

Market power and IP arrangements to be subject to new scrutiny under proposed Commerce Act changes

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17 June 2020

The Government has announced that it intends to change the current prohibition on misuse of market power under the Commerce Act 1986. The proposed change will align with recent changes made in Australia, and mean that conduct by entities with substantial market power will be subject to a competition test that considers the effect of the conduct (rather than just the purpose).

Other changes proposed as part of the reforms include the repeal of exemptions relating to intellectual property arrangements, and increases to the maximum penalties for anti-competitive mergers.

What is proposed?

Section 36 of the Commerce Act currently prohibits a person (eg a business or other entity) with a substantial degree of market power from taking advantage of that power for a proscribed purpose, such as preventing a person from engaging in competitive conduct in a market.

The proposed new test will look at whether conduct by a person with substantial market power has the purpose, effect, or likely effect of substantially lessening competition in a market. This is equivalent to the test that currently applies to arrangements between businesses under the Commerce Act. The key change is that the new test will be applied to unilateral conduct (where there is no relevant arrangement).

Summary of proposed changes

Current	Proposed
<p>A person that has a substantial degree of power in a market must not take advantage of that power for the purpose of—</p> <ul style="list-style-type: none"> Restricting the entry of a person into that or any other market Preventing or deterring a person from engaging in competitive conduct in that or any other market Eliminating a person from that or any other market. 	<p>A person that has a substantial degree of power in a market must not engage in conduct that has the purpose, or has or is likely to have the effect, of substantially lessening competition in a market.</p>

The change is intended to address concerns that the 'take advantage' element of the current test means that section 36 fails to capture some anti-competitive conduct, and makes enforcing section 36 costly, complex, and unpredictable.

How will the changes affect businesses?

The proposed new misuse of market power prohibition will only be directly relevant to entities that have a substantial degree of market power (eg businesses that have the ability to act in a way that is not constrained by competitors or potential competitors, or suppliers or customers).

While the new prohibition will continue to target typical types of conduct that can raise misuse of market power issues, such as predatory pricing, refusals to supply, exclusive dealing, and product tying, in our view the analysis required under section 36 will become more complex in some cases.

A difficulty with the new prohibition is that it does not incorporate an assessment of whether the relevant conduct is for an exclusionary purpose. As set out in a [submission](#) that we made on the proposed changes, this could create difficulties in the following scenarios:

- Steps taken by public funders of services:** Public funders of services (such as health, public transport, and waste

services) often face allegations of anti-competitive conduct if they make a decision to limit or reduce the number of private providers with whom they contract. The Regulatory Impact Statement on the changes does not directly address this concern but did give the example of a government agency (in trade) procuring all supplies from one provider, resulting in the exit of another provider from the market. The Impact Statement concluded that the provider's decision to exit the market would be separate to (albeit influenced by) the government's procurement decision and so the procurement decision is unlikely to 'cause' a substantial lessening of competition, and that if the government has secured favourable terms from the supplier in question, then such conduct may be pro-competitive. That may be the case, but we expect that public funder procurement decisions will need closer analysis if the change to section 36 is made.

- **Innovation by firms with a substantial degree of market power that results in competitors being driven out of the market:** The Government's response to this is that it is unlikely that the Commerce Commission would take a case in relation to such conduct, and that innovative conduct could be pro-competitive even if it results in firms exiting the market. However, we anticipate that competition analysis of such conduct will become less straightforward for businesses to apply under the new prohibition.

Having an exclusionary purpose test included in the prohibition would assist in ensuring that benign or potentially beneficial types of conduct (such as innovation) would be less likely to be caught under the new prohibition. Such an exclusionary purpose test has not been adopted in the announced changes, but we hope it will be further considered during the Parliamentary process.

Guidance on types of conduct likely to cause issues

Case law and Commerce Commission guidance will also assist in providing greater certainty about the application of the new prohibition. However, it is likely to take some time for case law to develop. For example, in Australia, the first case under the new prohibition was taken in late 2019 (more than two years after the changes came into force), and the hearing for the case is not scheduled until April-May 2021. That case involves allegations that a port company engaged in conduct to prevent a provider of marine pilotage and towage services from entering the market (for example, by introducing new charges and refusing to provide pilot training to the new entrant).

We expect that the Commerce Commission will publish guidance similar to the guidance published by the Australian competition regulator, the ACCC. The Australian [Guidelines on misuse of market power](#) set out examples of the types of conduct are likely to raise issues under the prohibition, and conduct that is less likely to raise issues. The table below summarises some of the examples given in the Australian guidance.

Examples in Australian guidance

Likely to raise issues where business has substantial market power	Less likely to raise issues
Bundling of a patented drug with a generic drug, which hinders the ability of other manufacturers of the generic drug to supply the generic drug	Developing an innovative new product
Refusal to supply a key input to a competitor in a downstream market, which prevents new entrants from entering the market	Discounting prices as a competitive response to match prices offered by competitors
Offering a volume rebate to customers, which prevents retailers from purchasing from competing suppliers	Investing in new production technology to lower costs and improve reliability of a product

However, the guidelines provide high level guidance only, and competition law advice will still be required in each case. It will ultimately be up to a New Zealand court to determine whether certain conduct breaches the new prohibition. Commerce Commission authorisation will also be able to be sought for conduct that may breach section 36, but in many cases will not be a desirable option because authorisation is a costly, lengthy, and public process.

Other proposed changes to the Commerce Act

Repeal of intellectual property exemptions

It is proposed that current exceptions in the Commerce Act relating to IP rights will be repealed. The current exceptions include exceptions:

- For granting IP licences that authorise something that would otherwise be prohibited by an IP right, so that such arrangements do not breach the prohibitions on cartels or anti-competitive agreements
- For attempts to enforce a statutory IP right, so that an entity with substantial market power does not automatically breach the Commerce Act in such cases.

In our experience, the exceptions are not often relied upon and their scope is unclear. The proposed repeal of the exceptions aligns with recent changes made in Australia.

To assist businesses that do rely on the exceptions, the Commerce Commission will be asked to prepare guidelines on its enforcement approach to IP. For businesses that are concerned about the repeal of the IP exceptions, the examples of conduct in the ACCC's [Guidelines on the repeal of the IP exceptions](#) may provide an indication of the types of arrangement that should be considered further (but the IP exceptions and the relevant prohibitions under Australian competition law are not directly equivalent to New Zealand law so the guidelines should not be directly relied on in New Zealand).

Increased penalties for anti-competitive mergers

It is also proposed that the maximum penalties for anti-competitive mergers will be increased, to align with maximum penalties for other breaches of the Act. This will mean that the maximum penalties for businesses will be increased from \$5m to the greater of \$10m, three times the value of any commercial gain from the breach, or 10 per cent of turnover. The rationale given for the change is that the number of investigations into mergers for which clearance was not sought ('non-notified mergers') in recent years suggests that the current penalties are not acting as a sufficient deterrent. While investigating non-notified mergers has been a recent focus of the Commerce Commission, we do not think that it is necessarily the case that the increase in investigations is linked to the maximum penalties.

Other clarifications

Other changes proposed include clarifications to the application of the Commerce Act to covenants (so that they are treated in the same way as contracts) and interests in land (so that prohibitions on anti-competitive arrangements apply to interests in land in the same way as other property).

Next steps

The Government plans to introduce a bill to implement the changes, and has indicated that it expects the changes to be introduced by early 2021 (although this will likely depend on the upcoming election). There will be an opportunity for submissions to be made on the changes during the Parliamentary process. In the meantime, we recommend that:

- If your business may have substantial market power, ensure that consideration has been given to how the changes may affect you
- IP arrangements such as licensing arrangements are considered from a Commerce Act perspective, and any instances in which you have relied on an IP exception under the Commerce Act are considered in light of the proposed changes.

If you have any questions about how the upcoming changes may affect you, please contact a member of our competition law team.

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