

**EVIDENTIARY ISSUES IN MERGER REVIEW:
NEW ZEALAND SUBMISSION**

- 1 New Zealand's primary competition legislation, the Commerce Act 1986 ('the Act'), provides for a voluntary notification regime for business acquisitions. If a proposed acquisition is likely to raise competition concerns under the Act, prospective acquirers of assets of a business or shares may either:
 - proceed with the acquisition with the risk of either the New Zealand Commerce Commission ('NZCC') or any other party initiating proceedings before the High Court in relation to that acquisition;
 - apply to the NZCC for clearance with or without offers of undertakings to dispose of assets or shares necessary to address the competition concerns; or
 - apply to the NZCC for authorisation on the basis that the public benefits of the acquisition outweigh the anticompetitive detriments.
- 2 This paper briefly discusses the impact of the forum in which the merger review process takes place on the collection and evaluation of evidence.

Enforcement proceedings before Court

- 3 If the acquirer elects not to apply to the NZCC and proceeds with the acquisition, the NZCC has a maximum of two to three years (depending on the remedy sought) from the time of the acquisition to initiate substantive proceedings before the High Court.¹ In practice, the NZCC will initiate proceedings as quickly as possible in order to minimise the potential for the merged entity to either co-mingle the acquired assets, or diminish the value of those assets, in such a way as to undermine the effectiveness of any competition remedies that may be imposed.
- 4 In an enforcement proceeding the NZCC has the burden of proving to the court that the transaction has the effect or likely effect of substantially lessening competition. The evidence necessary to meet this test is based on demonstrating likely competitive harm, and requires both a qualitative and quantitative analysis in relation to the affected markets. Qualitative analysis involves examining the structure of the markets and the behaviour of participants to establish to what extent participants were constrained in their behaviour by actual or potential competitors. Quantitative analysis might involve economic modelling techniques to estimate the likely effect of the proposed acquisition on prices and allocative efficiency.
- 5 This evidence may be gathered through a variety of means: research of publicly available information, voluntary interviews, receipt of submissions, and through the exercise of the Commission's compulsory information gathering powers; and from a range of sources, including competitors, suppliers and customers. The NZCC's

¹ Section 85(2) of the Act provides a statutory limitation period of two years for applications for divestment orders. A longer statutory limitation period of three years applies for applications for pecuniary penalties.

performance measures for its business acquisition investigations are 60 working days for routine cases and 120 working days for complex cases.

- 6 In order to introduce the evidence in court, the NZCC may select key witnesses to provide an overview of the affected markets and the impact of the transaction (and also to support the introduction of necessary quantitative data), plus at least one economic expert to introduce economic evidence and analysis. This evidence is subject to cross-examination by the counsel for the respondents.
- 7 Consequently, in order to prove a contravention of the Act, the NZCC must firstly detect the anticompetitive acquisition and obtain the necessary admissible evidence, and subsequently meet the onus of proving to the court that the acquisition would likely result in a substantial lessening competition. In an enforcement proceeding before the court, the evidence presented is targeted to identify the key competition concerns and is subject to a robust process to test the likely impact of the acquisition.

Proceedings before NZCC

- 8 The test in the context of a clearance is that the NZCC should only grant clearance if satisfied that the acquisition would not or would not be likely to the effect of substantially lessening competition.² In the context of an authorisation of a business acquisition the NZCC shall only grant an authorisation if satisfied that the acquisition will or will be likely to result in such a benefit to the public that it should be permitted.³
- 9 In contrast to an enforcement proceeding, the Act places a practical onus on the applicant to satisfy the NZCC of these matters.⁴ The acquirer has strong incentives to voluntarily provide the NZCC with evidence to assist the NZCC in making a timely determination. The NZCC has prescribed an application form that requires the applicant to identify what is to be acquired by whom and to outline the applicant's assessment of markets affected, existing and potential constraints on market power, and, in the case of an authorisation, the nature and extent of public benefits. This application is made available on a public register (subject to confidentiality for commercially sensitive information) and the NZCC may then test this information with interested parties.
- 10 The courts have also recognised that the Commission has a responsibility to ensure other interests (and in particular the public interest, which will often not be represented by any of the interested parties who submit on an application) are adequately taken into account:

We do not think it is appropriate to deal with this question on the ordinary application of an onus of proof. No doubt there is, to some extent, a preliminary or threshold onus on the applicant who makes his application but the matter cannot end there. The commission is an investigative body which has the function of inquiring into and deciding the matter before it. It is not a strictly adversarial procedure — there may be no opposing parties — but it is necessary at all times to consider the general public and community interests.⁵

² Section 66(3) of the Act.

³ Section 67(3) of the Act.

⁴ The standard of proof in both an enforcement and adjudication proceeding is the civil standard of the balance of probabilities.

⁵ *Foodstuffs (Wellington) Co-operative Ltd v Commerce Commission* (1992) 4 TCLR 713

- 11 This responsibility on the NZCC recognises that the effect of granting clearance or authorisation is to grant immunity to the acquisition from the application of the prohibition relating to anticompetitive acquisitions. However, this responsibility to consider other interests does not remove the primary onus on the applicant to satisfy the NZCC.
- 12 The Act provides that the NZCC has 10 working days to determine an application for clearance or 60 working days to determine an application for authorisation. These statutory timeframes may be extended with the agreement of the parties.⁶ Given these timeframes, the NZCC requires full and frank disclosure by the applicant to the NZCC, plus voluntary interviews with the parties, competitors, suppliers and customers, backed up with specific information requests, to inform its decision-making. If sufficient data is available, quantitative analysis may be carried out by in-house economists.
- 13 The voluntary nature of much of the information gathering encourages interested parties to freely give their opinions in order to develop a broad assessment of the market and the competition effects of the acquisition. This process quickly enables the NZCC to determine routine cases and, in the case of complex applications (which under a voluntary notification regime constitute the majority of applications), it emphasises the importance of continually going back to parties to test any inconsistencies in the material provided. As noted by the court:
- the views expressed are not always considered views or reinforced by empirical data. Often the parties consulted by the Commission will have a particular interest in the transaction, and will therefore be accused of self-interest. ...The Commission will sometimes have before it conflicting evidence from different market participants and must determine what weight to give the evidence of each party.⁷
- 14 The Act provides for the NZCC to hold a conference in relation to applications, which provides a further opportunity to test information provided to the NZCC. In order to test commercially sensitive information, the NZCC has the power under the Act to impose confidentiality orders over the information and accept undertakings from counsel and independent experts who may analyse the information subject to conditions.⁸ However, in practice, the NZCC predominately uses these procedures for authorisation applications.
- 15 If the NZCC declines clearance, the parties may still proceed with the proposed acquisition at their own risk. In such cases, the NZCC may elect to initiate enforcement proceedings in the courts in order to address its competition concerns.

Appeals against determinations of NZCC

- 16 For completeness, we also note that if the NZCC declines clearance or authorisation, the parties to the acquisition may appeal against that determination to the High Court to have the determination modified, reversed or referred back to the NZCC for reconsideration.⁹

⁶ On average, the NZCC determines an application for clearance within 37 working days.

⁷ *Brambles New Zealand Limited v Commerce Commission* (2003) 10 TCLR 868

⁸ Section 100(1) of the Act.

⁹ A right of appeal also exists for any person who participated in a NZCC conference in relation to that clearance or authorisation.

- 17 An appeal against an NZCC determination is heard by way of rehearing the evidence which was before the NZCC rather than de novo. Consequently, the appeal is largely heard on the record of evidence before the NZCC. The court has discretion to admit additional evidence, but in general this discretion is only exercised in relation to evidence that updates or improves the existing record. If significant new evidence comes to light, the court has the power to refer the matter back to the NZCC for reconsideration.
- 18 In terms of the onus of proof, the courts show a degree of deference to the NZCC's expertise:

In the usual way, the onus of proof is on the appellants. They must show that the decision appealed from was wrong. [There must be] clear and compelling grounds for the Court to depart from the findings of the Commission.¹⁰

Recent cases

- 19 Two recent cases have highlighted the tensions between the clearance and enforcement processes. In these two cases, the applicants withdrew their applications part way through the NZCC's proceedings, when it became apparent that the NZCC may have competition concerns, and proceeded with the acquisitions at their own risk. This strategy of withdrawing an application part way through an NZCC proceeding is a recent occurrence. Previously, when faced with competition concerns, the parties would either appeal the NZCC's decision to the High Court or reapply for clearance after modifying the transaction.

Telecom / Counties Power

- 20 In the first case, Telecom New Zealand Limited (Telecom) applied for clearance to acquire management rights to 7MHz of radio spectrum in the 3.5GHz band from Counties Power Limited. The application was lodged on 6 October 2005. In the course of the NZCC's consideration of the application, competitors of Telecom made claims as to future business plans that would take place in the absence of the acquisition (the counterfactual) that raised potential competition concerns with the proposed acquisition. The NZCC exercised its powers to obtain copies of board minutes and business plans relating to these claims, however, due to the passage of time, Telecom withdrew its application on 23 November 2005 and proceeded to acquire the rights without NZCC clearance.
- 21 The NZCC immediately opened an investigation. The NZCC received new evidence from Telecom and competitors relating to future business plans and found that the claims were unable to be justified to an extent to satisfy the NZCC that they should be given weight in the NZCC's analysis. Rather the NZCC was satisfied that evidence of potential competition from new entry and increased competition from regional providers using Crown spectrum meant that the acquisition was unlikely to substantially lessen competition. This investigation was subsequently closed on 22 May 2006 with a decision that no further action should be taken.

¹⁰ *Air New Zealand v Commerce Commission* (2004) 11 TCLR 347.

New Zealand Bus / Mana Coach Services

- 22 In the second case, New Zealand Bus Limited applied for clearance to acquire the shares of Mana Coach Services Limited. The application was lodged on 16 January 2006. On 15 March 2006, following receipt of advice from the NZCC that it was likely to have competition concerns with the proposed acquisition, New Zealand Bus withdrew the application.
- 23 On 28 March 2006, the NZCC applied to the court for an interim injunction and obtained an undertaking from the parties not to complete the acquisition pending resolution of the proceedings. In order to prepare for the substantive proceedings, the NZCC approached a selection of the industry participants that it had interviewed and asked them to give evidence. Those participants were briefed, provided written briefs of evidence (as required by the High Court Rules) and were subjected to cross-examination on those briefs in court. Most of these witnesses gave evidence under subpoena.
- 24 As a result, unlike an appeal situation where the NZCC's transcripts and file notes of interviews form the record on the basis of which the court proceeds, the material collected by the NZCC for the New Zealand Bus case only provided a starting point which assisted the NZCC and its counsel to identify potential witnesses and brief them. The outcome of proceedings was that the court found a contravention of the Act by two of the parties to the transaction, with pecuniary penalties to be determined. The decision has been appealed.
- 25 During the course of the court proceedings, the acquirer's strategy for withdrawing the application was revealed:

If the clearance application was declined, NZ Bus could seek an authorisation, appeal, or acquire without a clearance. The latter course would likely provoke Court action, and if that was the likely outcome it would be better to withdraw immediately.

[Mr X] recorded that NZ Bus' view was that the least risk, highest benefit strategy was to withdraw the clearance application and complete the acquisition. [Mr X] then examined the risk of litigation, noting that the Commission is overworked and short of resources, that NZ Bus would expect to win, and that there would be opportunities to "do a deal" with the Commission to divest Mana before the next major tender round occurs, while in the meantime NZ Bus would avoid losing the \$3 m deposit and gain more time to find an appropriate home for Mana.¹¹

- 26 The applicant also appears to have been influenced by the fact that in an enforcement proceeding the onus would be on the NZCC to prove a likely substantial lessening of competition, which was more attractive than the applicant having to show the NZCC was wrong on appeal from a clearance decision.

Observations relating to the NZCC's processes

- 27 A comparison of New Zealand's merger review processes and experience based on recent cases has highlighted tensions in the NZCC's adjudication processes.
- 28 The voluntary nature of the regime requires the NZCC to run a timely and cost effective process that encourages both prospective acquirers to apply to the NZCC and interested

¹¹ *Commerce Commission v New Zealand Bus Limited* (2006) 11 TCLR 679.

parties to give full and frank opinions on the transaction. This is necessary for the integrity of the regime, as the NZCC must act strategically to direct its limited resources to detect and investigate all acquisitions plus meet the high cost and burden of taking enforcement proceedings in every case in which it has concerns.

- 29 However, in contrast, the voluntary nature of the regime also means that proposed acquirers will generally only apply to the NZCC if there is some uncertainty as to whether the proposed acquisition would likely substantially lessen competition. Consequently, the issues to be analysed in the majority of applications received are complex.
- 30 The NZCC is assisted in its consideration by the Act placing the onus of proof on the applicant to satisfy the NZCC. However, the NZCC always needs to thoroughly test the evidence and opinions to address any inconsistencies (given the absence of an adversarial process). In addition, the NZCC has a responsibility to take into account the impacts of the proposed acquisition on interested parties and the public interest.
- 31 This tension between timeliness and robust analysis with due process is to be considered in two upcoming reviews.
- 32 The Minister of Commerce has recently announced her intention to review the authorisation and clearance procedures under the Act. The terms of reference for the review are available on the Ministry of Economic Development's website: www.med.govt.nz. In brief, the review will look to ensure that the authorisation and clearance provisions within the Act provide the appropriate degree of:
- accountability and transparency in decision making;
 - participation by interested parties;
 - analytical rigour and due process;
 - timeliness of decision making; and
 - business and administration costs.
- 33 The NZCC has also announced a best practices review of its business acquisition procedures to coincide with the legislative review.