

NEW ZEALAND RESPONSE

Predatory Pricing

Introduction

The following is the New Zealand Commerce Commission's (NZCC) response to the ICN unilateral conduct working group questionnaire on the analysis and treatment of predatory pricing claims in New Zealand. In preparing the response, the NZCC has used the definition of predatory pricing recommended by the working group, being a practice by which a firm temporarily charges low prices in order to limit or eliminate competition, and thereby allows the firm to raise prices subsequently. In addition, the response concerns only treatment of single product discounts; rather than pricing practices involving multiple products (including bundling, tying, and related prices). Unless otherwise stated, the response concerns conduct by a dominant firm or a firm with a substantial degree of market power.

The NZCC notes that there is limited case law on predatory pricing in New Zealand, with only two cases considered by the courts. The main predatory pricing case¹ on which New Zealand's case law is based, relates to a section of the Commerce Act 1986 that has subsequently been amended, although the essential elements of the new prohibition are similar to the previous prohibition. In addition, the court that finally determined the case, being the Judicial Committee of the Privy Council, has subsequently been replaced as the highest court of appeal in New Zealand. Since July 2004, the New Zealand Supreme Court is the final court of appeal and this court is yet to hear a case in relation to unilateral conduct.

Consequently, New Zealand case law on predatory pricing is not fully developed. However, despite the limited case law and the subsequent law and institutional reforms, the NZCC considers that the responses outlined in this questionnaire are likely to reflect the New Zealand position on predatory pricing for the foreseeable future. The current New Zealand position is closely aligned with Australian case law on predatory pricing.² The newly amended New Zealand prohibition is based on the existing equivalent Australian prohibition and New Zealand courts have referred with favour to Australian court judgments on the equivalent Australian prohibition.

If any questions relate to aspects of New Zealand's law or policy that are not well developed, the NZCC has noted this on the questionnaire and, in such cases, has not provided an answer.

¹ *Carter Holt Harvey Building Products Group Ltd v CC* [2006] 1 NZLR 145; (2004) 11 TCLR 200 (PC).

² Throughout the *Carter Holt Harvey* judgement, the Privy Council referred with favour to the Australian High Court decision *Boral Besser Masonry Ltd v ACCC* (2003) 195 ALR 609; (2003) 215 CLR 374.

Analysis (elements and evidence)

1. Please provide the main relevant texts (in English if available) of your jurisdiction's laws and guidelines on predatory pricing.

New Zealand's competition law, the Commerce Act 1986 ('the Act') does not contain a specific prohibition against predatory pricing. Rather predatory pricing would be one form of anticompetitive unilateral conduct covered under the generic prohibition in section 36 of the Act. Section 36 of the Act provides that:

- (2) A person that has a substantial degree of power in a market must not take advantage of that power for the purpose of –
 - a. restricting the entry of a person into that or any other market; or
 - b. preventing or deterring a person from engaging in competitive conduct in that or any other market; or
 - c. eliminating a person from that or any other market.

Section 36B of the Act provides that, for the purposes of section 36, the existence of any of the prohibited purposes, as the case may be, may be inferred from the conduct of any relevant person or from any other relevant circumstances.

These provisions may be compared to the prohibition that existed prior to the 2001 amendment on which the predatory pricing case law is based. Before May 2001, section 36 provided that:

- (1) No person who has a dominant position in a market shall use that position for the purpose of –
 - a. restricting the entry of a person into that or any other market; or
 - b. preventing or deterring a person from engaging in competitive conduct in that or any other market; or
 - c. eliminating a person from that or any other market.

The main amendment is a lowering of the threshold of requisite market power for persons subject to the prohibition from 'dominance' to 'substantial degree of power'. This change is likely to result in the prohibition applying to a greater number of persons and to a wider range of markets.

In other respects, the change from 'use' to 'taking advantage of', and the new section confirming that purpose may be inferred from objective evidence, is unlikely to significantly change the characterisation of the conduct that contravenes the prohibition, given the Privy Council's references to Australian precedents. Consequently, the NZCC shall not distinguish between the current and previous drafting of the prohibition in the remainder of this response.

Other sections that may impose liability for predatory pricing conduct relate to sections 27 and 36A of the Act.

Section 36A of the Act includes a further unilateral conduct prohibition relating specifically to persons with a substantial degree of power in Australian, trans-Tasman and/or New Zealand markets that take advantage of that power to harm competition in New Zealand markets. This prohibition was specifically introduced to replace anti-dumping trade remedies with a generic competition prohibition that would capture predatory pricing conduct. There has not been a contravention of this prohibition to date.

Section 27 relates to anticompetitive agreements. Section 27 provides that:

- (1) No person shall enter into a contract or arrangement, or arrive at an understanding, containing a provision that has the purpose, or has or is likely to have the effect, of substantially lessening competition in a market.
- (2) No person shall give effect to a provision of a contract, arrangement, or understanding that has the purpose, or has or is likely to have the effect, of substantially lessening competition in a market.

The New Zealand courts have been willing to find unilateral predatory pricing conduct liable under section 27 of the Act. The relevant case is *CC v Port Nelson Limited*, relating to charges for pilot services.³ However, unless otherwise stated, the responses in this questionnaire shall refer to section 36 of the Act.

The NZCC has not issued public guidelines on predatory pricing.

2. Please list your jurisdiction's criteria for an abuse of dominance/monopolization based on predatory pricing.

For liability under section 36 to be established, all three of the following elements must be established. It must be shown that a person:

- has a substantial degree of power in a market; and
- is taking advantage of that power; and
- is acting for one of the proscribed anticompetitive purposes.

The NZCC response to the ICN unilateral conduct questionnaire on assessment of dominance / substantial market power discusses the criteria to establish the first element of the prohibition. This analysis will not be repeated in this response.

In respect of the remaining two elements, the NZCC applies both general and specific criteria to assess a potential contravention based on predatory pricing.⁴ It is likely that both sets of criteria must be met to establish a predatory pricing contravention.

General rule

The Privy Council in *Carter Holt Harvey v CC* reaffirmed the notion that firms should not be prevented from competing vigorously.

³ *Port Nelson v CC* [1996] 2 NZLR 554 (CA); 5 NZBLC 103,762 (HC).

⁴ Mark Berry, *Competition Law*, NZ Law Review Commentary, 16 May 2005.

The public interest lies in preserving the ability of firms to compete with each other in a competitive market, on price as well as quality. It is not well served if a firm which has a dominant position in the market is penalised for cutting prices, when that same conduct if undertaken in the same circumstances by a firm which was not dominant would not be.⁵

The Privy Council outlined that the principle of ‘use’ (and by implication, ‘taking advantage of’) requires that a causal relationship is shown between the conduct which is alleged against the dominant firm and its dominance or market power. Consequently, the Council confirmed the need to apply a ‘counterfactual test’ to determine whether a firm has used its position of dominance. The Privy Council said:

It follows that if a dominant firm is acting as a non-dominant firm otherwise in the same position would have acted in a market which was competitive it cannot be said to be using its dominance to achieve the purpose that is prohibited.⁶

This counterfactual test is to be undertaken on an assessment of the facts of the case. In addition, the Privy Council referred to the Australian High Court decision in *Boral Besser Masonry Ltd* and confirmed that:

..the use by a dominant firm of its financial ability to cut prices must be distinguished from its use of its position of dominance, the measure of which is market power. The financial ability to cut prices is not market power. Cutting prices only becomes unlawful when the dominant firm is shown to have done so by use of its position of dominance.⁷

In terms of the ‘purpose’ element, the Privy Council has stated that anticompetitive purpose may be inferred from use of a dominant position producing an anticompetitive effect. However, it is dangerous to argue the converse that based on an anticompetitive purpose there has been a use of market power.⁸ The Privy Council stressed that it is not the purpose of section 36 to deny to a person who is in a dominant position in the market the opportunity to protect their market share when their position is threatened by competitors.

Specific rule

The Privy Council also developed a specific rule for predatory pricing conduct.

It is the ability to recoup losses because its price-cutting has removed competition and allows it to charge supra-competitive prices that harms consumers. Treating recoupment as a fundamental element in determining a claim of predatory pricing provides a simple means of applying the section without affecting the object of protecting consumer interests.⁹

Unfortunately, the Privy Council did not specifically discuss whether below-cost pricing is necessary for predatory pricing, although the firm in question was pricing

⁵ *Carter Holt Harvey* case, paragraph 66.

⁶ *ibid*, paragraph 52.

⁷ *ibid*, paragraph 60.

⁸ *Telecom Corp of NZ Ltd v Clear Communications Ltd* [1995] 1 NZLR 385; (1994) 6 TCLR 138.

⁹ *Carter Holt Harvey* case, paragraph 67.

below-cost. Rather it was the degree to which a firm can raise prices after the exit or deterrence of a competitor that was considered most important.¹⁰

3. Please explain the circumstances under which a firm’s pricing is, or may be, considered ‘predatory’ in your jurisdiction, by responding to the following questions:

a. As part of your analysis, does the price have to be below one or more measures of cost?

Yes. However, the choice of cost measure depends upon the facts of the case and the availability of suitable data.

i. If yes, please identify which of the following measures is/are used, as applicable:

Cost benchmark/measure	Used?		Comment
	Yes	No	
<u>Below marginal cost</u> (the cost of producing one more unit of output)	√		
<u>Below average variable cost</u> (cost that varies with output)	√		
<u>Below average avoidable cost</u> (all costs that can be avoided by not producing some or all output)	√		
<u>Below average long run incremental cost</u> (average variable costs and product-specific fixed costs)			
<u>Below average total cost</u> (cost including variable, fixed and sunk – non-recoverable – costs)			
<u>Other measure of cost</u> (Please identify)			

b. For each cost measure employed, please provide the definition of the measure used in your jurisdiction.

Cost measures are not explicitly defined. The NZCC uses internationally recognised economic concepts to calculate cost measures.

¹⁰ Similarly, McHugh J of the Australian High Court in *Boral Besser Masonry Ltd v ACCC* (at paragraph 273) commented:

In my view, what is required is not a bright line about costs but a more sophisticated analysis of the firm, its conduct, the firm’s competitors, and the structure of the market not only at the time in which the firm engaged in the conduct allegedly in breach of the Act but also before and after that conduct.

c. **Is the same cost measure applied in all cases?** No

i. **If different cost measures can be applied, for example on the basis of industry, please explain and provide examples, as available.**

To date, the NZCC has predominantly used average variable cost or average avoidable cost as the relevant cost measure. The choice of cost measure would depend on what makes economic sense in the context of the case and the particular market structure under investigation. For example, in a competitive market characterised by network effects, a firm may sell below cost early in the network's life cycle to attract sufficient customers to achieve scale economies on the demand-side (e.g. a telephone network). These features of market structure would be taken into account as part of the 'counterfactual test'.

ii. **If more than one cost measure can be applied in any individual case, please explain why and whether, in practice, this has raised issues.**

Not applicable.

d. **If price must be shown to be below cost, for which of the dominant firm's sales must this be shown?**

i. **Is the only relevant comparison between the cost measure and the dominant firm's average price for all of its sales in the relevant market?**

No.

(a) **If no, over which of the dominant firm's sales can cost be compared?**

The measure of price will depend on what makes economic sense in context of the case. In general, the NZCC has used the average or actual prices of the goods or services sold in that portion of the market in which the target of the predatory pricing competes. Examples of price measures are:

- in the *Carter Holt Harvey* case, the product market was that for building insulation products, in which the dominant firm sold a range of products, each having different composition. The NZCC focused on the average price of sales of the Wool Line product over the period of the below cost pricing, being the particular product that competed with the rival's product.
- in the *Tranz Rail Ferries* investigation¹¹, the NZCC used an estimate of incremental revenue as the relevant measure and

¹¹ Commerce Commission, *Tranz Rail Ferries Investigation Report*, 11 December 2003.

compared this to estimated incremental costs. The NZCC used this measure to test whether the dominant firm's conduct was only the most profitable action if it resulted in the rival exiting the market. The NZCC considered that, if incremental revenues were to exceed incremental costs even with the rival remaining in operation, the pricing strategy could not be regarded as predatory. However, if the reverse applied, with incremental costs exceeding incremental revenue, predation was likely, for without the additional benefit brought by the exit of the rival, the policy would result in a sacrifice of profits.

e. **Could a firm's price above average total cost ever be found to be predatory?**

Generally, no. The New Zealand courts have not considered cases relating to 'limit pricing'. However, there is likely to be a number of difficulties in establishing a contravention on this basis.

i. **If so, please explain the instances in which this might occur, and identify whether this has been the basis for actual enforcement.**

Not applicable.

f. **If prices do not have to be below a cost benchmark to be considered predatory, please explain the circumstances under which the firm's prices are considered predatory.**

Not applicable.

4. **To be unlawful, must the alleged predatory pricing occur in the market in which the firm holds a dominant position/substantial market power?**

Generally, yes. The alternative would be contrary to the Privy Council view that the financial ability to cut prices is not market power.

a. **If no, please explain.**

Not applicable.

5. **Apart from the cost criteria referenced in question 3 above, must other objective criteria, such as the duration or continuity of the pricing behavior, be demonstrated for a finding of liability under a predatory pricing theory?**

Yes.

a. **If so, please explain. For example, if the behavior must be sustained over a certain time period, why, and for what period?**

The duration of the pricing behaviour would be taken into account in considering whether the behaviour would be likely to occur in a competitive market.

There is some New Zealand precedent to suggest that predation can be short term. In *New Zealand Magic Millions Limited*, the court noted:

In *Victorian Egg Marketing Board v Parkwood Eggs Pty Ltd* (1980 20 ALR 129) the Federal Court of Australia indicated that one of the hallmarks of anti competitive or predatory conduct was if one found a party engaging in sporadic activity for a temporary purpose. Bowen, CJ said at page 137:

“The view has been expressed that the sporadic element, that is to say competition which is not intended to be permanent but is for a temporary purpose, is a hallmark of a predatory practice and distinguishes it from legitimate competition...”¹²

However, the predatory conduct would likely need to be of sufficient duration such that it is capable of harming competition consistent with the proscribed purpose.

6. **On what type of evidence do you rely to prove predatory pricing? Please explain, including examples as appropriate.**

a. **Are cost data used?** Yes

i. **If so, are cost data from the firm used?**

Yes. As an initial exercise the NZCC may use published financial statements, but in any major investigation, the NZCC will use its powers to require the dominant firm to provide relevant cost data.

b. **Are there circumstances when cost data of other firms can be used?**

Yes.

i. **If so, please specify the circumstances.**

The NZCC has used cost data of the rival to test the veracity of the dominant firms' cost data.

Theoretically, if the rival is more efficient than the dominant firm, the dominant firm's price relative to the rival's average variable costs may be relevant in assessing the likelihood of recoupment. That is, recoupment may only be likely if the pricing strategy means that the more efficient rival is incurring losses and it is forced to exit the market. However, the NZCC would not use a measure of rival's costs if the reverse was true. That is, if the dominant firm is more efficient than the rival.

c. **What other data or information is used, if any? Please provide examples as relevant.**

Not applicable.

¹² *New Zealand Magic Millions Limited v Wrightson Bloodstock Limited*, [1990] 1 NZLR 731; (1990) 3 NZBLC 101,501 (HC)

7. **Does pricing below a particular cost benchmark create a presumption of predatory pricing?**

No. Pricing below a measure of cost would be a necessary but not sufficient condition in determining whether the firm was predatory pricing.

a. **If yes, is this presumption rebuttable or irrebuttable? Please explain.**

Not applicable.

b. **If the presumption is rebuttable, what must be shown to rebut the presumption?**

Not applicable.

8. **Is there a “safe harbor” from a finding of predatory pricing for pricing above a particular cost benchmark?** No

a. **If yes, please explain, including the terms of the safe harbor.**

Not applicable.

9. **Is recoupment (obtaining additional profits that more than offset profit sacrifices stemming from predatory pricing) required for a finding of liability under predatory pricing rules in your jurisdiction?** Yes

If so:

a. **Is this assessment conducted separately from the analysis of the firm’s market power and the predation?**

Yes. However, if the firm is unlikely to be able to recoup its losses, this may call into question whether the firm holds the requisite level of market power necessary to contravene the prohibition. This matter was addressed by the Australian High Court in *Boral Besser Masonry*:

The greater the degree of recoupment that a firm can achieve, the greater is its market power. But a firm that is unable to recoup any of its losses has no market power.¹³

b. **What factors are employed in assessing recoupment in your jurisdiction?**

Recoupment is likely to be assessed in terms of the dominant firm’s likely ability to raise prices above costs following the intended exit of the rival firm. If the recoupment arises solely through increased demand for the dominant firm’s products following the exit of the rival firm, with no increase in prices or harm to consumers, this is unlikely to contravene the prohibition.

¹³ *Boral Besser Masonry Ltd v ACCC* (2003) 195 ALR 609; (2003) 215 CLR 374, paragraph 289.

In the *Carter Holt Harvey* case, the High Court considered that a form of recoupment was an intended consequence of the dominant firm's conduct. The building insulation market was a differentiated product market. The dominant firm's highly profitable Pink Batts glass wool product had high market share, but this was threatened by the rival's new wool insulation product. The dominant firm launched a comparable wool/polyester insulation product in response to the competitive threat. The High Court considered that recoupment was likely from pricing this comparable product at a level in circumstances which it knew would undermine a rival's business and preserve a highly profitable product from further harm.

INZCO could recoup the cost of the Wool Line special pricing arrangement if the scheme meant that NWP was constrained from expanding in the market or eliminated from it. The recoupment would take the form of maintaining the list prices of Pink Batts at levels that were otherwise threatened by NWP, and at the same time increasing its market share for Pink Batts and other INZCO products.¹⁴

The Privy Council did not specifically address this theory of recoupment in its decision, except to note that

..there was no evidence that the '2-for-1' pricing of Wool Line was resorted to by INZCO with a view to charging supra-competitive prices at a later date on that or any other of its products.¹⁵

This view may have been based on the fact that the High Court considered that the South Island retail insulation market at this time was intensely competitive. The Privy Council noted that:

It is probable that, if NWP's ability to remain in business had been ended by the "2-for-1", another wool-based product similar to Wool Bloc would have been available within a short time. Merchants would have marketed such a product if it was worth their while to do so.¹⁶

Consequently, the Privy Council did not find evidence of likely recoupment.

c. Is there a specific recoupment calculation or amount to be shown?

No.

i. If so, what is this?

Not applicable.

¹⁴ *CC v Carter Holt Harvey Building Products Ltd* (2000) 9 TCLR 535, Supplementary Judgement of Professor Lattimore, paragraph 51.

¹⁵ *Carter Holt Harvey Building Products Ltd v CC* (2004) 11 TCLR 200, paragraph 68.

¹⁶ *Ibid*, paragraph 21.

d. **Is there a relevant time period for recoupment?** No

ii. **If so, what is it?**

Not applicable.

e. **Is it possible for recoupment to occur in a market different than the one in which the predatory pricing took place?**

This has not been tested in New Zealand.

i. **If so, please explain and provide relevant examples.**

Not applicable.

f. **What degree of likelihood of recoupment is required (e.g., possibility or probability)?**

i. **Please provide examples of the recoupment standard of likelihood employed as part of your recoupment assessment.**

This has not been tested in New Zealand.

10. **Is the firm's intent relevant in predatory pricing cases?** Yes.

a. **If so, please describe the relevant type(s) of intent, and the evidence used to show the required intent, providing available examples.**

To successfully establish predatory pricing, an anticompetitive purpose must be established. The three proscribed anticompetitive purposes are outlined in section 36. Section 36B provides that the existence of one of the anticompetitive purposes may be inferred objectively from the conduct of any relevant person or from any other relevant circumstances.

As outlined in the response to question 2, the courts have said that anticompetitive purpose may be inferred from the firm having taken advantage of its market power. Consequently, in predatory pricing cases inferences of anticompetitive purpose might be drawn from such things as:

- whether the price cuts were directed at a particular competitor or competitors in terms of the timing, duration and focus;
- the level of the price;
- the ability to recoup; and
- the absence of a legitimate business justification.

For example, in *Carter Holt Harvey*¹⁷ the Court of Appeal noted ample evidence in the form of company documents indicating that the firm's objective was to restrict the competitor's growth in the market and expansion into other regions. The court noted that such rhetoric would be common in

¹⁷ *Carter Holt Harvey Building Products Group Ltd v CC* (2001) 10 TCLR 247 (CA), para 78.

firms competing vigorously and legitimately. But when the stated intentions were considered together with the conduct in the circumstances, being those in which the firm was found to have used its dominant position, it could be concluded that the requisite purpose existed.

- b. **If objective conditions for predatory pricing -- for example, pricing exceeding a certain cost benchmark or recoupment – are not demonstrated, does intent matter?**

No. As outlined in the response to question 2, in the absence of proof of taking advantage of market power it is dangerous to infer an anticompetitive purpose.

11. **In addition to proving below-cost pricing, must effects, such as market foreclosure or consumer harm, be demonstrated to establish liability?**

Strictly, no. Section 36 is concerned with anticompetitive purpose rather than effects. However, purpose can be inferred from objective likelihoods. In addition, while the general and specific criteria for establishing predatory pricing are primarily focused on the form of the conduct, these criteria are based on theories of harm and such matters could be taken into account by the courts.

The courts have recognised that harm to consumers arises from the ability of dominant firms to subsequently recoup losses through raising prices. In addition, harm may arise from the exclusion of an equally or more efficient competitor from the market. Therefore, evidence of the likelihood of recoupment (as discussed in question 9) would indicate likely harm to consumers, as would evidence of the likely removal of a more efficient competitor. But liability under the section would not require that the recoupment or exit took place.

Evidence of the effects of the proscribed conduct, if available, would likely be relevant in assessing penalties.

- a. **If yes, please explain the elements assessed (e.g., exit or delayed entry of competitors, price increases, prevention or delay of price decreases) and the types of evidence required to do so.**

Not applicable.

Justifications and Defenses

12. **What type of justifications or defenses, if any, are permitted for predatory pricing, e.g., an efficiency, meeting competition or objective necessity defense? Please explain and provide examples, as relevant.**

The Privy Council ‘counterfactual test’ enables any price-cutting conduct by a firm with market power to be characterized in ways that would not contravene section 36. As outlined in response to question 2, this test requires that it be shown that the firm acted in a way that a firm otherwise in the same position but in a competitive market would have acted. Consequently, there is a range of price-cutting conduct that could

occur in a competitive market that may not contravene the prohibition, but there is no statutory defence to section 36 *per se*.

Examples of alternative explanations of the conduct are:

- promotional pricing – a firm may price below cost to induce consumers to try a new product;
- network effects – in a market with network effects, a firm may sell below cost early in the network’s life cycle to attract sufficient customers to achieve scale economies on the demand-side (e.g. a telephone network);
- loss leaders for complementary products or services – a firm may price below cost on one product or service to boost demand (and profits) in a complementary product or service (e.g. free car parking at a supermarket);
- meeting competition – a firm may match its competitors’ prices, even if the prices are below its own costs, in order to retain market share for a period.
- clearance of old stock or excess product – a firm may face a demand shock and price below cost to stimulate demand or clear obsolete stock.¹⁸

The *Carter Holt Harvey* case explores the issues of promotional pricing and meeting the competitor’s prices. At the High Court, it was argued in evidence that the below cost pricing related to promotional pricing of a new product by the dominant firm. The High Court judgment discusses the benefits of promotions. Promotions result in reduced prices to consumers and may increase market efficiency by providing valuable information to potential customers on the attributes and availability of new products. However, the High Court considered that there should be limits on the extent that dominant firms should engage in promotional pricing. It considered:

..promotional arrangements by dominant firms cannot involve such a large proportion of total market demand over a given time period that they cause significant harm to the sales of competitors. If a dominant firm were permitted to sell a large proportion of total market demand for a product, priced significantly below cost for a long period of time, competition would be harmed.¹⁹

In addition, the facts of the case were that the promotional price set by the dominant firm for the new product, while being significantly below cost, was at a level roughly the same as the price of the competitor’s products. The dominant firm also set this price in response to demands by retailers for a ‘competitive price’. The High Court judgment discusses:

It follows that in this case there is no price matching defence to allegations of predatory pricing. Predatory pricing involving setting a price, which matches (is roughly the same as) the price of the product of another firm, demonstrates competitiveness in the marketing or business management sense. This is price aping. It can imply the use of dominance.²⁰

¹⁸ Paul G Scott, *Is a Dominant Firm’s Below Cost Pricing Always a Breach of Section 36 of the Commerce Act?*, New Zealand Universities Law Review, Vol. 21, June 2004.

¹⁹ *CC v Carter Holt Harvey Building Products Ltd*, [200] 9 TCLR 535, Supplementary judgement of Professor Lattimore, paragraph 54.

²⁰ *Ibid*, paragraph 17.

On appeal, the Privy Council considered the same conduct in terms of ‘meeting the competition’ in relation to the ‘counterfactual test’.

..its is by no means self evident that [the dominant firm] would have behaved any differently if it had not been in a dominant position in the market when it was deciding what it should do to meet the competition which it was facing in that market from Wool Bloc. It would have been presented with the same complaint that the price which was originally set for Wool Line was uncompetitive. The obvious response, in a truly competitive market, was to cut the price of Wool Line to a level that was competitive.²¹

In referring to the High Court’s reasoning that setting a price which matched the price of the product of another firm, or so-called “price aping”, could imply the use of dominance, the Privy Council said:

It is hard to reconcile this process of reasoning with the Board’s advice in *Telecom v Clear*.²²

More generally, the Privy Council also cites with approval a statement from the Australian High Court case on *Boral Besser Masonry* that:

..if the impugned conduct has a business rationale, that is a factor which points against a finding that the conduct constitutes a taking advantage of market power.²³

It is likely on the basis of this decision, that ‘meeting competition’ is a matter that would be considered when establishing whether the firm has taken advantage of its market power for an anticompetitive purpose. There is also an indication that other legitimate business justifications may be considered.

However, it is not clear that any business justification, even if objectively valid in the circumstances of the case, would be determinative in not finding a contravention if there was also evidence of below cost pricing and the likelihood of recoupment. This would be assessed in the circumstances of the case.

- a. **What is the standard of proof applicable to these defenses? Who bears the burden of proof? What evidence is required to demonstrate that these defenses or justifications are met?**

As outlined above, any business justification for the conduct is not a statutory defence *per se*, but rather relates to whether the firm has taken advantage of its market power for an anticompetitive purpose. Consequently, the normal civil standard of proof applies and the burden is on the plaintiff to show a causal connection between the alleged anticompetitive conduct and the requisite market power.

The NZCC’s experience is that the ‘counterfactual test’ has not proved easy to apply in many cases. Determining what the hypothetical firm and competitive market would look like is a complex and contentious task. One has to consider (relative to existing market conditions) such matters as what the firm

²¹ *Carter Holt Harvey* case, paragraph 19.

²² *Ibid*, paragraph 46.

²³ *Ibid*, paragraph 54.

would look like, how many competitors there would be, what the conditions of entry would be, the level of market prices, and the extent to which customers would be contracted. Different assumptions can produce different results in the analysis of whether the firm would or could legitimately engage in the same conduct in a competitive market.

Enforcement

13. **Please provide the following information for the past ten years (as information is available):**

a. The number of predatory pricing cases your agency reviewed (investigated beyond a preliminary phase).

The NZCC has carried out approximately 19 investigations into predatory pricing in the last 10 years.

b. The number of these cases that resulted in:

i. an agency decision that the conduct violates antitrust rules;

In New Zealand, the NZCC does not make findings of contraventions. Only the courts may determine a contravention. However, the NZCC made a decision to initiate court proceedings for one of the 19 cases (i.e. the *Carter Holt Harvey* case).

ii. a settlement with relief (i.e. the NZCC may issue warnings or enter into administrative settlements).

None.

c. The number of agency decisions issued, if any, that held that the practice did not violate your jurisdiction's predatory pricing rules (i.e., "clearance decisions").

The NZCC does not make findings as to contraventions and, as such, it does not issue 'clearance' decisions. However, the NZCC did not take any enforcement action in relation to 18 of the 19 investigations.

d. Each of the number of agency decisions or settlements that were: challenged in court and, of those, either (i) overturned by court decision, or (ii) confirmed by court decision.

In relation to the one case that proceeded to court, the High Court, being the court of first instance, found a contravention of section 36. Pecuniary penalties of NZ\$525,000 were imposed. The case was further appealed, to the Court of Appeal and finally to the Privy Council (being the final court of appeal at that time). The Court of Appeal upheld the decision, but the Privy Council overturned the finding and found no contravention on a 3:2 split decision.

The NZCC's only other predatory pricing case heard by the courts was in 1995, over 10 years ago. In *CC v Port Nelson Ltd* the High Court found a contravention of section 27 in relation to predatory pricing, amongst other conduct. Pecuniary penalties of NZ\$100,000 were imposed in relation to the predatory pricing contravention. The case was appealed to the Court of Appeal, where the decision in relation to predatory pricing was upheld.

14. **Does your jurisdiction allow private cases challenging predatory pricing?**

Yes.

- a. **Please provide a short description of representative examples, as available.**

There have been no private predatory pricing cases before the courts.

15. **Is predatory pricing a civil and/or a criminal violation of your jurisdiction's antitrust laws?**

Predatory pricing is a civil violation. Sanctions may include pecuniary penalties, injunctions or other court orders.

- a. **If both, what are the differences in the criteria applied to these categories?**

Not applicable.

- b. **On what basis does the agency choose to bring a criminal or civil case?**

Not applicable.

16. **As relevant, please provide a short English summary of the leading predatory pricing decisions/cases in your jurisdiction, including information on the method used to calculate costs, to the extent applicable, and, if possible, a link to the English translation, an executive summary or press release of the case.**

Port Nelson Limited²⁴

Port Nelson Limited (PNL) carried on the business of providing port facilities and associated services at Nelson, New Zealand. PNL provided tug services to shippers using two tugs it owned and pilot services secured under contract to a private firm, Tasman Bay Maritime Pilots Ltd (TBMP). In 1990, TBMP decided to operate independently and offer pilotage at Port Nelson direct to shippers. PNL elected to continue to offer pilotage using employees, thus for the first time, shippers had a choice of pilot services at Port Nelson.

PNL responded to this competition by introducing three changes:

²⁴ *Port Nelson v CC* [1996] 2 NZLR 554 (CA); 5 NZBLC 103,762 (HC).

- refusing to supply its tugs for towing services to any shipper that is piloted by an independent pilot ('the tug tie');
- offering a 5 percent discount to shippers that acquired the full package of port services, being tugs, pilotage, and ship lines, ('the discounted bundle'); and
- setting a \$100 minimum charge for PNL pilot services ('the below-cost service').

It is the third element relating to the \$100 minimum charge that the NZCC alleged to be predatory. The High Court firstly considered the scale of fees, being pilot services charged on the basis of gross registered tonnage (GRT) of vessels and noted that such a scale did not necessarily equate the fee with the costs of vessel movement at each point on the scale. A GRT scale almost certainly will undercharge actual costs of movement of small vessels, and overcharge actual costs of movement of large vessels, however cost is calculated. This was not considered objectionable, so long as overall there is full recovery of costs.

The \$100 minimum charge related to the provision of pilot services to vessels under 2500 GRT. The High Court considered various methodologies for calculating PNL's actual costs of vessel movement, including fully allocated costs and an opportunity or avoidable costs approach. Regardless of the methodology used, PNL's cost of providing pilotage for vessels under 2500 GRT exceeded the \$100 minimum charge. TBMP's costs also exceeded this charge.

The High Court noted that the GRT scale may have resulted in cross-subsidisation for pilotage services between vessel classes. However, it noted that the effect of the 'tug tie' and 'discounted bundle' was to prevent TBMP from providing services to shippers with vessels over 2500 GRT, so that it could only compete for pilotage services in relation to small vessels. In addition, the extent of the below cost pricing for vessels at this point in the fee scale and PNL's lack of an alternative business justification for the apportionment of certain costs at that portion of the scale, led the High Court to conclude that the conduct was likely to result in a substantial lessening of competition in contravention of section 27 of the Act.

This decision was upheld on appeal to the Court of Appeal.

Carter Holt Harvey²⁵

From the early 1990s, INZCO, a subsidiary of the Carter Holt Harvey group and a major participant in the building insulation materials market, was facing threats to its market share for its fiberglass Pink Batts product. The major threat came from a new wool product Wool Bloc produced by a Nelson firm NWP. Wool Bloc was successfully launched in the Nelson/Marlborough region.

Under pressure from retail merchants, INZCO developed and marketed a wool/polyester product called Wool Line. At first Wool Line was introduced on the market at too high a price and sales were not good. INZCO then introduced a '2 for

²⁵ *CC v Carter Holt Harvey Building Products Ltd*, [2000] 9 TCLR 535 (HC); *Carter Holt Harvey Building Products Group Ltd v CC* (2001) 10 TCLR 247 (CA); *Carter Holt Harvey Building Products Group Ltd v CC* [2006] 1 NZLR 145; (2004) 11 TCLR 200 (PC).

1' strategy, whereby retail merchants were given two bales of Wool Line for the price of one. INZCO knew the merchants would pass on the price decrease to the public. The '2 for 1' strategy was maintained for 7 months in 1994, and was extended to Queenstown where Wool Line was also enjoying success. There was a sharp reduction in NWP's sales of Wool Bloc although the effect of the '2 for 1' pricing on those sales could not be precisely determined.

The High Court noted the strength of INZCO's relationships with its distributors, which extended to all of the large hardware merchants in the Nelson/Marlborough region. In addition, the High Court noted the significant evidence of below-cost pricing for Wool Line. It made references to INZCO's prices being 30 – 40 percent below average variable cost and 17 – 28 percent below the costs of production. In addition, it considered that, while INZCO would not be able to recoup its losses on Wool Line in the ordinary sense, this strategy was likely to result in commercial gain. That is, by pricing Wool Line at a level and in circumstances in which it knew would undermine NWP's business, INZCO was able to preserve the position of its highly profitable product, Pink Batts, from further harm.

The High Court found that INZCO had contravened section 36 of the Act. This was upheld on appeal by the Court of Appeal, but overturned by the Privy Council on a 3:2 split decision.

The Privy Council considered that INZCO had not used its market power for an anticompetitive purpose. Rather INZCO had acted in the same way that a firm in a competitive market would act by meeting the competition.

Media releases for the cases are available on the NZCC's website:
www.comcom.govt.nz

17. **Please provide any additional comments that you would like to make on your experience with predatory pricing rules and their enforcement in your jurisdiction, including, as appropriate but not limited to:**
- a. **Whether there have there been or you expect there to be major developments or significant changes in the criteria by which you assess predatory pricing, explaining these developments as relevant.**
- No comments.
- b. **Whether there are significant policy and/or practical considerations that may lead to greater or lesser agency enforcement against predatory pricing pursuant to unilateral conduct rules in your jurisdiction, e.g., concern with the risks of false positives/false negatives, the existence of related laws such as a general ban on below-cost pricing, limited evidence of consumer harm, and/or difficulties in obtaining reliable cost data (please provide explanation as relevant).**

No comments.

Exclusive Dealing/Single Branding

Introduction

The following is the New Zealand Commerce Commission's (NZCC) response to the ICN unilateral conduct working group questionnaire on the analysis and treatment of exclusive dealing (referred to as single branding in some jurisdictions) by ICN member competition authorities. For the purposes of this questionnaire, the NZCC refers to 'exclusive dealing' and 'single branding' as conduct that requires or induces customers or suppliers to deal solely or predominantly with that firm. Also excluded from this definition is conduct related to tying, bundling, loyalty discounts, rebates or related practices. Unless otherwise stated, the questions and responses concern conduct by a dominant firm or a firm with a substantial degree of market power.

The NZCC responses are based on agency practice, legal guidelines, relevant case law, etc. If any questions relate to aspects of New Zealand's law or policy that are not well developed, the NZCC has noted this on the questionnaire and, in such cases, has not provided an answer.

Legal Basis and Specific Elements

1. **Please provide the main relevant texts (in English if available) of your jurisdiction's laws and guidelines on exclusive dealing/single branding.**

New Zealand's competition law, the Commerce Act 1986 ('the Act') does not contain a specific prohibition against exclusive dealing. Rather exclusive dealing would be one form of anti-competitive unilateral conduct covered under the generic prohibition in section 36 of the Act. Section 36 provides that:

- (2) A person that has a substantial degree of power in a market must not take advantage of that power for the purpose of –
 - d. restricting the entry of a person into that or any other market; or
 - e. preventing or deterring a person from engaging in competitive conduct in that or any other market; or
 - f. eliminating a person from that or any other market.

Section 36B of the Act provides that, for the purposes of section 36, the existence of any of the prohibited purposes, as the case may be, may be inferred from the conduct of any relevant person or from any other relevant circumstances.

These provisions may be compared to the prohibition that existed prior to the 2001 amendment on which the exclusive dealing case law is based. Before May 2001, section 36 provided that:

- (1) No person who has a dominant position in a market shall use that position for the purpose of –

- d. restricting the entry of a person into that or any other market; or
- e. preventing or deterring a person from engaging in competitive conduct in that or any other market; or
- f. eliminating a person from that or any other market.

The main amendment is a lowering of the threshold of requisite market power for persons subject to the prohibition from ‘dominance’ to ‘substantial degree of power’. This is likely to result in the prohibition applying to a greater number of persons and to a wider range of markets.

In other respects, the change from ‘use’ to ‘taking advantage of’, and the new section confirming that purpose may be inferred from objective evidence, is unlikely to change the characterisation of the conduct that contravenes the prohibition. Consequently, the NZCC shall not distinguish between the current and previous drafting of the prohibition in the remainder of this response.

Another section that may impose liability for exclusive dealing is section 27 of the Act relating to anti-competitive agreements. Section 27 provides that:

- (1) No person shall enter into a contract or arrangement, or arrive at an understanding, containing a provision that has the purpose, or has or is likely to have the effect, of substantially lessening competition in a market.
- (2) No person shall give effect to a provision of a contract, arrangement, or understanding that has the purpose, or has or is likely to have the effect, of substantially lessening competition in a market.

Under section 3(5) contracts can be aggregated to determine whether there is an effect of substantial lessening of competition in a market.

The only New Zealand case law on exclusive dealing considered the issue under section 27. The NZCC has not issued public guidelines on exclusive dealing.

2. **Please list your jurisdiction’s criteria for an abuse of dominance/ monopolization based on exclusive dealing.**

Section 36 (taking advantage of market power)

For liability under section 36 to be established, all three of the following elements must be established. It must be shown that a person:

- has a substantial degree of power in a market;
- is taking advantage of that power; and
- is acting for one of the proscribed anti-competitive purposes.

The NZCC response to the ICN unilateral conduct questionnaire on assessment of dominance / substantial market power discusses the criteria to establish the first element of the prohibition. This analysis will not be repeated in this response.

The Privy Council in *Carter Holt Harvey v CC* reaffirmed the notion that firms should not be prevented from competing vigorously.

The public interest lies in preserving the ability of firms to compete with each other in a competitive market, on price as well as quality. It is not well served if a firm which has a dominant position in the market is penalised for cutting prices, when that same conduct if undertaken in the same circumstances by a firm which was not dominant would not be.²⁶

The Privy Council outlined that the principle of ‘use’ (and by implication, ‘taking advantage of’) requires that a causal relationship is shown between the conduct which is alleged against the dominant firm and its dominance or market power. Consequently, the Council confirmed the need to apply a ‘counterfactual test’ to determine whether a firm has used its position of dominance. The Privy Council said:

It follows that if a dominant firm is acting as a non-dominant firm otherwise in the same position would have acted in a market which was competitive it cannot be said to be using its dominance to achieve the purpose that is prohibited.²⁷

Testing whether the behaviour would have occurred without the market power indicates whether the market power can be said to have caused the behaviour. This test does not ask whether the behaviour is the cause of any anti-competitive effect.

Anti-competitive effect is relevant to the issue of anti-competitive purpose. In terms of the ‘purpose’ element, the Privy Council has stated that anti-competitive purpose may be inferred from use of a dominant position producing an anti-competitive effect. However, it is dangerous to argue the converse that based on an anti-competitive purpose there has been a use of market power.²⁸ The Privy Council stressed that it is not the purpose of section 36 to deny to a person who is in a dominant position in the market the opportunity to protect their market share when their position is threatened by competitors.

The New Zealand Courts have not applied section 36 to exclusive dealing contracts. It is not clear how the New Zealand courts might apply the counterfactual test to exclusive dealing. Given exclusive dealing commonly occurs in competitive markets it may be difficult to satisfy the counterfactual test. However, application of the counterfactual test will always depend on the facts of the particular case.

There are two situations in which it may be more likely that it could be argued that the behaviour would not be likely to occur in a competitive market. First, if the behaviour could not be justified on efficiency grounds. Second, a breach of section 36 is more likely to be found in circumstances in which a dominant supplier imposes exclusivity as a condition of supply.

²⁶ *Carter Holt Harvey Building Products Group Ltd v CC* [2006] 1 NZLR 145; (2004) 11 TCLR 200 (PC) paragraph 66.

²⁷ *ibid*, paragraph 52.

²⁸ *Telecom Corp of NZ Ltd v Clear Communications Ltd* [1995] 1 NZLR 385; (1994) 6 TCLR 138.

Section 27 (anti-competitive arrangements)

Section 27 prohibits a person from entering into a contract, arrangement or understanding containing a provision which has the purpose, effect or likely effect of substantially lessening competition in a market. Substantial is defined in section 2 as “real or of substance”. The Courts have described substantial as more than insubstantial or nominal.²⁹

Although market power is not specifically referred to as an element of section 27 it is generally recognised that market power concerns underlie the ‘substantial lessening of competition threshold’. In assessing whether a substantial lessening of competition has occurred (or is likely to occur) in the market under consideration, the question is not whether or not a party has attained an absolute level of market power, or reached some other point on the spectrum of market power. Rather it is concerned with any changes that may have occurred to one or more of the parties’ market power, as a result of the behaviour at issue. A substantial lessening of competition is a lessening of competition which creates, enhances or maintains market power, and refers to the ability to raise prices or otherwise act independently of competition.³⁰

The lessening of competition should be assessed by reference to the impact of the practice on the functioning of the particular market.³¹ The question is whether the practice in question has affected the functioning of the market such that unilateral or coordinated market power has been created, maintained or enhanced.

In order to assess the impact of the practice on the level of competition in the market the Courts have applied a counterfactual analysis. The Courts consider the level of competition that would otherwise have existed in the market but for the particular practice in question.

The Courts have also taken a net approach to pro-competitive and anti-competitive effects. This allows efficiencies to be considered in determining whether or not a substantial lessening of competition has occurred.³²

²⁹ *Port Nelson Ltd v Commerce Commission* [1995] 6 TCLR 406

... reference in s 27(1) to ‘substantially lessening competition’ is taken as meaning ‘lessening competition in a way which is more than insubstantial or nominal’. The merely ephemeral and minimal will not suffice. Inevitably, that will involve some attention to relativity; and in the end be a question of judgment on a matter of degree.

³⁰ *Weddel Crown Corp* (1987) 1 NZBC (Com) 104,200:

To what extent does the lessening of competition strengthen market power of the applicants in the defined market?

³¹ In *Radio 2 UE Sydney Pty Ltd v Stereo FM Pty Ltd* (1982) ATPR 40-318 Lockhart J said at p 43,918:

In the context of sec 45 the word “substantial” is used in a relative sense. The very notion of competition imports relativity. One needs to know something of the businesses carried on in the relevant market and the nature and extent of the market before one can say that any particular lessening of competition is substantial.’

³² *Fisher & Paykel Ltd v Commerce Commission* (1990) 2 NZLR 731

The pro-competitive benefits of exclusive dealing are claimed by F&P to be product quality, cost savings, lower real prices and higher level of efficiency. These are said to furnish both consumer advantage and the protection of F&P’s investment from “free riding”. These pro-

In the *Fisher & Paykel* case³³ the High Court specifically considered whether or not an exclusive dealing contract had the purpose, effect or likely effect of substantially lessening competition in a market. Fisher & Paykel's contracts with dealers for the supply of whiteware contained exclusive dealing provisions terminable on 90 days notice. Fisher & Paykel's market share was 80 percent and the foreclosure of retail outlets represented 55 percent.

Exclusive Purchasing and Supply Arrangements

3. **How does your jurisdiction define single branding or exclusive dealing? For example: Must a firm require that all purchases come from it or that all sales go to it? Can something less than “all purchases” or “all sales” be considered single branding or exclusive dealing? Please specify (providing actual percentages, as relevant).**

There is no specific definition of exclusive dealing in the Commerce Act or any guideline issued by the NZCC.

Section 36 of the Act focuses on the behaviour of the dominant firm and asks whether it would have behaved the same way in a competitive market. Under this section it is not necessary to show an 'all sales' requirement. Section 27 of the Act focuses on 'effect or likely effect' of the provision. Exclusive dealing would contravene that section if the exclusive dealing requirement results in or is likely to result in a substantial lessening of competition. This effect may arise at some level less than 100 percent of sales.

In the *Fisher & Paykel* case, the exclusive dealing arrangement related to 100 percent of purchases of whiteware by the participating retail merchants. In addition, the retail merchants were required to 'give preference' to Fisher & Paykel 'brown goods' (TVs, stereos, etc).

4. **Is the duration of the arrangement relevant to your assessment?**

Yes

- a. **If so, please explain how and why, providing examples.**

When determining the 'effect or likely effect' of an exclusive dealing provision, duration will be relevant but not determinative. As noted above, it is section 27 which specifically considers the effect or likely effect of an exclusive dealing provision. Effect is also relevant when considering the likelihood that an anti-competitive purpose should be inferred under section 36.

An exclusive dealing provision in a contract of short duration is unlikely to raise competition concerns. However, the term of the contract is not

competitive effects are first weighed in the balance with the “substantially lessening competition” effects in the market as found by the majority.

³³ *Fisher & Paykel Ltd v Commerce Commission* (1990) 2 NZLR 731.

necessarily the key factor in determining the duration of the contract. In particular, the ability to terminate the contract and the notice period required may mitigate the competition effects of a longer term contract. In the *Fisher & Paykel* case a crucial factor in determining that the contract did not substantially lessen competition was the fact that the contract could be terminated on 90 days notice.

Alternatively, the existence of barriers to switching can increase the effective duration of the contract. Such barriers include the significance of the brand or the existence of bundling arrangements or other switching costs. For example:

- If the brand of the product is strong this may create a barrier to switching even in the absence of a long term. The nature of exclusive dealing arrangements are such that the retailer is forced to forego product variety. In the case of a differentiated product market a retailer may prefer the most popular brand. The brand advantage becomes much more significant under exclusive dealing arrangements. However, in the *Fisher & Paykel* case the High Court recognised that:

... F & P has earned its reputation which should not be lightly taken away from it under the guise of protecting competition.

- If a supplier conditions the supply of a bundle of products to the retailer on the basis of exclusivity, a new entrant or supplier that cannot supply that bundle of products may be unsuccessful in attracting the business of the retailer. Again in this situation exclusive dealing could raise the concern that even in the absence of the long term it would be unlikely that retailers would switch.

5. **Must the firm's use of such arrangements cover a substantial portion of the market?**

Yes

- a. **If so, how do you interpret this requirement, including any relevant percentage thresholds for the purchase or supply covered, and the evidence needed to determine whether this is met?**

The Courts have not specified a minimum threshold of market foreclosure in order to determine a contravention. In the *Fisher & Paykel* case the proportion of the market covered by the exclusive dealing provision was not sufficient to raise concerns. Fisher & Paykel had 80 percent of market sales, and had entered into exclusive dealing provisions for 55 percent of retail outlets relating to 75 percent of sales.³⁴

The presence of scale economies is also relevant to deciding whether the level of foreclosure resulting from an exclusive dealing provision is sufficient to raise competition concerns. If the level of market foreclosure is sufficient to

³⁴ The additional 5 percent of Fisher & Paykel's sales related to non-exclusive sales of a second brand of whiteware.

prevent the new entrant or existing competitor achieving economies of scale then the new entrant or existing competitor would not be an effective competitor. In such cases, the dominant firm may be able to maintain higher prices with a lower level of market sales subject to exclusive contracts.

In the *Fisher & Paykel* case economies of scale was not considered relevant:

Minimum efficient scale of retail operation is not of particular significance in whitegoods retail marketing as a whole.

6. **Does it matter whether the arrangement was requested by the non-dominant customer or supplier?**

Yes and No.

a. **If so, how and why?**

Under section 36, which focuses on the behaviour of the dominant firm, the fact that the non-dominant customer (or supplier) requested the exclusive arrangement would suggest the behaviour was unlikely to contravene the section. In accordance with the ‘counterfactual test’ required under this section, the request by the customer would likely indicate that the behaviour would also occur in a competitive market.

Under section 27, which applies the effects based test, the fact that the non-dominant customer (or supplier) requested the exclusive arrangement is not a relevant consideration. However, if the arrangement was requested, it may indicate that there are pro-competitive efficiencies from the arrangement which would be taken into account.

7. **Might otherwise legal exclusive dealing/single branding arrangements be deemed abusive if they contain other provisions, e.g., an “English Clause” (requiring e.g., the customer to report any better offers to the supplier, and prohibiting the customer from accepting the offer unless the supplier does not match it), rights of first refusal (right of, e.g., the supplier to enter into an agreement with the customer according to specified terms, before the customer is entitled to enter into an agreement with a third party)?**

This issue has not been considered in the New Zealand jurisdiction.

a. **If so, please explain and provide examples.** N/A.

Presumptions and Safe Harbors

8. **Are there circumstances under which a firm’s use of single branding or exclusive dealing arrangements is presumed illegal?** No

a. **If so, please identify the circumstances.** N/A

- b. **Is the presumption rebuttable?** N/A
 - i. **If so, what must be shown to rebut the presumption?** N/A
- 9. **Is there a “safe harbor” from a finding of liability under your single branding/exclusive dealing provisions?** No
 - a. **If so, please explain, including its terms.** N/A

Effects

- 10. **Must a market foreclosure effect be shown for an abuse?**

Yes.

- a. **How is market foreclosure defined in your jurisdiction?**

There is no specific definition of foreclosure. Foreclosure of 55 percent of retail outlets was insufficient to raise concerns in the *Fisher & Paykel* case. A number of factors should be taken into account when considering whether the level of foreclosure raises competition concerns and these are set out below.

- b. **Which factors are taken into account to assess a market foreclosure effect (level of dominance, percentage of market demand/purchases or supply covered by the arrangement, existence of alternative sources of supply, entry barriers, scale economies, possibility and practicability of switching, others)? Please specify the factors considered, including, as relevant, the percentage of demand/supply covered.**

The comments above in relation to duration and portion of the market (questions 4 and 5) are also relevant here and assist in determining whether there is any real foreclosure. The factors set out above are:

- term/termination;
- switching costs;
- brand;
- bundling; and
- scale economies.

Additional factors include:

- The existence of barriers to entry for new or alternative wholesalers or retailers to enter the market. Foreclosure of existing retailers or wholesalers does not necessarily indicate a problem if alternative could easily enter and alleviate the foreclosure concerns.
- The foreclosure of the most efficient retailers. By foreclosing the most efficient retailers or distributors the supplier may be able increase the new entrant or competitor’s costs. This may result in an increase in the final price of the new entrant or competitor’s product. Such foreclosure

increases the likelihood that the exclusive dealing arrangement represents a barrier to entry.

In the *Fisher & Paykel* case the High Court commented as follows on the likely foreclosure of retail space for whiteware:

We think the supply of suitable retail space throughout the country is reasonably elastic. If there is demand, good retail space will be made available, whether by (a) existing retailers selling brown goods and/or other goods; (b) the expansion of space in existing outlets; (c) new retail space being built; or (d) F & P dealers converting to non exclusive outlets.

c. **What evidence is used to demonstrate these effects and must the effects be actual, likely or potential effects?**

Section 27 specifically prohibits contracts arrangement or understandings that have the purpose, effect, or likely effect of substantially lessening competition in a market.

In order to assess whether a substantial lessening of competition has occurred the Courts have applied a counterfactual analysis. The Courts consider the level of competition that would otherwise have existed in the market but for the exclusive dealing provision.

11. **Must other effects, e.g., on consumer welfare, be shown for an abuse?**

Yes and No.

If yes, please specify what must be demonstrated and the evidence required.

For section 36 strictly speaking no. Section 36 is concerned with anti-competitive purpose rather than effects. However, purpose can be inferred from objective likelihoods. Evidence of the effects of the proscribed conduct, if available, would likely be relevant in assessing penalties.

For section 27 a substantial lessening of competition is a lessening of competition which creates, enhances or maintains market power. The New Zealand courts would consider whether the contract, arrangement or understanding affects competition in the market to the extent that consumers may be harmed through increased prices. The New Zealand courts would also consider whether any anti-competitive effects are offset by pro-competitive effects.

Justifications/Defenses

12. **What justifications/defenses are available to the dominant firm, e.g., an efficiency, meeting competition or objective necessity defense? Please specify.**

There are not specific defences available under the Commerce Act for exclusive dealing. However the Courts would consider any pro-competitive or efficiency claims in assessing whether the conduct or arrangement contravenes the provisions.

In terms of section 27 the Courts have taken a net approach to pro-competitive and anti-competitive effects. This allows efficiencies to be considered in determining whether or not a substantial lessening of competition has occurred. In the *Fisher & Paykel* case, the High Court considered the possibility that competitors could free ride on the relationship between Fisher & Paykel and its dealers:

...F & P's side by side selling in a multi-brand outlet had anti-competitive effects because it discouraged each retailer fully supporting its product ... We accept the force of this argument but feel it must be weighed against the pro-competitive aspects of side by side selling which include price competition.

In terms of section 36, the 'counterfactual test' enables a dominant firm to enter into exclusive dealing arrangements if they would have done so in a competitive market. A dominant firm may enter into exclusive dealing arrangements in a competitive market for efficiency reasons and the firm would argue that it would have behaved the same way in a competitive market.

- a. **If there is an efficiencies defense, what efficiencies are considered (e.g., relationship-specific investments, facilitating innovation, reduced transaction costs)? How are claims of improved service quality or reputation assessed?**

There is no specific efficiencies defence set out in the legislation. The Courts would consider the legitimacy of any claim of efficiency on a case by case basis. In the *Fisher & Paykel* case, the court considered that the exclusive dealing arrangements increased Fisher & Paykel's distribution efficiencies and prevented rivals from free-riding on Fisher & Paykel's reputation.

- b. **Are efficiencies balanced against competitive harm to determine whether liability attaches, or do they provide a complete defense without consideration of harm?**

This is the approach under section 27 but not section 36.

- c. **Is there a meeting competition defense? Yes and No.**
i. **If yes, please explain.**

As discussed above, under section 36 when applying a 'counterfactual test' it would be possible to argue a meeting competition defence.

- d. **What is the standard of proof applicable to these defenses? What type of evidence is required to demonstrate that the defenses are met?**

The normal civil standard of proof applies and the burden is on the plaintiff.

Enforcement

13. **Please provide the following information for the past ten years (as information is available):**
- a. **The number of exclusive dealing/single branding cases your agency reviewed (investigated beyond a preliminary phase).**

Three.

- b. **The number of these cases that resulted in:**
- (i) **an agency decision that the conduct violates antitrust rules;**

In New Zealand, the NZCC does not make findings of contraventions. Only the courts may determine a contravention. However, the NZCC did not initiate court proceedings for any of the three cases.

- (ii) **a settlement with relief.**

None.

- c. **The number of agency decisions issued, if any, that held that the practice did not violate your jurisdiction's exclusive dealing/single branding rules (i.e., "clearance decisions").**

The NZCC does not make findings as to contraventions and, as such, it does not issue 'clearance' decisions. However, the NZCC closed the three cases without any enforcement action.

- d. **Each of the number of agency decisions or settlements that were (i) challenged in court and, of those, either (ii) overturned by court decision or (iii) confirmed by court decision.**

None

14. **Does your jurisdiction allow private cases challenging exclusive dealing/single?**

Yes.

- a. **Please provide a short description of representative examples, as available.**

An example of a private case is *Bond & Bond Ltd v Fisher & Paykel Ltd* (1986) 2 TCLR 79; (1987) 1 NZBLC 102,622. This case involved an

application for interim injunction which was not granted.

15. **As relevant, please provide a short English summary of the leading exclusive dealing/single branding cases in your jurisdiction and, if possible, a link to the English translation of the decision, an executive summary or the press release of the case.**

In the *Fisher & Paykel* case, the High Court specifically considered whether or not an exclusive dealing contract had the purpose, effect or likely effect of substantially lessening competition in a market. Fisher & Paykel's contracts with dealers for the supply of whiteware contained exclusive dealing provisions terminable on 90 days notice. Fisher & Paykel's market share was 80 percent and the foreclosure of retail outlets represented 55 percent.

The High Court pointed to the following factors as indicating that the exclusive dealing contract did not substantially lessen competition

- although Fisher & Paykel had significant market power, low barriers to entry meant that it was significantly constrained;
- in the absence of low barriers to entry the High Court acknowledged that exclusive dealing contracts can have pro-competitive effects, provided there is not significant foreclosure;
- no significant retail space had been foreclosed; and
- the contract could be terminated on 90 days notice.

It appears that the High Court considered that, absent significant foreclosure and absent market power, it is unlikely that an exclusive dealing arrangement would have any anti-competitive effects.

16. **Please provide any additional comments that you would like to make on your experience with exclusive dealing/single branding rules and their enforcement in your jurisdiction, including, as appropriate but not limited to whether there have there been or you expect there to be major developments or significant changes in the criteria by which you assess exclusive dealing/single branding, explaining these developments as relevant.**

No comment.