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Submission on Discussion paper: Review of section 36 of the Commerce Act and other matters

Introduction

1. This submission is made by Matthews Law, a specialist competition & regulatory law firm.[1] We have previously been involved in consultation regarding unilateral conduct (domestically and internationally) and thank the Ministry of Business, Innovation & Employment (**MBIE**) for this opportunity to comment on its *Discussion Paper: Review of section 36 of the Commerce Act and other matters* (**Discussion Paper**).

2. The proposed amendments to section 36 will represent a significant change to how unilateral conduct is regulated. We commend MBIE for an excellent paper.

3. We recommend that MBIE carefully considers:

   a. whether the proposed effects test (as drafted) would meet MBIE's stated objective;

   b. clarifying the impact of amending section 36 on established access pricing principles;

   c. clarifying the relevance of the "purpose" element in an economic effects-based test;

   d. whether minimalist drafting provides sufficient guidance to the courts and/or businesses; and

   e. the potential uncertainty created by removing the IP exceptions at the same time as amending section 36.

4. We briefly expand on these points below.

Commentary

Does the proposed effects test (as drafted) meet MBIE's stated objective?

5. The Discussion Paper is critical of the current section 36, and how it has been interpreted by the courts. We understand this criticism – in particular, the comments that the courts' interpretation of section 36 may make the "take advantage" element of the test challenging (subject to our comments on ECPR below). We also see benefit in an economic effects-based test for anti-competitive unilateral conduct, which is consistent with the purpose of the Commerce Act 1986 (**Act**).

6. However, it is useful to reflect on the reasoning behind the design of section 36 and its forebears. These were intended to capture unilateral conduct directly aimed at harming a particular target (most likely a new entrant) in the context of concentrated markets. There may be logic to this approach – in most situations there may be one dominant player or an oligopoly structure, and the concern might be that those players could seek to prevent effective competition from new entrants developing. It is possible that the (assumed) "targets" of the unilateral conduct may not have reached a scale to be viewed as competitively significant.

[1] Matthews Law is recognised in leading directories, including Chambers Asia-Pacific (leading firm, and leading individuals – Band 1 & Associates to Watch), GCR 100 (19th edition – "Highly Recommended"), Best Lawyers (Competition & Consumer Law, and Regulatory Practice), Legal 500 (leading firm, and leading individuals – Band 1 and Next Generation Lawyers), and Who's Who Legal (Competition, TMT, and Transport – Aviation). We have significant international experience and are actively involved in international competition fora including the International Bar Association, the Inter-Pacific Bar Association and the American Bar Association and have represented New Zealand as a Non-Governmental Advisor at the International Competition Network.

7. The Discussion Paper seems to see this as a concern, stating "*New entrants intent on challenging the incumbents also require a degree of certainty that they will be able to compete on their merits and not be subject to anti-competitive responses by the incumbent*."

8. One could also see arguments as to whether the incumbent lacked *substantial market power* (particularly in oligopolistic industries), which the Discussion Paper does not see benefit in defining (*cf*. Australia). More relevantly, one could see arguments that restricting, preventing or deterring a new entrant might not in itself have a substantial impact on competition.

9. As such it may be worth MBIE reflecting further on whether the proposed effects-based test (as currently drafted) would address MBIE's concerns and stated objective. There may be some analogies with the concerns raised by some commentators around "creeping acquisitions" in the merger context, which have attracted significant publicity in relation to the technology industry lately.

The impact of amending section 36 on established access pricing principles should be considered

10. A significant portion of day-to-day section 36 issues seen by competition law experts relate to access pricing and/or refusals to grant access. There is certainty in this area, which does not appear to be mentioned in the Discussion Paper. Yet there seems scope for, at the very least, challenges to well-established case law on this point under the proposed amendments.

11. In *Telecom Corporation of New Zealand Ltd v Clear Communications Ltd* [1995] 1 NZLR 385 the Privy Council held that access pricing set in accordance with the Efficient Component Pricing Rule (ECPR) does not amount to a "use" of a dominant position, as pricing in this way is consistent with how a firm would act in a competitive market. The Privy Council in that case also endorsed Dr Kahn's principle of competitive parity, stating this principle and ECPR both, "*are designed to ensure that Clear and Telecom compete on a level playing field in the area in which they are to be competitors*."

12. The Discussion Paper does not appear to consider the potentially significant impact that amending section 36 may have on the applicability of these established pricing principles. For example, on one reading, a non-vertically integrated monopolist simply seeking to capture monopoly rents through ECPR pricing could be viewed – or at least argued – as having anti-competitive effects in downstream markets. Yet as the Discussion Paper notes, "*unilateral conduct laws do not seek to prohibit firms with substantial market power from charging higher prices and thus earning "monopoly rents.*""

13. An option could be to consider codifying these established access pricing principles in secondary legislation. If alternative pricing principles are to be adopted, then perhaps these should be clearly set out (as has been the case under the Telecommunications Act 2001).

The reasons for retaining a "purpose" element are unclear

14. The Discussion Paper states, "*the current 'purpose' requirement is misaligned with the rationale for having competition laws, which is to protect against harmful effects on the competitive process.*" As such, it would be useful if MBIE could explain why it proposes that the economic effects-based test should retain a "purpose" element, considering that section 80(1)(b) provides that businesses may be liable for attempts to breach Part 2 of the Act (including section 36).

Minimalist drafting provides minimal guidance

15. There may be an inconsistency in the Discussion Paper's approach. It expresses a concern that, if the existing section 36 was simply clarified or amended, the courts may still impose a comparative counterfactual test or some variant of it (ie courts would not interpret section 36 as intended). Yet the Discussion Paper also favours a minimalist drafting approach that provides little guidance to the courts (and businesses) about how section 36 *should* be interpreted (for example, by not introducing equivalents to the Australian sections 46(4)-(7) or including a list of proscribed prohibited conduct). This approach seems to have more confidence in the likely approach of the courts. We note that the Act previously listed factors for assessing whether a business had a "dominant position in a market." Australia also opted to define market power. The preference for clear, simple drafting (which we generally favour) seems inconsistent with prescriptive and complex drafting of the civil and criminal cartel prohibitions (and exceptions).

Removing the IP exceptions at the same time as amending section 36 may lead to uncertainty

16. We can see why MBIE may view the IP exceptions (and their removal) as inconsequential given the *current* interpretation of section 36.

17. However, it is more appropriate to consider the relevance of those exceptions under the proposed law, which does not appear certain. Arguably there is scope for considerable uncertainty around the treatment of intellectual property rights and their use under a new test. We recommend that further consideration be given to explaining exactly how an amended section 36 would apply to common situations (eg refusals to license IP, know-how etc) and/or what pricing principles might apply to any licensing obligations.

Matthews Law – 9 April 2019