Chapman Tripp
Barristers & Solicitors NEW ZEALAND

PARTNERS, PRINCIPALS AND CONSULTANTS

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| D S Alderslade | M N Berry◊ | P J England | J C Holden⋆ | A J Keenan | H C McQueen | D M M Ross | A J Wilkinson⋆ |
| L M Alexander⋆ | H M Bowie | M A Gilbert | J L Holland | J A Knight⋆ | A R McRae | W A Sandston | T G R Williams |
| G S Anderson⋆ | A J Brewer⋆ | T C Gould◊ | L C Holley⋆ | A F Lester⋆ | F Miller | B A Scott | R J Wilson |
| M G Anderson | B J Brown | N E Gray◊ | F L Howard⋆ | S B Lowe | P W O'Regan | J G M Shirtcliffe | M W Woodbury⋆ |
| J M Appleyard | S Brown⋆ | J P Greenwood | E C Huston⋆ | B L McArthur | R I Parker | J G Sproat | A N C Woods⋆ |
| M D Arthur⋆ | R A Bycroft | B G Hall⋆ | B H W Hutchinson◊ | R K Macdonald | L J Partridge⋆ | D J Stock | M E Yarnell |
| J S Baguley⋆ | D J Cochrane | J J Hassan | P R Jagose | A G McDonald | A S G Poole | C J Street | A W Young |
| P A Barnett^ | K M Daly◊ | L I Hinton | S M Janissen | J A McKay | P M Reese | W J Strowger | C D L Young⋆ |
| R J Beech | G W David | J E Hodder | M D Jonas | P A McLeod◊ | R J Roche | R F Wallis | |
| P W Bennett | C M Elliffe | S A Hodge | L Jones | F D McLaughlin | A S Ross | J M Warnock⋆^ | |

*Principals and Consultants do not share Partners' liabilities for the firm.* ⋆*Principals* ◊*Consultants* ^*Notary Public*

Chapman Tripp Sheffield Young. 1-13 Grey St, PO Box 993, Wellington, New Zealand.
Telephone 64-4-499 5999. Facsimile 64-4-472 7111. DX SP20204. www.chapmantripp.com

*Our ref:* Grant David
*Direct dial:* 64-4-498 4908
*E-mail:* grant.david@chapmantripp.com

**6 August 2002**

The Secretary
Trade Practices Review Committee
C/- Department of the Treasury
Langton Crescent
PARKES ACT 2600
AUSTRALIA
Email: TPAReview@treasury.gov.au
Facsimile: 00 61 2 6263 3939

## THE NEW ZEALAND EXPERIENCE

1 I am a partner in the New Zealand law firm Chapman Tripp, and am convenor of that firm's national competition law practice group. I am also a member of the Commercial and Business Law Committee of the New Zealand Law Society. However, the views that I express in this letter and the attached paper are expressed in a purely personal capacity and should not be attributed to either my firm or the New Zealand Law Society.

2 As partner of this firm since 1989, I have concentrated on mergers and acquisitions and, in particular, the application of competition law to such arrangements. I have been counsel to a number of successful applicants under the New Zealand Commerce Act seeking clearance or authorisation of mergers and acquisitions, as well as to successful applicants for authorisation of restrictive trade practices. Those mergers and acquisitions in which I have been involved that have had substantial trans-Tasman aspects include:

- BHP in its acquisition of New Zealand Steel;
- HJ Heinz Company in its acquisition of Wattie's Limited;
- News Limited in its acquisition of Ansett New Zealand and other acquisitions;
- Elders IXL in its acquisition of the then New Zealand Forest Products.

3 In 2000 I was counsel to Shell Exploration Company in its acquisition of Fletcher Challenge Energy (being the largest acquisition in monetary terms ever carried out in New Zealand); and, the previous year, was counsel to the New Zealand dairy industry in the attempted "mega merger" of New Zealand Dairy Board and the major co-operative dairy companies.

4 Before joining Chapman Tripp I had three years' experience as a senior manager with the then New Zealand Department of Trade and Industry, being the government department responsible for the administration of the Commerce Act 1986. My time there included a three month secondment with the then Australian Trade Practices Commission immediately prior to the coming into force here of that legislation. During my time with the TPC I studied the TPC's procedures and participated in its investigation of several merger proposals.

5 Upon returning to New Zealand, I took up a senior role with the reconstituted Commerce Commission. My initial responsibility was to prepare the Commission's first procedural manual under the then new (and substantially changed) legislation, using the benefit of my Australian experience. I then led several of the Commission's initial investigations of mergers and acquisitions under the new regime, including *Magnum/DB*, being the first major decision in which the Commission set out and applied the new "dominance" threshold.

6 More recently, I was counsel to the last unsuccessful applicant under the "dominance" threshold before our law changed again in May 2001; and was counsel to three of the first four successful applicants under the "substantial lessening of competition" threshold which replaced it.

*continued*

7 All that is a very lengthy way of saying that I have considerable first hand experience with the administration, enforcement and application of the New Zealand Commerce Act - from the perspective of both the body which must apply it and many of the major firms to which it is applied. Consequently, I have a fair understanding whence both our substantive law and the Commerce Commission's procedures derive.

8 Last weekend I addressed the Thirteenth Annual Workshop of the Competition and Law Policy Institute of New Zealand. That workshop included a number of Australian speakers who were commenting on both the Australian merger experience and the recent changes to the New Zealand Commerce Act.

9 I presented a paper in which I suggested that the significant - but mostly procedural - differences that still exist between the merger regime under the Australian Trade Practices Act and the merger regime under the Commerce Act may go some way to addressing some of the issues before the Trade Practices Review Committee. In this regard, I should stress that my understanding of those issues derives solely from my reading of the submissions which the Committee has received and/or media reports of those submissions. In particular, I am not in a position to either concur or disagree with the criticisms that have been made of the ACCC, as I do not have sufficiently detailed current experience of the Australian Trade Practices Act or the ACCC's enforcement of it.

10 However, I do have considerable experience of the New Zealand Commerce Act and its administration and enforcement by the Commerce Commission. Those are the matters that I have endeavoured to set out in my paper.

11 I forward a copy of the paper which I presented to the workshop to the Committee for its consideration. Doing so, I should stress that I have no direct interest in the outcome of Committee's deliberations. My comments are those of a detached observer.

12 You will see that the conclusion I reach is that a number of the concerns that have been addressed to the Committee in submissions have not arisen – and, in my view, are unlikely to arise – in the New Zealand context because of the quite different processes that the Commerce

*continued*

Commission has developed. There are historical, policy and practical reasons for those differences.

13 I am certainly not advocating that the Committee recommend the uncritical adoption of the Commerce Commission's processes. But I do think that, especially in relation to a formal clearance mechanism, transparency of decision making, greater detachment of Commission Members from applicants, more limited scope of undertakings, and restricted appeal rights, there may be some elements of the procedures developed in New Zealand that warrant your consideration.

14 I would be happy to respond to any questions that the Committee may have, or to give my more detailed comments on any aspect, if that would assist the Committee in its task.

*Yours faithfully*

Grant David
*Partner*

*continued*

## THE NEW ZEALAND MERGER EXPERIENCE – LESSONS FOR AUSTRALIA?

### Introduction

1 The publicity surrounding the Dawson Committee and the 147 submissions it has received to date has been fascinating for all those in New Zealand with an interest in competition law. And more than a little disconcerting.

2 As all will be aware, a major feature of the Commerce Amendment Act 2001 was to substitute a new business acquisitions test in section 47 of the principal Act. That is, the previous prohibition on the acquisition of assets of a business or shares which would, or would be likely to, result in any person acquiring or strengthening a dominant position in a market (the "dominance" test) was replaced by a "substantial lessening of competition" test. Section 47(1) now reads:

> *A person must not acquire assets of a business or shares if the acquisition would have, or would be likely to have, the effect of substantially lessening competition in a market.*

3 This is effectively the same test as is applied in section 50 of the Australian Trade Practices Act 1974, subject to any differences which the express inclusion of the matters set out in section 50(3) of the Australian legislation, which has no New Zealand equivalent, may import. That similarity, of course, is not co-incidental. Among the reasons given by the government and its advisors for the new threshold were the perceived advantages in bringing the New Zealand legislation – especially the merger regime – more closely into line with Australia. The Minister of Commerce, in his Second Reading speech on the Amendment, said:

> *…the prohibition against anti-competitive mergers in Section 47 is amended to adopt the equivalent Australian provisions. Merger and business acquisitions that substantially lessen the competition will be prohibited. However, the Commerce Commission will retain the ability to authorise mergers if the public benefit outweighs any anti-competitive detriment. The adoption of the Australian model has a number of advantages:*
>
> - *it results in domestic competition policy being more closely aligned with international best practice and the approach taken by almost all OECD countries;*

- *it will reduce transaction costs to business by spreading the cost of testing the limits of competition policy across market participants in New Zealand and Australia; and*

- *in addition, it will increase the level of certainty as to the interpretation of the legislation. The Commerce Commission will be able to adopt tested analytical frameworks and apply them to the New Zealand situation."*

4 The fact that New Zealand showed so much apparent enthusiasm to adopt an Australian model which itself has so soon after been subject to so much criticism, gives cause for concern. For three reasons. First, we may have adopted a model which, to those most familiar with its workings, seemingly now is perceived to be seriously flawed.

5 Second, if the findings of the Dawson Committee do result in significant changes being made to the Australian statutory test and/or procedure, those changes will have to be considered in this jurisdiction, too – raising the prospect of more substantial change. And, as the Minister rightly pointed out in the above speech, the best competition law is one that promotes certainty and enables predictability.

6 Third, to make best possible use of the focus on competition as a means of co-ordinating commercial activity requires the confidence of the community – especially the business community. That needs a carefully thought-out legal framework, in which both the existing and past legal rules are free from grave defects. In short, the risks and costs associated with bad laws and biased institutions must be seen to be minimised.

7 The current widespread criticism in Australia of the Trade Practices Act and its enforcement body, the ACCC, following so soon after the policymaker inspired criticism here of our former dominance regime, must carry a real risk of bringing the whole concept of competition law into disrepute.

**So what's wrong with the Australian regime?**

8 I shall not pretend to pre-empt, or predict, the findings of the Dawson Committee. But I set out below some of the criticisms it has heard that are relevant to the current mergers regime:

- proper governance of the ACCC is required. Various firms and organisations have proposed the establishment of a Charter of Competition Regulation and a Board of Competition to guide the

development and implementation of the legislation. This Board would comprise individuals with an expertise in economics and law, including persons drawn from the business community as a whole. The Board could also receive complaints about the ACCC and provide an annual report to Parliament reviewing the operation of the ACCC and any major complaints received during each year. The appointment of an Inspector-General of Competition to investigate complaints about the ACCC has also been suggested;

- many submissions call for a code of practice limiting the ACCC's use of media and the "trial-by-media" approach that has emerged in the daily operation of the ACCC;

- increased accountability of the ACCC is required. The Trade Practices Act should provide clear guidance as to the proper principles to be followed when applying the Act. The ACCC should be required to give substantial reasons for its decisions to clear or oppose merger or acquisition proposals;

- various submissions recommend that section 50 provide expressly for an exception where the public benefits (including efficiency gains, export potential, import replacement and international competitiveness) of an acquisition would, or are likely to, outweigh any public detriment. Specifically, the section 50(3) list of matters to be taken into account should include considerations such as efficiency gains, impact on Australian jobs and failing companies;

- Shell Australia wants increased efficiency of the authorisation process for mergers and acquisitions. Specifically, Shell argues that the Government should raise the threshold for determining when parties are sufficiently interested to appeal an ACCC decision to grant an authorisation. The current threshold is seen to significantly prolong the process. While all interested parties should retain a full opportunity to put their points to the ACCC during its hearing of an authorisation application, the only parties permitted to appeal should be those parties directly involved in the merger itself;

- some submissions propose that merger proponents be able to elect to take applications directly to the Australian Competition Tribunal. Alternatively, an independent Competition Panel, similar to the successful Takeovers Panel, is proposed to arbitrate disputed merger or acquisition proposals;

- more checks and balances are needed on ACCC powers. In particular, the Trade Practices Act should provide greater certainty in relation to the ACCC's ability to receive undertakings.

**But the New Zealand regime is still different**

9 Despite New Zealand's adoption of the substantial lessening of competition test, there are still significant differences between the merger regime under the Australian Trade Practices Act and the merger regime under the Commerce Act. Briefly, they are:

- there is no formal clearance mechanism under the Trade Practices Act, simply an informal review facility and an authorisation mechanism that has very seldom been used;

- parties approach the ACCC seeking its view of a specific merger proposal whereas under the New Zealand regime clearance or authorisation may be sought well in advance of any specific agreement having been reached;

- parties are able to, and generally do, approach the ACCC on a confidential basis, in which case the ACCC is not able to seek the views of other interested parties. While in theory the Commerce Commission is able to grant confidentiality as to the fact of a proposal notified to it, in practice it is very unlikely to be sufficiently satisfied to give clearance or grant authorisation without the proposal being in the public domain and the views of interested parties being sought;

- if satisfied that a proposed merger will not breach section 50, the ACCC simply informs the parties that it does not propose to take any action at that time. If it receives further information or circumstances change, however, it may do so subsequently. In any event, third parties (with standing) are not precluded from challenging the merger unless formal authorisation has been obtained. By contrast, a clearance or authorisation from the Commerce Commission endures for twelve months from the date it is given despite changed market conditions and immunises the merger from all challenge under section 47 (and section 27) so long as it is in force;

- the ACCC frequently negotiates undertakings from the merger parties which may be either behavioural (for example, promised access or pricing) or structural in nature. The Commerce Commission is limited by statute to undertakings to divest assets or shares;

- as indicated above, section 50(3) of the Trade Practices Act sets out an extensive list of factors to which the ACCC must have regard in considering whether there is a substantial lessening of competition. Section 47 of the Commerce Act contains no such list, meaning the Commerce Commission must rely on precedent;

- section 50 of the Trade Practices Act focuses solely on the effect of the merger on the competitive process, rather than the resulting market position of the merged entity. Section 47 now combines these two concepts by adopting the substantially lessening competition threshold (focusing on movement) in section 47(1), but expressly retaining the interconnected and associated person extensions (focusing on status) under section 47(2);

- the declared purpose of the legislation – and thus the respective merger regimes – now is different in the two jurisdictions. The object of the Australian Trade Practices Act is still *to enhance the welfare of Australians through the promotion of competition …* . In contrast, since last year's Amendment the overriding purpose of the Commerce Act has been *to promote competition in markets for the long-term benefit of consumers within New Zealand.* It is an open question as to how New Zealand courts will apply this new "deferred consumer interest" approach.

**Why those differences matter**

10 It is readily apparent that there is a correlation between some of the criticisms heard by the Dawson Committee and the differences between the two regimes. I have endeavoured to identify the cross-overs, below:

**Proper process**

11 Section 66 of the Commerce Act prescribes a detailed procedure for seeking clearance, and section 67 sets out an even more detailed procedure for seeking authorisation, by applying appropriate provisions of section 60, which prescribes the process for applying for authorisation of restrictive trade practices. Additional procedural requirements, specific to merger applications, are set out in section 68. In particular:

- the application must be in the form prescribed by the Commission;

- the Commission must formally register receipt of every complying notice seeking clearance or authorisation;

- there is a process for rejecting non-complying applications;

- the applicant must furnish such further documents and information as the Commission may require;

- the Commission may consult with any person who it thinks is able to assist it;

- the Commission may only give a clearance or grant an authorisation if it is satisfied that the relevant statutory test is met;

- the Commission must state in writing its reasons for its determination;

- the Commission must make its determination within the prescribed time.

**Transparency**

12 The Commerce Commission not only registers all complying notices seeking clearance or authorisation (except those few granted interim confidentiality as to fact), but also makes a brief press statement to the effect that it has received the notice on the day it is registered. The details on the public register together with that press statement then are available on the Adjudication Section of the Commission's website. A public version of the notice itself, from which market sensitive information in respect of which confidentiality has been granted is excluded, is available from the Commission on application.

13 Similarly, the Commission's determination is recorded on the register; and a press statement setting out the fact of the determination, together with brief reasons, is made on the day that the determination is made. The written decision of the Commission, setting out the detailed findings of the Commission's investigation and reasoning, is subsequently available from the Commission on request. Pressure of work sometimes means that there will be a one or two week delay between determination and decision. While such delay is unfortunate, and can disadvantage those seeking to exercise appeal rights or make a new, modified application, it is nothing like the delay that can be experienced with other judicial bodies.

14 In terms of content, the Commission's press release may be described as factual and restrained. Prior to determination there is no comment on the merits or otherwise of a proposal; and after determination, the comment is generally confined to the findings and reasoning as set out in the decision.

**Access to Commission Members**

15 While the Chairman of the Commerce Commission operates a relatively "open door" for those contemplating an acquisition for which clearance or authorisation may be sought, and will be helpful in pointing out potential areas of concern to the Commission, that door closes firmly as soon as the Commission receives a formal application.

16 Further, the Commission adheres strictly to its view that the framing of any application –including, importantly, the formulation of any divestment undertaking that the proposal may include – is a matter for the applicant and its advisers.

17 Once an application has been received and registered, Members of the Commission meet with those Commission officers who will be investigating the proposal, but there is no direct interface between Commission Members and the applicant or other interested parties. The clearance/authorisation process is not intended to be adversarial – rather the Commerce Act contemplates that there will be an interactive attempt by the applicant and the Commission to identify, assess and, if necessary, ameliorate by divestment or otherwise, any competition concerns that are seen in the course of the investigation to arise in markets affected by virtue of the proposed acquisition.

**Other parties**

18 Of course, in most cases the Commission will also receive the views of other parties. While many of those persons will be able to assist the Commission in disinterested fashion, some will have a commercial or strategic interest in preventing the acquisition, either in its entirety or by forcing the divestiture of an asset in which they have a keen interest. However, the clearance/authorisation process does not – or should not – require the applicant, or the Commission itself, to engage in a protracted debate of the issues with any person whose views the Commission may have sought on the application, or whose views may have been volunteered to he Commission. That was made clear in *Foodstuffs (Wellington) Co-operative Society Limited* v *Commerce Commission* 4TCLR 713, 721-722 where the High Court said:

> *The Commission is an investigative body which has the function of inquiring into and deciding the matter before it. It is not a strictly adversarial procedure – there may be no opposing parties – but it is necessary at all times to consider the general public community interests. In the end, the Commission has to be brought to the point where it is satisfied, that it is more probable than not, that as a result*

> *of the acquisition a person would not be or be likely to be in a dominant position or have that position strengthened …*

19 While the Commission may have regard to accurate factual material, or views expressed by interested persons on relevant matters, in discharging its obligation to determine community interests, it is not required to engage in a lengthy testing of those views – especially where they comprise assertion rather than fact. The observations by the English Court of Appeal on the discretion of the Monopolies & Mergers Commission, in terms of the United Kingdom Fair Trading Act 1973, as set out in the *R v Monopolies Commission* [1986] 2 All ER 257 at 266 (cited with approval by New Zealand High Court in *Broadcast Communications Limited* v *Commerce Commission* 4 TCLR 537) are especially pertinent in this regard:

> *Good public administration is concerned with the speed of decision, particularly in the financial field …*
>
> *Good public administration requires a proper consideration of the legitimate interests of individual citizens, however rich and powerful they may be and whether they are natural or juridical persons. But in judging the relevance of an interest, however legitimate, regard has to be had to the purpose of the administrative process concerned. Argyll has a strong and legitimate purpose in putting Guinness in baulk, but this is not the purpose of the administrative process under the 1973 Act. To that extent their interest is not therefore of any great, or possibly any, weight.*

20 Although the clearance/authorisation process may not be adversarial, the Commission is, of course, always mindful that its process and determination may be subject to judicial review and, in some cases, appeal. But, while it must deal with an application in an effective and fair manner, it must also do so as expeditiously as possible. The fact that section 66(3) and section 67(3) prescribe strict time limits – which were deliberately left unchanged by last year's Amendment – gives rise to fair expectation that those limits generally will be complied with.

21 In many instances the timing problem is compounded by opposing parties seeking confidentiality in respect of much or all the information they have provided, or assertions they have made, to the Commission.

22 In practice, the Commission responds to those competing tensions – namely, fairness v. expedition – by simply providing the applicant with a

summary of the issues raised, and inviting the applicant's response to those issues. The shortcoming of this process is that its effectiveness depends very much on the ability of the individual Commission officer to identify the issues that are relevant to the statutory criteria which the Commission Members themselves must apply, and the likely weight that they will give those issues.

23 Despite the specificity of those criteria – that is, no effect of substantially lessening competition for clearance, and such a benefit to the public that it should be allowed for authorisation – the Commission frequently receives submissions or views that relate to matters which either predate or are not affected (or exacerbated) by the proposal itself. The Commission needs to be constantly vigilant that those other parties from whom it hears may be seeking to use its investigation process as an opportunity to remedy extant commercial difficulties or other underlying problems in the industry that would persist with or without the proposed merger. And such vigilance, to be effective, may require substantial experience of the particular industry on the part of the Commission officer.

24 In this regard, it is appropriate to recall the words of Richardson J. in *Telecom v Commerce Commission* [1992] NZLR at 446, to the effect that:

> *…pure speculation as to the impact of [behavioural] constraints and simple intuition are no substitute for hard data drawn from empirical studies and evidence from participants in the industry. In the end, the [Commission's] value judgment should be as informed by practical evidence as possible.*

**Undertakings**

25 It is perhaps in the area of undertakings that the Commerce Commission's powers – and resulting practice – diverge most from the ACCC's.

26 Under section 87B of the Trade Practices Act, the ACCC *may accept a written undertaking given by a person for the purposes of this section in connection with a matter in relation to which the Commission has a power or function under this Act ….* The ACCC maintains a register of section 87B undertakings, which is available on its website.

27 As to the ACCC's policy in accepting such undertakings in relation to mergers, this is set out in detail in paragraphs 7.1 to 7.15 of the ACCC's *Merger Guidelines.* To quote from the *Guidelines*:

> *7.6 The Commission is likely to look most favourably on proposed undertakings which are able to address structural issues in the relevant market(s). Structural solutions provide an ongoing basis for the operation of competitive markets. The regulatory costs are one-off rather than a permanent burden …*
>
> *7.9 The Commission is not likely to favour behavioural undertakings such as price, output, quality and/or service guarantees and obligations. Such undertakings may well interfere with the ongoing competitive process through their inflexibility and unresponsiveness to market changes. The duration of such undertakings is also highly problematic …*
>
> *7.10 In addition, such undertakings gives substantial regulatory difficulties. They are extremely difficult to make certain and workable in detail, particularly in the short time frames in which mergers are considered, they require continuing monitoring, and where breaches are detected they are often dependent on enforcement after the event. There is also likely to be substantial associated costs to the Commission of compliance and enforcement.*

28 Nevertheless, the *Guidelines* go on to say that there will be some circumstances in which behavioural undertakings may be acceptable in relation to mergers:

> *7.11 A vertical merger may involve the integration of a party in a competitive market with the party which has a natural monopoly, for example a gas pipeline. This will usually raise concerns about access, access pricing and protection of confidential information. In some cases the Commission's concerns may be able to be addressed by way of quasi-structural undertakings like ring-fencing and access undertakings. For example, in considering a number of port privatisations the Commission has accepted undertakings regarding non-discriminatory access …*
>
> *7.13 When considering applications for authorisation of a proposed merger the Commission may consider proposed undertakings which address the balance between public benefit and detriment, particularly the anti-competitive detriment. Again the Commission prefers structural*

> *remedies, but where these are not feasible it may consider proposals for behavioural undertaking, taking account of regulatory costs and balancing the likely public benefit and detriment.*

29 Some recent examples of the kinds of behavioural undertaking accepted by the ACCC in relation to section 50 of the Trade Practices Act, as recorded on its website, are attached as Appendix A. To the New Zealand competition lawyer, some of those undertakings take on the appearance of an industry specific regulatory or pricing regime. Certainly, their frequency and wide-ranging nature bear scant regard to the cautious, exceptional approach described in the *Guidelines*.

30 The New Zealand position with regard to undertakings has been quite clear, and in stark contrast, at least since the 1990 Amendment came into effect. Section 69A(2) provides expressly that the Commerce Commission shall not accept an undertaking in relation to the clearance or authorisation other than an undertaking given under subsection (1) of that section. Section 69A(1) provides that the Commission may accept a written undertaking given by or on behalf of the person seeking clearance or authorisation *… to dispose of assets or shares specified in the undertaking*.

31 Section 69A was inserted to make it clear that such "structural" undertakings were the only undertakings that might be given. In particular, undertakings which relate to future conduct were precluded.

32 Prior to the 1990 Amendment, the Commerce Act did not specifically provide for the Commerce Commission to impose conditions or accept undertakings in relation to mergers or takeovers. However, in *Goodman Fielder Limited* and *Watties Industries Limited* v *Commerce Commission* [1987] 2 NZLR 10 the Court of Appeal found that a merger proposal could include undertakings in relation to the sale or divestment of assets or shares as an integral part of the proposal. While the Court's decision clarified the position regarding structural undertakings, it did not deal with the enforcement of such undertakings or the issue of whether more wide-ranging undertakings would be allowed. To obviate the suggestion that the Court's decision opened the way for behavioural undertakings under the still new Commerce Act, section 69A was inserted by the first substantial amendment.

33 The thinking of the policy-makers then was that Part II of the Commerce Act provides a statutory code for controlling anti-competitive behaviour and

it was inappropriate that additional requirements above those generally provided in Part II should be imposed contractually in the merger context. For that reason, undertakings were expressly limited to those for the sale or disposal of assets or shares of the parties to the particular merger.

34 That restriction on the power to accept undertakings did not pass without criticism. The Hon Philip Burdon speaking on the introduction of the Bill said that the Opposition perceived section 69A *as restricting the ability of the Commerce Commission to achieve agreed settlements between two disputing parties*. *We believe it is important that the Commerce Commission be in a position to achieve an agreement out of court between the parties at dispute.*

35 My own criticism of behavioural undertakings is a pragmatic one. Namely, they have a tendency to endure well beyond the particular concern to which they relate and, as a matter of practice, are likely to be unenforceable. For example, there are good arguments that the access to saleyards undertaking accepted by the previous Commerce Commission in 1986 in its last decision under the Commerce Act 1975, *Wrightson/Dalgety*, is still extant but possibly not enforceable.

36 Whatever the rationale, since 1990 an applicant for clearance or authorisation has had to confine their undertakings to a disposal of assets or shares that will arguably mitigate the adverse competition consequences. Examples of such divestment undertakings range from individual radio licences to interests in entire gas fields. But, they are all very specific; and their performance readily measurable.

37 That said, however, there is some scope for ingenuity. For example, the term “assets” is defined to include intangible assets, which includes contractual obligations. So, it may be open to an applicant for clearance or authorisation to effectively restrict its future behaviour by way of contract with another party and then divest its rights but not its obligations under that contract.

38 But, such ingenuity has its limitations. As a general rule, the behavioural constraints to which the Commerce Commission will have regard are confined to those set out in Part II of the Act. And merger parties are restricted to promising to divest those structural assets which they have or control. That imposes considerable limitation on the scope that the applicant and the Commerce Commission have to “negotiate” an agreed solution. Especially, given the Commission’s strict policy that the applicant

must itself define its own application, including any divestment undertaking.

39 At the same time, this approach effectively prevents the Commerce Commission from seeking to create its own industry specific regulation or price control regime additional to those imposed by the legislature.

**Authorisation**

40 While the more public, and more protracted, nature of the authorisation process (as opposed to the clearance process) has meant that authorisation is far less frequently sought, it is not virtually unknown in New Zealand. Attached as Appendix B is a list of the merger authorisation applications from the past 10 years of which I am aware. Indeed, I was counsel for the applicant in four of them.

41 Of those 12 applications, half were successful, three were declined and three were withdrawn prior to final determination.

42 The prospect of a public conference, the attendant publicity, the need to employ economic experts to identify and assess public benefits, and the ongoing impost on senior executive time are all deterrents to more applicants taking the authorisation route. But, it is there; it is always contemplated in difficult cases; and it is sometimes used - sometimes successfully.

43 The authorisation process is in binary by nature. That is, it involves an assessment of competition concerns, then an assessment and weighing of "countervailing" public benefits. Nevertheless, the advent of the substantial lessening of a competition test for mergers in section 47 does now allow for some consideration of pro-competitive efficiency resulting from the merger, in cases not involving authorisation.

44 It had been judicially recognised, as long ago as *Fisher & Paykel* v *Commerce Commission* [1991] 1 NZLR 569, that, in assessing "substantial lessening of competition", a net approach to assessing anti-competitive effects was required. That net approach now has been imported into section 47 by the new test.

45 That significant change is recognised in the *Business Acquisitions Guidelines* issued last year by the Commerce Commission, as follows:

> *The Commission recognises that while efficiencies are often best considered in the context of a business acquisition authorisation,*

> *there may be circumstances where they are also relevant to an application for clearance. In the context of a business acquisition, the combined entity might be able to make efficiency gains that are not obtainable by other means, such that its unit cost of production would decline. It is conceivable that this could result in the entity reducing its price below that obtaining prior to the acquisition, even though with the acquisition it would otherwise be considered to have substantially lessened the competition, and would be able to raise price above costs. In these circumstances, the acquisition could be regarded as having a "pro-competitive" effect overall, as the lower price would serve to enhance the constraint of the unilateral behaviour of other firms in the market, that might undermine the propensity for co-ordinated conduct to be sustained.*

46 Such recognition goes some way to opening the door for "efficiency based" arguments in the clearance context, as some submissions to the Dawson Committee seek. For example, it could be argued that although a merged entity may have more market share initially, the merger itself will trigger significant structural change in the industry – perhaps through the entry of a new player taking up a divestment. Thus, focusing on net movement rather than status as section 47 now requires, on balance the merger should be permitted.

47 Obviously, the boundaries of that argument have not yet been tested. But, it would be very disappointing to see the development of New Zealand precedent effectively curtailed by a pre-emptive amendment of section 50(3) of the Trade Practices Act. Especially one that has not been drafted against the backdrop of the reasoned Commission decision-making and judicial precedent that the New Zealand system allows for.

**Appeal rights**

48 There is frequent criticism that pre-merger control regimes are an example of regulation that is excessively burdensome in proportion to its benefits. That criticism applies especially to competition laws which require mergers to be notified to, vetted by, and approved by the relevant agency before proceeding. In such a regime too many mergers, especially those that ultimately would be approved, may well be defeated simply by passage of time.

49 To minimise such risk, the Commerce Act provides:

- that pre-notification is voluntary;

- strict time limits are imposed on the Commission by sections 66(3) and 67(3);

- there are restrictions on those parties who may appeal the Commerce Commission's decisions.

50 With regard to the last, section 92(c) provides that, in the case of an appeal against the determination of the Commission under section 66 or section 67, the only persons entitled to appeal are –

- the person who sought clearance or authorisation;

- any person whose assets, or shares in which, are proposed to be acquired;

- any person who participated in any conference held by the Commission in relation to the clearance or authorisation.

51 As further protection against the delays of process, section 95 expressly provides that, where an appeal is brought against the Commission's determination, that determination – that is, the clearance or authorisation – *shall remain in full force pending the determination of the appeal, unless the Court orders to the contrary*.

52 The adequacy of those protections against delay were tested – and found wanting – in the protracted litigation arising out of the Commerce Commission's determination in 1995 to give clearance to Telecom's proposed acquisition of Sky. Very unusually, the Commission had held a conference in relation to that clearance application, thereby giving appeal rights to Clear and other parties who had participated at the conference.

53 Clear and BellSouth filed appeals against the clearance, which would have remained in force regardless of appeal unless the High Court ordered otherwise. Three days later, the High Court did order a stay of the clearance. The dominant consideration in the Judge's view was not to render the appeal nugatory by allowing Telecom to proceed.

54 The Court of Appeal in *Telecom* v *Clear* [1992] 3 NZLR 429 dismissed Telecom's appeal, holding that an acquirer cannot expect a stay to be withheld simply because, commercially, it presents them with problems of choice – that is, abandoning the merger or awaiting resolution of the appeal. While the acquirer has a right to immediate benefit of the clearance, that right has to be read in context. The Court said that the

appropriate threshold test to apply when granting a stay is, at least, an arguable case. Beyond that, the prospects of success, so far as ascertainable, are simply a factor in the overall balance. Importantly, a stay supporting an appeal against clearance will not be automatically granted simply because the appeal would otherwise be rendered nugatory. However, it is a powerful consideration.

55 The language of that decision suggests that a stay will be granted in all those cases where, it seems, reasonable arguments can be raised at the appeal irrespective of the commercial consequences to the merger parties who have voluntarily submitted themselves to the clearance process. The practical effect of that decision – which reverses the literal wording of section 95 - has been to deter clearance applicants from agreeing to a conference; and, I suspect, the Commission from seeking one.

56 To the extent that the draft determination and conference process can be an effective forum for hearing contentious mergers, especially where efficiency based arguments or public benefits are raised, it is an area where there is scope for legislative clarification.

**Conclusion**

57 In summary, many of the criticisms received by the Dawson Committee seem to relate to the ACCC's processes, rather than the substantive law as contained in section 50 of the Trade Practices Act.

58 Further, it seems that at least some of those concerns have not arisen – and are unlikely to arise - in the New Zealand context because of the quite different processes that the Commerce Commission has developed and the New Zealand legislature has enshrined. The reasons for those differences are both historical and complex.

59 They could be traced, no doubt, by detailed analysis of the development of the Australian merger regime from the Swanson Committee onwards (after which the formal clearance procedure was removed) and comparing that development to the historical development of our own merger regime since the almost contemporaneous introduction of the first general merger control in this country by the Commerce Act 1975.

60 But, that is far too detailed a task for now. Ideally, however, someone should do it, before the Dawson Committee makes its recommendations.

61 And a fortiori, before anyone rushes to legislate again!

G. W. David
Partner
Chapman Tripp

## APPENDIX A

## Index - Section 50 Trade Practices Act 1974 behavioural undertakings

| | |
|---|---|
| 1. | Manildra Starches Pty Limited |
| 2. | AES Environmental Pty Limited |
| 3. | Wesfarmers Dalgety Limited / IAMA Limited |
| 4. | One Steel Limited / Smorgon Steel Group Limited |
| 5. | Ansett Holdings Limited |
| 6. | Gunns Limited |
| 7. | Qantas Airways Limited |
| 8. | Woolworths Limited |
| 9. | Dairy Farm Management Services Limited and Franklins Limited |
| 10. | PaperlinX Limited |
| 11. | Smorgon Steel Group Limited |

**Section 50 behavioural undertakings**

(The summaries below are taken from the ACCC's Public Register of s87B Trade Practices Act 1974 undertakings – http://www.accc.gov.au/pubreg/pubreg.htm)

1 **Manildra Starches Pty Limited and Shoalhaven Starches Pty Limited**
21/02/2002

The Manildra Group ("Manildra") proposed to acquire the business and certain assets of Weston Bioproducts and the Narrandera Flour Mill from George Weston Foods Ltd ("GWF") ("the proposed acquisition").

The Commission conducted market enquiries and examined submissions from the parties, and considered that it appeared that the proposed acquisition would have led to a substantial lessening of competition in the markets for starch and starch sugars in Australia. The main reasons for this were the Commission's concerns that the remaining alternative domestic supplier had limited manufacturing capacity; and that import competition was not expected to provide an effective constraint on starch and starch sugar prices in the foreseeable future.
The Commission therefore decided to oppose the proposed acquisition on the basis that it was likely to substantially lessen competition in breach of section 50.

Manildra then offered an enforceable undertaking to address the Commission's competition concerns. This undertaking requires Manildra to divest the Queensland and Western Australian plants of Weston Bioproducts in good working order and to provide the Commission with six monthly reports by an independent auditor on the starch and starch sugar industries including changes in Manildra's prices and costs for a period of 36 months.

The Commission considered that this undertaking would address its competition concerns and decided not to oppose the acquisition.

2 **AES Environmental Pty Limited**
7/02/2002

Undertaking provided by AES Environmental Pty Ltd in relation to its acquisition of the Clyde Apac Division of the Downer Group Limited. Under the terms of the undertaking, AES Environmental Pty Ltd will support

moves to harmonise Australian standards for laminar flow products with international standards.

3 **Wesfarmers Dalgety Limited / IAMA Limited**
7/02/2001

After conducting market inquiries, the ACCC determined that the proposed merger would not substantially lessen competition in the markets for the retailing of rural merchandise in Western Australia and the distribution of fertiliser in Western Australia on the basis that certain undertakings would be provided by Wesfarmers Dalgety and IAMA. The undertakings provide that Wesfarmers Dalgety and IAMA will sell one of two rural merchandise outlets that the new business will have in Esperance, Katanning, Merriden, Narrogin and Geraldton. The new business is required to sell in the first instance to another unaffiliated retailer of rural merchandise. The undertakings further provide that Wesfarmers Dalgety and IAMA in the next two years will take no steps to constrain the terms upon which the agents and affiliates of the new business will deal with fertiliser suppliers and will continue the existing distribution agreement between IAMA and Summit Fertilisers.

4 **OneSteel Limited and Smorgon Steel Group Limited**
16/02/01

Smorgon Steel Group Limited (SSG) and OneSteel Limited (OS) have provided the Commission with an undertaking in relation to their joint bid for Email Limited. The undertaking has been offered in response to competition concerns expressed by the Commission. The undertaking requires SSG and OS to divide certain Email assets between them and divest the remaining assets. It specifies the time period in which this must be achieved and what is to happen at the end of that time period. The undertaking also restricts the amount of information SSG and OS can share about the Email assets to be divided between them (ie OS may receive very limited information in relation to Email assets destined for SSG and vice versa), the establishment of independent management for certain Email assets and limits on the level of co-operation between the two companies in the joint bidding vehicle. It also specifies what action is required should the takeover offer result in less than total control of Email.

5 **Ansett Holdings Limited**

This undertaking relates to Ansett's takeover of Hazelton Airlines. The undertaking requires Ansett to make available up to 4000 slots pa at Sydney Airport to new entrants to the NSW regional airline market, limit the swapping of slots within the Ansett group and limit price rises on the Albury and Wagga routes.

6 **Gunns Limited**
23/03/01

Gunns Limited ('Gunns') have provided the Australian Competition and Consumer Commission with an undertaking in relation to its acquisition of North Forest Products. The undertaking requires Gunns to make certain pricing and cost information available for five years. The undertaking facilitates greater price transparency within the forestry industry and reduces information asymmetries that may exist between Gunns and private suppliers of hardwood logs.

7 **Qantas Airways Limited**
17/05/01

Qantas Airways Limited ("Qantas") and Impulse Airlines Holdings Limited ("Impulse") publicly announced a proposal to enter into a commercial arrangement on 1 May 2001. Qantas provided a draft submission to the ACCC on 2 May 2001. The parties argued that Impulse is a failing firm and would become insolvent on 14 May 2001. Therefore, the parties requested that the ACCC reach a view on whether the acquisition was likely to breach section 50 of the Act before 14 May 2001.

As part of its investigation of the proposed acquisition, the ACCC conducted market inquiries and submissions were sought from interested parties. The ACCC also engaged an auditor to analyse and report on Impulse's financial status.

On the basis of the information gathered during its market inquiries, the ACCC identified a number of areas of concern. In particular, the Commission was concerned that the acquisition of Impulse by Qantas would:

- Preclude new entry into domestic aviation services. The ACCC was particularly concerned that any new entrant airline into the Australian aviation industry would be unable to access scarce takeoff and landing slots at Sydney Airport. Currently, there are severe slot constraints in the peak time periods of 7 am to 9 am,

and 5 pm to 7 pm. The ability of new competitors to access slots during these periods represents a substantial barrier to entering domestic air services in Australia and in particular, the high yield Sydney-Melbourne route.

- The ACCC was also concerned that a new entrant could not access the multi user domestic terminal at Sydney Airport.

- Result in an increase in the price of fares on those routes currently operated only by Qantas and Impulse. Routes of this type are primarily regional NSW routes.

The undertakings accepted from Qantas address the ACCC's concerns by including assurances on:

- The requirement for Qantas to make available to Virgin Blue up to a total of 12 slots during the morning and afternoon peak periods, each weekday, in order to provide Sydney-Melbourne services. This represents almost 60% of Impulse's slots in these peak periods.

In the event that Virgin Blue withdrew from the Australian airline industry as an independent entity, Qantas will be required to make available to a new entrant on interstate trunk routes up to 16 slots during the morning and afternoon peak periods each weekday. This represents almost 80% of Impulse's slots in these peak periods.

The undertaking by Qantas to make a significant proportion of Impulse's slots in these periods available to Virgin Blue or new entrants was fundamental to satisfying the ACCC's concerns.

- The requirement that Qantas will facilitate access to terminal space at the multi user domestic terminal at Sydney Airport to a new entrant airline.

- Restrictions on air fare increases on those routes currently operated only by Qantas and Impulse.

The Commission was also concerned about the possible reduction in the number of services to Tasmania. The Commission welcomed the commitment made by Qantas to the Tasmanian Government regarding the maintenance of services to Tasmania.

After taking into consideration the undertakings provided by Qantas, the ACCC considered that any anti-competitive detriment caused by the Qantas merger with Impulse will be minimised. Under these circumstances, the ACCC decided not to oppose the proposed merger.

8 **Woolworths Limited**
07/06/01

The undertakings determine and limit:

- What Franklins stores Woolworths may acquire; Limit Woolworths use of Franklins brands;
- Prevent Woolworths from interfering in the JIDA process; Require divestiture of certain stores;
- Require acts in relation to other existing and proposed stores;
- and require the fulfilment of obligations to facilitate the sale of Franklins stores in accordance with a package accepted by the Commission.

9 **Dairy Farm Management Services Limited and Franklins Limited**
05/06/01

The undertakings detail:

- the sale of Franklins stores;
- limits on stores to be sold to Woolworths;
- limits on Woolworths' use of Franklins product brands;
- and obligations to facilitate the sale of Franklins stores to independent operators.

10 **PaperlinX Limited**
28/5/2002

On 17 January 2002, the ACCC accepted Court-enforceable undertakings from PaperlinX Limited. The undertakings address the ACCC's competition concerns regarding the proposed acquisition by PaperlinX of the shares in Spicers Paper Limited not already owned by PaperlinX. Prior

to the proposed acquisition, PaperlinX owned approximately 42% of the shares in Spicers.

The undertakings provide for the divestiture of both the Edwards Dunlop and Commonwealth Paper Company paper merchant businesses which operated within the Spicers group. The divestiture of these businesses was completed in September 2001.

In addition, the undertakings provide for:

- the use of a major brand name by the divested entity;
- conditions relating to the supply of fine paper products manufactured by PaperlinX to the divested entity for 3 years from the date of divestiture;
- and the process that PaperlinX is required to follow should it seek to make an “anti-dumping” application under Part XVB, Division 2 of the Customs Act 1901 in the 3 years from the date of the divestiture (refer to Clause 3.1).

11 **Smorgon Steel Group Ltd**
23/02/00

Smorgon has undertaken to supply foundry grades of ferrous scrap to foundries in Queensland and New South Wales at prices reflecting no greater premium over prices for standard grades of ferrous scrap, than the premium paid by Metalcorp's customers in Queensland and New South Wales in 1998 and 1999. the sale.

The following lists Commerce Commission s67 authorisation decisions in the years 2002 to 1991 (inclusive)

| Decision No. | Transferee(s)/Applicant(s) | Transferor(s) | Draft Determination | Conference | Result |
|---|---|---|---|---|---|
| 410 | Ruapehu Alpine Lifts Limited | Turoa Ski Resort Limited | 28 August 2000 | 18 to 20 October 2000 | Successful |
| 393 | Teamtalk Limited | Telecom New Zealand Limited | 24 March 2000 | 3 May 2000 | Successful |
| | Newco | New Zealand Dairy Board, Kaikoura Co-op, Kiwi Co-op, Marlborough Cheese Co-op, New Zealand Co-op Dairy, Northland Co-op, South Island Dairy Co-op, Tasman Milk Products, Tatua Co-op and Westland Co-op | 27 August 1999 | | Withdrawn 29 October 1999 |
| | Kiwi Co-operative Dairies Limited | South Island Dairy Co-operative Limited | 30 March 1999 | | Withdrawn 30 April 1999 |
| 302 | Powerco Limited (Pukeariki Holdings Limited) | Egmont Electricity Limited (South Taranaki District Council) | 20 May 1997 | 30 June 1997 and 31 July 1997 | Successful |
| 279 | Ravensdown Corporation Limited | SouthFert Limited | 8 May 1996 | 5 to 7 June 1996 | Unsuccessful |
| 278 | Air New Zealand Limited | Ansett Holdings Limited | 26 January 1996 | 12 to 15 March 1996 | Unsuccessful |
| | Enerco NZ Limited | Capital Power Limited | 14 October 1994 | | Withdrawn (Media statement 1 November 1994) |
| 272 | Enerco NZ Limited | Progas Systems Limited | 3 December 1993 | | Successful |
| 270 | Natural Gas Corporation of NZ Limited (Fletcher Challenge Limited) | Enerco NZ Limited | 27 September 1993 | 27 to 29 October 1993 | Unsuccessful |
| 269 | Natural Gas Corporation of NZ Limited | Wanganui Gas Limited (to be formed) (Wanganui District Council) | 23 September 1992 | | Successful |
| 267 | Kiwi Co-operative Dairies Limited | Moa-Nui Co-operative Dairies Limited | Preliminary Report: 27 February 1992 | | Successful |

APPENDIX B