TAKING RETAIL FURTHER // Retail NZ

9 February 2016

Targeted Commerce Act Review
Competition and Consumer Policy
Ministry of Business, Innovation and Employment
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To whom it may concern,

TARGETED REVIEW OF THE COMMERCE ACT

1. Retail NZ is a trade association representing the interests of retailers. We have around 5,000 members, ranging from small family-run stores through to major retail chains, including businesses across all retail categories. Together, our members account for around two-thirds of New Zealand's total retail sales expenditure.

2. We submit that the Commerce Act is currently working well. It supports innovation and risk taking, but provides a framework that allows issues to be identified and action taken when those issues could negatively impact consumers.

3. The retail sector is highly competitive and consumers are benefiting from lower prices as a result. There are no significant barriers to new entrants entering the retail market and this is borne out by the number of international retailers that have recently established a presence in New Zealand.

4. The Productivity Commission noted in its 2014 report, 'Boosting Services Sector Productivity', that New Zealand's "geographic remoteness and small domestic markets partially explain why competition in New Zealand's service markets is less intense than in some other countries. Exposure to foreign competition can increase the intensity of competition."

5. We argue that this is less true for the retail sector. Our sector is highly exposed to foreign competition - both directly on high streets but also because we operate in a global marketplace where foreign retailers can sell direct to New Zealanders over the Internet 24 hours a day, 7 days a week. Online offshore trading competes strongly in many retail categories and continues to grow at a faster pace than domestic retail.

Anti-competitive exclusionary conduct (s36)

6. Section 36 of the Commerce Act 1986 aims to deter and prevent dominant firms from misusing their market power to damage the competitive process.

7. DLA Piper notes in its submission to the Targeted Review of the Commerce Act that:
   Fundamentally, the task of competition law is to ensure that firms with market power "do not exclude their competitors by means other than competing on the merits of the products or services they provide" (Official Journal of the European Union - Communication from the Commission regarding Enforcement). But the question is how should regulators and Courts distinguish between unlawful conduct (for example, predatory pricing) and lawful competing on the merits (rigorous discounting). The question has not been resolved 100% satisfactorily in any jurisdiction.

8. Retail NZ agrees with the Ministry for Business, Innovation and Employment (MBIE) position, set out in the issues paper, that prohibiting anti-competitive exclusionary conduct should protect competition within the marketplace, not individual competitors. In a competitive marketplace some firms will fail and others will succeed. The law should not seek to punish those who achieve success in a competitive marketplace just because they are large in size. The paper also correctly notes that market power

should not be discouraged, and is in fact essential. It encourages innovation and, if achieved, drives a business to continue to innovate. This drives efficiency and improved services and products which benefits consumers. Businesses should not be penalised for achieving size and scale as a result of their success in the market place.

9. In addition, we note that specific examples of unsuccessful business ventures should not be held up as examples of a failure of our competition law. The natural outcome of fair competition is that successful businesses will thrive and grow.

10. Ultimately the purpose of the Commerce Act is to promote competition for the long term benefit of consumers. Consumers will not benefit if the effect of the Act is to chill competitive behaviour (and, as a result, innovation) by large firms (just because they may have market power). Section 36 must be flexible enough to deal with buyer power which results in lower prices for consumers. In our view, the current section 36 with its focus on an anti-competitive purpose, and the way the Courts interpret it, achieves this.

The current 'purpose test'

11. Currently section 36 prohibits conduct that has the purpose of being exclusionary. The court must determine whether a company had market power and whether there was intent to take advantage of that market power before the action was taken. A casual connection must be established between a businesses' dominant market position and it taking advantage of that position.

12. Our organisation is strongly supportive of retaining the 'purpose test' and retaining the causal link between dominant market position and the action taken.

Moving to an 'effects test'

13. Changing the test to an effects test and prohibiting conduct that has the effect of being exclusionary, regardless of the intent, is strongly opposed. The introduction of an effects test would result in uncertainty for all businesses and harm the wider economy. The current law is well understood by the business community and there is an extensive body of case law from which business can draw guidance.

14. An effects test would require businesses to predict the real world results of an action which would be very difficult, or impossible, as some implications could be outside of the control of the business itself. It will increase costs for businesses and encourage more cautious decision making. The overall result will be a chilling of innovation and risk taking.

15. New Zealand with many markets serviced by a number of large firms is not an appropriate guinea pig for an untested and uncertain effects test.

No case has been made for change

16. In our view it has not been established that there is an issue with the current wording that warrants radical change. It could be argued that the evidence of a problem is merely several difficult cases which were highly contested against a backdrop of complex and unusual factual scenarios.

17. In our view it is illogical to see the list of proceedings undertaken under section 36 of the Commerce Act as evidence then the law should be changed. This analysis is simplistic and doesn't consider how the law is actually working within business. Our members generally have a good understanding of section 36, and what is permitted under the current law. It is preventing and deterring anti-competitive behaviour and is likely having the result of avoiding Commerce Commission from taking action at all.

18. For this reason, a major departure from current section 36 wording would be very disruptive. We currently have 20 years of case law and a good understanding of how the law works. Change will create years of uncertainty for business, make firms more risk-averse in their decision-making and potentially stifle innovation.

The impact of introducing an effects test

19. There are two main reasons why an effects test is harmful:

    a. An effects test would have a negative effect on competition because it will not only catch pro-competitive conduct but will also prevent it from happening in the first place.

    b. An effects test would introduce uncertainty and ambiguity to many business decision, thereby driving up the overall costs of doing business and may well result in deferred investment decisions, particularly those relating to innovation.

20. Business needs certainty in order to make decisions and compete. Law changes can have a profoundly negative impact on this. The proposed changes to section 36 will create legal uncertainty. Without this certainty, business will find it difficult to make decisions on investment and strategy given the risk that its actions may impact upon competitors under a change in law. The result of change may be a stagnation of competition.

21. A business should only be expected to determine the own purpose of its decisions and actions and to assess whether it can be objectively justified against the established criteria of section 36. An effects test would require a business to speculate on the likely effect of its conduct on competitors and the market. It presupposes that a firm is in possession of perfect information about its competitors, which is very rarely, if ever the case. This uncertainty is a risk to the economy and be potentially harmful to consumers.

Authorisations

22. While authorisations conceptually might seem a good idea, in our view they are of limited commercial benefit in the real world where parties do not have the luxury of extensive empirical analysis and careful weighing up of economic costs and benefits.

23. Commercial decisions are made many times every day. It is impractical to ask business to request authorisation for every decision that is made that might negatively affect competition.

24. The process of seeking an authorisation is expensive and time consuming, both for a business to put together and to receive an outcome. Such time delays could jeopardise contract negotiations and have the effect of deterring commercial behavior.

25. A clearance process would ultimately involve the public disclosure of commercially sensitive information, potentially including proprietary information that firms may not wish to share with the market. Overall, in practice, we think a clearance process would be little used, or would likely reduce innovation and prevent firms seeking to compete.

Alignment with Australian legislation

26. We note that the Australian Government is planning to consult further on the recommendation relating to misuse of market powers included in the Harper Review. In principle we support alignment with Australian legislation as this will create certainty for businesses operating in both markets.

27. However, should the Australia Government pursue a more experimental approach and introduce an effects test we would strongly prefer the New Zealand Government to take a wait and see position before testing it in this market.

Alternative enforcement mechanisms

28. Retail NZ supports broadening the Commerce Commission abilities to hand down 'enforceable undertakings', allowing them to make action against companies without going to court. Avoiding the court process saves all parties money, and give a faster results which benefits all parties including consumers. However, we consider there needs to be safeguards in place to ensure that these enhanced powers are properly used and affected parties have an opportunity to be heard.

Expanding the government's ability to undertake 'market studies'

29. Businesses are currently required to keep keeping detailed documentation to which government agencies can request access. The government also has existing powers to investigate areas of concern as part of the standard policy process through MBIE; but also market studies can effectively be undertaken by the Productivity Commission and by select committees (as in the case of milk pricing). The Commerce Commission already has significant powers to investigate perceived competition issues.

30. It is not clear that tasking a government agency with specific powers to undertake market studies will lead to improved outcomes for consumers. Again, the case for change is not clear.

31. Being subject of a market review is expensive, time consuming and distracting. As a result being subject to a market review creates costs for business, which ultimately will be passed onto consumers

32. The retail supply chain is diverse and some categories have highly concentrated supply chains. There is a risk that retailers could frequently be drawn into multiple market studies, outside their direct industry. For instance, retailers could be drawn into market studies into logistics chains or the supply chain of a particular product. This would impose further costs and distractions.

33. Should the review recommend an agency be tasked with undertaking market studies, it should sit with MBIE not the Commerce Commission. The purpose of a market study is to obtain data to determine if a policy intervention is necessary to improve the operation of a market. This would conflict with the Commerce Commission's investigation and enforcement function.

34. Market studies should also only be imposed at the direction of a Minister, where there is clear evidence of significant public or industry concerns that need to be addressed. This is an important restriction given market studies can impose significant costs on industry participants and can have serious consequences on the composition of markets.

Yours sincerely,