-factual of a firm in the same position but without market power.
3. It creates some unpredictability for day-to-day decision making.

Proposed Reform

On February 12, 2020, Cabinet decided to amend Section 36 of the Commerce Act to prohibit persons with a substantial degree of power in a market from engaging in conduct that has the purpose, or has or is likely to have the effect, of substantially lessening competition in a market.¹⁰ Thereby proposing to introduce an "effects test."

The government's intended reforms will align Section 36 with Australia's equivalent provision (Section 46 of Australia's

Competition and Consumer Act), to read as follows:

A person that has a substantial degree of power in a market must not engage in conduct that has the purpose, or has or is likely to have the effect, of substantially lessening competition in a market.

The Cabinet paper argues that this change would focus the prohibition directly on the anticompetitive nature of the conduct, and is likely to significantly decrease the cost and complexity of enforcement.

The Commerce Amendment Bill was introduced into parliament on March 11, 2021. This Bill replaces Section 36 with the following:

(1) A person that has a substantial degree of power in a market must not engage in conduct that has the purpose, or has or is likely to have the effect, of substantially lessening competition in—

(a) that market; or

(b) any other market in which the person, or an interconnected person, -

(i) supplies or acquires, or is likely to supply or acquire, goods or services; or

(ii) supplies or acquires, or is likely to supply or acquire, goods or services indirectly through 1 or more other persons

⁹ Hon. Kris Faafoi *Impact Statement: Review of Section 36 of the Commerce Act and other matters* (Ministry of Business, Innovation and Employment, February 18, 2020) at 11.

¹⁰ Hon. Kris Faafoi Cabinet Paper: Review of Section 36 of the Commerce Act and other matters (Ministry of Business, Innovation and Employment, February 18, 2020) at 2. <https://www.mbie.govt.nz/dmsdocument/11261-review-of-section-36-of-the-commerce-act-1986-and-other-matters-policy-decisions-minute-of-decision-proactiverelase-pdf>.

Arguments in Favor of Reform

The arguments in favor of proposed reform can be summarized into three main headings:

1. The current law is difficult to enforce.
2. The proposed reform aligns the test with other sections in the Commerce Act relating to both restrictive trade practices and the merger prohibitions.
3. The proposed reform would bring the law in New Zealand in line with Australia, and with other comparable jurisdictions.

Enforcement Difficulties

The Commerce Commission has publicly stated that it considers there are practical difficulties in enforcing Section 36 and that reform is needed. The Commission in particular has issues with the way in which the counter-factual test has to be applied and, in the Commission's view, the analysis is problematic as it may require the Commission to "ignore... commercial realities and the impact on the market of the conduct, and ask a purely hypothetical question."¹¹

The proposed changes would remove the need to apply a hypothetical test, and would significantly lower the threshold for enforcement against firms with market power.

The Government believes that an effects test will capture a broader range of unilateral conduct, and will be more straightforward to enforce.

In its impact statement in support of the proposed reform, MBIE noted:¹²

It is concerning that, after more than 30 years of experience with section 36, the Commission regards a central plank of the Act as difficult to enforce.

It is interesting to note that the Commission has not commenced any court proceedings under Section 36 in some time and the last case to come before the Court was the so-called "data-tails" case, which was decided in 2012.¹³

Consistency within the Commerce Act

An "effects test" is used in other sections of the Commerce Act, including Section 27, which prohibits contracts, arrangements or understandings that have the purpose, effect or likely effect of substantially lessening competition in the market. Similarly, Section 47, which prohibits mergers which have or would be likely to have the effect of substantially lessening competition in the market, also includes an effects test.

As such, there would be previous case-law to rely on to help determine whether a particular conduct has substantially lessened competition, and an effects test is well-established and familiar to those who work in this area.

Consistency with Australia

Section 36 in New Zealand is the equivalent of Section 46 of the Competition and Consumer Act 2010 in Australia. Until 2017 the wording

¹¹ Letter from Mark Berry (Chairman of Commerce Commission) to Hon. Paul Goldsmith (Minister of Commerce) regarding the review of the Commerce Act 1986 (June 2, 2016) at 22-23. <https://www.mbie.govt.nz/assets/d14295e4f8/commerce-commission-letter-to-Minister.pdf> at 22 and 23.

¹² Hon. Kris Faafoi *Impact Statement: Review of Section 36 of the Commerce Act and other matters* (Ministry of Business, Innovation and Employment, February 18, 2020) at page 13.

¹³ *Telecom Corp of New Zealand Ltd v. Commerce Commission* [2012] NZCA 278 – the "data-tails" case.

of Sections 36 and 46 was essentially the same.

However, in 2017 the Australian legislation was amended to introduce an effects test into their prohibition on unilateral conduct, and it is desirable for there to be consistency in the provisions that apply across Australia and New Zealand.

MBIE noted in its Impact Paper that:¹⁴

New Zealand is the only country (with a modern competition law) without any direct consideration of the effects of unilateral conduct. In theory, given New Zealand's size and remoteness, any variation from the global standard of an effects-based test should require a very high level of proof of superior outcomes from an alternative approach.

Arguments Against

There were mixed submissions on the proposed law change and it is fair to say that there is a considerable degree of controversy around the need for the proposed change. Those opposed to the change support the status quo and argue that an effects test is likely to introduce uncertainty and ambiguity to everyday business decisions.

Other arguments include:¹⁵

1. There is little evidence of anti-competitive conduct going undeterred.
2. The current prohibition is predictable and easy for businesses to apply in their day-to-day decision-making.
3. Any reform would chill competition and investment by slowing down decision-making, increasing compliance costs, and introducing uncertainty and ambiguity.
4. Reform could result in pro-competitive conduct (such as price decreases as a result of efficiencies that lead to competitors exiting the market) being treated as breaches of the law.

However, the Minister rejected those concerns as over-stated and said that the costs and risks associated with the report are likely outweighed by the potential benefits.¹⁶

I note that the reform will mean that firms that may have market power will have to carefully consider a range of commercial conduct (such as competitors' access to key inputs and even rebate and discount arrangements). This may increase compliance and other costs for these firms. It is also may be difficult to ascertain whether there would be a substantial lessening of competition because this can often hinge on the definition of the relevant "market" at issue, whereas under the current test a firm has to

¹⁴ Hon. Kris Faafoi *Impact Statement: Review of Section 36 of the Commerce Act and other matters* (Ministry of Business, Innovation and Employment, February 18, 2020) at 15.

¹⁵ Hon. Kris Faafoi *Cabinet Paper: Review of Section 36 of the Commerce Act and other matters* (Ministry of Business, Innovation and Employment, February 18, 2020) at paragraph 29. <https://www.mbie.govt.nz/dmsdocument/11263-review-of-section-36-of-the-commerce-act-and-other-matters-policy-decisions-proactiverelase-pdf>.

¹⁶ Hon. Kris Faafoi *Cabinet Paper: Review of Section 36 of the Commerce Act and other matters* (Ministry of Business, Innovation and Employment, February 18, 2020) at 5-6. <https://www.mbie.govt.nz/dmsdocument/11263-review-of-section-36-of-the-commerce-act-and-other-matters-policy-decisions-proactiverelase-pdf>.

ask itself whether it would do the same thing in a competitive market.

However, the competition assessment is not a test that should be unfamiliar to firms, particularly those with market power, because it is currently used in other provisions of the Commerce Act, and all contracts, arrangements and understandings have to be

assessed through the same lens. Therefore, I agree with the Minister that these concerns appear to be overstated.

The introduction of an effects test into Section 36 of the Commerce Act is a welcome reform, in light of the real and perceived issues with enforcement of the current provision.