COMPETITION ALIVE & KICKING IN NEW ZEALAND

By Andrew Matthews & Gus Stewart [1]

I. INTRODUCTION

New Zealand's competition regulator, the Commerce Commission ("Commission") has had a busy first three quarters of 2016, actively investigating and enforcing a wide range of competition and consumer laws under the Commerce Act 1986 ("Commerce Act") and the Fair Trading Act 1986 ("FTA") respectively. The Commission, on the back of its increased advocacy and media engagement, has been influential in driving an increased awareness of competition and consumer laws in New Zealand.

In this update we discuss the Commission's activity in relation to recent and impending consolidation in the media & communications sector, and its more active enforcement action in the consumer law space – with a focus on telecommunications.

II. MEDIA & COMMUNICATIONS: A CASE FOR CONSOLIDATION?

As with many other jurisdictions, New Zealand print media and traditional communications providers have struggled to maintain pace with new technologies, declining subscriber bases, and other international threats in recent years – particularly in the wake of a surge in "over

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the top" ("OTT") players. There has also been a trend towards bundling as traditional communications players seek to reduce churn and to avoid becoming old-style utility companies, i.e. the metaphorical "dumb pipe". While those market conditions may inevitably lead to periods of consolidation in any jurisdiction, the issues seem particularly acute for a relatively small and isolated economy like New Zealand's which has likely already experienced greater levels of consolidation in media and communications markets.

One recent example of this consolidation in action is that of fixed-line operator CallPlus. After acquiring Orcon (New Zealand's fourth largest internet service provider) in 2014, CallPlus was then itself acquired twice in quick succession by Australian companies – firstly by M2 Group in April 2015, followed by the Vocus/M2 Group merger in 2016. After the merger with M2, Vocus became the third largest telecommunications company in New Zealand (CallPlus lacks its own mobile presence; the fourth telecommunications company, 2degrees, is predominantly known as a mobile player).

More immediately, the Commission is currently scrutinizing two high profile mergers in the media, communications and content space. Both mergers are conditional on the Commission's approval, with one seeking authorization on public benefit grounds if it is unable to be cleared on competition grounds.

A. SKY TV and Vodafone Apply for Clearance for NZ Merger

In early June 2016, SKY Television and Vodafone Group plc announced that they were considering a merger of their respective New Zealand businesses whereby Vodafone Europe B.V. would directly or indirectly own 51 percent of the shares in SKY, and SKY would own 100 percent of Vodafone NZ ("SKY/Vodafone"). In essence, Vodafone Europe B.V. would own 51 percent of the merged entity with the balance being listed on the New Zealand Stock Exchange. The Commission received two applications for clearance in relation to the proposed merger on June 29, 2016, one for each of the respective business "acquisitions."

According to the parties, the SKY/Vodafone merger would create "a leading integrated telecommunications and media group in New Zealand [with] the ability to offer New Zealand's best entertainment content across all platforms and devices in a rapidly evolving media and telecommunications market."

Vodafone's application notes that "the parties currently enjoy a successful and complementary strategic relationship, under which Vodafone resells SKY's pay television services, and SKY promotes Vodafone's broadband products and refers customers to Vodafone." It also sought to pre-empt concerns about whether the merger would allow the parties to bundle their services in an anticompetitive way, noting that the merged entity "would not have the ability or incentive to engage in any foreclosure strategy" and "will continue to make inputs available on a wholesale basis [and] offer SKY services and Vodafone telecommunication services separately."

However, the proposed merger has certainly not been met with open arms by its competitors or other industry players. Twelve submissions, many with supporting economists' reports, have been published on the Commission's website objecting to the merger. A

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recurring theme in those submissions was that:

- a likely counterfactual was that SKY would be forced to shift from being a "reluctant wholesaler" to a proactive one, because customers want to watch TV content everywhere and at any time; whereas
- in the "factual" scenario, the merged entity would be an "even more reluctant wholesaler" and have the ability and the incentive to engage in anti-competitive bundling, especially in relation to sports content.

In their response to submissions, Vodafone's lawyers have rejected those arguments and questioned the objectors' basis for making them, stating that there is "no basis for the 'enthusiastic wholesaler' counterfactual" and that third parties "offer no credible 'bundling' theory of harm."

> "[...] the third party submissions are largely premised on a wholly unrealistic counterfactual of SKY becoming an "enthusiastic wholesaler" of content in New Zealand, offering bespoke packages of content selected entirely at the option of third parties, at cut-down prices for them to use to build their own pay TV offerings [...] When objectively analysed, the [objections] are not founded on a sound premise of reduced competition to the detriment of consumer. Rather, they reflect the commercial concerns of the submitters about the improved competitive offering that the [merged entity] will have."

A number of submitters also pointed to submissions made by Vodafone entities in other jurisdictions and the Vodafone Group 2016 Annual Report in an effort to discredit arguments about "no competition issues" that were made in Vodafone's application. For example, a number of the submitters referenced excerpts from the Vodafone Group 2016 Annual Report to demonstrate internal inconsistencies with Vodafone's approach to sports content in its clearance application:

> "In several markets, incumbents have sought to gain exclusive access to key content rights. [...] We will also encourage regulators to prevent incumbents from using content – in addition to their dominance in fixed access markets – as a lever to reduce competition."

In response, Vodafone's lawyers have suggested that such arguments ignore New Zealand's unique market structure, in particular noting that the quote from the Vodafone Group 2016 Annual Report "specifically refers to 'incumbents' with 'dominance in fixed access markets' [whereas] in New Zealand the structural separation of Chorus and other fibre companies means that no RSP has dominance in fixed access markets – which is borne out by [the] presence of some 80+ suppliers of broadband in New Zealand."

The merger has also sparked what some might call "professional banter" among practitioners and academics about the merits of behavioral undertakings in the merger context in New Zealand. Unlike its contemporaries in other jurisdictions, the Commission is unable to accept behavioral undertakings under the Commerce Act. However, it is our view that if considered necessary, Vodafone could theoretically enter arrangements (contracts or

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deeds), enforceable by third parties, that effectively provided sufficient access rights to mitigate competition concerns. These could be conditional on clearance being granted. (It is a common strategy to seek to ensure that customers of a merged entity would be happy with the merged entity's terms of supply and in many cases these are negotiated in advance of a proposed merger.) The Commission naturally has some reservations about this sort of approach and would need to be satisfied with how such a *de facto* behavioral undertaking may work in practice. While acknowledging those concerns, we consider that they would necessarily form part of the "factual" against which the counterfactual would need to be measured.

Further complicating matters, there are (at least) two controversial background features to the proposed merger:

- Firstly, SKY was investigated by the Commission in 2013 for (among other things) allegedly engaging in anti-competitive refusals to supply potential retailer competitors, or at least imposing restrictions forcing them to be mere "resellers." Controversially, despite its view that "certain provisions in SKY's contracts with telecommunications retail service providers ("RSPs") are likely to have previously breached" the provisions of the Commerce Act prohibiting anti-competitive arrangements, the Commission declined the opportunity to take enforcement action and instead issued a warning to SKY. The Commission took this action after its investigation found that those provisions were at that time "unlikely to have" anti-competitive effects and were "unlikely to cause harm in the future."
- Secondly, in 2006 SKY was cleared to acquire Prime Television which, at that time, was the third free to air broadcaster out of a total of five channels. A key factor in granting clearance appeared to be the Commission's treatment of free to air and pay TV as separate markets.

Objectors have raised these and many other issues – perhaps for strategic reasons. For example, Television New Zealand ("TVNZ"), the largest free to air broadcaster which is state-owned, has suggested that the merged entity would need to divest Prime in order to obtain clearance. Similarly, TVNZ and another objecting party have requested that the Commission hold a "conference" at which submitting parties would give oral evidence, and the Commission could "test" those arguments. Again, that request may be for strategic reasons – the Commission last held a conference in relation to a clearance application (as opposed to an authorization application) in 1995 when it granted Telecom (now Spark) clearance to acquire 25 percent of SKY. Submitters favor these conferences because it gives them appeal rights, which are not otherwise available in relation to a clearance (i.e. if no conference is held, a clearance can only be appealed by the merging parties). The Commission has since made it clear that it has no plans to hold conferences, explaining that it believes that its current processes, which include a public version of the clearance application, and can include public submissions and cross-submissions, are sufficient.

A number of the submissions also argue that some or all of the pay TV content currently held by SKY is an "essential input" in relation to relevant telecommunications

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markets. However, those arguments could face some challenges given that, in New Zealand at least, the Commission does not tend to define "overlapping" markets. Traditionally, vertical effects have been a small part of merger analysis in New Zealand competition law, and conglomerate effects have largely been ignored. The Commission's Statement of Preliminary Issues for the Vodafone/SKY merger indicated that it would be looking at vertical and conglomerate effects, perhaps recognizing that SKY's pay TV content may not be an essential input, but that the merged entity's likely conduct may still have the ability to harm consumers by depriving them of innovation in pay TV packages. But again, there are obvious challenges with such arguments given OTT options and (what appears to be) a far greater fragmentation of pay TV services (for example, Spark offers its own content free of charge to its broadband and certain monthly mobile customers).

Lastly, and perhaps ironically, while one of the key concerns in the submissions appears to be about access to an essential input (where access seekers would usually rely on "abuse of market power" or monopolization laws), some of the submitters have separately made submissions in relation to the Ministry of Business, Innovation and Employment's targeted review of the Commerce Act that the case for strengthening New Zealand's monopolization laws has not been made out (i.e. that our monopolization laws are not broken and remain "good law"). The Commission's decision on the proposed merger is expected in November 2016.

B. NZME Applies for Clearance or Authorization to Merge with Fairfax

In the media space, the Commission registered a joint application from Wilson & Horton, now NZME ("NZME") and Fairfax seeking clearance or authorization to merge their media operations in New Zealand ("NZME/Fairfax") on May 27, 2016. The merger would essentially be a "two to one" in newspaper supply (national dailies), with overlap in community publications, magazine supply and (news) websites. The merger is in "response to the dramatically transforming media landscape [where] print readership and revenue [are] in decline and revenue from online news/information provision [is] becoming highly competitive."

The applicants have sought "clearance, or in the alternative authorization" for the proposed merger. The practical impact of this approach is that clearance can still be granted if there is no substantial lessening of competition, but if there is a substantial lessening of competition, the transaction can be "authorized" by the Commission if the public benefits (essentially economic efficiencies) exceed anti-competitive detriments. Those benefits must be quantified, although the Commission can account for qualitative factors. The Commission applies a "total welfare" test.

The NZME/Fairfax merger attracted a significant volume of submissions. The Commission published 50 submissions on the Statement of Preliminary Issues on its website, including a late submission from TVNZ which was noticeably missing from the original tranche of submissions. Submitters included competitors, journalists and academics/public policy lobby groups, with the overwhelming majority being regional newspapers – many of which submitted similar (or identical) points in objection. A common complaint was that "a merger

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between the two largest media companies in the country is not in the best interests of the existing media industry and residents of this country."

In response, the applicants' lawyers have suggested that the submissions made no significant points to undermine the key premises of the application, and have invited the Commission to treat certain views from third party submitters with "considerable skepticism." In particular, the response notes that:

> "many of [the] submissions relate to issues that fall outside the scope of the competition framework of the Commerce Act 1986 [which] are not relevant to the substantial lessening of competition analysis and are, at best, only tangentially relevant to the authorisation process (as unquantified subjective "detriments"). These include: (a) "Fourth Estate" issues; (b) A subjective assessment of what is "valuable" news / information content; (c) Plurality of media ownership; (d) Foreign ownership of media; and (e) Reduction in employment of journalists by the merged entity."

The Commission's decision on the proposed merger is expected in March 2017. In the meantime, the Commission has earmarked December for a possible conference, should the matter proceed to an "authorization." The purpose of a conference, if held, is to allow the Commissioners to ask questions of the applicants and interested parties on topics where the Commission requires further information. While participation in the conference is restricted to parties who the Commission considers it can best test its preliminary views and gain further information and evidence, the conference will be generally open to the public.

III. CONSUMER PROTECTION LAWS: A RE-PRIORITISATION ON ENFORCEMENT?

For a number of years, consumer laws have been recognized worldwide as a valuable tool for enhancing competition (antitrust) laws, and ensuring markets are more competitive. New Zealand, by all accounts, is no exception. Whether the Commission has re-prioritized its attention towards consumer issues, or businesses have become complacent and begun pushing boundaries – or neither – we have seen an increased level of enforcement action by the Commission in this area.

A. Commission Brings a Number of High Profile Fair Trading Proceedings

Among other things, the Commission has brought proceedings against eight (mostly) well-known companies in New Zealand in the eight weeks from August 1, alleging various breaches of the FTA: Reckitt Benckiser, peer-to-peer lender Harmoney, insurer Youi, energy and telecommunications provider Trustpower, retailers 123 Mart and Budge, discount vacuum retailer Godfreys, and Bike Barn. A number of the defendants have pleaded (or are expected to plead) guilty to their respective charges. The charges are varied, and include allegations of:

- misleading packaging and promotion of four different types of pain-specific Nurofen products (Reckitt Benckiser)

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- sending misleading loan pre-approval letters (Harmoney);
- engaging in misleading sales techniques when selling insurance policies (Youi);
- misleading advertising in relation to a bundled electricity and unlimited data broadband offer (Trustpower);
- failing to meet mandatory product safety standards (123 Mart);
- misrepresenting how much alpaca fibre was in duvets (Budge);
- failing to comply with the written disclosure requirements for extended warranty agreements (Godfreys); and
- misleading consumers over sale prices (Bike Barn).

B. Prevalence of Repeat Offender Industries

The proceedings illustrate another year in which the Commission has actively (and pro-actively) investigated potential breaches of consumer laws, particularly where vulnerable consumers may be involved. In some cases, they also highlight industries that appear to be "repeat offenders" under New Zealand's fair trading laws. For example, in its August 24, 2016 announcement that Budge and its sole director, Sun Dong Kim, had been convicted and fined a total of NZD $71,250 in the Auckland District Court, the Commission noted that it "has previously prosecuted nine companies and eight individuals for selling imported alpaca rugs as "Made in New Zealand," and for claiming duvets were predominantly alpaca or merino wool when they were not." Mobile "truck stops" have also been a focus for the Commission, with charges being laid under both the FTA and the Credit Contracts and Consumer Finance Act of 2003 in many cases.

C. Telecommunications is the "Most Complained About" Industry

The telecommunications industry has historically been a major source of competition and consumer related issues in New Zealand, including being the subject of protracted litigation and record fines. This has continued to be the case, particularly in relation to consumer laws. The Commission's latest Consumer Issues Report (published September 27, 2016) notes that telecommunications providers "remain the most complained about industry to the Commission," comprising nine percent of all consumer FTA complaints in 2015. This was followed closely by domestic appliances (also nine percent), motor vehicle retail (six percent) and airlines (three percent). Of the 459 telecommunications-related complaints, New Zealand's two largest operators – Spark and Vodafone – accounted for more than half of those complaints, with 140 and 133 each respectively. The report notes that the complaints data "does not establish that any harm has been caused to any consumer or competitors."

The Commission's prosecutions have also resulted in significant fines in the telecommunications sector. In September, Trustpower was fined NZD $390,000 after pleading guilty to misleading consumers over the price and terms of its bundled electricity and unlimited data broadband offer. A week earlier, Vodafone was fined NZD $165,000 after pleading guilty to making false price representations in relation to invoices sent to customers

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who signed on to the "Red Essentials" mobile phone plan between January and December 2014. This was Vodafone's fourth sentencing under the FTA in the past five years, with previous fines of NZD $82,000 and NZD $400,000 in 2011 and NZD $960,000 in 2012 (in relation to various broadband and mobile phone promotions). Vodafone also paid out over NZD $260,000 to customers in a settlement reached with the Commission concerning the company's promotion of its "Broadband Lite" service in 2014.

IV. CONCLUSION

If the first nine months of 2016 are anything to go by, one might expect that the next six months will spell an increase in the number of competition & consumer prosecutions and fines for businesses, countered by a decrease in the number of media & communications companies in New Zealand as the current phase of consolidation truly takes hold. Only time will tell.

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