

JANUARY 2018

# Competitor Collaboration Guidelines



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# Introduction by the Chairman

The Commerce (Cartels and Other Matters) Amendment Act 2017 (Amendment Act) amends New Zealand's laws on cartel conduct. The changes include refreshment of the substantive prohibition (section 30) and the introduction of new exceptions to that prohibition.

## Our role

Our role is not limited to taking enforcement action or adjudicating when parties apply for a clearance or authorisation. We also have a role to play in providing information and guidance. These Guidelines aim to provide guidance on the way we will approach the new provisions.

## The role of the Guidelines

These Guidelines are just that: guidelines. They provide a broad overview of our proposed approach to the new provisions. They do not replace legal advice. Readers should remember that the Guidelines are principles-based, and the examples we have provided are illustrative. They provide general guidance that is equally applicable to all industries.

These Guidelines do not and cannot address every issue that might arise. Rather, we have tried to provide a sense of how we are thinking about the new provisions, and the questions we will be asking about any agreements that come before us under the new provisions.

## Our approach will evolve over time

It is also important to recognise that the amendments to the Commerce Act introduce new concepts. The Guidelines represent our interpretation of those concepts at this point in time. But, as with our approach to mergers, our approach will naturally evolve. We will gain valuable experience working with the new provisions as new issues come before us. And as matters come before the courts we will benefit from clarity about the interpretation and application of the new concepts.

We intend to reflect those evolutions in our decision-making over time and that may result in changes to the Guidelines.

## Observations on the changes to section 30

The Amendment Act replaces the prohibition on price fixing with a new prohibition on cartel conduct. Under the old law, agreements between competitors which fix, control or maintain prices were unlawful. Under the new law, it is unlawful for competitors to agree to:

- fix, control or maintain prices;
- restrict output or capacity; or
- allocate markets or customers.

While on its face the new cartel prohibition may look wider than the old price fixing prohibition, we do not see the new cartel prohibition as representing a significant shift in the types of conduct that should be regarded as breaching section 30.

We see the new section 30 as describing cartel conduct in more detail than the former section 30. For the most part, we consider that conduct that was price fixing before the relevant provisions of the Amendment Act came into force will remain cartel conduct under the new section 30.

Furthermore, as a general rule we regard agreements between competitors to restrict output or capacity, or to allocate markets or customers, as price fixing conduct under the former section 30, and therefore as unlawful. Under the new section 30 those types of conduct are specifically mentioned as cartel conduct that will remain unlawful.

## Observations on the new exceptions

We have explained our interpretation of the new exceptions in the Guidelines.

Naturally, when we have interpreted the new provisions we have done so in light of the intended purpose of those provisions and the Commerce Act more generally. In particular, we have had regard to the fact that the role of the exceptions is to mitigate the potential for overreach by the cartel prohibition. The cartel prohibition itself reflects a policy decision that cartel conduct is so likely to damage competition that it should be condemned without further enquiry into its actual competitive effects.

Since the inevitable consequence of such a per se rule is that it may capture some conduct that is in fact pro-competitive or competitively neutral, it is reasonable to have exceptions to mitigate any overreach.

But equally, the exceptions should not be interpreted in a way that undermines the fundamental per se nature of the cartel prohibition, which Parliament has chosen not to change.

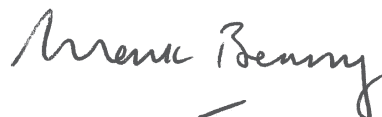
## Our consultation process

These Guidelines are the result of a comprehensive consultation process with the business and legal community. We published Draft Guidelines in October 2013, presented those Guidelines in Auckland, Wellington and Christchurch, called for submissions, and met individually with a number of parties.

We received valuable feedback during that process, which we took into account before issuing revised Draft Guidelines in August 2014. We have subsequently made amendments to the Guidelines to reflect changes to the Amendment Act before it was passed in August 2017. In particular, the removal of criminalisation has resulted in some adjustments to our proposed process for assessing collaborative activity clearances.

Preparing guidelines for new law has been a challenging task. We have tried to balance the provision of detail – for the expert reader seeking guidance – with the provision of accessible guidance for the business community.

While our approach will continue to evolve, we trust these Guidelines will assist businesses to understand our intended approach.



**Dr Mark Berry**  
Chairman

## Purpose and use of these Guidelines

The Commerce (Cartels and Other Matters) Amendment Act 2017 (the Amendment Act) amends a number of provisions of the Commerce Act 1986 (Commerce Act). In particular, the Amendment Act:

- introduces a new cartel prohibition, which replaces the former prohibition on price fixing;
- provides three exceptions to the cartel prohibition for collaborative activities, vertical supply contracts, and joint buying agreements; and
- enables parties involved in a collaborative activity that enter into an agreement containing a cartel provision to seek clearance from the Commission for that agreement.

The purpose of these Guidelines is to explain:

- the cartel prohibition and the consequences of engaging in cartel conduct;
- the three exceptions to the cartel prohibition for collaborative activities, vertical supply contracts, and joint buying agreements; and
- the clearance regime for collaborative activities.

The Amendment Act also provides a transition period of two years before the application of a new exception relating to certain international liner shipping agreements.<sup>1</sup>

The Guidelines are not law and are not intended to be legally binding. The Guidelines are necessarily general and are not an attempt to codify the Commission's approach. We will exercise our judgement as to how best to apply them to the facts of each case. The Guidelines also represent the Commission's intended approach at this point in time. The Commission's approach is likely to evolve and we may amend these Guidelines from time to time to reflect those changes.

While we have also provided examples in the Guidelines to help illustrate key concepts, these are provided for illustrative purposes only. The specific facts of each case will determine how the Commerce Act applies and you should seek legal advice on the application of the Commerce Act to your circumstances.

These Guidelines also do not bind the courts. It is ultimately up to the courts to determine whether conduct breaches the cartel prohibition or if an exception applies.



1. Until 17 August 2019, international liner shipping agreements are subject to the exception in section 44(2) of the Commerce Act concerning the carriage of goods by sea to and from New Zealand. These Guidelines do not address the exception relating to certain international liner shipping agreements. See s 4, Part 1, Schedule 1AA, Commerce (Cartels and Other Matters) Amendment Act 2017.

# Chapter 1. INTRODUCTION

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- 1 The purpose of the Commerce Act is to promote competition in markets for the long-term benefit of consumers within New Zealand.<sup>2</sup> Effective competition plays an important role in driving the performance of New Zealand's economy.<sup>3</sup>
- 2 Competition generally delivers lower prices, increases firms' incentives to innovate, and results in a better allocation of resources. Ensuring our markets are competitive enables us to better build sustainable economic growth that creates jobs, increases income, and allows New Zealand firms to compete internationally.
- 3 Two of the ways the Commerce Act promotes competition are by prohibiting agreements that substantially lessen competition and by prohibiting cartels. Anti-competitive agreements – including cartels – are prohibited because they can result in higher prices, resources being misallocated, and firms having a decreased incentive to innovate.<sup>4</sup> These outcomes are not in the long term interests of New Zealand consumers.
- 4 However, the Commerce Act also recognises that competition is not an end in itself.<sup>5</sup> In some situations, the long-term benefit of New Zealand consumers may be achieved through collaboration.

## Prohibition on anti-competitive agreements

- 5 The Commerce Act prohibits any person from entering into or giving effect to a contract, arrangement or understanding containing a provision that has the purpose, effect, or likely effect of substantially lessening competition in a New Zealand market.
- 6 The prohibition on anti-competitive agreements applies to all agreements and to all provisions of an agreement. This means that even where a provision is not prohibited by the cartel prohibition (either because it is not a cartel provision, or because an exception applies) it will be prohibited if it has the purpose, effect, or likely effect of substantially lessening competition.<sup>6</sup>
- 7 We use the term 'agreement' in these Guidelines as shorthand for the phrase 'contract, arrangement, or understanding'. We explain what an agreement is in Chapter 2.

## The cartel prohibition

- 8 Cartels are considered so likely to substantially lessen competition that they should be prohibited without considering whether the cartel in fact has that purpose, effect, or likely effect. By definition, a cartel exists when competitors agree to reduce or remove competition that exists or would otherwise exist between them.
- 9 Entering into or giving effect to an agreement containing a cartel provision (or attempting to do so) is unlawful unless an exception applies. This is true regardless of whether or not the cartel provision has a harmful effect on competition.
- 10 A cartel provision is any provision in an agreement between competitors that has the purpose, effect, or likely effect of:
  - 10.1 fixing prices – an agreement not to compete on price, or on an element of price;
  - 10.2 restricting output – an agreement to prevent, restrict, or limit output, production, capacity, supply, acquisition, etc; or
  - 10.3 allocating markets – an agreement not to sell to or buy from certain customers or suppliers, or in particular areas.
- 11 We describe what a cartel provision is and the penalties for breaching the Commerce Act in Chapter 2.

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2. Commerce Act 1986, s 1A.

3. See *Tru Tone Ltd v Festival Records Retail Marketing Ltd* [1988] 2 NZLR 352.

4. *Commerce Commission v Visy* [2012] NZCA 383 at [32].

5. *Godfrey Hirst NZ Ltd v Commerce Commission* (2011) 9 NZBLC 103,396, at [46].

6. Commerce Act 1986, s 27.

## Exceptions from the cartel prohibition

- 12 While cartels are unlawful, the Commerce Act recognises that in some circumstances cartel provisions are much less likely to harm competition.
- 13 Cartel provisions can form part of agreements that have pro-competitive or benign competitive effects. Such agreements may increase innovation, reduce production costs, enhance product quality, and/or result in lower prices.
- 14 Therefore, the Commerce Act provides three different exceptions to the cartel prohibition for cartel provisions in certain types of agreements. If an exception applies, then the cartel provision is lawful provided the provision does not have the purpose, effect, or likely effect of substantially lessening competition. The three exceptions cover:
  - 14.1 vertical supply contracts – explained in Chapter 3;
  - 14.2 joint buying and promotion agreements – explained in Chapter 4; and
  - 14.3 collaborative activities – explained in Chapter 5.

## Clearances for collaborative activities

- 15 A person that is, or will be, involved in a collaborative activity can apply for clearance to enter into an agreement that contains one or more cartel provisions. We explain the clearance regime in Chapters 6 and 7.
- 16 We will grant the clearance if the cartel provision in the agreement is reasonably necessary for the purpose of the collaborative activity and entering into the agreement or giving effect to any provision of the agreement will not or will not be likely to have the effect of substantially lessening competition in a market.
- 17 If we clear such an agreement, that agreement cannot be challenged by any person on the basis it contains a cartel provision, or as being an agreement that has the effect, or likely effect of substantially lessening competition in a market.<sup>7</sup>

## Authorisation for cartel provisions

- 18 A person can apply for authorisation of any anti-competitive agreement. This includes an agreement containing a cartel provision which does not fall within the exceptions and where clearance is not available.
- 19 We will authorise an agreement that lessens competition where the agreement is likely to result in such a benefit to the public that it outweighs the lessening in competition that would be likely to result.
- 20 As with a clearance, if we authorise an agreement, that agreement cannot be challenged by any person as being in breach of the prohibitions against cartel provisions or anti-competitive agreements.
- 21 The authorisation regime is briefly explained in Chapter 8. We have Authorisation Guidelines explaining our process for considering authorisations. These are available on our website.<sup>8</sup>

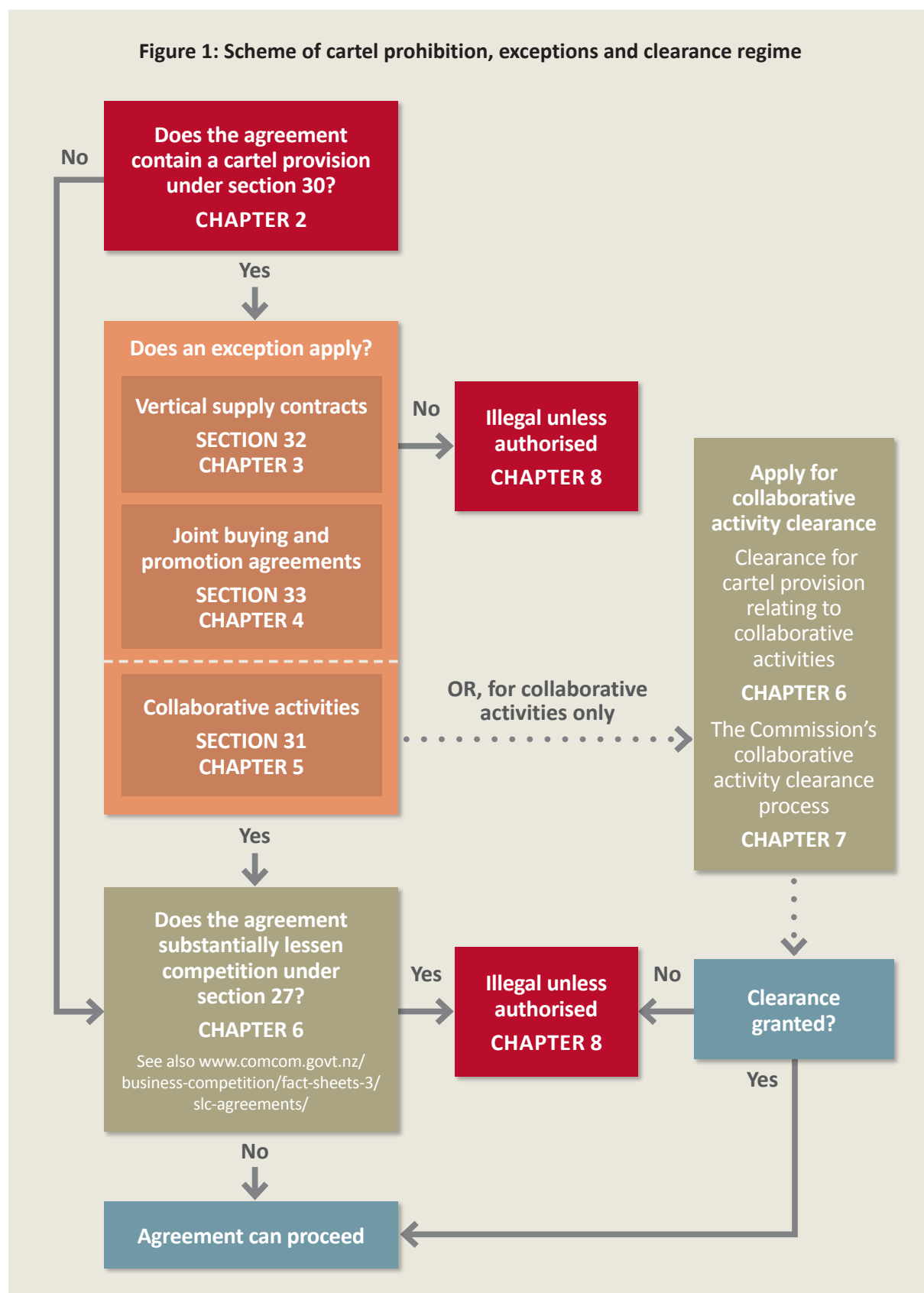


7. This is because to grant a clearance we must be satisfied that the collaborative activity exception applies, and that the agreement will not have, or would not be likely to have, the effect of substantially lessening competition in a market. See Chapter 6.

8. <http://www.comcom.govt.nz/business-competition/guidelines-2/authorisation-guidelines/>.

## Summary of the scheme of the amended Commerce Act

- 22 The following diagram summarises how the prohibition against anti-competitive agreements, the new cartel prohibition, the new exceptions to the cartel prohibition, and the clearance regime interact.





## Transitional provisions relating to the cartel prohibition

- 23 The new cartel prohibition applies:
- 23.1 to agreements that are entered into after the new section 30 comes into force – 15 August 2017; and
  - 23.2 to parties seeking to give effect to a cartel provision on or after 15 August 2017 even where the agreement containing that cartel provision was entered into before 15 August 2017.
- 24 However, the Amendment Act includes a nine-month transition period commencing on 15 August 2017. During this transition period:
- 24.1 we cannot commence legal proceedings seeking pecuniary penalties under the new section 30 against any person giving effect to an agreement containing a cartel provision that was entered into prior to 15 August 2017; but
  - 24.2 we can commence proceedings seeking pecuniary penalties against any person giving effect to an agreement entered into prior to 15 August 2017 that contravenes the previous section 30 price fixing prohibition.



## Chapter 2. CARTEL PROHIBITION

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### Cartel provisions unlawful

- 1 Entering into or giving effect to an agreement that contains a cartel provision is prohibited.<sup>9</sup> In this Chapter we explain what an agreement is, and what cartel provisions are.
- 2 If a provision of an agreement is a cartel provision and none of the three exceptions apply, that provision is unlawful. This is the case regardless of the provision's actual effect on competition. This is because cartel provisions are considered so likely to substantially lessen competition that they are presumed to do so.
- 3 A cartel provision is a provision of an agreement between competitors that has the purpose, effect or likely effect of:<sup>10</sup>
  - 3.1 fixing price;
  - 3.2 restricting output; or
  - 3.3 allocating markets.
- 4 These three types of cartel provisions are not mutually exclusive and may overlap. For example, a provision may both fix prices and allocate markets.
- 5 As explained in the Introduction, there are three exceptions to the cartel prohibition. The three exceptions are explained in Chapters 3 to 5. If an exception applies, then the cartel provision is not unlawful.
- 6 However, even if an exception applies to a cartel provision (or even if the provision is not a cartel provision), the agreement would be unlawful if it has the purpose, effect, or likely effect of substantially lessening competition in a market.<sup>11</sup>

### What is an agreement?

- 7 As explained in the Introduction, we use agreement in these Guidelines as shorthand for contract, arrangement, or understanding.
- 8 The essence of all three terms is that two or more parties reach a shared expectation about how at least one of them will act or refrain from acting.<sup>12</sup> The terms contract, arrangement, and understanding are used to denote varying degrees of formality.
- 9 A contract means a legally enforceable contract (which can be written or oral, implied or express). An arrangement or understanding is something short of this: the key question is simply whether the parties have a shared expectation as to what at least one of them will do or not do.

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9. Commerce Act 1986, s 30.

10. Commerce Act, 1986 s 30A.

11. Commerce Act 1986, s 27.

12. *Giltrap City Ltd v Commerce Commission* [2004] 1 NZLR 608, at [15], [17].

- 10 An agreement can be established through direct evidence that a party entered into an agreement, or it may be inferred from a course of conduct or circumstantial evidence.<sup>13</sup> Even a ‘nod and a wink’ between parties may be evidence of an agreement.<sup>14</sup>

### Examples

#### Car dealership cartel

In *Giltrap City Ltd v Commerce Commission* a price fixing agreement was reached at a meeting between several car dealers where the car dealers unanimously agreed to limit the discounts applied to the vehicles they would sell. The agreement was recorded in the Chair’s meeting minutes.

Despite being at the meeting, one meeting participant denied that he was a party to the agreement. He claimed that he stayed silent – he did not say whether he was willing to be part of the agreement or not.

However, given that the Chair’s meeting minutes noted unanimous agreement, the Court concluded that the dealer’s silence deliberately gave the impression he agreed with the proposal. The Court therefore held that dealer was party to the agreement.

#### Car wash cartel

*Commerce Commission v Caltex NZ Ltd* involved an agreement between oil companies to jointly end a promotion which gave petrol buyers a free carwash with every fuel purchase over \$20.

The Court did not find direct evidence of an agreement between the oil companies. However, the Court inferred an agreement based on the “concurrence of time, character, direction and result” of the parties terminating free car washes. Specifically, the Court relied on the fact that all car wash promotions ended on the same day, the existence of opportunities for relevant employees of the oil companies to discuss the promotion with each other, and the incentive on all parties to cease the promotion.

## Agreements between competitors and potential competitors

- 11 The cartel prohibition only applies where the provision is part of an agreement between competitors or potential competitors.
- 12 Parties are potential competitors if, but for the cartel provision, they would or would be likely to compete in the same market. In these Guidelines, when we refer to competitors we are also referring to potential competitors.

### Example

A computer manufacturer has an agreement with a hard drive manufacturer for the supply of hard drives. This is not an agreement between potential competitors as each company operates at different levels of the supply and distribution chain.

However, if there is evidence to suggest that the hard drive manufacturer is planning on entering into computer manufacturing, then the computer manufacturer and the hard drive manufacturer are likely to be potential competitors. In that situation, provisions in the supply agreements between the hard drive manufacturer and the computer manufacturer risk being cartel provisions.

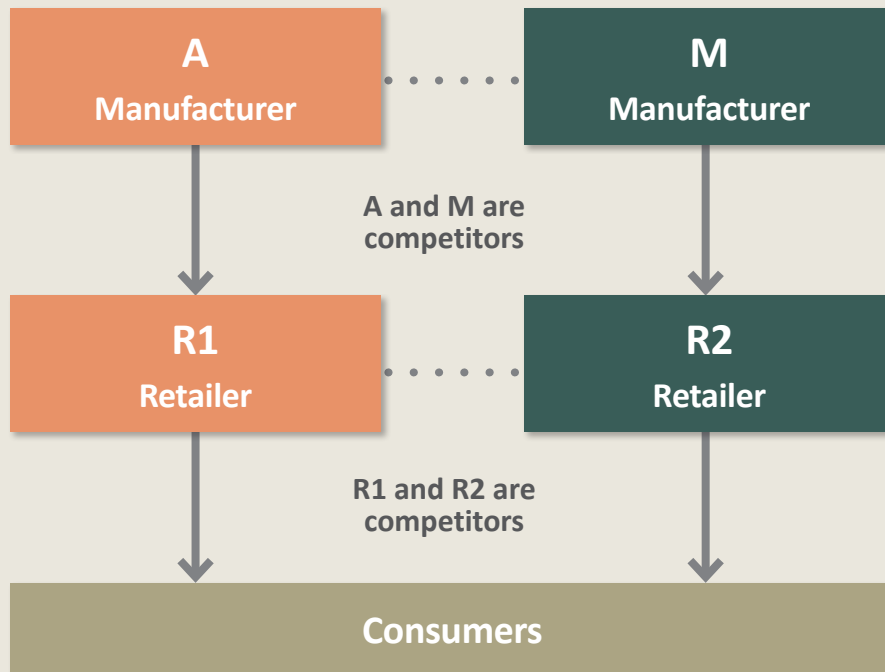
13. *Commerce Commission v Qantas Airways Ltd* (No 2) (1992) 5 PRNZ 227 at p 7.

14. *Re Mileage Conference Group of the Tyre Manufacturers’ Conference Ltd’s Agreement* (1966) LR 6 RP 49, [1966] 2 All ER 849 at p 102, p 859.

## Horizontal agreements

- 13 Agreements between competitors are often referred to as ‘horizontal agreements’. They are considered horizontal because they are between parties operating at the same level of the supply chain. That is, they supply or could supply the same customers, or buy from or could buy from the same suppliers.

Figure 2: Horizontal agreement



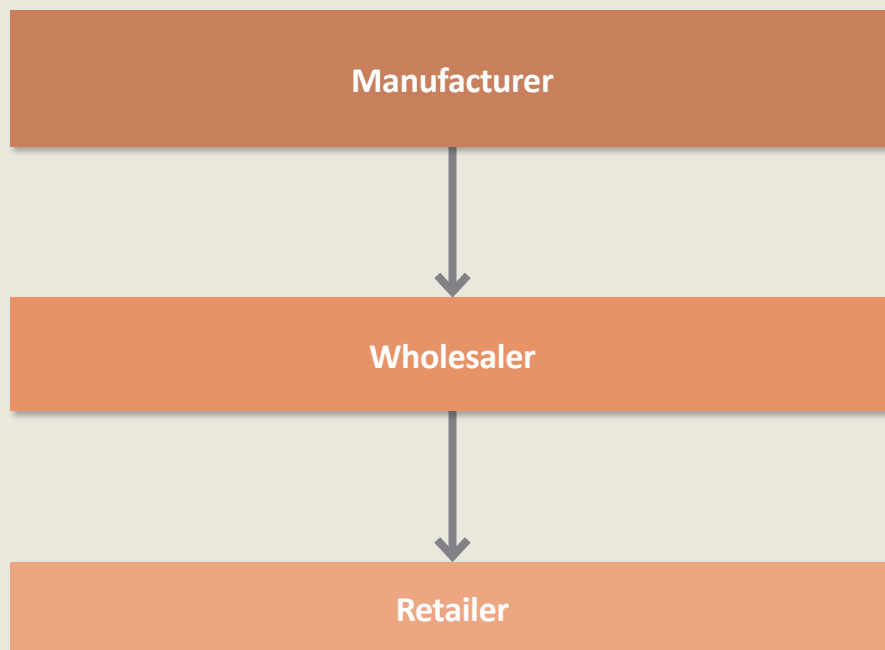
### Examples

An agreement between two tennis ball manufacturers is an agreement between competitors.

## Vertical agreements

- 14 In contrast with a horizontal agreement, a vertical agreement involves persons operating at different levels of the supply chain. That is, they do not supply the same customers, and do not buy from the same suppliers. An example of a vertical agreement is an agreement between a manufacturer and a wholesaler, or between a wholesaler and a retailer.

Figure 3: Vertical supply agreement



### Example

An agreement between a tennis ball manufacturer that does not supply tennis balls at the retail level (either directly or via an interconnected body corporate) and a retailer *is not* an agreement between competitors.

- 15 Purely vertical agreements are not subject to the cartel prohibition. However, vertical agreements which involve an agreement between competitors will be subject to the cartel prohibition. As explained in Chapter 3, there is an exception for certain vertical supply contracts.
- 16 More generally, any vertical agreement is subject to the general prohibition against anti-competitive agreements that substantially lessen competition and the prohibition against resale price maintenance (RPM).<sup>15</sup>
- 17 RPM occurs when a supplier of goods enforces, or tries to enforce, a minimum price at which the re-supplier must on-sell those goods. You can find more information in our RPM fact sheet available on our website.<sup>16</sup>

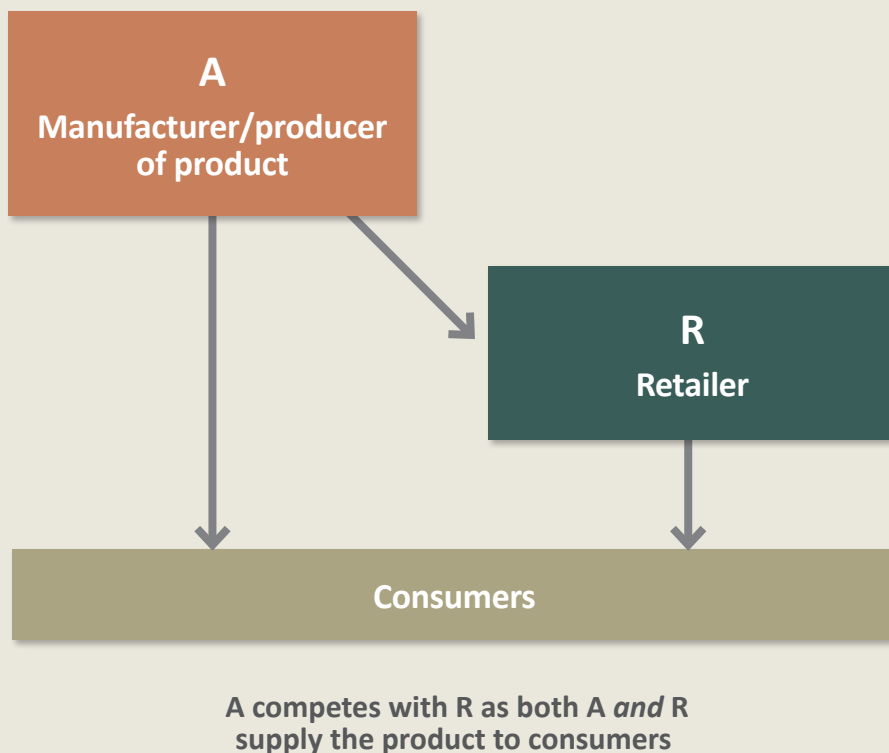
15. Commerce Act 1986, s 37.

16. <http://www.comcom.govt.nz/resale-price-maintenance-2/>.

## Agreements containing both horizontal and vertical aspects

- 18 Many agreements will have both horizontal and vertical aspects. An example is where a supplier (A) supplies goods to a retailer (R) who re-supplies those goods to customers (eg, in a retail store). A also supplies directly to customers (eg, over the internet or in its own retail stores). In those circumstances, A and R are in a vertical agreement in which A supplies goods to R and in a horizontal relationship in which both A and R also compete to sell to customers.

**Figure 4: An agreement with horizontal and vertical aspects**



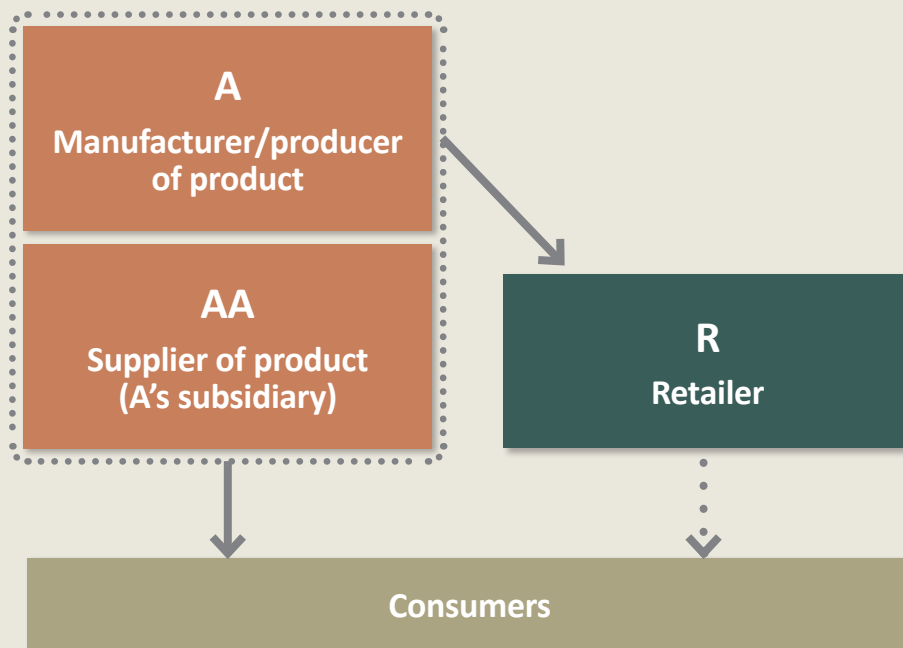
- 19 In assessing whether a firm competes with another firm, each of the firm's interconnected bodies corporate is taken to be a party to the agreement.<sup>17</sup>



17. Commerce Act 1986, s 30B.

- 20 Building on the example above, suppose that instead of A supplying goods to consumers directly, it supplies goods to its subsidiary AA, which then resupplies those goods to consumers. In that scenario, AA competes at the retail level with R. However, as can be seen in *Figure 5*, since A and AA are interconnected bodies corporate,<sup>18</sup> A is also considered a competitor of R.

**Figure 5: Manufacturer competing with a retailer via a subsidiary**



**A competes with R through its subsidiary, AA.**

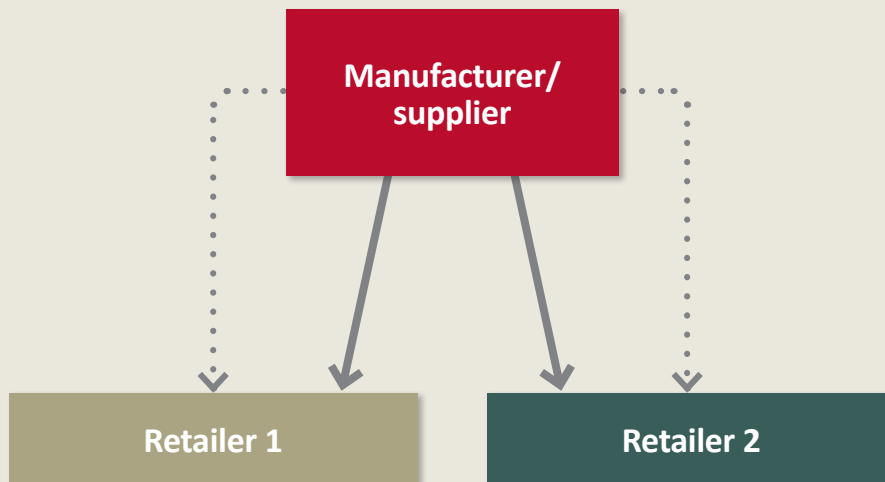
#### Example

An agreement between a tennis ball manufacturer that also supplies tennis balls at the retail level (either directly or via an interconnected body corporate) and a retailer *is* an agreement between competitors.

18. Two bodies corporate are treated as interconnected if one of them is a body corporate and the other is a subsidiary; both bodies corporate are subsidiaries of the same body corporate; or both are interconnected with bodies corporate that are interconnected. Commerce Act 1986, s 2(7).

- 21 Where an agreement involves competing and non-competing parties, the fact that some parties are not competitors does not mean the agreement falls outside the prohibition.<sup>19</sup> Such an agreement is often referred to as a ‘hub and spoke’ agreement. This is illustrated in *Figure 6* below.

**Figure 6: ‘Hub and spoke’ agreement**



The manufacturer has two separate contracts with retailers 1 and 2, but facilitates an agreement between the retailers by acting as a conduit between the parties. The manufacturer is considered to be a party to the agreement between competitors.

#### Example

### A hub and spoke agreement

Hasbro, a UK toy supplier, arranged with UK toy retailers Argos and Littlewoods that those retailers would not sell popular Hasbro toys below a set price, to ensure they did not undercut other stores.

Each retailer shared its future retail prices for Hasbro toys with Hasbro. That took place in circumstances where the retailer knew or must have known that Hasbro was talking to the retailer’s competitors about retail pricing. Both retailers were found to have relied on the information discussed in determining their own pricing.<sup>20</sup>

19. This is provided for through the definition of the cartel provisions in ss 30A(2), (3), and (4).

20. Director General of Fair Trading decision No. CA98/18/2002.



## Price fixing

- 22 Price fixing occurs when parties enter into or give effect to an agreement fixing, controlling, or maintaining:
- 22.1 the price<sup>21</sup> of goods and services that two or more of the parties to the agreement supply or acquire in competition with each other; or
  - 22.2 any discount, allowance, rebate, or credit of goods or services that two or more of the parties to the agreement supply or acquire in competition with each other.

### Example

#### Wood preservatives cartel

We brought proceedings against Koppers Arch Wood Protection (NZ) Ltd, its Australian parent company, three Nufarm companies, two Osmose companies and some executives for breaches of the price fixing provisions of the Commerce Act in relation to wood preservatives.<sup>22</sup> The unlawful conduct included competitors agreeing to share pricing information, simultaneously raise prices, and not compete on price.<sup>23</sup>

- 23 An agreement need not establish a specific price to be price fixing. Rather, price fixing occurs when competitors agree to directly or indirectly fix prices for goods or services.<sup>24</sup> Price includes a component of a price such as a surcharge or fee.
- 24 As a result, price fixing includes agreements to fix prices at a predetermined level, to eliminate or reduce discounts, to increase prices, to set a minimum price, to agree a price to bid for a contract, to maintain prices above a certain level, or to apply a formula to calculate prices.

### Example

#### Carwash cartel

*Commerce Commission v Caltex NZ Ltd*<sup>25</sup> involved an agreement between oil companies to jointly end a promotion which gave petrol buyers a free carwash with every fuel purchase over \$20.

While the companies had independently priced their fuel, the Court held that the agreement to end the carwash promotion amounted to price fixing as the discount was an 'inseparable part' of the price of the petrol.

- 25 Price fixing can also occur when competitors acquire goods or services.

### Example

#### Meat processing cartel

In *Commerce Commission v Taylor Preston Ltd*<sup>26</sup> the High Court found that North Island meat companies had entered into agreements relating to the price at which they would acquire livestock from farmers. These were held to be price fixing agreements in breach of the Commerce Act.

21. This includes fixing the component of a price, see *Commerce Commission v Air New Zealand* [2013] NZHC 1414.

22. See *Commerce Commission v Koppers Arch Wood Protection (NZ) Ltd* [2009] NZCCLR 1.

23. The unlawful conduct also included an agreement not to compete for each other's customers, which may now be considered as market allocation.

24. *Commerce Commission v Caltex NZ Ltd* [1998] 2 NZLR 78, at pp 84-85.

25. *Commerce Commission v Caltex NZ Ltd* [1998] 2 NZLR 78.

26. *Commerce Commission v Taylor Preston Ltd* [1998] NZLR 389.

## Restricting output

- 26 Output restrictions between competing suppliers of goods or services occur where two or more of those competing suppliers arrange to prevent, restrict, or limit:<sup>27</sup>
  - 26.1 their supply, production, or likely supply or production of those goods; or
  - 26.2 their supply, capacity, or likely supply or capacity to supply those services.
- 27 Output restrictions between competing buyers of goods or services occur where two or more competing buyers of goods or services arrange to prevent, restrict, or limit their acquisition or likely acquisition of those goods or services.

### Example

#### Tasmanian salmon growers cartel

In 2003 the ACCC commenced proceedings against salmon producer Tassal and the Tasmanian Salmonid Growers Association, alleging the members of the association entered into an agreement to limit the supply of salmon and to fix, control, or maintain the price of salmon.<sup>28</sup>

The ACCC alleged that Tassal and the Association had agreed that the five major growers would 'grade out' 10% of salmon from the 2001 year class, and that they would later consider a possible grading out of a further 5%. The purpose of these agreements was to reduce fish numbers to ensure the financial viability of the salmon farming industry in Tasmania. At the time the agreement was entered into, the Tasmanian salmon industry was in financial difficulty and supply was outstripping demand.

The Federal Court of Australia held that there was an agreement or understanding between competitors. The agreement was to limit the supply of fish and it would likely have had the effect of controlling or maintaining price, in breach of the anti-competitive provisions of the Australian Trade Practices Act 1974.

## Market allocation

- 28 Market allocation occurs where two or more competing suppliers arrange to allocate between themselves the customers to whom, or the geographic areas in which, each will supply their respective goods or services.<sup>29</sup> A particular situation where market allocation can arise is when parties are competing for contracts, eg, by competing for tenders.
- 29 Market allocation not only concerns sales to final customers. The prohibition covers agreements between suppliers to allocate sales to any persons, including distributors and re-suppliers.
- 30 Market allocation also occurs where two or more competing buyers arrange to allocate between

27. Commerce Act 1986, s 30A(3). Such agreements are illegal because having less of something for sale will generally lead to prices increasing. However, it is not necessary to show that prices are actually affected.

28. *ACCC v The Tasmanian Salmonid Growers Association Ltd* (2003) ATPR 41-954.

29. Commerce Act 1986, s 30A(4).

themselves the particular suppliers from whom, or the particular geographic areas in which, each will acquire their goods or services.

## Examples

### Customer allocation between competing suppliers

In *Commerce Commission v Eli Lilly & Co (NZ) Ltd*,<sup>30</sup> two wholesale suppliers of animal remedies reached an agreement by which one supplier would only proactively sell the Elanco brand of animal remedy products to large purchasers (ie, those that spent \$10,000 or more per annum on Elanco products), while the other would only proactively sell to those below that threshold. The agreement was held to constitute market allocation through dividing the market by customer.

### Bid rigging – customer allocation between competing suppliers

For about 10 years until 1997 most of the companies in the fire alarm and fire sprinkler installation industry in Brisbane held regular meetings at which they agreed to allow certain tenders to be won by particular competitors.

Calling themselves the ‘Sprinkler Coffee Club’ and the ‘Alarms Coffee Club’, the groups would meet up over coffee at hotels, cafes, and various sporting and social clubs. At these meetings they would share tenders and decide who was to submit ‘cover prices’ (prices just above the winning bid amount) to make the tender process look legitimate, while ensuring the agreed company won the tender.<sup>31</sup>

### Geographic market allocation between competing suppliers

In *Commerce Commission v Christchurch Transport Ltd*<sup>32</sup> the defendant admitted that its Chief Executive Officer approached its next biggest competitor in the market for subsidised passenger bus services in metropolitan Christchurch. He proposed an exchange of tender information with a view to each party submitting tenders that would ensure each company retained the routes it had historically serviced.<sup>33</sup>

In that way, the companies would have been allocating the geographic areas in which they supplied their competing services.

The Court accepted that this was ‘bid rigging’ conduct and accepted the defendant’s admission that it had breached the then section 30 of the Commerce Act. Christchurch Transport Limited was ordered to pay a penalty of \$380,000 (under the pre-2001 penalty regime) and its Chief Executive Officer was ordered to pay a penalty of \$10,000.

### Geographic market allocation between competing buyers

Two New Zealand fishing companies agree that one will acquire its filleting and processing services from South Island providers, while the other will acquire the services from North Island providers.

30. *Commerce Commission v Eli Lilly & Co (NZ) Ltd* (HC) Auckland CL 19/98, 30 April 1999.

31. <http://www.accc.gov.ac/business/anti-competitive-behaviour/cartels/cartels-case-studies-legal-cases/>.

32. *Commerce Commission v Christchurch Transport Ltd* CP72/98, 21 August 1998.

33. Despite the discussions, the businesses did not reach an agreement. The conduct, therefore, amounted to an attempt to breach the Commerce Act.

## Penalties for breaching the cartel prohibition

- 31 Those who engage in cartel behaviour may be subject to civil sanctions.
- 32 Where the Commission takes civil proceedings, if a court considers that a person has entered into, or given effect to a cartel provision,<sup>34</sup> then the court may order various remedies, such as:
  - 32.1 for an individual, a penalty of up to \$500,000, and/or an order that a person must not be a director, promoter, or involved in the management of a body corporate for a period of up to 5 years; and/or
  - 32.2 in any other case, a penalty of up to the greater of \$10 million, or three times the commercial gain, or, if this cannot be easily established, 10% of turnover.<sup>35</sup>
- 33 Where a third party takes civil proceedings, a court can make an award of damages and/or exemplary damages.

## Enforcement Response Guidelines

- 34 Our Enforcement Response Guidelines describe in general terms what enforcement responses are available to us and what factors we take into account when deciding which response to use.<sup>36</sup>

## Cartel Leniency Policy

- 35 We become aware of potential breaches of the Commerce Act in a number of ways, including via complaints, our own enquiries, and engagement with business. In relation to cartels, one of the key ways we become aware of cartel conduct is through our Cartel Leniency Policy.
- 36 Our Cartel Leniency Policy aims to encourage people to report cartels they have been or are involved in.
- 37 Under the policy we grant immunity to the first member of a cartel to approach us, provided they meet the immunity requirements under the Cartel Leniency Policy. Immunity means we will not take legal action against that person.
- 38 Where a person does not qualify for immunity, we encourage them to cooperate with our investigations. Our policy on cooperation allows us to recommend a lower level of penalty to the court for cartel members that cooperate fully but are not the first member of a cartel to approach us. Cartel members that cooperate as early as possible in an investigation are likely to get greater reductions in penalty.
- 39 You can find more information on our Cartel Leniency Policy on our website.<sup>37</sup>



34. The Commerce Act also prohibits any person from aiding, abetting, counselling, or procuring any other person to contravene the cartel prohibition, inducing, or attempting to induce, any other person to contravene the cartel prohibition, or otherwise being in any way, directly or indirectly, knowingly concerned in, or party to, a contravention by any other person of the cartel prohibition. Commerce Act 1986, s 80(1).

35. 'Turnover' means the turnover of the person and all of its interconnected bodies corporate (if any) in each year in which the contravention occurred.

36. Available at <http://www.comcom.govt.nz/the-commission/commission-policies/enforcement-response-guidelines/>.

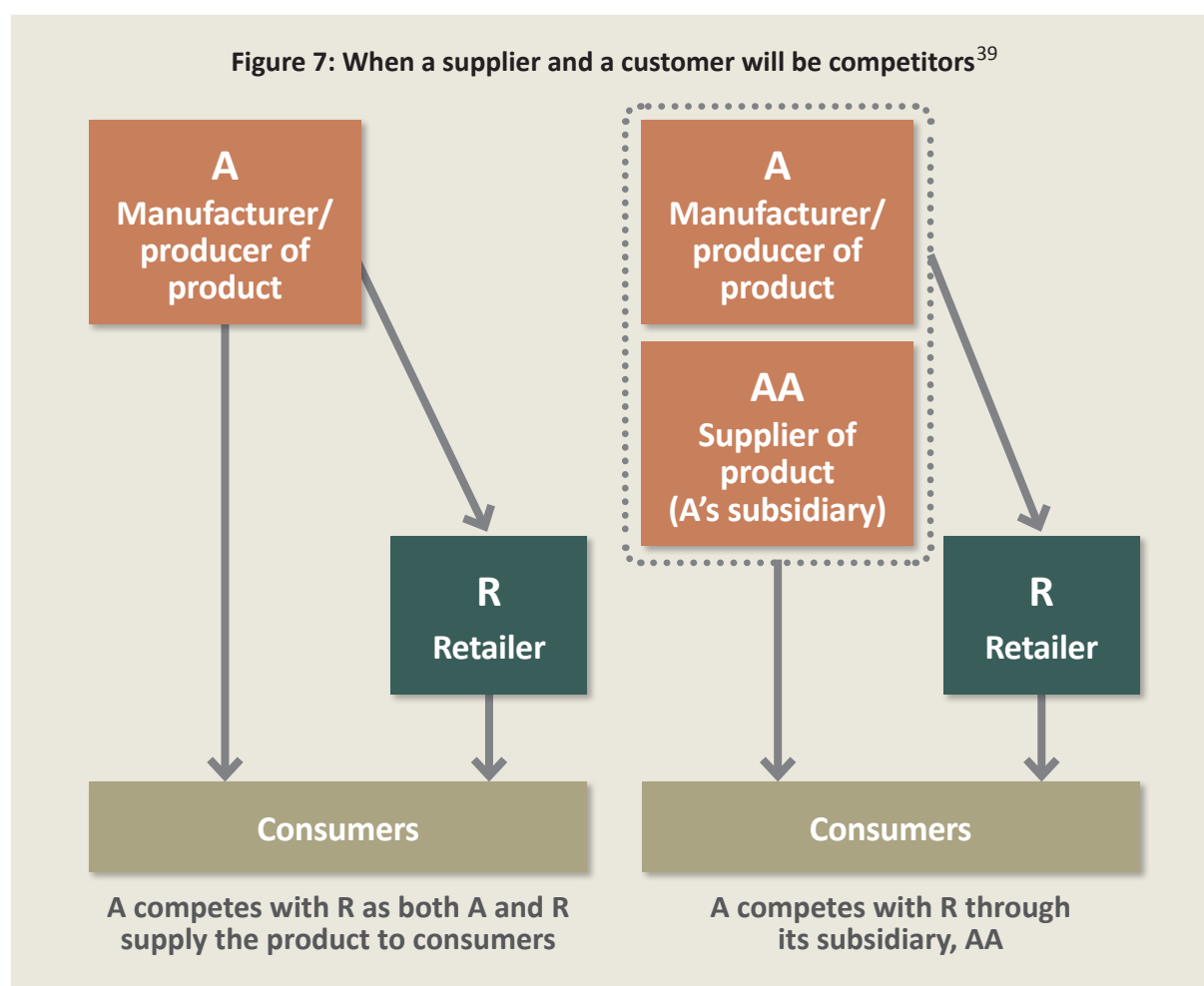
37. Available at <http://www.comcom.govt.nz/leniency-policy-for-cartels/>.

## Chapter 3. EXCEPTION FOR VERTICAL SUPPLY CONTRACTS

- 1 As explained in Chapter 2, vertical agreements that involve a contract between competitors will be subject to the cartel prohibition.
- 2 There are many situations where a supplier and a customer may be in competition with each other. A common situation is where a supplier supplies goods directly to end customers (eg, through its own stores or over the internet) and also supplies to wholesale customers who resupply those goods to consumers (eg, in a retail store). In that situation, the supplier and its wholesale customer are competitors at the retail level. As a result, provisions in any supply agreement between them risk being cartel provisions.
- 3 However, the vertical supply exception may apply to provisions in supply contracts between a supplier and a customer that would be prohibited as cartel provisions but for the exception.
- 4 As with the other two exceptions, it is up to a person relying on the vertical supply exception to prove on the balance of probabilities that the exception applies.

### When will a supplier and a customer be in competition with each other?

- 5 *Figure 7* below provides an example, in general terms, of situations where a supplier and a customer may be in competition.<sup>38</sup> The particular example in *Figure 7* is of a manufacturer (A) supplying product to a retailer (R) in circumstances where both A (either directly or through its subsidiary AA) and R compete to sell that product to consumers.



38. As can also be seen from Figure 7, if the supplier supplies to customers via a subsidiary, the supplier is still considered to be in competition with the re-supplier: Commerce Act 1986, s 30B.

39. In this example, both A and AA are party to the agreement (Commerce Act 1986, s 30B). As a result, either or both may be subject to enforcement action.

## When does the exception apply?

- 6 There are four criteria that must be met for the vertical supply exception to apply.<sup>40</sup>
  - 6.1 A supplier or likely supplier of goods or services (A) and a customer or likely customer of that supplier (B) must have entered into a contract. The exception is not available where the parties only have an agreement or understanding. This means the exception is only available where the parties have entered into a legally enforceable supply contract for consideration.
  - 6.2 The contract must contain a cartel provision. If there is no cartel provision, then there is no need for the exception in the first place.
  - 6.3 The cartel provision in the contract must relate to the supply or likely supply of goods or services by A to B, including to the maximum price at which B may resupply the goods or services supplied by A to B ('B's maximum resale price').
  - 6.4 The cartel provision must not have the dominant purpose of lessening competition between A and B.
- 7 We describe how we approach the last two of those criteria below.

### Relates to the supply of goods or services from A to B

- 8 The term 'relate to' is imprecise as to the degree of connection required. However, we consider it requires a relatively close connection between the cartel provision and the act of A supplying goods or services to B for B to resupply.
- 9 Whether there is a sufficiently close connection between a cartel provision and the supply of goods or services from A to B will depend on the facts of each case. It is a question of substance rather than form. This means that a cartel will not automatically 'relate to' the supply of goods from A to B simply because it is included in a supply contract.
- 10 However, at one end of the spectrum some provisions will invariably 'relate to' the supply of goods from A to B.
  - 10.1 Supply contracts will, for example, set the price at which A will supply goods or services to B. Such a provision will relate to the supply of goods or services from A to B.
  - 10.2 Similarly, a provision which does no more than prevent B selling goods or services supplied by A above a maximum price will relate to B's maximum resale price and therefore be regarded as related to the supply of goods from A to B.
- 11 At the other end of the spectrum, some provisions are far less likely to 'relate to' the supply of goods from A to B. For example, if A restricted B's ability to price or sell different goods or services to those being supplied by A.
- 12 Other restrictions which A may impose on B (or vice versa) fall in between these ends of the spectrum. Examples of such restrictions might be: A setting out where B can resupply A's goods or services, A dictating the quantity of A's goods B can resupply, or A dictating B's resupply price other than by setting a genuine maximum resale price.
- 13 The facts we would examine in determining whether the cartel provision relates to the supply of goods from A to B may overlap with the facts we would examine in determining the purpose of the cartel provision (which we discuss below).

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40. Commerce Act 1986, s 32

- 14 Particularly in the context of determining whether a cartel provision in a contract relates to the supply of goods or services from A to B, we would look at the history and nature of the supply relationship between the parties of which the relevant cartel provision forms part. For example, if A would not supply B in the absence of the cartel provision, then the cartel provision is likely to relate to the supply of goods or services from A to B. That said, such an argument will be less persuasive where A has supplied B with the goods or services in the past without the cartel provision.

### **Dominant purpose of lessening competition**

- 15 The exception does not apply where the cartel provision has the dominant purpose of lessening competition between any two or more of the parties to the contract.<sup>41</sup>
- 16 In contrast to other parts of the Commerce Act, the words ‘lessening competition’ are not qualified by ‘substantially’. All that is required is a dominant purpose of lessening competition between the parties.<sup>42</sup> The absence of the qualifier ‘substantial’ means that there is no need for the provision’s dominant purpose to be to lessen competition between the parties in a way that is real or of substance. Any lessening of competition is sufficient.
- 17 The dominant purpose is the main or principal reason for the provision.<sup>43</sup> In other words, the prevailing objective of the cartel provision must not be to lessen competition between the parties. If it is – that is, if the cartel provision is simply a device to engage in anti-competitive conduct – then the exception will not apply.
- 18 This ‘not for the dominant purpose’ test is primarily an objective test for the courts or the Commission to assess. While primarily an objective test, evidence of subjective purpose may be relevant.
- 19 There is no bright line as to when an aim or objective of a cartel provision becomes the dominant purpose. It is up to the parties to the agreement to show that the cartel provision does not have the dominant purpose of lessening competition.
- 20 A key question we will ask in assessing the dominant purpose of the cartel provision is whether the cartel provision is designed to increase output or lower prices to consumers. In making that assessment, we will consider matters including:
- 20.1 the parties’ conduct;
  - 20.2 the broader context of the supply relationship between the parties of which the relevant supply contract and the cartel provision form part; and
  - 20.3 the cartel provision’s role in that supply contract and the relationship between the parties.
- 21 It may also be relevant to know whether such provisions are common in similar supply contracts.
- 22 If the provision is not designed to increase output or lower prices to consumers, and the parties are unable to point to any other legitimate purpose for the cartel provision, then we are likely to consider that the dominant purpose of the provision is to lessen competition between the parties. In that case, the exception would not apply.

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41. This is compared to the collaborative activity exception, where the focus is on the dominant purpose of the collaborative activity rather than the cartel provision.

42. A lessening of competition includes hindering or preventing competition. Commerce Act 1986, s 3(2).

43. As discussed in more detail in Chapter 5, a ‘dominant’ purpose can be contrasted with the definition of purpose in section 2(5) of the Commerce Act, which defines purpose as meaning a “substantial purpose”. Our approach to defining dominant purpose is consistent with the ordinary meaning of dominant which includes ‘prevailing’ and ‘most influential’.

## Examples

### Maximum resale price

A shoe manufacturer operates a website through which it sells its shoes to consumers.

The manufacturer also sells shoes to a high street retailer, which then resells those shoes to consumers along with other brands of shoes.

The manufacturer and the retailer are likely to be competitors. Therefore, agreements between them relating to shoes could contain provisions which amount to cartel provisions.

In its supply contract with the retailer, the manufacturer includes a provision that prevents the retailer from selling any of the manufacturer's shoes at a price greater than the wholesale price plus 25%.

The maximum resale price provision would likely amount to price fixing and therefore be a cartel provision.

However, the vertical supply exception is likely to apply. The cartel provision is in a vertical supply contract and it sets the maximum price at which the retailer can sell the manufacturer's shoes. The exception would apply unless the dominant purpose of the provision is to lessen competition between the manufacturer and the retailer. Where there is a genuine maximum price that parties are free to sell below, that is unlikely to be the case, especially if there is a good competition reason for setting the maximum (like a desire to drive demand).

### Minimum resale prices

Suppose the shoe manufacturer operates its own retail stores. In discussions about their supply relationship, the retailer and manufacturer discuss the dire state of the retail prices of the manufacturer's shoes and the profits they are each earning on those shoes.

As a result the manufacturer issues a recommended retail price (RRP) list to its own retail stores, the retailer, and all its other retailer customers. The manufacturer and the retailer also agree that the manufacturer and the retailer will not sell the manufacturer's shoes below the RRP in their respective retail stores.

The agreement not to sell the manufacturer's shoes below the RRP would amount to price fixing and would on its face be a cartel provision.

The vertical supply exception is not likely to apply to that provision for a number of reasons.

First, the provision is not in a supply contract between the manufacturer and the retailer. Rather it forms part of a verbal agreement or understanding between them outside their formal supply contract.

Even if it the provision was included in the supply contract:

- The cartel provision is unlikely to 'relate to' the supply of shoes from the manufacturer to the retailer. The manufacturer has been supplying the retailer for some time and there is no evidence to suggest that the continued supply of shoes is contingent on the retailer agreeing to price in accordance with the RRP. As such, there is unlikely to be a sufficiently close connection between the cartel provision and the supply of goods from the manufacturer to the retailer for the cartel provision to relate to that supply.
- The cartel provision, on its face, and in light of the surrounding circumstances, appears to have the dominant purpose of lessening competition between the manufacturer and the retailer. The main or principal reason for the provision is to increase prices to the benefit of the parties.



## Promotional price for a new product

Suppose that in either of the above two examples, the shoe manufacturer wishes to introduce a new type of shoe. In order to promote its new type of shoe, the manufacturer decides that it wants to make sure that the shoes are priced below its current range for two months.

The manufacturer offers an initial promotional wholesale price to its retailer for the new shoes. The manufacturer does not change the wholesale price of the other shoes it sells to the retailer.

To ensure the lower wholesale price is passed on, the manufacturer includes in its supply contract with the retailer a provision that requires the retailer to sell the new shoe type at a price at least 10% below the price at which the retailer sells the manufacturer's other shoes. This obligation lasts for the two months of the promotion.

This provision would likely amount to price fixing and therefore be a cartel provision.

### Does the vertical supply exception apply?

The vertical supply exception could only apply to the provision if that provision is in a formal supply contract between the parties. If it is not in a supply contract, the exception could not apply.

The provision here is likely to relate to supply of the new shoe type by the manufacturer to the retailer. The provision appears to be sufficiently closely connected to the manufacturer's supply of the new shoe type to the retailer.

Therefore, the vertical supply exception would apply if the dominant purpose of the provision is not to lessen competition between the manufacturer and the retailer. In assessing that question, we would look to evidence of what the provision, seen in context, is designed to achieve. Assessed objectively, is it designed to increase output or lower prices to consumers?

In this example, if the evidence supported a conclusion that the provision was included by the manufacturer to increase sales of its new shoe type and its sales overall, then it is unlikely to have the dominant purpose of lessening competition between the manufacturer and the retailer. Conversely, if the evidence suggested that the provision was a device to increase or maintain the price of the manufacturer's other shoe types, then it would likely have the dominant purpose of lessening competition.

## Geographic restrictions in a vertical supply contract

A new kitchen appliance manufacturer K has started selling its products in New Zealand through its own 'concept' stores in Auckland and Christchurch, in competition with other manufacturers' products. Those competing manufacturers' products are sold through various competing retailers throughout New Zealand.

K considers its point of difference is that its products are premium products. K invests in providing promotional and educational material for consumers, in-store demonstrations, extended warranties, training sales staff, and in providing installation and after-sales service.

K wants to start selling its products in Wellington, Tauranga, Dunedin and Hamilton. However, it does not want to invest in its own stores and in providing its own installation and after-sales service team. Rather, it wishes to distribute through existing retailers and have them provide the in-store service and the installation and after-sales service.

As a new product to these cities, and given K wants to position itself as a premium service driven product, K appoints one retailer as its distributor in each city. It includes in its supply contract with each retailer a provision that, for two years:

- prevents the retailer from selling any of the manufacturers' products in any other city where that retailer has a store; and
- prevents K, the manufacturer from establishing its own store or its installation and service team in that city.

This provision is likely to amount to market allocation and would on its face be a cartel provision. However, the vertical supply exception may apply for the following reasons.

First, we would assess whether the cartel provision has a sufficiently close degree of connection to the supply of the products from the manufacturer to the retailer to relate to that supply. Here, on the facts, the restriction would likely relate to the supply from the manufacturer to the retailer. There is a connection between the cartel provision and the supply of products from the manufacturer to the retailer.

If the cartel provision did relate to the supply from the manufacturer to the retailer, the provision would fall within the exception provided its dominant purpose is not to lessen competition between the manufacturer and the retailer. In a case like this, to answer this question we would be interested in evidence, including internal documents, describing the manufacturer's distribution strategy and its rationale for that strategy.

As described above, the dominant purpose of the provision may not be to lessen competition provided the cartel provision was designed to increase output (the manufacturer's sales in this case) or lower prices to consumers. The cartel provision's purpose may be to incentivise retailers to invest in advertising, promoting and educating consumers about K's product as well as providing the required after-sales service.

## Chapter 4. EXCEPTION FOR JOINT BUYING AND PROMOTION AGREEMENT

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- 1 The joint buying and promotion exception applies when competing buyers arrange to purchase goods or services collectively on terms that an individual buyer would be unlikely to be able to negotiate on their own.
- 2 The exception applies only to price fixing, not to the other forms of cartel conduct.
- 3 As an example of joint buying, a group of small grocers might get together to collectively purchase a large order of tinned fruit at a volume discount, or real estate businesses might jointly purchase advertising in a newspaper. While such agreements between competing buyers could be regarded as price fixing, the conduct will be exempt if the provision:<sup>44</sup>
  - 3.1 relates to the price of goods or services some or all of the competing buyers collectively acquire (either directly or indirectly);
  - 3.2 provides for the competing buyers to collectively negotiate the price for goods or services which they then purchase individually;<sup>45</sup> or
  - 3.3 provides for an intermediary to take title to the goods and resell or resupply them to one or more of the competing buyers.
- 4 If buyers have collectively acquired goods or services, any agreement between those buyers to jointly advertise the price at which they will resupply those goods or services is also exempt from the cartel prohibition. However, the parties to the advertising agreement must remain free to sell the goods at whatever price they choose.
- 5 This is illustrated by Figure 8. In the grocers example above, one of the grocers might decide to advertise and sell the collectively acquired tinned fruit at a price lower than the agreed advertised price.
- 6 Even if the exception applied, it would still be illegal if the provision:
  - 6.1 amounts to market allocation or capacity restriction and the collaborative activity exception did not apply;<sup>46</sup> or
  - 6.2 has the purpose, effect, or likely effect of substantially lessening competition in a market.



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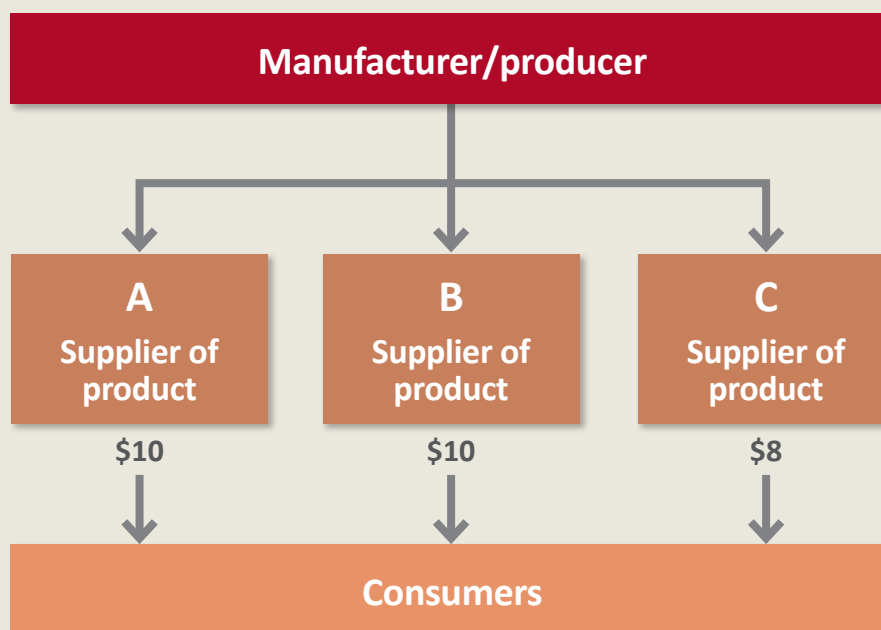
44. Commerce Act 1986, s 33.

45. We do not regard collective negotiation as requiring all buyers who are parties to the agreement to be actively involved in the negotiations. What is required is that the parties take a collective approach to those negotiations, even if that collective approach is represented by one party on behalf of the other parties.

46. The collaborative activity exception is discussed in Chapter 5.

- 7 It is up to the person relying on the joint buying exception to prove that the exception applies, on the balance of probabilities.<sup>47</sup>

**Figure 8: Joint buying and promotion agreement**



### Examples

#### Joint buying

Several small computer repair companies arrange to jointly purchase components in bulk to save costs. The companies are then free to price the components as they see fit.

The computer repair companies are likely to be competitors for the acquisition of the computer components. The agreement to jointly purchase is likely to be price fixing and therefore a cartel provision.

However, as the cartel provision relates to the price of goods to be collectively acquired by the repairers, the joint buying exception would apply.

The exception also covers the computer repair companies if they jointly advertise the collectively acquired components. However, each company must be free to sell the components at a different price from that jointly advertised.

On the other hand, the exception would not cover a scenario where the companies jointly advertise the price for a repair service using the jointly acquired components to repair computers. This is because the repair price includes other costs, such as labour and overheads, which have not been jointly acquired.

47. Commerce Act 1986, s 80(2C).

## Acquisition at a collectively agreed price

Three car yards jointly negotiate a contract with a radio station for a regular advertising space for a two-year period. The car yards then rotate the advertising space between them, with each purchasing the advertising space directly from the radio station during their allotted time. This allows the car yards to benefit from the more favourable terms of a long-term contract that they would not have been able to commit to individually.

The car yards are likely to be competitors for the acquisition of advertising space. Therefore, the agreement to purchase at an agreed price is likely to be price fixing and be prohibited by the cartel provision.

However, the exception is likely to apply as the cartel provision provides for collective negotiation of the price for goods or services followed by individual purchasing at the collectively negotiated price.

Although this agreement may not breach the cartel prohibition, the parties would need to satisfy themselves that the agreement did not have the purpose, effect, or likely effect of substantially lessening competition in breach of section 27.



## Chapter 5. EXCEPTION FOR COLLABORATIVE ACTIVITIES

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- 1 The collaborative activity exception applies to a cartel provision in an agreement if:<sup>48</sup>
  - 1.1 the parties to the agreement are involved in a collaborative activity; and
  - 1.2 the cartel provision is reasonably necessary for the purpose of the collaborative activity.<sup>49</sup>
- 2 The collaborative activity exception also applies to a cartel provision in an agreement that constitutes a restraint of trade if:
  - 2.1 the collaborative activity has ended; and
  - 2.2 the cartel provision was reasonably necessary for the purpose of the collaborative activity; and
  - 2.3 the collaborative activity did not end because the lessening of competition between any two or more parties became its dominant purpose (as detailed below).
- 3 It is up to the person relying on the collaborative activity exception to prove on the balance of probabilities that the exception applies.<sup>50</sup>
- 4 However, a party to a collaborative activity who proposes to enter into an agreement containing a cartel provision may apply to us for clearance of the agreement. We explain how the clearance regime works in Chapter 6.

### Defining a collaborative activity

- 5 The collaborative activity exception replaces the former joint venture exception. The joint venture exception was criticised as focusing on the form by which the parties were ‘cooperating’ to determine whether that exception to the price fixing prohibition applied. In contrast, the collaborative activity exception is focused on the substance of the parties’ cooperation.
- 6 At the simplest level, the exception asks: does this look like a cartel? And that is the lens through which we view the two parts of the definition of a collaborative activity.
- 7 To be engaged in a collaborative activity two or more persons must:
  - 7.1 be carrying on an enterprise, venture, or other activity, in trade in cooperation; and
  - 7.2 not be doing so for the dominant purpose of lessening competition between them (or any two of them).<sup>51</sup>



48. Commerce Act 1986, s 31.

49. As explained in Chapter 2, even if this exception applies to a cartel provision, the provision may nonetheless be prohibited if it has the purpose, effect, or likely effect of substantially lessening competition in a market.

50. Commerce Act 1986, s 80(2C).

51. Commerce Act 1986, s 31(4)(b).

## When will parties be carrying on an enterprise, venture, or other activity, in trade in cooperation?

- 8 This first part of the collaborative activity definition establishes the scope of the collaboration between the parties, ie, the activity the parties are doing collaboratively.
- 9 Simply labelling an agreement as a collaborative activity will not be sufficient to bring the collaboration under the protection of the exception.
- 10 To qualify as a collaborative activity the parties need to be combining their businesses, assets, or operations in some way in a commercial activity, or otherwise operating a commercial activity jointly. They need to be doing something more than simply agreeing how to run their separate businesses. This interpretation is consistent with the focus of the exception being on the substance of what the parties are doing – ie, does this look like cartel conduct or not?

### A commercial activity

- 11 The Commerce Act requires that the parties must be carrying on ‘an enterprise, venture, or other activity, in trade’ in cooperation. Given the way ‘trade’ is defined in the Commerce Act,<sup>52</sup> we consider that what the parties need to be carrying on in cooperation is something relating to the buying and selling of goods or services or the acquisition of land. We use ‘commercial activity’ to denote this.
- 12 So it follows from this that the parties must be ‘carrying on [a commercial activity] in cooperation’.

### Carrying on in cooperation

- 13 It is the ‘carrying on ... in cooperation’ language that indicates that the parties must be combining their businesses, assets, or operations in some way in a commercial activity, or otherwise operating a commercial activity jointly. This is consistent with both the ordinary meaning of ‘cooperate’ – ‘work jointly towards the same end’<sup>53</sup> – and the Court of Appeal’s comment that the ordinary and natural meaning of ‘carrying on’ suggests some degree of continuity or repetition.<sup>54 55</sup> It is also consistent with the fact that the ‘carried on ... in cooperation’ language is different from the ‘contract, agreement or understanding’ language used in section 30, implying Parliament intends something different for an activity to be ‘carried on ... in cooperation’ than simply a shared expectation about how at least one of the parties will act or refrain from acting, in relation to its own business.
- 14 What this means in practice is that an agreement between competitors about how to run their separate businesses would not have the necessary quality of ‘carrying on ... in cooperation’ to amount to a collaborative activity. For example, suppose two businesses enter into an agreement to add a surcharge to the products that they sell in competition with one another. Regardless of the rationale behind this surcharge, this agreement would be unlikely to meet the first criteria of the collaborative activity test.



52. As any trade, business, industry, profession, occupation, activity of commerce, or undertaking relating to the supply or acquisition of goods or services or to the disposition or acquisition of any interest in land. Commerce Act 1986, s 2.

53. Oxford English Dictionary.

54. *Commerce Commission v Visa Board Pty Limited* [2012] NZCA 383, at [28].

55. We recognise that in some cases the commercial activity may not be ongoing. This will not automatically disqualify such an activity from the exception. As explained, it is a question of fact in each case. What matters is that the parties can demonstrate that they are carrying on a commercial activity in cooperation.

- 15 Parties should be able to identify and to explain how they intend to combine their businesses, assets, or operations in a commercial activity, or otherwise operate in a commercial activity jointly.

### Examples

#### Cover charge for bars

Following incidents of alcohol related harm in the central city, a group of concerned local bar owners agree to impose a minimum cover charge on Friday and Saturday nights from 11pm until closing to reduce alcohol related harm. The agreement emerged after suggestions from the Police and the local council.

The agreement to charge a minimum cover charge is a (price fixing) cartel provision and therefore prohibited unless the collaborative activity (or another) exception applies.

However, this is unlikely to be a collaborative activity as defined in the Commerce Act. The parties are not carrying on an enterprise, venture, or other activity, in trade in cooperation with each other.

- While reducing alcohol harm is a worthy objective, it is not an enterprise, venture, or activity in trade carried on by the bar owners in cooperation. The enterprise, venture, or activity in trade the bar owners carry on separately (but not collectively) is providing hospitality services.
- Each bar owner is simply agreeing to impose a surcharge on their separate businesses. As such, there is unlikely to be the necessary cooperation to take this beyond what is simply an agreement between competing business owners as to how they will each run their businesses.

While such an agreement may have socially beneficial effects, these effects are not sufficient to bring the agreement within the exception. However, the parties could apply for authorisation from the Commission to be able to impose the minimum cover charge, and through that process would be able to explain and outline the public benefits arising from their conduct. For more information on our authorisation criteria, refer to our Guidelines at <http://www.comcom.govt.nz/dmsdocument/10187>.

#### Decision 735: Refrigerant License Trust Board

This case involved an authorisation application by the Refrigerant License Trust Board for authorisation of an agreement between refrigerant wholesalers to supply refrigerants only to customers who were trained and licensed or certified to safely handle refrigerants.

The cartel provision here would have been the restriction of customers to whom members could sell refrigerants.

However, the collaborative activity may have been broader. Here the Board established a scheme to develop refrigerant license training courses to improve compliance with the Hazardous Substances and New Organisms Act 1996. This is likely to have been an activity in trade in which the members were cooperating to establish and provide. It is therefore likely to have satisfied the 'in cooperation' element of the collaborative activity exception.



## Not for the dominant purpose of lessening competition between the parties

- 16 To qualify for the exception, the collaborative activity must not be carried out for the dominant purpose of lessening competition between the parties to the agreement.<sup>56</sup> This limitation “reflects the need to guard against the use of sham joint ventures or other sham collaborations to evade operation of the per se civil prohibitions against cartel conduct”.<sup>57</sup>

### Dominant purpose is the main or principal purpose

- 17 While an agreement may have more than one purpose, a dominant purpose is the main or principal reason for the collaboration. This is in contrast to the definition of purpose in section 2(5) of the Commerce Act, which defines purpose as meaning a ‘substantial purpose’. Our approach to defining dominant purpose is consistent with the ordinary meaning of dominant which includes ‘prevailing’ and ‘most influential’.
- 18 The prevailing objective that the parties are jointly working towards must not be to lessen competition between them. If it is – that is, if the collaborative activity is simply a device to reduce competition – then the exception will not apply.
- 19 If a collaborative activity has multiple purposes, we will identify the dominant purpose of the collaborative activity and assess whether it is to lessen competition.

### Focus is on lessening competition between the parties

- 20 The collaborative activity test asks whether the parties have a dominant purpose of lessening competition between each other (including hindering, reducing, or eliminating competition between the parties), rather than in the market generally. A wider enquiry into market effects is not required by the test.<sup>58</sup>

### Test is primarily an objective test

- 21 The ‘not for the dominant purpose’ test is primarily an objective test for the courts or the Commission to assess, although evidence of what the parties were trying to achieve will be relevant. The focus will be on the substance of the activity being undertaken. We will also look at the parties’ conduct and any other relevant circumstances.<sup>59</sup>
- 22 The mere fact that the parties do not believe that they are lessening, or intend to lessen, competition between them will not be determinative.
- 23 There is no bright line as to when an aim or objective becomes the dominant purpose. It is a matter of judgement for the court (when applying the collaborative activity exception) or the Commission (in the context of a clearance) based on the facts of the case.



56. The exception for vertical supply contracts (discussed in Chapter 3) also requires consideration of whether the cartel provision has the dominant purpose of lessening competition. These general principles also apply to the exception for vertical supply contracts.

57. Hampton L, *Scott Guide to Competition Law* Lexis Nexis 2013, at 196.

58. Further, in contrast to other parts of the Commerce Act, the words ‘lessening competition’ are not qualified by ‘substantially’. The absence of the qualifier ‘substantial’ means that there is no need for the provision’s dominant purpose to be to lessen competition between the parties in a way that is real or of substance. Any lessening of competition is sufficient.

59. Commerce Act 1986, s 31(3).

## Parties must show that they are not collaborating for the dominant purpose of lessening competition between them

- 24 Where a cartel provision exists, parties must be able to explain why they are collaborating – ie, they must be able to explain that the dominant purpose of their activity is benign or pro-competitive. If they cannot persuasively do so, then it is likely that the Commission or a court will infer that their dominant purpose is to lessen competition between the parties.
- 25 We recognise that parties collaborate for a number of reasons other than to lessen competition. Examples may include the following.
  - 25.1 A collaboration may allow parties to combine their different capabilities or resources to improve their ability to compete. One party may have special technical expertise that usefully complements another party's manufacturing process, allowing the latter party to lower its production cost or improve the quality of its product.
  - 25.2 Similarly, collaboration may help the parties attain economies of scale or scope beyond the reach of one of them individually, again improving the parties' ability to compete. For example, two parties may be able to combine the production of their complementary goods to lower the cost of bringing their products to market.
  - 25.3 There may also be reasons why parties collaborate that are not directly related to improving their ability and incentive to compete, yet do not indicate a dominant purpose not to compete. For example, parties may collaborate to achieve some environmental, health and safety, or other social welfare purpose, which is unrelated to their individual or collective competitiveness.

### Example

## Where parties may not have a dominant purpose of lessening competition between them

Two computer manufacturers have different design and technology expertise. They decide that by combining different capabilities or resources they will be able to offer more affordable computer hardware and software.

Two firms combine their research or marketing activities to reduce the time needed to develop and sell a new product.

Decision 735: Refrigerant License Trust Board: This case involved an authorisation application by the Board for authorisation of an agreement between refrigerant wholesalers to supply refrigerants only to customers who are trained and licensed or certified to safely handle refrigerants. This provision, while a cartel provision, was designed to improve industry compliance with the Hazardous Substances and New Organisms Act 1996.

## How we assess whether the collaboration is carried on for the dominant purpose of lessening competition between the parties

- 26 Although the test is primarily objective, when assessing whether the parties are collaborating for the dominant purpose of lessening competition between them, we will consider what the parties were trying to achieve. Documents created during the evaluation and negotiation of the collaboration (rather than those created at some later date) may be useful in demonstrating the objectives of the agreement.
- 27 We will also consider questions such as:
  - 27.1 Is the collaboration designed to lower prices or increase output, or is it designed to increase prices or reduce output?
  - 27.2 Is the collaboration likely to create significant new productive capacity, new products, etc?
  - 27.3 Are there cost savings associated with the collaboration that explain its existence?

## Cartel provision must be reasonably necessary for the purpose of the collaborative activity

- 28 To gain the benefit of the exception, the cartel provision must be reasonably necessary for the purpose of the collaborative activity. In this context, we take ‘purpose’ to mean all substantial purposes of the collaborative activity.

### Reasonably necessary: an objective test

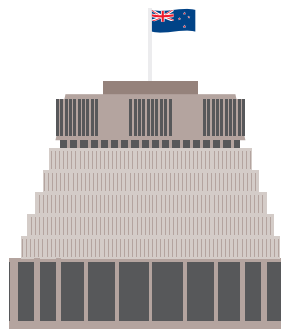
- 29 Whether a cartel provision is reasonably necessary for the purpose of the collaborative activity is assessed objectively.<sup>60</sup> That assessment is made by the courts or by the Commission at the time the cartel provision was entered into or given effect to.<sup>61</sup>
- 30 What is reasonably necessary will depend on the particular facts and circumstances of the case.

### Reasonably necessary: an everyday standard

- 31 The phrase ‘reasonably necessary’ has been described as being a standard used in everyday language and one that should require no undue elaboration.<sup>62</sup> Nevertheless, we have outlined some general principles we will apply when assessing whether something is reasonably necessary.

### Cartel provision need not be essential to be reasonably necessary

- 32 By using the term ‘reasonably necessary’, Parliament has signalled that a cartel provision need not be essential for the collaborative activity. This means that a party does not need to show that, ‘but for’ the cartel provision, the collaborative activity would not occur.<sup>63</sup>
- 33 We say this for two principal reasons.
- 33.1 While ‘necessary’ reflects a high standard – its dictionary definitions include ‘indispensable, requisite’ – Parliament has chosen to qualify it by ‘reasonably’, ie, within reason.
- 33.2 ‘Reasonably necessary’ is used in other legal contexts in New Zealand<sup>64</sup> and in other jurisdictions. Most relevantly it is used in the United States Federal Trade Commission and the United States Department of Justice’s Antitrust Guidelines for Collaborations Among Competitors (US Guidelines) and section 45 of Canada’s Competition Act. It is clear from the explanatory materials to the Amendment Act that when including the phrase in the collaborative activity exception, Parliament had in mind the US Guidelines and the way the US Guidelines used the phrase ‘reasonably necessary’. The US Guidelines do not require a cartel provision to be essential in order to be excluded from the US per se price fixing rules.<sup>65</sup>



60. See *Mana v Fleming* [2007] NZCA 324.

61. Commerce Act 1986, s 31(1).

62. *Queenstown Airport Corporation Ltd v Queenstown Lakes District Council* [2013] NZHC 2347, at [93].

63. Of course, however, if the collaboration could not be achieved absent the cartel provision, then this would be sufficient to demonstrate that the cartel provision is reasonably necessary for the collaborative activity.

64. For example the phrase is used in s 171(c) of the Resource Management Act 1991.

65. However, the explanatory materials also note that “in contrast with the approach in the US Guidelines, the exception for collaborative activity does not require efficiency enhancing integration”. Ministry of Economic Development *Cartel Criminalisation – Cartel Criminalisation – Exposure Draft Commerce (Cartels and Other Matters) Amendment Act 2011: Explanatory material* June 2011 at [51].

## **Requires something more than merely desirable, expedient, or preferable**

- 34 However, a cartel provision will not be reasonably necessary if it is merely desirable, expedient, or preferable. Something more than that is required. When interpreting 'reasonably necessary' in the context of the Resource Management Act, Whata J said for something to be reasonably necessary it must be 'clearly justified'.<sup>66</sup>

## **Assessment requires consideration of other available options**

- 35 Determining whether something is reasonably necessary requires consideration of the alternative available options open to the parties. By alternative available options we mean options that are practically workable – as opposed to theoretical or extravagant possibilities – and which either:
- 35.1 do not involve a cartel provision; or
  - 35.2 involve a cartel provision that is significantly less restrictive in scope than the cartel provision in issue.

## **How we will assess whether a cartel provision is reasonably necessary for the purposes of a collaborative activity**

- 36 In assessing whether a cartel provision is reasonably necessary for the purposes of the collaborative activity, we will first look to understand what interest or interests the parties are trying to protect or promote by using the cartel provision. That is, what are the parties trying to achieve with the cartel provision? For example, is the cartel provision designed to:
- 36.1 significantly reduce the parties' risk in achieving the collaborative activity's purpose(s) (eg, it deters free-riding or ensures an equitable sharing of profits derived from the collaboration);
  - 36.2 significantly reduce the cost of achieving that purpose;
  - 36.3 significantly shorten the timeframe for parties to achieve that purpose; or
  - 36.4 align the parties' incentives?
- 37 Second, it will be important for us to understand how important or significant that interest(s) is in assisting the parties to achieve the collaboration's purpose(s).
- 38 In essence, these two questions ask: why have the parties included the cartel provision?
- 39 Third, in assessing whether the cartel provision is reasonably necessary we will then consider the following types of factors.
- 39.1 The scope of the cartel provision itself, including its duration, its geographic scope, relationship to the parties' businesses, and the products and markets to which the provision applies. A cartel provision may not be reasonably necessary when it applies for a significantly longer period of time, or has a significantly greater geographic scope than is required for the parties to achieve the purpose(s) of the collaborative activity.
  - 39.2 The available alternatives that would enable the parties to pursue their collaboration/protect the relevant interest. Parties should be able to explain why they have chosen the cartel provision as opposed to other alternatives. It is not enough for a party to simply say that they would not enter into the collaboration in the absence of the cartel provision.

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66. *Queenstown Airport Corporation Ltd v Queenstown Lakes District Council* [2013] NZHC 2347, at [93].

- 40 Evidence of alternative options the parties considered at the time the agreement was negotiated may be relevant. Similarly, evidence showing that other comparable collaborations have failed or succeeded (in New Zealand or overseas) without such a provision would be relevant.
- 41 If there is more than one cartel provision in an agreement, each cartel provision must be reasonably necessary for the purpose of the collaborative activity.

#### *Exception for cartel provisions that constitute a restraint of trade*

- 42 The cartel prohibition does not apply to a cartel provision that constitutes a restraint of trade if:
  - 42.1 the parties were involved in a collaborative activity that has ended;
  - 42.2 the cartel provision constitutes a restraint of trade and was reasonably necessary to achieve the aims of the collaborative activity; and
  - 42.3 the agreement did not end because the lessening of competition between two or more parties became its dominant purpose.
- 43 This provision is potentially relevant when a franchisor that is involved in a collaborative activity is seeking to enforce a restraint of trade clause in a franchise agreement that comes to an end.

#### **Example**

Rata Cleaning Services operates a nationwide domestic cleaning franchise. Its standard franchise agreement includes a clause restricting the franchisee from owning or operating a competing business within five kilometres for a period of three months after the franchise agreement comes to an end.

The collaborative activity exception will apply after the franchise agreement comes to an end if the restraint of trade was reasonably necessary for the purposes of establishing the franchise. To test this, we would, for example, ask Rata Cleaning Services to explain why the restraint of trade is more than simply desirable, easier or preferable. We would also need to consider whether the restraint is reasonable at common law.



## Example

### Development of gas field with joint selling

A is a gas explorer, producer and wholesaler that has discovered an economically viable petroleum resource in deep water off the coast of New Zealand. Due to the size of the discovery, and the costs and risks of developing the field, A is unwilling to develop the field itself.

As a result A invites B and C to enter into an agreement to develop the field in collaboration. B and C are both gas producers and wholesalers who compete with A in the wholesale market.

A, B and C agree that each will invest capital to develop the field. They also agree that the field will be operated by B.

They also agree that all the petroleum produced from that field will be sold jointly in the wholesale market – ie, the parties will act as one seller – and profits distributed to the joint venture partners in proportion to their interests in the collaboration.

As A, B and C are competitors outside the ambit of the collaboration, they should consider whether the collaborative activity exception applies to the joint selling provisions.

#### **Are A, B and C engaged in an enterprise, venture, or other activity, in trade carried on in cooperation?**

Yes. A, B, and C are jointly developing and running a gas field operation. This is the case even though they have appointed B to run the field.

#### **Does the parties' collaboration have the dominant purpose of lessening competition between them?**

As described in the Guidelines, this test is primarily an objective one, with the focus being on the substance of what is being undertaken. Why is it that the parties want to collaborate? Internal documents will help us answer these questions.

We will consider whether:

- the development collaboration is designed to lower prices or increase output, or designed to increase prices or reduce output;
- the development collaboration is likely to create significant new productive capacity, new products, etc; and
- there are cost savings associated with the development collaboration that explain its existence.

Particularly relevant here would be B's and C's involvement.

- Did A involve B or C because it made the development of the field feasible, thereby bringing new capacity to market? If so, this is likely to suggest that the parties did not have a dominant purpose of lessening competition between them.
- Conversely, if the evidence showed that A involved B and C to discourage B or C from developing its own competing field, or otherwise to influence the way B or C competed, that may lead to a different conclusion.

*Continued...*

### **Are the cartel provisions – the joint selling provisions – reasonably necessary for the purposes of the collaboration?**

As described in the body of the Guidelines, in making our assessment we will first seek to understand the interests the parties are trying to protect or promote through the use of the cartel provision. Second, we ask how important the interest(s) are.

We would then consider:

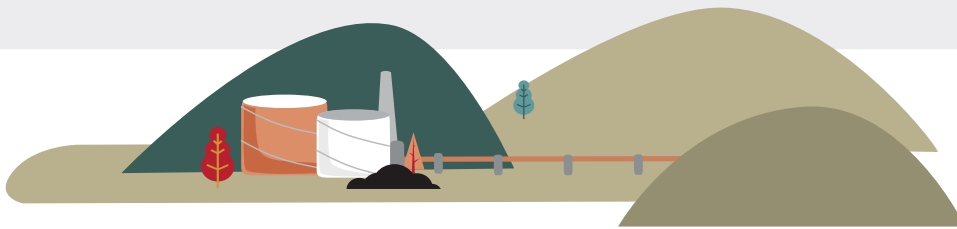
- the scope of the cartel provision – for example, how long does it apply for, how are the rest of the parties' businesses affected or protected; and
- the available alternatives.

The key relationship is between the joint selling provisions and the development of the field.

- If the evidence showed that the field would not be developed by these parties without these provisions, then the provisions would be reasonably necessary. The parties would have to explain and provide evidence to support why the field would not be developed without the provisions.
- Conversely, if the development of the field was unaffected by whether the joint selling agreements were in place or not, then the joint selling agreements would not be reasonably necessary.

Where the line falls within those two extremes is difficult to draw and would depend on the scope of the cartel provision, what interest the parties are trying to protect, and whether there were practical alternatives available to them.

The parties would have to show that the joint selling provisions are more than merely desirable, expedient, or preferable.



## Example

### Development of a new product with price fixing provision

Firms A and B are competing software companies. They enter an agreement to develop, produce, and market a new software product, Product Z. Neither A nor B had any plans to independently develop a product similar to Product Z.

Both A and B contribute their own proprietary assets to the product's development, but both acknowledge that A's assets are more valuable than B's (in that A's assets have more valuable uses outside the agreement with B).

A and B agree that once Product Z is developed, they will jointly set the price at which A and B will sell Product Z.

As A and B are competitors, they should consider whether the collaborative activity exception applies. Neither the vertical supply, nor the joint buying and promotion exceptions are likely to apply here.

The exception will apply if the parties are engaged in a collaborative activity and the cartel provision – the agreement to jointly set Product Z's price – is reasonably necessary for the purposes of the collaboration.

#### **Are A and B engaged in a collaborative activity?**

Yes it is likely A and B engaged in a collaborative activity.

A and B are working jointly together for the purpose of developing, producing, and marketing Product Z.

The dominant purpose of the collaboration is not to lessen competition between the parties. Indeed, the collaboration appears designed to introduce a new product into the market, Product Z. On its face, this is a pro-competitive outcome.

However, the position may well be different if there was evidence that either or both parties already had well-developed plans to develop a similar product, or if there was other evidence that suggested that the collaboration was primarily about removing competition between the parties in relation to their other product lines.

#### **Is the joint price setting reasonably necessary for the purposes of the collaborative activity?**

A and B say that the joint price setting provision is necessary because A is expected to invest more in developing Product Z than B. This is because the assets A is contributing are more valuable than the assets B is contributing. The result, they say, is that B could undercut A's price and still make a positive return on its investment. In other words, absent the price fixing agreement, B would be able to free-ride on A's more valuable assets. The result is that A may not have incentive to enter into the agreement in the first place.

Our initial focus will be to identify the interests the parties are trying to protect or promote through the use of the cartel provision. Here it is to reduce the parties' risk in achieving the collaborative activity's purpose by deterring B free-riding on A's investments.

Given the investments appear crucial to the development of the product, this would appear to be a significant factor in the parties achieving their ultimate objective of developing Product Z.

We would examine the scope of the joint price setting clause, (including whether it just applies to Product Z) and its duration (does it apply in perpetuity, or for a limited initial period tied to the initial investment in the product?).

We would then look at why other available alternatives would be inadequate or unavailable. For example, in this case, alternatives may include other contractual mechanisms such as payments by B to A to compensate A for its more valuable assets.



## Chapter 6. CLEARANCES FOR CARTEL PROVISIONS RELATING TO COLLABORATIVE ACTIVITIES

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- 1 A party proposing to enter into an agreement containing a cartel provision that is part of a collaborative activity can apply for clearance for that agreement. This is a voluntary regime; there is no statutory requirement to seek clearance.
- 2 Where we clear an agreement, parties to the agreement will not contravene the cartel prohibition or the prohibition on agreements that substantially lessen competition. In essence, a clearance provides certainty that the agreement is lawful under the Commerce Act.
- 3 If the parties to the agreement subsequently want to enter into a new, amended, or additional agreement that contains a cartel provision, they must seek a further clearance for that new agreement. Similarly, if a new party joins an agreement that has been given clearance, the agreement is considered to be a new agreement and therefore no longer has the benefit of clearance.
- 4 We can only consider clearance applications if the agreement containing a cartel provision has not yet been entered into or given effect to.<sup>67</sup> We also do not have jurisdiction to clear agreements that we do not have reasonable grounds to believe contain a cartel provision.
- 5 However, that does not mean that the collaborative activity cannot already exist. It may be possible that an existing collaboration may require a new agreement with a cartel provision.

An example of this may be where two parties are engaged in a joint selling collaboration and the advent of a new product requires a new agreement containing a cartel provision. The clearance regime would be available for the new agreement.

### When we will grant clearance

- 6 We will give clearance if:
  - 6.1 the applicant and any other party to the agreement are or will be involved in a collaborative activity; and
  - 6.2 every cartel provision in the agreement is reasonably necessary for the purpose of the collaborative activity;<sup>68</sup> and
  - 6.3 entering into the agreement, or giving effect to any provision of the agreement, will not have, or would not be likely to have, the effect of substantially lessening competition in a market.<sup>69</sup>
- 7 The applicant must satisfy us that each of these criteria is met.<sup>70</sup> If we are not satisfied that all of the criteria are met, we must decline clearance.
- 8 The first two requirements of the clearance test are identical to the collaborative activity exception criteria. Therefore, the same analysis applies as outlined in Chapter 5. The third requirement is designed to determine whether the agreement (or any provision within the agreement) will substantially lessen competition in a market.<sup>71</sup>

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67. Commerce Act 1986, s 65A(1).

68. We do not need to determine whether a particular provision is in fact a cartel provision, providing there are reasonable grounds for believing it might be. Commerce Act 1986, s 65A(3).

69. Commerce Act 1986, s 65A.

70. The standard of proof is the balance of probabilities.

71. This requires the same analysis of an agreement as under section 27 of the Commerce Act.

## Satisfying the Commission that the collaborative activity exception applies

- 9 The criteria that parties must meet for the collaborative activity exception to apply are explained in Chapter 5. Chapter 5 also explains how we will assess these criteria.

## Satisfying the Commission that the agreement is not likely to substantially lessen competition

- 10 We assess whether entering into the agreement or giving effect to any provision in the agreement would be likely to have the effect of substantially lessening competition in a market.<sup>72</sup> To carry out this assessment, we look at all the provisions in the agreement, not just the cartel provisions.<sup>73</sup>

### Substantial lessening of competition

- 11 Competition means workable or effective competition.<sup>74</sup> When assessing whether a market is competitive, we examine the extent to which participants within it possess ‘market power’, ie, the ability to, for example, profitably and sustainably raise price above competitive levels.
- 12 The substantial lessening of competition (which includes a hindering and/or prevention of competition)<sup>75</sup> test is a relative standard.<sup>76</sup> It asks whether the parties’ market power would increase relative to what it would be without the agreement.<sup>77</sup> A number of factors are relevant when assessing whether competition is or is likely to be substantially lessened, including:
- 12.1 the nature of the restrictions contained in the agreement;
  - 12.2 the nature of the products involved;
  - 12.3 the number and size distribution of independent suppliers, and the degree of market concentration;
  - 12.4 the conditions of entry, that is the ease with which new firms may enter and secure a viable market, and the resulting likelihood that entry will be timely and constraining; and
  - 12.5 other restraints, such as countervailing buyer power.
- 13 A lessening of competition – or an increase in market power – may manifest in a number of ways, including in higher prices or reduced quality (relative to levels without the agreement).
- 14 However, only a lessening of competition that is substantial would prevent us from clearing an agreement containing a cartel provision. A lessening of competition will be substantial if it is real, of substance, or more than nominal.<sup>78</sup> Some courts have used the word ‘material’ to describe a lessening of competition that is substantial.<sup>79</sup>

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72. Commerce Act 1986, s 65A(2)(c).

73. We also apply a substantial lessening of competition test when assessing mergers. Our Mergers and Acquisitions Guidelines set out how we assess a substantial lessening of competition in the merger context. These are available at <http://www.comcom.govt.nz/business-competition/guidelines-2/mergers-and-acquisitions-guidelines/>

74. Commerce Act 1986, s 3(1).

75. Commerce Act 1986, s 3(2).

76. *ANZCO Foods Waitara Ltd & Ors v AFFCO New Zealand Ltd* [2006] 3 NZLR 351 at [240].

77. See the discussion in *ANZCO Foods Waitara Ltd & Ors v AFFCO New Zealand Ltd* [2006] 3 NZLR 351 at [245]–[246]. The test captures the creation, preservation and enhancement of market power.

78. *ANZCO Foods Waitara Ltd & Ors v AFFCO New Zealand Ltd* [2006] 3 NZLR 351 at [239]. See also *Re Closure of Whakatu and Advanced Works* (1987) 2 TCLR 215.

79. *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102, 128 (HC) at [129].

- 15 Consequently, no bright line separates a lessening of competition that is substantial from one which is not. What is substantial is a matter of judgement and depends on the facts of each case.<sup>80</sup> However, a lessening of competition that affects a significant section of the market may be enough to amount to a substantial lessening of competition.<sup>81</sup>

### Effect or likely effect

- 16 As we can only clear agreements that are yet to be implemented, our focus is the agreement's likely effects.
- 17 A substantial lessening of competition will be 'likely' if there is a real and substantial risk, or a real chance, that it will occur. This requires a substantial lessening of competition to be more than a possibility, but does not mean it needs to be more likely than not to occur (ie, it does not need to have a greater than 50% probability of occurring).<sup>82</sup>



80. *ANZCO Foods Waitara Ltd & Ors v AFFCO New Zealand Ltd* [2006] 3 NZLR 351 at [240].

81. *Dandy Power Pty Ltd v Mercury Marine Pty Ltd* [1982] FCA 178, at 43, 887.

82. *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102, 128 (HC) at [111].

# Chapter 7. THE COMMISSION'S COLLABORATIVE ACTIVITY CLEARANCE PROCESS

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- 1 In this Chapter we describe the process we follow when considering whether to give clearance for an agreement containing a cartel provision that is part of a collaborative activity.
- 2 We also describe our approach to confidential information.

## How to apply for clearance

### Pre-clearance discussions with the Commission

- 3 We encourage potential applicants to inform us (by contacting the Trade Practices Manager)<sup>83</sup> about potential clearance applications as early as possible.
- 4 We treat the fact and content (including any documents provided) of all pre-notification discussions as confidential until an application is registered.
- 5 While pre-notification discussions are not compulsory, they are designed to reduce the time we need to investigate once we have received a clearance application. Pre-notification discussions can benefit both the applicant and the Commission by:
  - 5.1 educating our investigation team about industries that are complex or unfamiliar;
  - 5.2 setting the scene for the agreement, including its rationale, at an early stage;
  - 5.3 clarifying the information and evidence we are likely to need, and identifying useful evidence that may assist our analysis;
  - 5.4 allowing the applicant and us to have a preliminary discussion about likely competition issues (although our comments are only indicative and not binding); and
  - 5.5 providing us with an opportunity to indicate further information that should be included in the application.
- 6 These pre-notification discussions allow us to plan more effectively for a clearance process, and to allocate appropriate resources. This means we can provide the applicant with a better indication of the likely timeframe for our investigation.
- 7 To get the most out of these discussions, we encourage at least one of the applicant's senior employees to attend. We also expect an applicant to provide us with a substantially developed draft clearance application at least five working days before meeting with us, to allow us to review the application prior to meeting.<sup>84</sup>

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83. The Registrar can be contacted at [registrar@comcom.govt.nz](mailto:registrar@comcom.govt.nz).

84. A longer timeframe may be appropriate for more complex agreements that contain a cartel provision.

## Making an application for clearance

- 8 Only one of the parties to the proposed agreement needs to apply for clearance of a cartel provision.
- 9 Clearance applications must be made in the prescribed form,<sup>85</sup> and be accompanied by payment of a filing fee. Payment can be made by cheque or electronic payment into our bank account. Please use the applicant's company name as the reference when depositing funds electronically.  
Our bank account details are:  
Commerce Commission  
BNZ North End  
02-0536-0329867-00
- 10 After receiving a clearance application and payment, we check that the application is in the correct form and completed to a sufficient standard to enable us to proceed with our investigation.
- 11 If the application does not meet our requirements, we inform the applicant at the earliest opportunity and give them the opportunity to remedy this.
- 12 If the applicant does not address our concerns, or does not pay the fee, we may decline to register the application.<sup>86</sup>
- 13 Once we have been provided with a public version of the clearance application and agreed with the applicant which information is confidential, we then register the clearance application.
- 14 We publish a public version (a version that omits the confidential information) on the clearance register on our website and issue a media release.

## Treatment of confidential information

- 15 While we will consider requests for fact confidentiality on a case-by-case basis, we are highly unlikely to grant requests for fact confidentiality. Fact confidentiality limits our ability to investigate an application as it effectively prevents us from speaking to anyone other than the applicant. As a result, it is unlikely that we will be able to be satisfied that the requirements for giving clearance are met where fact confidentiality exists.
- 16 All information we receive is subject to the principle of availability under the Official Information Act 1986.
- 17 However, the Official Information Act does not require us to disclose information if (among other grounds) it would prejudice our investigation, or where the public interest in making the information available is outweighed by the fact that, in our view:
  - 17.1 disclosure would unreasonably prejudice the commercial position of the supplier or subject of the information; or
  - 17.2 we received the information under an obligation of confidence, and if we were to make that information available it would:
    - 17.2.1 prejudice the supply of similar information to us (by any person) where it is in the public interest that such information continues to be supplied to us; or
    - 17.2.2 be likely otherwise to damage the public interest.

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85. <http://www.comcom.govt.nz/business-competition/guidelines-2/competitor-collaboration-guidelines/>.

86. Commerce Act 1986, s 60(4)(c).

- 18 We acknowledge that some of the information we seek during our investigations will be commercially sensitive. We also recognise that this information is generally highly relevant to our investigation. As such, we recognise that preserving the confidentiality of commercially sensitive information and providing protection against disclosure is necessary. This ensures that parties continue to supply such information to us, and that we can deal with clearance applications as quickly and efficiently as possible.
- 19 That said, because we aim to carry out our investigations quickly, transparently, and adhering to the principles of natural justice, we take a cautious approach in accepting assertions of confidentiality. We test all claims to ensure that the information provided is truly commercially sensitive.
- 20 We also rarely accept 'blanket' claims of confidentiality over entire documents as we cannot give weight to these submissions. Parties should clearly set out the reasons why specific information within documents should be treated as confidential, with reference to the provisions of the Official Information Act.<sup>87</sup>
- 21 We also expect parties to provide us with a public version of any submission made, which can be provided to the applicant, interested parties, or in some circumstances published on our website.<sup>88</sup> Confidential information should be clearly marked (by highlighting the information and enclosing it in square brackets). Watermarks across documents should not be used.
- 22 In some cases, we may need to test confidential information provided by one party with the applicant or other interested parties. If possible, we hypothetically test the confidential information to avoid disclosure. Where this is not possible, we may release confidential information to interested parties' legal counsel or expert advisers on a counsel- or expert-only basis, if recipients have signed confidentiality undertakings.

## Public Records Act 2005

- 23 The Commission is subject to the Public Records Act 2005 which means that we must create and maintain full and accurate records, until their disposal is authorised.
- 24 This means that parties are not able to withdraw submissions provided to us once they have been submitted. If a party no longer wishes the Commission to place any weight on submissions provided, we may in some circumstances disregard it, but it cannot be withdrawn and remains on our record and subject to the Official Information Act.
- 25 If we receive a request under the Official Information Act that includes any submission or evidence that a party no longer wishes to be taken into account, we will consult with the party before making a decision on its release.

## How we investigate and determine a clearance application

### Who determines a clearance application

- 26 Each clearance application is decided by a Division of Members of the Commission appointed by the Chair for that purpose.
- 27 The Division is supported by a multi-disciplinary team of Commission staff, comprising one or more investigators, and economic and legal staff. The Commission may procure external advice on a clearance application.
- 28 Members of staff will brief the Division during the investigation. The Division provides staff with guidance and direction.

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87. Detailed guidance on the application of the Official Information Act can be found on the Ombudsman's website [www.ombudsman.parliament.nz](http://www.ombudsman.parliament.nz).

88. Commerce Act 1986, s 65A(4).

## Clearance timeframe

- 29 The Commerce Act sets out a 30 working day statutory timeframe in which we must either give or decline to give clearance. If this time elapses without an extension being agreed, we are deemed to have declined to give clearance.<sup>88 89</sup>
- 30 We will try to give the most accurate timeline we can at an early stage. However, we may have to seek further extensions during the process.

## Communication with the applicant

- 31 A member of the investigation team contacts the applicant early in the investigation to let them know who the main point of contact will be.
- 32 Throughout our investigation we keep in regular contact with the applicant about progress. How often this is depends on the circumstances of the case.

## Seeking views from interested parties

- 33 When we assess clearance applications, we take into account a party or parties' submissions, submissions of interested parties, and any other relevant evidence gathered during the course of our investigation.
- 34 We will contact those interested parties we consider are likely to have information that is relevant and useful to our investigation.
- 35 However, anyone who has information that they believe is important for our investigation, or wants to provide us with a written submission in response to the statement of preliminary issues can contact us at [registrar@comcom.govt.nz](mailto:registrar@comcom.govt.nz).

## How we gather information

- 36 We gather information from applicants and other parties in a variety of ways, depending on the circumstances. This can include through face-to-face interviews, telephone interviews, letters, or emails.
- 37 We usually seek information on a voluntary basis, although in some cases we use our information gathering powers to require parties to provide information. We discuss our powers to do so in more detail below.
- 38 It is an offence for any person to attempt to deceive or knowingly mislead us through communications with us, interviews, emails or telephone conversations.<sup>90</sup>

## The interview process

- 39 Where we wish to interview someone, we make contact to request a time for a face-to-face or telephone interview. Before the interview, we provide a public version of an application for clearance, explain our processes, and provide an agenda or a list of topics to be discussed (including any specific information we require).
- 40 We prefer to conduct these interviews on a voluntary basis. However, under our powers to require information we can require persons to appear before us to give evidence under oath.<sup>91</sup>
- 41 We prefer to record interviews and can provide a copy to the interviewee on request. Recording interviews ensures that both parties have access to an accurate record of what was discussed, and allows us to converse freely without the need to take extensive notes.

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89. We make extension requests verbally in the first instance, although we will follow that request with a written request by email or letter.

90. Commerce Act 1986, s 103.

91. Commerce Act 1986, s 98(c).

- 42 Interviews often include discussion of information that is confidential. Interviewees are encouraged to identify all commercially sensitive and confidential information during the interview.
- 43 We often request that interviewees provide evidence or information to substantiate their arguments. This is more likely to happen where such arguments are key considerations in our assessment of a clearance application.

### Information requests

- 44 We also often ask applicants or other persons to provide information relevant to our investigation.
- 45 When we make an information request, we usually specify a deadline for the information to be provided. This allows us to progress our investigation as quickly as possible. We encourage parties to contact us as soon as possible if they think they cannot meet the deadline.

### Our statutory information-gathering powers

- 46 We can require a person to supply information or documents or give evidence by issuing a statutory notice (a section 98 notice). We can issue a section 98 notice where we consider it necessary or desirable for the purposes of carrying out the Commission's functions and exercising its powers under the Commerce Act.
- 47 There are a number of reasons why we may decide to use a section 98 notice, including that:
  - 47.1 it ensures information is gathered in a timely manner;
  - 47.2 parties may prefer it because, for example, they might be under a duty such as a confidentiality obligation not to reveal that information unless compelled to do so; or
  - 47.3 parties with relevant information are unwilling to disclose the information voluntarily.
- 48 A section 98 notice explains what is required under the notice (for example, information, documents, and/or giving evidence in person), and provides a timeline for providing the information or documents.
- 49 A section 98 notice creates a legal obligation for the recipient to provide us with the information requested. It is an offence to refuse or fail to comply with a section 98 notice without reasonable excuse.<sup>92</sup>
- 50 Similarly, if the recipient wishes to seek an extension to the deadline, they should make a request stating the reasons and allowing sufficient time for us to process the request before the original deadline.



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92. Commerce Act 1986, s 103.



## Documents we prepare during the assessment of a clearance application

- 51 There are a range of documents we may prepare at different stages during our investigation which may include a statement of preliminary issues, and a letter of issues, and a letter of unresolved issues.

### Statement of preliminary issues

- 52 A statement of preliminary issues sets out our preliminary view on whether competition issues arise from the application. That view will be based on the information we have at that time.
- 53 Its aim is to:
  - 53.1 increase the transparency of our process;
  - 53.2 provide interested parties with an opportunity to consider the issues we have identified; and
  - 53.3 uncover further information which might assist our investigation.
- 54 We publish a statement of preliminary issues on our website and issue a media release inviting responses. Where the issues are very straightforward and publishing a statement of preliminary issues is likely to delay our decision, we may choose not to do so.

### Letter of issues and letter of unresolved issues

- 55 We send a letter of issues to an applicant where, following our initial investigation, we have concerns about potential competition issues arising.
- 56 A letter of issues is not a final decision. Rather, a letter of issues aims to clearly outline our concerns and invite the applicant to provide further information that might address these concerns. We often meet with applicants to discuss a letter of issues, although we prefer that applicants also provide a written submission (and supporting evidence) as part of their response.
- 57 If, following an applicant's response to the letter of issues, we consider some issues remain unresolved, we are likely to send a letter of unresolved issues to the applicant. A letter of unresolved issues provides the applicant with a further opportunity to provide additional information or submissions to allay our concerns. In most cases, we will publish the letter of issues and the letter of unresolved issues.

## Post-determination: publication of decisions and written reasons

- 58 When a Division makes a decision to give or decline to give clearance, the Chair of the Division gives effect to that decision by signing a notice of clearance/decline of clearance.
- 59 We inform the applicant of our decision by telephone and then issue a media release and update the clearance register on our website. Where the applicant is listed on the New Zealand stock exchange, we issue the media release outside of trading hours. We may also inform other interested parties of our decision.
- 60 We also publish written reasons to explain our decision and to provide guidance for the business community. In the case of collaborative activity clearances, these are likely to be less comprehensive than merger clearance decisions.
- 61 While we draft written reasons during our investigation, we can only finalise these following our decision. This may mean that we do not publish written reasons on the day we issue our decision.
- 62 We do, however, recognise that businesses want to understand the reasons for our decisions as soon as possible, particularly when we decline clearance and because of this we aim to publish reasons as soon after our decision as we are able. Where we have declined clearance, we aim to publish the reasons within 10 working days.

## Appeals against a clearance decision

- 63 The Commission's clearance decision can be appealed to the High Court by the applicant, or any other person who is a party to the agreement to which the application for clearance relates.<sup>93 94</sup>

## Revocation of clearances

- 64 We may revoke clearance if we are satisfied that:<sup>95</sup>
- 64.1 the clearance was given on information that was false or misleading in a material particular; or
  - 64.2 there has been a material change of circumstances.
- 65 If we are considering revoking clearance, we will request submissions from the person to whom clearance was given and any other person we consider is likely to have an interest in the matter.

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93. Commerce Act 1986, s 92(ba).

94. The High Court Rules provide that a party must file any appeal within 20 working days of the date on which the decision is made. As the decision date will often be different to the date on which we publish our reasons, we generally indicate to parties that we will not oppose a party filing an appeal out of time provided they file any appeal within 20 working days of the date on which we publish our written reasons.

95. Commerce Act 1986, s 65D.

## Chapter 8. SEEKING AUTHORISATION

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- 1 If an agreement containing a cartel provision does not qualify for an exception, we may nonetheless give authorisation.
- 2 We can only grant authorisation for agreements that we consider are likely to lessen competition. If we are not satisfied that an agreement will lessen competition, we must decline to authorise the agreement.
- 3 We must grant authorisation where we are satisfied that the agreement will be likely to result in a benefit to the public that would outweigh the lessening in competition. We call this the 'public benefit test'.
- 4 When we authorise an agreement containing a cartel provision, it cannot be challenged by us or by a third party as being a breach of sections 27 or 30C of the Commerce Act.<sup>96</sup>
- 5 We authorise agreements for a period for which we can be satisfied there are net public benefits. Typically, applicants seek authorisation for the length of the relevant agreement.
- 6 For more information on when we will authorise agreements and the standard process that we follow when determining authorisation applications, you can refer to our Authorisation Guidelines.<sup>97</sup>

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96. Section 30C provides that a cartel provision is unenforceable.

97. Available at <http://www.comcom.govt.nz/business-competition/guidelines-2/authorisation-guidelines/>.

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This is a guideline only and reflects the Commission's view. It is not intended to be definitive and should not be used in place of legal advice. You are responsible for staying up to date with legislative changes.

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Contact us with information about possible breaches of the laws we enforce:

**Phone:** 0800 943 600

**Write:** Enquiries Team, PO Box 2351, Wellington 6140

**Email:** [contact@comcom.govt.nz](mailto:contact@comcom.govt.nz)

**[www.comcom.govt.nz](http://www.comcom.govt.nz)**

