

I

Submission on Ministry of Economic Development  
discussion document:  
*Review of the Clearance and Authorisation Provisions  
under the Commerce Act 1986*

Bell Gully

10 August 2007

## Introduction

1. The Ministry of Economic Development (**MED**) has invited submissions on its Discussion Document "Review of the Clearance and Authorisation Provisions Under the Commerce Act 1986" (the **Discussion Document**) published in May 2007. Bell Gully welcomes the opportunity to provide this submission in response to the Discussion Document.
2. This submission addresses four matters relating to New Zealand's current merger regime, namely:
  - (a) where the onus of proving a substantial lessening of competition should lie in the clearance regime (an issue not specifically dealt with in the Discussion Document);
  - (b) whether to increase the statutory number of working days for the Commerce Commission (the **Commission**) to reach a decision (Q1 of the Discussion Document);
  - (c) whether the status quo should be altered so as to compel the Commission to publish written merger clearance decisions within a certain timeframe (Q2 of the Discussion Document); and
  - (d) whether the Commerce Act (the **Act**) should be amended to enable the Commission to accept behavioural undertakings in appropriate cases (Q5 of the Discussion Document).
3. This submission also addresses issues relating to the proposed clearance process for restrictive trade practices (**RTP**) (Q7, Q8 and Q9 of the Discussion Document).

## Summary of submission

4. Bell Gully is a leading supplier of competition law services and advises many major New Zealand and overseas businesses on competition law issues (details of our experience are contained on our website <http://www.bellgully.com/areas/competition.html>). We are well placed to comment on procedural issues, which are the focus of the Discussion Document, as our dedicated competition law team regularly deals with the Commission on merger (and other) matters and are required to manage the interface between the Commission and our commercial clients.<sup>1</sup>
5. Bell Gully is concerned that some of the MED's preliminary conclusions are unduly constrained by consideration of the Commission's current resource constraints rather than focusing on establishing a "best practice" regime. It is vital to New Zealand businesses and our international competitiveness that New Zealand has robust, well functioning laws that provide certainty but also, in appropriate cases, flexibility. The current review provides an excellent opportunity to achieve this and Bell Gully supports the MED's review of these issues.
6. New Zealand is a small open economy, which is reliant on the global economy for economic growth. To encourage international competitiveness, New Zealand's merger clearance regime should not be overly conservative. Bell Gully considers that the MED should give detailed consideration to amending the Act to ensure that clearances are only declined where the Commission is satisfied, on the balance of probabilities, that the proposed merger will have the effect of substantially lessening competition in a market. In our experience, the current provisions - whereby the applicant has the onus of satisfying the Commission that a merger will not have, or would not be likely to have the effect of substantially lessening competition - encourages an overly conservative approach and places the barrier too high for some potentially wealth creating mergers to proceed. We believe that the current approach has led to the Commission declining some applications simply because it says "it cannot be sure". In our view the current onus encourages the Commission to respond conservatively and when in doubt to say no rather than

---

<sup>1</sup> Acknowledged that Phil Taylor, who heads the national competition law team at Bell Gully, was part of the original working group assisting the MED in respect of Part 5 of the Review.

making a decision based on the balance of probabilities on what is really likely to occur. It does not encourage a rigorous analysis of the future, whether with or without the merger in place.

7. A best practice merger regime should seek to provide certainty to businesses. Uncertainty can have a significant effect on investment decisions and, in the case of publicly listed companies, a significant impact on a company's valuation. Bell Gully therefore supports increasing the statutory default number of days in which the Commission is expected to provide a clearance decision. However, to provide the required certainty, we consider it would be preferable to provide an even more realistic timeframe, for example 40 working days, in the Act but to limit the circumstances in which extensions to that timeframe can be made. Such circumstances may be, for example, where the proposed merger raises complex factual matters. Similarly, we consider that encouraging certainty also requires that the Commission be statutorily obliged to provide written reasons for its decisions within a settled timeframe.
8. Bell Gully considers that the Commission should, in appropriate merger cases, be empowered to accept behavioural undertakings in support of structural undertakings. As set out in the Discussion Document, both the Australian and the United Kingdom's competition authorities have this power. In our view, best practice for New Zealand would see this option also available here. Given that structural undertakings themselves are required relatively infrequently, we doubt that the monitoring and enforcement costs of any additional behavioural undertakings would be as significant as the Discussion Document suggests.
9. Bell Gully supports the MED's proposal that a clearance regime be introduced for RTP's. We comment in more detail on some of the features of the suggested regime further below.

#### **Merger: Onus**

10. In our view it would be preferable to amend section 66(3) so that the statutory test allows the Commission to only decline the merger for positive reasons. In other words, the Commission could only decline the clearance if it is satisfied the merger will, on the balance of probabilities, substantially lessen competition.
11. The reasons supporting our view for a change in onus are twofold. Section 1A of the Act is designed to promote economic welfare in New Zealand markets:

The purpose of this Act is to promote competition in markets for the long-term benefit of consumers within New Zealand.
12. New Zealand is a small open economy, and has become even more so since the introduction of the Act. Today, New Zealand is totally integrated with the world economy and the majority of New Zealand markets are driven by competitive conditions in world markets. Against this backdrop, the ability of New Zealand businesses to compete at an international level is becoming increasingly important and New Zealand's economic growth is dependent on having strong and internationally competitive firms. New Zealand's dairy, meat, beer and wine, air transport, fisheries, forestry, horticulture and new technology firms offer the best opportunity in the foreseeable future to increase our export returns and create sustainable economic growth. These primary industries require domestic efficiency to become profitable and competitive on an international scale. This approach is consistent with the MED's note under Issue P of the Discussion Document that "mergers which are likely to increase New Zealand's competitiveness should be treated favourably". We are advocating a variation that places international competitiveness at the forefront of New Zealand's competition policy.
13. The current section 66(3) test presents a risk to New Zealand's economic welfare because the Commission is required to decline mergers where it is not satisfied that the merger will not have, or would not be likely to have, the effect of substantially lessening competition. In other words, the Commission is required to decline mergers where it feels uncertain about the future impact of the merger on competition in New Zealand. Declining mergers in this "grey area" is a conservative and inefficient approach and fails to promote New Zealand's overall economic welfare. In order for New Zealand to become, and remain, globally competitive, and successfully

integrated into the world economy so as to achieve sustained economic growth, it is important that mergers which increase the international competitiveness of New Zealand businesses are not stifled.

#### **Merger: Default Number of Working Days for Clearance Time Frames (Q1)**

14. The MED suggests that the Act's current 10 working day time frame to determine merger clearances should be increased to 30 working days with retention of the power to extend the deadline. The MED notes that the current 10 working day time frame is unrealistic.
15. Bell Gully agrees that the statutory time frame should better reflect reality so as to provide the commercial community with an accurate picture of the time involved in seeking clearance. However, in light of recent Commission investigations, we consider that it would be preferable to provide a longer statutory time frame for the Commission to determine a clearance, such as 40 working days, but limit the circumstances in which the Commission can obtain an extension to that time frame.
16. Bell Gully agrees with the MED that the 10 working day timeframe, based on historical justifications, is unrealistically short in today's environment where the type of clearance applications the Commission now receives always raise some competition issues and therefore involve detailed analysis and extensive market inquiries. As a result, extensions are routinely agreed between the parties.
17. Like the current 10 working day timeframe the proposed 30 working day time frame would be unrealistically short. The Discussion Document itself notes that from July to June years, other than for 2006/2007 which covers the 9 months to 31 March, only 48% of merger applications were decided within 30 days, compared to 71% within 40 days. This year alone, three of the clearance applications in which Bell Gully has been involved (Goodman Fielder Limited and River Mill Bakeries Limited, Carter Holt Harvey Limited and Lakesawn Lumber Limited, and Woolworths Limited and the Warehouse Limited), all of which were submitted on 17 January 2007 took 41, 80 and 102 working days respectively to be decided. A further application before the Commission in which Bell Gully is also involved, Schering-Plough Corporation and Organon BioSciences N.V. (Akzo Nobel N.V.), submitted on 5 July 2007 has been extended until 6 September 2007 (46 working days).
18. In our view, the Act should provide a deadline for a clearance decision which businesses can expect to be met in the vast majority of cases. Based on our more recent experience, we consider that 40 working days is more realistic than the 30 working days tentatively proposed by the MED.
19. The MED proposes that the Commission's powers to extend the statutory deadline should be retained even with a longer time frame being included in the Act. Extensions, however, add an unnecessary step to the clearance process and as a matter of course create commercially unacceptable uncertainty for contracting parties.
20. Furthermore, the uncertainty associated with the Commission routinely seeking extensions is likely to drive some contracting parties to circumvent the formal clearance process. This is on the basis that it is becoming too burdensome for businesses operating in the small New Zealand economy where the need to act quickly and to be nimble is an essential element for success in competing with global participants. This is particularly so given that many mergers involving market aggregation face competition from overseas acquirers who do not have a market aggregation issue, for example, private equity funds.
21. Given these concerns, we consider that if the Act is amended to provide a realistic 40 working day deadline for a clearance decision, and the onus in its current form is retained, the Commission should only be able to seek extensions from parties in exceptional circumstances relating to the merger itself. Circumstances justifying an extension may be, for example, where the clearance application raises complex factual issues which can be identified to the applicant. The provision that the merger parties can agree to an extension sought by the Commission should be removed

from the Act. As long as the provision that the merger parties can agree to an extension remains in the Act, and the onus remains in its current form, those provisions combined can only have one result: agreement that the Commission can have more time to make further inquiries, otherwise the application will simply be declined because the Commission will say it cannot be satisfied. The provision allowing merger parties to agree to an extension effectively enables the Commission to determine the timeframe of the investigation regardless of the applicant's wishes and irrespective of commercial realities. However if the onus changes, as suggested above, and an applicant has provided sufficient information to the Commission to show that the merger does not result in a substantial lessening of competition, if the Commission seeks more time, and the case is not complex or involve special circumstances, the applicant can decide not to grant an extension.

22. This approach is more consistent with Australia's new formal clearance regime where the ACCC has the power to extend the deadline for its clearance decisions in complex cases, special circumstances or if the merger parties agree.

### **Merger: Publication of Written Merger Clearance Decisions (Q2)**

23. The MED's preliminary view is that the Commission should not be required to publish written clearance decisions and section 91(2) of the Act should not be amended because problems would only arise if both the Commission and the Court lacked pragmatism.
24. We disagree with this view. Bell Gully considers that the Act should be amended to require the Commission to publish full reasons for its decisions within, say, 15 working days after the date of the Commission's decision, with the reasons being in the same form as is presently the case. Making this a statutory requirement would again add more certainty to New Zealand's merger process and would avoid the unsatisfactory position whereby parties considering an appeal of a Commission decision are reliant on the Commission and third parties not opposing an appeal lodged outside the statutory 20 working days. In our view, it is no answer that the Commission is currently under resourced and may, on occasions, struggle to meet this statutory time-frame: businesses should not have to bear this burden.
25. We understand that the average time between the Commission reaching a clearance decision and publishing its reasons was 35 working days in the 33 months preceding 31 March 2007.<sup>2</sup> This time frame is too long. It is the reasons for the Commission's decision which will generally determine whether an interested party has grounds for an appeal (or for judicial review). If the reasons are not released promptly, the opportunity for interested parties to take Court action to preserve their position in relation to a target business or asset may be lost. (This is particularly so given the Commission's current practice of providing little or no guidance on the reasons for its decision until the full written reasons are published.) This creates uncertainty for business and the potential for undesirable share market effects. To avoid these issues, we consider that the Commission's reasoning needs to be made available to the applicant well before the applicable 20 working day appeal period.
26. Other than determining whether parties have grounds for an appeal (or for judicial review) there are other important reasons why the Commission's reasons for its decisions need to be released promptly. Because of competitive nature of the mergers and acquisition environment in New Zealand, particularly because of the presence of private equity funds, in the event of an application being declined, buyers must be able to swiftly identify exactly the Commission's concerns in the detailed way necessary to understand how they can be resolved, for example, by way of a structural undertaking or restructuring the sale of the business or asset with the vendor. If businesses do not have the opportunity to identify the Commission's reasons for a declined clearance decision, often the opportunity to acquire a business or asset will disappear. There are

---

<sup>2</sup> In the case of Solid Energy and Newvale Coal Co Limited, in which Bell Gully was advising an interested third party, the time between the release of the Commission's decision and the release of the written reasons was approximately 6 months.

examples of this occurring. It should be acknowledged, however, that in the past the Commission has indicated that a divestment might resolve a problem but that does not always happen.

27. Making the Commission's practice of producing written decisions into a legal requirement within a certain timeframe should not be an onerous change. At the time the Commission reaches its decision it must, by the very nature of reaching a concluded view, clearly know the basis on which it has reached that decision.
28. An alternative suggestion is that publication of the Commission's decisions could involve a two stage process: At the date of release of the Commission's decision the Commission would release a summary document outlining the reasons for its decision in sufficient terms so the applicant can identify the potential for resolution by way of divestment, restructuring of the acquisition or appeal. A full detailed reasons for the decision would then follow at a later date.

#### **Merger: Acceptance of Behavioural Undertakings (Q5)**

29. The MED proposes that the Commission should not be able to accept behavioural undertakings relating to the post acquisition conduct of the merged entity under section 69A(2) of Act.
30. Bell Gully considers that the Commission should have the flexibility to accept behavioural undertakings as part of a divestment package proposed by the applicant. However, the Commission should not be obliged to accept such undertakings.
31. We acknowledge that accepting behavioural undertakings can be problematic in some circumstances and we note the Commission's concerns in this regard were recorded in its Air New Zealand Limited and Qantas Airways Limited decision. In that case, the Commission considered a number of the behavioural undertakings offered by the applicants and noted concerns with the ability to enforce those undertakings and the level of oversight and monitoring required by the Commission.<sup>3</sup>
32. However, there are cases where behavioural undertakings may assist the Commission to grant a clearance without unacceptable ongoing issues for the Commission in enforcing and monitoring them. In particular, there are instances where behavioural undertakings would be useful in conjunction with structural undertakings, or in assisting the implementation of structural undertakings. Given that structural undertakings themselves are given relatively infrequently, we doubt that the monitoring and enforcement costs of any additional behavioural undertakings would be as significant as the Discussion Document suggests. In any case, giving the Commission the discretion to accept such undertakings means it would be able to assess the practicality of enforcing and monitoring such undertakings on a case by case basis. As we note above, it is not intended that the Commission should be obliged to accept any such behavioural undertaking, simply that it be available as a tool in appropriate circumstances.
33. As noted in the Discussion Document, the flexibility and use of behavioural undertakings is recognised by other jurisdictions, including Australia and the United Kingdom. We consider that New Zealand's merger regime would be enhanced by having this option also available here.

#### **Possible Clearance Process for Restrictive Trade Practices (Q7). Assuming its introduction, how the clearance process should apply to price fixing and resale price maintenance (Q8), and what features the system should have (Q9)**

34. The MED's preliminary view is that:
  - (a) A clearance system should be introduced for trade practices; and

---

<sup>3</sup> Paragraph 82 of the Decision.

- (b) Conduct that falls within the definition of the per se offences should be able to be cleared.
35. We agree with the MED's view. In particular, Bell Gully considers that a clearance system for RTP's should apply for all of sections 27, 28, 29, 30 and in the case of section 37, to the extent that the RTP arises directly from any contract, arrangement or understanding. Bell Gully considers that the clearance process for RTP's should essentially mirror the clearance process for mergers.
36. The policy arguments for a formal clearance mechanism for RTP's are essentially the same as those for mergers and are well set out in the Discussion Document. We note that the European Union (EU) dispensed with its system of prior clearance of RTP agreements in 2002. With the notification system gone, it meant all agreements caught by Article 81(1) of the EC Treaty (because they have the requisite adverse effect or potential effect on trade between Member States) were prohibited if they failed to satisfy the criteria for exemption in Article 81(3) (where the criteria require all relevant restrictions to be indispensable to achieving the pro-competitive ends of the agreement and the intended benefits accrue to consumers). However, there are significant differences between EU and New Zealand. Under the previous notification system in the EU, parties were able to seek a level of comfort from the European Commission (formally or informally) to confirm whether an agreement satisfied Article 81(3). Consequently parties in today's environment are well positioned to make careful market assessment of commercial agreements to assess their validity under the Articles because they can rely on past decision serving as precedents. The European Commission also has a great deal more case law and practice notes assisting businesses, and their advisors, make informed decisions. Furthermore, the European Commission provides standard form block exemptions which enable commercial advisors to determine with greater certainty the likelihood or otherwise of a RTP occurring. The Block Exemptions are workable and well received by the European business community.
37. The situation in New Zealand is quite different. We do not have a readily accessible register of past RTP decisions serving as precedents, and the Commission's current RTP guidelines simply restate the Act providing very few practical examples. As a result, businesses in New Zealand are heavily reliant on their lawyers to provide advice. Particularly for large-scale investment projects (e.g. those involving joint venture arrangements), parties will at times require more certainty as to the legal status of their proposals than their legal advisers necessarily are able to provide. A formal clearance process would provide greater certainty for business and, ultimately, enable businesses to compete more effectively and efficiently.
38. Moreover, as noted by the MED, jurisdictions like the United States have advocated the application of a rule of reason approach to per se offences. In New Zealand, however, the per se provisions of the Act make certain activities illegal regardless of their competitive effect. In respect of per se provisions, in our experience there are a number of situations where a technical breach may occur but the competitive impact is benign or de minimis. For example, an agreement between two small players in a highly competitive and unconcentrated market. Allowing the Commission to grant a clearance in such situations would be efficiency enhancing. While, in theory, applications for authorisation are available for such circumstances, in practice the cost and time involved render that route impracticable.
39. In theory there is no reason why the RTP clearance process should not extend to section 36, however we acknowledge the substantial resources required in investigating matters arising under that section.
40. As noted above, we consider it would be desirable for the RTP merger process to essentially mirror the merger processes. Further:
- (a) In appropriate cases the Commission should have the flexibility to place a timeframe on the length of the clearance for RTP's as a condition of clearance. However there should be no arbitrary expiration timeframe; the length of the clearance should be dependent on the life of the agreement.

- (b) The Commission should be able to revoke, vary or extend any clearance granted for RTP's once the initial timeframe has expired. Issue I of the Discussion Document signals that the circumstances under which the Commission can revoke, amend or replace an authorisation under section 65(1) may be altered. The circumstances in which an authorisation can be revoked, amended or replaced should be equally applicable to RTP clearance decisions.
- (c) With respect to appeal rights and undertakings, the rights under the merger clearance process should mirror the rights available under the process for clearance for RTP's for consistency given the policy reasons for clearance of mergers and restrictive trade practices are the same.

Bell Gully