BARNZ **Board of Airline Representatives New Zealand Inc**

SUBMISSION BY BARNZ ON THE EXPOSURE DRAFT OF THE COMMERCE (CARTELS AND OTHER MATTERS) AMENDMENT BILL

1. EXECUTIVE SUMMARY

The Board of Airline Representatives of New Zealand (BARNZ) represents most international airlines which operate into New Zealand. BARNZ participates in the consultation processes undertaken by the main airports under the Airport Authorities Act 1966 in relation to airport charges. BARNZ also participates in many committees at the various airports, as well as having its own internal committees, which consider and make operational decisions regarding the use of essential airport facilities and services, and related aeronautical facilities such as airspace, and operational conduct of airlines. As such, BARNZ has to be extremely cognisant of the provisions of the Commerce Act, particularly s30 and its associated exemptions. BARNZ' profile and list of members is attached to this submission. Any questions or enquiries regarding this submission should be addressed to:

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BARNZ does not consider that criminalisation of cartel conduct is necessary. The size of the existing fines, the damage to an individual's reputation and the cost of participating in any investigation or resulting legal proceeding, all combine to produce a significant deterrent to any firm or individual considering engaging in cartel activity. Adding criminal sanctions will only make law abiding firms more wary and hesitant of engaging in any form of interaction with their competitors – even if such conduct does not in fact constitute price fixing or would be within the proposed exemptions. Firms might act conservatively, not prepared to risk breaching competition laws, and beneficial co-operative initiatives may be lost forever. The addition of criminal sanctions is therefore more likely to damage the long term interests of consumers than to promote them.

BARNZ considers that the more significant component of the Exposure Draft is the implicit (and long overdue) recognition that the price fixing provisions and exemptions currently contained in the Commerce Act deter efficiency enhancing co-operative conduct between competitors from occurring, and are thus harming NZ's competitive markets and failing to promote the long term benefit of consumers. The Exposure Draft seeks to address this deficiency by replacing the current technical and constrained joint venture exemption in section 31 with a principled based collaborative activities exemption, by clarifying the joint acquisition exemption in section 33 and through the introduction of a clearance regime. BARNZ supports all of these changes and strongly urges the Government to proceed with these extremely important, indeed crucial, amendments, even if the criminalisation component of the Exposure Draft is deferred.

The key points made by BARNZ in the following submission are:

- That the prohibition of cartel conduct in sections 30 and 30A needs to be designed so as to avoid the risk of literal over-broad interpretations which would chill competition and inhibit efficiency enhancing initiatives between competitors. Section 30A should require that agreements must artificially interfere with the competitive determination of price, output or market allocation in order for them to constitute a cartel provision.

- While BARNZ supports the widening of the joint venture exemption in section 31 to collaborative activities, there is significant uncertainty with respect to what will constitute 'collaborative conduct', particularly between acquirers which are using common facilities or services provided by a third party, such as bottleneck essential infrastructure facilities.

- BARNZ supports the clarification of the s33 joint acquisition exemption to expressly include joint negotiation followed by separate acquisition and seeks that this amendment takes force as soon as the amendments are passed rather than one year later

- While BARNZ supports the introduction of the new clearance process contained in proposed section 32, BARNZ considers that the scope of the proposed clearance regime (which is limited to whether a provision is within the collaborative activity exemption) has been too narrowly drafted. BARNZ submits that the clearance process should also allow firms to apply for clearance on the grounds that a provision is not a cartel provision, in situations where this is not clear.

- BARNZ also considers that a broad principle based efficiency exemption should be included as an additional exemption. This would perform a similar role to an ancillary restraint exemption – but as it is based on the core principle of efficiency, it would avoid the perennial difficulty of ascertaining whether a restraint is ancillary or not. This reflects the OECD principle that arrangements reasonably related to cost-reducing or output-enhancing efficiencies are not within the category of conduct considered to be hard core cartels.

- While BARNZ does not consider that criminalisation of cartel conduct is necessary, (given the high potential fines, damage to reputation and cost of defending proceedings) if criminalisation proceeds, then it should be limited to the most egregious conduct. The proposed amendments do not provide sufficient guidance as to how prosecutorial discretion should be exercised or limit potential criminal liability to the most egregious conduct. BARNZ suggests that criminal liability, if it is introduced, should include the additional element of the provision having the purpose, effect or likely effect of substantially lessening competition.

2. INTRODUCTION

While naked price fixing is one of the most egregious forms of conduct designed to undermine competitive free markets and deserves to be condemned *per se*, not all agreements among competitors affecting price are inherently anti-competitive. It is well accepted that co-operative efficiency enhancing agreements among competitors can improve efficiency and provide long term benefits to consumers through reduced costs of production, improved dynamic efficiency and innovation and through the creation of new markets and products. Economic understanding of how co-operative agreements among competitors can enhance efficiency and promote the interests of consumers has advanced considerably in the four and a half decades since the Commerce Act was enacted.

Competition laws therefore need to be able to distinguish between hard core price fixing with no redeeming values which deserves automatic condemnation; and cooperative conduct which is necessary within certain markets or which is being undertaken as part of an efficiency enhancing joint venture. If price fixing is defined too widely it will prevent legitimate joint ventures or cooperative activities designed to legitimately increase operational efficiency, thereby inhibiting the development of co-operative innovative and efficiency enhancing initiatives. Such a result would adversely affect the long term benefit of consumers – the very purpose of most competition laws.

As it currently stands s30 enshrines in stone the structurally focused jurisprudence of the middle of the last century. In doing so it significantly inhibits the ability of NZ Courts, the Commission, practitioners and firms to reflect improved economic understanding of the effects of agreements between competitors.

The OECD Council recommends exclusions of cartel conduct '*be reviewed periodically to assess whether they are both necessary and no broader than necessary to achieve their overriding policy objectives'.* It has been some time since s30 and its subsequent exemptions have been fully reviewed, and the development of economic theory since the introduction of the Commerce Act in 1986, has left the rather technical and structural price fixing provisions contained in the Act lagging behind economic learning.

The review of the price fixing prohibitions and accompanying exemptions contained in the Exposure Draft and accompanying materials is well overdue. BARNZ strongly urges the Government to proceed with this review, irrespective of whether or not criminalisation of cartel conduct proceeds.

3. DESIGN OF THE PROHIBITION

The Exposure Draft proposes replacing the current definition of price fixing with the OECD categories of hard core cartel conduct. The OECD definition has the advantage of being substantially clearer than the tortuous drafting of s30.

However, the broad nature of the definitions create a significant risk of over-reach with consequential chilling of competitive behaviour. Firms are likely to avoid behaviour which risks falling within the categories of conduct which constitute a cartel provision.

The move from a focus on the outcome of the agreement on price (as per the current s30) to the form of the conduct, means that conduct of the type listed in proposed s30 and 30A, which is not likely to effect the price of goods or services, risks being illegal under the proposal.

This risk is particularly acute with respect to output restrictions. There are numerous operational agreements required where competitors use essential infrastructure facilities in common. Such agreements are necessary in order for the safe and efficient use of the common facilities and provision of services to consumers. Often the agreements seek to maximise throughput of the facility for the benefit of all users – and ultimately consumers. Yet, literally, some of the agreements will constitute output restrictions.

BARNZ' experience and specific concern is with airports where the use of airport owned facilities such as the runway, check in counters, gate lounges, air-bridges, baggage halls, parking aprons, fuel hydrant system, ground power units, baggage conveyor system and air-space all require operational agreements and understandings between users. Operationally, there is a high degree of co-operation among airlines regarding the use of common assets and facilities at airports in New Zealand. This is efficient and is in the long term benefit of consumers in New Zealand. Such operational agreements may impose what might literally be an output restriction. For example, there are agreed limitations on aircraft movements in adverse weather conditions or during periods where runway maintenance is required. In addition, there is recognition that the capacity of an asset or service is limited by physical or technological constraints, with a maximum throughput being accepted by all users as a matter of fact. Users often then endeavour to work together to maximise throughput through operational efficiencies. Such agreements do not have the purpose, effect or likely effect of fixing maintaining or controlling price as per the current s30. But, on a literal interpretation of the proposed s30A(3), they may well constitute an output restriction. The fear of industry participants that such an interpretation may be applied is highly likely to chill co-operative efficiency enhancing initiatives between market participants. If criminalisation of cartels occurs, this chilling effect will be exacerbated.

This same concern over whether decisions between users of essential infrastructure assets on operational, safety and quality matters will constitute an output restriction will also apply to users of other essential infrastructure network assets where operational co-operation is needed such as fibre networks, gas pipelines, electricity lines, railway lines and terminals, port facilities and ferry terminals.

BARNZ acknowledges that the approach of the Commerce Commission under s30 has been to apply a purposive approach, in line with the direction contained in the Acts Interpretation Act, such that only arrangements which artificially constrain or interfere with the price setting process fall within the four corners of s30. Conduct which fixes, controls or maintains prices in a literal sense, but which does not prevent prices being determined by competitive market forces, is not considered to fall within s30. Thus in the Electricity Governance determination, the Commission summarised its approach under s30 as being:[1]

[1] *Electricity Governance Board*, CC Decision 473, 30 September 2002 at [174]

> … that a price will be fixed, controlled or maintained for the purposes of s30 where there is some artificial interference with, or constraint on, the finding of a price or prices by competitive forces or processes (in particular the interaction of supply and demand).

The approach of the Commission reflects that of the United States Supreme Court which in the iconic *BMI v Colombia Broadcasting* case observed that while the *per se* rule is a *'valid and useful tool of antitrust policy and enforcement'… 'easy labels do not always supply ready answers'.*[2] Criticising lower Courts for focusing on the fact the licence involved price fixing in the literal sense, without considering whether the particular practice was 'plainly anticompetitive' or 'without redeeming virtue', the Court noted *'literalness is overly simplistic and often overbroad'*. The Court stated:[3]

> It is necessary to characterise the challenged conduct as falling within or without that category of behaviour to which we apply the label '*per se* price fixing'. That will often, but not always, be a simple matter'.

Having examined the substance of the proposed blanket licence to play musical compositions, the Court summed up its views as follows:[4]

> Finally, we have some doubt – enough to counsel against application of the *per se* rule – about the extent to which this practice threatens the 'central nervous system of the economy,' … that is, competitive pricing as the free market's means of allocating resources. Not all arrangements among actual or potential competitors that have an impact on price are *per se* violations of the Sherman Act or even unreasonable restraints.

Several years earlier, the US Supreme Court had observed that *'departures from the rule of reason standard must be based upon demonstrable economic effect rather than ... upon formalistic line drawing'*.[5]

In order to avoid an approach which can be criticised as *formalistic line drawing*, the Commerce Act needs to provide the Commission, Courts and practitioners with the ability to lift the *per se* label and examine the economic reality beneath the impugned provision in order to first, ensure it is only agreements that threaten the 'central nervous system of the economy' that are deemed illegal, and secondly to take account of any potentially beneficial economic effects of the arrangement.

While it is the role of the exemption sections to perform the second task of taking account of any beneficial economic effects, the first task of limiting the prohibition to agreements that threaten the 'central nervous system of the economy', falls squarely within the definition of the prohibition. The current proposed drafting of the new sections 30 and 30A does not fulfil this requirement.

There is a significant difference between the US Sherman Act, which is of almost constitutional brevity, and has been able to be developed by the US Courts as if it were common law, and New

[2] 441 US 1 (1979) at 8.
[3] Ibid at 9.
[4] Ibid at 23.
[5] *Continental TV v GTE Sylvania* 433 US 36 (1977) at 58-59.

Zealand's Commerce Act which is a statutory codification, and subject to the rules and limits of statutory interpretation. New Zealand Courts have a limited ability to develop competition law laid down in a statute, as was recently demonstrated in *Astrazeneca Ltd v Commerce Commission*[6] where the Supreme Court reversed a purported use of the purposive approach by lower Courts to read down an immunity to Part 2 of the Commerce Act contained within s53 of the NZ Public Health and Disability Act 2000. In doing so, the Supreme Court not only affirmed the primacy of the statute's text, it reminded Courts there are limits on the ability of a purposive approach to read down the words of the statute or add glosses.

Drafters designing the amendments to the Commerce Act therefore need to ensure that the design of the cartel prohibition is unambiguously clear that only agreements that interfere with the free market's determination of price, output or market allocation constitute a cartel provision prohibited by the Commerce Act, and that agreements which merely incidentally affect price, outputs or market allocation without interfering with the competitive determination of such matters, do not constitute cartel provisions.

BARNZ strongly submits that the proposed s30A should expressly include the principle that there must be *an artificial interference with, or constraint on, the determination of price, output or market allocation by competitive forces or processes in order for a provision to have the purpose of price fixing, restricting output or market allocating.*

If this does not occur, then there is a very real risk that using the form of the conduct to define the prohibition against cartel conduct, rather than the effect of the conduct, will result in a formalistic line drawing approach, and in market participants taking an exceedingly cautious approach and declining to enter into arrangements with competitors which, although efficiency enhancing, and not interfering in the competitive interaction of market supply and demand forces, literally constitute cartel conduct. Many firms will choose to forgo co-operative arrangements and investments thereby limiting innovation and the benefits it engenders due to the perceived risk of breaching the law. This risk is particularly high in relation to output restrictions where many operational agreements between competitors using the essential monopoly facilities in common, will literally constitute an output restriction, even though there has been no interference or constraint upon the determination of output by competitive forces.

Given the serious consequences of being found to have engaged in price fixing (or cartel behaviour), which is second only to fraud in seriousness for corporate crime, BARNZ considers that the Legislature has a duty to ensure that the scope of cartel conduct is limited to conduct which interferes with the operation of the competitive markets. Relying on the Commission or Courts adopting a particular interpretation is not sufficient given the seriousness of the consequences.

[6] [2010] 1 NZLR 297 (SC).

4. THE PROPOSED CHANGES TO THE EXEMPTIONS

As noted above, competition laws need to be able to distinguish between hard core price fixing with no redeeming values, which deserves automatic condemnation, and cooperative conduct which is necessary within certain markets or which is being undertaken as an efficiency enhancing initiative. Most jurisdictions therefore have exemptions to the *per se* rules against price fixing. Consistent with this, the OECD 1998 'Recommendation Concerning Effective Action Against Hard Core Cartels' specifically excludes arrangements that *'are reasonably related to the lawful realisation of cost-reducing or output-enhancing efficiencies'* from its classification of what amounts to hard core cartel conduct.

The rationale for per se rules of illegality are that the conduct:

- Would always or almost always tend to restrict competition and decrease output
- Has manifestly anticompetitive effects
- Has no redeeming virtue

Therefore, the underlying basis for creating an exemption to the pre se illegality of price fixing, must be that the particular type of conduct or agreement does not always or almost always tend to restrict competition and decrease output and may, depending on the particular facts of the case, have redeeming virtues or pro-competitive effects.

There are currently three exemptions to price fixing contained in the sections following section 30. The Exposure Draft proposes retaining one of the exemptions with amendment, significantly redesigning the second, and repealing the third. Each exemption will be commented on in turn.

<u>Section 31 – current joint venture exemption – proposed collaborative activity exemption</u>

The current narrow drafting of s31 means the joint venture exemption is very likely to deter many forms of co-operative integration among competitors. It has therefore been almost universally criticised as unsatisfactory.

BARNZ supports the replacement of section 31 with a new collaborative activities exemption.

BARNZ supports the exemption being drafted on a principled basis, which will allow new methods of business organisation and improved economic understanding to be incorporated within decisions on an ongoing basis as these develop, which should enable the ongoing evolution and modernisation of the law.

BARNZ however has some concerns over the interpretation of the definition of a collaborative activity as 'an enterprise, venture, or other activity, in trade … carried on in co-operation by 2 or more persons …'. In particular BARNZ is uncertain over:

- Whether common use of an essential facility by a number of acquirers constitutes 'an activity in trade'?
- What degree of 'co-operation' will be required to come within the exemption?

This concern specifically relates to the situation of users acquiring essential infrastructure services for bottleneck facilities from monopoly providers and whether collaborative decisions by users relating to their individual use of such assets will fall within the exemption?

Where users are all utilising the same facility, then co-operative decisions are required on day to day operational matters so as to facilitate the use of the common facility or service by all users in an efficient, safe and productive manner. Such decisions only relate to an input to the product or service each party ultimately offers separately to the public. The decisions do not themselves form any service or product provided in co-operation by the parties. Will such decisions be held to constitute 'an activity in trade'? Or would the Commission or a Court consider that rather than an activity in trade occurring, this situation is actually a series of individual activities being undertaken separately, and therefore outside the scope of the exemption.

In addition, assuming there is an activity in trade, the question remains as to whether it is 'carried on in co-operation'. There is a risk the Commission or a Court may require a high degree of co-operation, such that decisions by users are held not to be an 'activity carried on in co-operation', but merely activities carried on 'in parallel'. This was the approach taken by the Commerce Commission to a proposed agreement between Transpower and users of the national grid regarding the quality of electricity to be transmitted over the grid.[7] The Commission's draft determination was that the proposed agreement did not constitute a collective acquisition under s33 as the parties were not acting collectively in acquiring the common elements of quality – rather they were acting in parallel.

If the same approach were taken to the proposed collaborative activities exemption, then competitors that use essential infrastructure assets in common to individually provide services, would be significantly constrained from being able to rely upon the exemption in relation to collaborative decisions regarding the use of such assets.

This concern relates to all essential infrastructure network assets where operational co-operation is needed such as such as fibre networks, gas pipelines, electricity lines, railway lines and terminals, port facilities and ferry terminals and airports.

Current Section 32 – Price Recommendation Exemption

Section 32 currently exempts price recommendations by groups of more than 50 persons, who trade in the relevant goods or services, from the application of s30.

Section 32 is best seen as a historical relic or long standing 'transitional' provision, designed to bridge the highly regulated attitudes and behaviour which were the status quo prior to the Commerce Act coming into force, and the competitive markets the Act is designed to promote. Given that competition is now well accepted as being the best means (in most situations) of promoting efficiency, and consequentially the long term benefit of consumers, the original justifications for s32 no longer exist. The time is well over-due for s32 to be repealed, as has occurred in Australia.

[7] Commerce Commission, *Transpower Draft Determination*, 30 June 1999 at [70]

New Section 32 – notified arrangements between bidders

The Exposure Draft proposes utilising the gap left by the repeal of the price recommendation in s32 to introduce an exemption for collective bids – where the recipient is notified that a collective bid is being considered and agrees to accept the bid on this basis. BARNZ supports this proposed exemption.

Section 33 - Joint Buying and Promotion Arrangements

Section 33, titled 'joint buying and promotion arrangements', currently exempts agreements which:

- Relate to the price of goods or services collectively acquired (whether directly or indirectly) by the parties to the agreement; or
- Provide for the joint advertising of the price for the resupply of collectively acquired goods.

The collaboration of competitors to make joint acquisitions can have significant pro-competitive outcomes and redeeming virtues, particularly in terms of improved efficiency. Reflecting this, co-operative purchasing agreements between competitors are not treated as *per se* illegal by US courts, which recognise that they are *'designed to increase economic efficiency and render markets more, rather than less, competitive'* and *'are not a form of concerted activity characteristically likely to result in predominantly anti-competitive effects'*. [8]

The Exposure Draft proposes clarifying s33 by expressly providing that collective negotiation, followed by individual purchase, is within the exemption. BARNZ supports this clarification, as the degree of 'collectiveness' required in order for an acquisition to fall within the exemption has been the subject of some debate among academic commentators and has not, in the 25 years of the Commerce Act, yet been the subject of any judicial decision. Complicating matters, the Commerce Commission in 1999 indicated that users of the national grid were acting in parallel – and not jointly – when they agreed elements of quality with Transpower – and were outside the s33 exemption. Some BARNZ members are therefore unwilling to rely on the exemption and have not been prepared to participate in any joint acquisitions.

BARNZ therefore supports the proposed clarification of s33 through the additions of paragraphs (c) and (d), and indeed, considers that this amendment should become effective as soon as the Amendment Bill has been passed into law, rather than waiting for a year as currently proposed for the entire amendment package.

[8] *Northwest Wholesale Stationers v Pacific Stationary and Printing Co* 472 US (1995) 295

5. ARE ANY FURTHER EXEMPTIONS WARRANTED?

The proposed collaborative activity exemption, while significantly wider than the joint venture exemption it will replace, is still hostage to the need to fit the impugned conduct within the elements of the section. No matter how efficient the outcomes of an agreement, if it is a cartel provision, then it will be per se illegal under the Commerce Act unless it is able to be brought within one of the three proposed exemptions.

A concern with efficiency is at the heart of contemporary analysis of horizontal restraints between competitors. It directly relates to the Commerce Act's purpose of achieving the long term benefit of consumers in New Zealand. The OECD 1998 'Recommendation Concerning Effective Action Against Hard Core Cartels' specifically excludes arrangements that *'are reasonably related to the lawful realisation of cost-reducing or output-enhancing efficiencies'* from hard core cartel conduct.

As understanding of potential benefits of horizontal cooperation matured, economic learning has demonstrated improvements in productive and dynamic efficiency represent the strongest means of promoting long term benefit for consumers as they lead to new products, technologies and processes. Innovation has public good characteristics as a result of the new and improved products and processes dispersing throughout society. Dynamic efficiency gains from allowing competitors to co-operate and innovate jointly often significantly exceed static efficiency gains achieved from maintaining strict policies of competitively determined prices.

Successful new product and process development and innovation often requires horizontal co-operation. Deterring firms from engaging in efficiency enhancing initiatives, through over-reaching *per se* rules, which do not permit consideration of accompanying economic benefits, is potentially just as harmful to consumers as the anti-competitive conduct itself. While anti-competitive conduct may raise costs, the over-reaching *per se* rule may prevent cost reducing efficiencies from occurring. In both cases the outcome is the same - consumers end up paying more for goods and services than in an efficiently operating market.

Erroneous *per se* condemnation of conduct does not just affect a few individuals – it can impact an entire industry or industries, with forgone wealth creation through the missed efficiencies being potentially very substantial.[9]

'Improvements to efficiency' therefore has much to merit it as the basis on which to ground a principled based exemption to per se illegality of cartel prohibitions. It would enable the Courts and Commission to examine the economic reality of a provision and ensure that agreements which improve efficiency are not condemned without consideration of those efficiencies.

An exemption based purely on efficiency grounds would eschew the structural restrictions contained in the three proposed exemptions and enable the underlying economic effect of the agreement to be examined.

An efficiency based exemption is superior to an exemption based on the doctrine of ancillary restraints, which was suggested by Cabinet. This is because people hold legitimately different

[9] Frank Easterbrook, "The Limits of Antitrust" 63 Tex.L.R. 1 (1984) at 2 and 9-10.

opinions as to whether a restraint is ancillary and truly necessary, and there is often not a clear answer as to whether an agreement is ancillary. Commentators endeavouring to define the concepts of ancillary agreements, as opposed to naked agreements, consistently do so by reference to the effect of the agreement on efficiency. Bork, for example, describes a naked pricing restraint as being one which gives rise to either non-existent or de minimus efficiencies and an ancillary agreement as one which 'contributes to the efficiency of a contract integration'.[10]

If the concepts of naked and ancillary need to be defined with reference to their effect on efficiency in order to make the test workable, then why not just be transparent and phrase the test explicitly in terms of efficiency?

The effect of an arrangement on efficiency can be quantified. Improvements in productive efficiency can be measured and predicted by accountants. Improvements in allocative efficiency can be seen through changes in resource requirements. Dynamic efficiency improvements in terms of investment and innovation in the short term can be measured relatively accurately (although it must be acknowledged it is more difficult to accurately forecast medium to longer term improvements in future dynamic efficiency and innovation). Nevertheless, overall economists and accountants have become quite adept at calculating the effect on efficiency of a particular arrangement. An efficiency based exemption could therefore be applied in a relatively certain, predictable and objective manner. Judges would not be setting sail 'on a sea of economic doubt' but would rather be guided by quantitative analysis.

BARNZ therefore considers that an efficiency based exemption should be included within the Commerce Act, exempting cartel provisions which improve efficiency from the per se condemnation contained in s30. This would be in addition to the three exemptions proposed in the Exposure Draft.

Such an exemption could be worded along the following lines:

> A person does not contravene section 30(1) if the contract, arrangement or understanding that contains the cartel provision:
>
> i. improves efficiency for the long term benefit of consumers in New Zealand; and
> ii. is not carried on for the dominant purpose of lessening competition.

Requiring that efficiency be improved for the long term benefit of consumers makes it clear that an assessment focusing primarily on dynamic efficiency and incentives to invest, with no consideration of other benefits to consumers such as lower charges or improved quality and service, would not satisfy the exemption. It should not be necessary to define efficiency, which has a well understood economic concept of including productive, allocative and dynamic efficiency and which has been included within s3A of the Commerce Act for twenty years without being defined.

[10] Robert Bork *The Antitrust Paradox: A Policy` At War With Itself*, (Free Press, New York, 1993) at 268.

6. THE PROPOSED CLEARANCE REGIME

The Exposure Draft proposes introducing a clearance regime for collaborative activities.

BARNZ fully supports the concept of a clearance regime. However, BARNZ considers it essential that this should extend to all provisions that may be cartel provisions – not just collaborative activities.

The clearance regime as currently proposed is only applicable where:

- the applicant has reasonable grounds for believing that the provision is a cartel provision;
- the cartel provision is reasonably necessary for a collaborative activity; and
- competition will not be (or be likely to be) substantially lessened

BARNZ considers that the clearance regime should enable persons to apply for clearance on the grounds that the contract, arrangement or understanding does not contain a cartel provision.

Given the substantial redesign of the prohibition in s30, and the movement away from a focus on the purpose, effect or likely effect of the provision on price, to a direct prohibition of particular types of conduct, there will necessarily be a considerable period of uncertainty while the parameters of the prohibition are clarified. A key issue which will need to be worked through is the question of how far a purposive interpretation will take the Court and Commission in relation to agreements which literally fall within the prohibited forms of conduct, but which do not artificially interfere with or constrain the competitive forces of supply and demand. Is the process of characterisation which is applied by the US Courts under the Sherman Act relevant? Will '*formalistic line drawing'* be avoided or will it be the automatic consequence of the section?

If the clearance regime is not able to consider whether or not particular agreements constitute a cartel provision, then this period of uncertainty will be considerably longer, and a significant chilling effect will evolve to envelope co-operative, efficiency enhancing agreements between competitors.

BARNZ suggests that proposed s65A(2) should be altered so as to enable the Commission to give a clearance if it is also satisfied that '*the contract, arrangement or understanding does not contain a cartel provision'*. There would also need to be consequential changes to proposed s65A(1) and (3).

A floodgate of un-necessary applications can be prevented by requiring the applicant to have reasonable grounds for believing that the provision may be a cartel provision before applying.

7. CRIMINALISATION OF CARTEL CONDUCT?

BARNZ does not consider that criminalisation of cartel conduct is necessary. The size of the fines already provided for (which for a firm are up to $10 million for <u>each</u> instance and for an individual, $500 000 for <u>each</u> instance), the damage to one's reputation and the cost of participating in any investigation or resulting legal proceeding, all combine to produce an extremely significant deterrent to any firm or individual considering engaging in cartel activity. Being found guilty of price fixing is already one of the most serious white collar crimes, second only to fraud.

Adding criminal sanctions will only make law abiding firms (and the individual employees and officers) more wary and hesitant of engaging in any form of interaction with their competitors – even if it does not in fact constitute price fixing or would be within the proposed exemptions. Firms might act conservatively, not prepared to risk breaching competition laws, and beneficial co-operative initiatives may be lost forever. If over applied, criminal sanctions will have the opposite effect than intended and may hamper the competitive and efficient functioning of markets. The addition of criminal sanctions is therefore more likely to damage the long term interests of consumers than to promote them.

If criminalisation proceeds (which BARNZ does not support), then it should be limited to the most egregious instances of cartel behaviour.

The Exposure Draft proposes using knowledge that the provision is a cartel provision as the means of distinguishing between cartel conduct which would be proceeded against civilly and that which could be prosecuted criminally. While BARNZ supports there being a distinction between the civil and criminal provisions, it does not consider knowledge provides a sufficient distinction.

BARNZ considers that a 'substantial lessening of competition' should also be required as an element in any criminal cartel offence. Proof that the provision had the purpose, effect or likely effect of substantially lessening of competition would provide a more meaningful distinction between conduct which should be proceeded against civilly and that which is egregious and deserving of criminal punishment. It would confine criminal sanctions to where there had been proof of harm to consumers, leaving the — still very substantial — civil penalties to be applied to price fixing which did not (for whatever reason) result in a substantial lessening of competition.

John Beckett
Executive Director
25 July 2011

BARNZ Board of Airline Representatives New Zealand Inc

BARNZ PROFILE

The Board of Airline Representatives New Zealand Inc ("BARNZ") is an incorporated society comprising 22 member airlines operating scheduled and code share international and domestic services. Its members are:

Full membership:

Air Calin
Air Pacific
Air Tahiti Nui
Cathay Pacific Airways
Emirates
Fieldair
Korean Air
Malaysia Airlines
Qantas Airways (incl Jetstar)
Singapore Airlines
Thai Airways International
Air New Zealand (Group)
Airwork
Air Vanuatu
China Southern
EVA Airways (code share)
Japan Airlines (code share)
LAN Airlines
Pacific Blue
Royal Brunei
Tasman Cargo Airlines

Associate membership:

Menzies Aviation (NZ) Ltd

The objectives of BARNZ include:

- the establishment of recognised means of communication between member airlines, on the one hand, and other bodies whose interests or actions affect member airlines and the aviation industry, on the other hand;
- representation of members in matters affecting their common interests;
- determining the position of members on legislative, judicial and administrative actions affecting the provision of air services and the representation of member airlines before decision-making bodies;