THE MEANING OF "COMPETITION" AND THE COMMERCE ACT 1986

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I INTRODUCTION

> The word "competition" is to economists what the word "justice" is to lawyers; everybody favours it, but it means different things to different people.[1]

There is probably no concept in all of economics that is at once more fundamental or pervasive, yet less satisfactorily developed than the concept of "competition".[2] Its complexity and ambiguity manifest themselves in the different formulations of the concept often along ideological lines. It is a trite, but nevertheless accurate, observation that competition is a rich, multifaceted notion.

Whilst fundamental to economics, competition also occupies an integral place, naturally enough, in competition policy.[3] The Commerce Act 1986 is the legislative expression of competition policy in New Zealand. The concept of competition is obviously fundamental to it. Thus, the Long Title of the Act provides that it is:

> An Act to promote competition in markets within New Zealand and to repeal the Commerce Act 1975.

This article explores the multidimensional nature of competition, examining various conceptions of the term from the viewpoint of economic theory. Attention is then focused on the meaning of competition under the Act and how the concept has been interpreted by the Commerce Commission.

II THE MULTIDIMENSIONAL NATURE OF COMPETITION

Broadly speaking, conceptions of competition amongst economists tend to emphasise an aspect (or aspects) of the Structure-Conduct-Performance Model.

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1 Taperell, Vermeesch and Harland, *Trade Practices and Consumer Protection* (3rd ed 1983) 155. See also Johnson and Ferrill, "Defining Competition: Economic Analysis and Antitrust Decisionmaking" (1984) 36 Baylor L Rev 583 at 588: "Like 'justice' or 'democracy', competition is both viewed and valued by different people in different ways."

2 McNulty, "Economic Theory and the Meaning of Competition" (1968) 82 Quarterly Journal of Economics 639.

3 "Competition policy seeks to influence industrial structure indirectly by maintaining or creating a framework within which the pursuit by independent firms of their private interests in accordance with market forces results in a desirable economic performance." Devine et al, *An Introduction to Industrial Economics* (3rd ed Allen & Unwen 1979) 330.

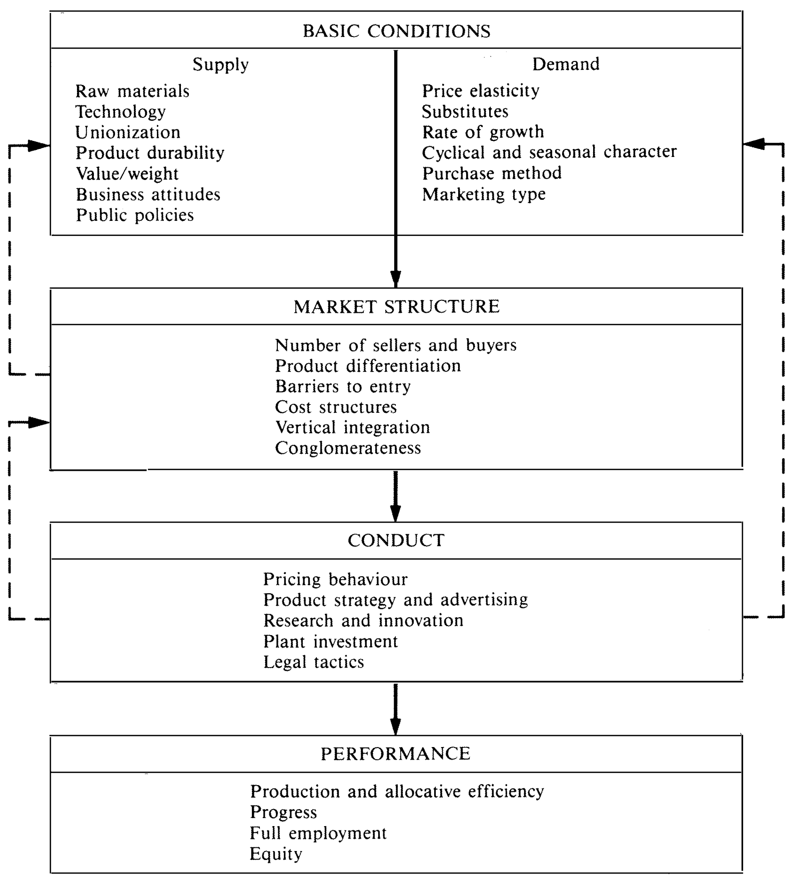
1 The Structure-Conduct-Performance Paradigm

Since the 1930s economists have with increasing frequency used a simple paradigm to analyse the functioning of markets.[4] This basic descriptive model has occupied a central position in the study of industrial economics:[5]

> This basic paradigm of industrial organisation holds that there is a causal link between structure and conduct and between conduct and performance in an industry. Under this theory, market structure, together with the basic conditions of supply and demand, limits the range of possible conduct which will ultimately affect industry performance.

The Structure-Conduct-Performance ("SCP") model, as formulated by Scherer,[6] is set out in Figure 1:

FIGURE 1



4 See Carstensen, "Antitrust Law and the Paradigm of Industrial Organisation" (1983) 16 U C Davis L Rev 487; Weiss, "The Structure-Conduct-Performance Paradigm and Antitrust" (1979) 127 U Pa L Rev 1104.

5 Note, "An Economic Analysis of the 1982 Justice Department Guidelines for Horizontal Mergers" (1983) 67 Minn L Rev 749 at 753.

6 *Industrial Market Structure and Economic Performance* (2nd ed Rand McNally 1980) 4.

Basic Conditions are those factors given at any moment which establish the supply, demand and legal elements of the market for an industry. Basic conditions define the parameters of market structure. *Market Structure* refers to the external conditions that affect the way a firm determines price and output. These conditions include the number and size of firms in an industry, barriers to entry, cost functions and product differentiation. *Conduct* (also called *Behaviour*) describes how firms behave in a market or the types of output and pricing decisions such firms make. Some economists break conduct down into two categories: pricing and promotional policies.[7] The pricing practice of firms is usually of central importance, however, especially in determining whether firms are colluding to restrict output and raise prices (collusive market power). *Performance* refers to the results of market interaction in a given industry and whether that outcome is socially desirable given certain macroeconomic objectives.

> The most frequently articulated (but not the only) prediction of the paradigm is that high seller concentration leads in various ways to a greater elevation of prices above unit costs and hence to higher profit returns.[8]

The SCP paradigm is not without criticism.[9] The most forceful objection is the one-way determinism between structure, conduct and performance which the model postulates. In criticising the uni-directional nature of the flow, some economists go to the opposite extreme and assert that a reverse causation operates:[10]

> The standard paradigm should have its causation flow reversed. Exceptional performance and competitive conduct lead to a concentrated structure. *Structure is a result not a cause.* (original emphasis)

The real world is undoubtedly more complicated than the model would suggest. The relationships between structure, conduct and performance are more probabilistic than deterministic. Furthermore, feedback effects, for example from conduct to structure, should be taken into account.[11] Recent formulations of the paradigm such as Scherer's sophisticated presentation (Figure 1) explicitly embrace such feedback effects. So far as the determinism criticism is concerned, Scherer comments:[12]

> I know of no economist who holds that this SCP relationship is applicable for every industry at every moment in time. Rather, it is believed to be a statistical tendency – prevailing on the average over a large sample of cases like (but perhaps stronger than) the tendency for lung cancer to be contracted more frequently by heavy smokers.

7 See eg Howe, *Industrial Economics: An Applied Approach* (Macmillan 1978) 65.
8 Scherer, "Structure-Performance Relationships and Antitrust Policy" (1977) 46 Antitrust LJ 864 at 864.
9 See generally Carstensen, supra n 4 at 501-504.
10 Brozen, *Concentration, Mergers and Public Policy* (Macmillan 1982) 118. See also Armentano, *Antitrust and Monopoly: Anatomy of a Policy Failure* (John Wiley & Sons 1981) 40.
11 See Phillips, "Structure, Conduct and Performance – Performance, Conduct and Structure"; in Markham and Papanek (eds), *Industrial Organisation and Economic Development* (Houghton-Mifflin 1970) ch 2.
12 Supra n 8 at 864.

Different conceptions of competition in turn approach the meaning of competition from a structural, conduct or performance perspective.

2 Competition: The Structural Conception

The structural approach defines competition indirectly by describing those market conditions that are expected to influence the competitive process. Competition is seen as a market setting in which there is a large number of small firms and entry is relatively easy. Competition is a fragmented (ie unconcentrated) market structure consisting of many small competitors.

This notion of competition is closely akin to the economist's model of perfect competition. The "perfection" of the concept of competition, that is, the emergence of the idea of competition as itself a market structure, was a distinguishing contribution of neoclassical economists.[13] Perfect competition is readily defined in any leading economics textbook.[14] Armstrong explains:[15]

> To qualify as perfect competition, the market has to offer a product every unit of which is exactly like every other (the condition of homogeneity) and it has to be made up of a large number of small buyers and sellers acting independently, with perfect knowledge, and with freedom to enter or leave the market. If all these conditions are met, price would be set by the interaction of total market supply and demand, and all individuals would be virtually powerless "offer takers". Buyers and sellers alike would have to accept the product and price as given.

Perfect competition is the only basic type of market situation in which individual firms possess no degree of power over price. Contrast pure monopolists, oligopolists and monopolistic competitors who all possess varying degrees of power over price.[16] The idealness of perfectly competitive markets in contrast to other market forms is that they promote economic efficiency and thus economic welfare.[17] Neoclassical welfare economics predicts that under perfectly competitive conditions societal (economic or consumer) welfare will be maximised in terms of the Pareto Criterion.[18] Pareto optimality is achieved when, given the distribution of income, it would be impossible to make some consumers better off without making others worse off. The perfectly competitive equilibrium ensures that allocative efficiency is maximised and that no resource misallocation is occurring.[19]

The structural conception of competition, with its theoretical underpinning of perfect competition, is thus a static equilibrium notion — an idealised situation. Competition is therefore reduced or injured when this optimal market setting is departed from. Reference to the perfect com-

13 McNulty, supra n 2 at 644.

14 See eg Scherer, supra n 6 at 10-11; Stonier and Hague, *A Textbook of Economic Theory* (5th ed Longman 1980) ch 6.

15 *Competition versus Monopoly: Combines Policy in Perspective* (Fraser Institute 1982) 9-10.

16 Scherer, supra n 6 at 11.

17 Clarkson and Miller, *Industrial Organisation* (McGraw-Hill 1982) 111.

18 Sawyer, *The Economics of Industries and Firms* (Croom Helm 1981) 224.

19 Idem.

petition model enables those propounding a structuralist conception to talk of "more competition" as an industrial situation that more closely mirrors atomistic competition. From this neoclassical perspective:[20]

> Competition declines and some economic waste occurs as we move away from perfect competition and competition increases and markets become more efficient as we move toward perfect competition.

That perfect competition is a utopian state, incapable of actual realisation in the real world, is a unanimous, if somewhat trite, observation. The limitations of the model are well catalogued.[21] The model ignores the possibility of divergence between social and private costs – the problem of externalities. Pareto optimality runs up against income distribution. As there is no general agreement on the ranking of different income distributions, one cannot compare one individual's gain with another's loss and it is impossible to measure the changes in welfare for the community as a whole. Fundamental assumptions in the model such as perfect information or product homogeneity are not fulfilled in commercial reality. Significant scale economies may be unobtainable unless one departs from the model to some imperfect market setting.

Perhaps the most forceful objection lies in the theory of "second best". Perfect competition is an unrealistic objective. Given this, the intuitively plausible suggestion follows: if we cannot attain the ideal state of competition (the "first best") the next best thing would be to approximate it as close as possible.[22] Lipsey and Lancaster in their seminal article[23] postulate that if it is not possible to achieve Paretian conditions of perfect competition for some part of the economy, welfare may actually be decreased by achieving them elsewhere in the system. If some monopoly element is inevitable, an attempt to foster as much "competition" as possible may actually be detrimental to economic welfare.[24]

The inadequacies of the perfect competition model have led many commentators to reject the static equilibrium framework as an objective for public policy.[25] As Johnson suggests:[26]

> . . . [T]he [perfectly] competitive model of economic theory not only offers little guidance [to the analysis of antitrust], but actually points us in the wrong direction. The confusion arises because many courts and many economists fail to realize that the "competitive model" is silent on the subject of competition.

20 Armentano, supra n 10 at 18-19.

21 See eg Swann et al, "The Theory of Competition Policy" in *Competition in British Industry: Restrictive Trade Practices in Theory and Practice* (Allen & Unwin 1974) ch 3; Tarr, "Consumer Protection and the Market Place" (1983) 5 Otago LR 397 at 399-404.

22 See Johnson and Ferrill, supra n 1 at 602-603.

23 "The General Theory of Second Best" (1956) 24 Review of Economic Studies 11.

24 See Asch, *Economic Theory and the Antitrust Dilemma* (John Wiley & Sons 1970) 114-117.

25 See eg Clarkson and Miller, supra n 17 at 114; DiLorenzo, "The Origins of Antitrust: An Interest Group Perspective" (1985) 5 International Review of Law and Economics, 73 at 86: "It is hard to argue that by focusing on 'perfect' competition as a normative ideal rather than on the actual process of competition modern economists have not done more harm than good in their approach to the study of antitrust."

26 "Can Economic Analysis Give Better Guidance to Antitrust Policy?" (1983) 21 Economic Inquiry 1 at 3.

Perfect competition means simply the existence of an indefinitely large number of non-competing firms. It is a market situation which, although the result of free entry of a number of competing firms, has evolved or progressed to the point of equilibrium where no further competition within the industry is possible. In short, perfect competition implies absence of rivalry. This in essence is the fundamental objection to the structuralist approach to defining competition. It ignores the more non-technical, business understanding of competition as a process or as rival conduct.

3 *Competition: The Conduct Conception*

> Our inability as economists to adequately define and measure competition other than as a state of affairs, a static structural notion, seems to me to be a major problem in devising and implementing antitrust policy.[27]

The uneasiness with competition as a static idealised equilibrium has led many writers to characterise competition in dynamic disequilibrium terms, ie as a "force" or "process". This conduct-oriented conception differs markedly from the neoclassical formulation of competition as atomistic optimality. Instead it reflects the businessman's perception of competition as conscious rivalry.[28] Neoclassical metamorphosis of the term into a complex and rigorously defined state of affairs was a departure from the earlier classical behavioural conception. For Adam Smith, competition was the independent striving for patronage by the various sellers in the market. Competition was a market process whereby the seller tried to undersell, or the buyer outbid, his rivals in the marketplace.[29] The furthering of this theme of competition as a dynamic process is attributable to two prominent twentieth century economists — Joseph Schumpeter and F A Hayek.

(a) Schumpeterian Dynamics

Schumpeter's concern was with innovation in products and techniques rather than the neoclassical preoccupation with resource allocation.[30] Competition was always a process of "creative destruction" that came from invention and innovation.[31] The innovative dynamic process was incompatible with perfect competition and the ideal business enterprises envisioned under competitive conditions. Instead, large, dynamic, typically semi-monopolistic firms were the causative impetus required to maintain this dynamic process. The small price-taking firm of perfect competition would not in the Schumpeterian view have sufficient resources to maintain the "creative destruction".

27 Hatch, "Commentary" upon Norman, *Mergers, Trade Practices and Internal Competition* ANU Discussion Paper No 6 (1980) 45.
28 Scherer, supra n 6 at 10.
29 McNulty, supra n 2 at 647, 656. Walter Block in his preface to Armstrong, supra n 15 at xvii, explains: "It is now well documented that when classical economists spoke of competition, they mean rivalrous activities consistent with the verb 'to compete'. Coincident with the development of the price theory of the neoclassical structuralist economists, however, competition lost virtually all of its behavioural meaning."
30 See Swann, *Competition and Consumer Protection* (Penguin 1979) 100.
31 Schumpeter, *Capitalism, Socialism and Democracy* (Harper 1942) 82.

(b) Hayek and the Austrian Critique

F A Hayek, the elder stateman of the Austrian school of economics, has long been critical of the dominant role of perfect competition in both pure analysis and policy.[32] Hayek argued that the neoclassical conception of competition assumed away or ignored the competition process or simply took it for granted:[33]

> The modern theory of competitive equilibrium assumes the situation to exist which a true explanation ought to account for as the effect of the competitive process.

Competition is thus the discovery process itself, not the final static equilibrium condition. The exclusion of rivalry, which is the essence of this process, from the equilibrium of perfect competition was "profoundly disturbing".[34] Echoing the classical conception of competition as striving for patronage, the Austrians favour a dynamic behavioural definition:[35]

> Competition is not simply a mechanical optimization within known constraints but is seen as an exploratory process whereby opportunities for profit are discovered and exploited over time under uncertain circumstances.

It should not be thought that Austrians are unconcerned with maximising consumer welfare or attaining economic efficiency. It is merely that the attainment of such a state is not "competition" but rather the *result* of competition, that is, the end product of the process of inter-firm rivalry.[36]

4 Competition: The Performance Conception

An alternative approach to competition stresses the performance objectives which the competitive process is believed to attain. Economists from the Chicago school of antitrust view maximisation of consumer welfare as the sole goal of antitrust policy.[37] Leading Chicagoan, Robert Bork, contends that "competition" is merely a shorthand expression or term of art designating "any state of affairs" in which consumer welfare cannot be increased by moving to an alternative state of affairs through judicial decree.[38] Bork contends:[39]

> Surely, on the face of it, this meaning is consistent with everyday speech. When we talk of the desirability of competition we ordinarily have in mind such things as low prices, innovation, choice among different products — all things we think of as good for consumers . . . . Moreover, because "competition" as a shorthand expression for consumer welfare enables us to employ basic economic theory, it avoids the pitfalls inherent in . . . other definitions.

32 See Utton, *The Political Economy of Big Business* (Martin Robertson 1982) 171.
33 Hayek, *Individualism and Economic Order* (Routledge & Kegan Paul 1949) 94.
34 Reekie, *Industry Prices and Markets* (Philip Allan 1979) 11.
35 Armentano, supra n 10 at 14.
36 Idem.
37 See Posner, *Antitrust Law: An Economic Perspective* (1976) 4; Kauper, "The Goals of United States Antitrust Policy — The Current Debate" (1980) 136 Zeitschrift für die gesamte Staatswissenschaft 408 at 423-424.
38 *The Antitrust Paradox: A Policy at War with Itself* (Basic Books 1978) 61.
39 Idem.

This performance-oriented conception of competition as consumer welfare maximisation is closely related to the structuralist, perfect competition-based notion. The essential difference, however, is that emphasis is not placed upon a fragmented market structure of many small competitors. Rather, the phrase "any state of affairs" envisages that various forms of imperfect competition, even up to monopolistic levels, are consistent with "competition" provided consumer welfare is being maximised.

5 Effective Competition

Dissatisfaction with the manifest inadequacies of static neoclassical theory, together with a desire to produce some sensible criteria for policy and to incorporate into them dynamic considerations, all combined to produce the theory of "workable" or "effective" competition.[40] John M Clark, the originator of the concept, recognised the unreality of perfect competition and placed emphasis instead on "rivalry in selling goods".[41] Competition to Clark was essentially dynamic. Nevertheless, he also acknowledged that competition depended on numerous conditions.[42] Thus, effective competition in its inception and in its later development became a hybrid conception encapsulating both static structural and dynamic behavioural criteria.

Formulations of effective competition ensued attempting to set out minimum criteria for judging the "workability" of competition. Perhaps the most comprehensive formulation was Sosnick's scheme of criteria translated into the standard SCP trichotomy.[43] These criteria of workability included such things as no artificial inhibitions on mobility and entry (a structural norm), absence of collusion (conduct norm) and efficiency in firm operations (performance norm). An interesting alternative pragmatic formulation, eschewing predetermined norms, is that of J W Markham:[44]

> An industry may be judged to be workably competitive when, after the structural characteristics of its market and the dynamic forces that shaped them have been thoroughly examined, there is no clearly indicated change that can be effected through public policy measures that would result in greater social gains than social losses.

Critics question whether the approach of workable competition is operationally meaningful, given the question-begging nature of the criteria.[45] What is an *artificial* inhibition on entry, how does one adjudge performance to be *efficient,* what is a *clearly indicated change*? Value judgements and measurement difficulties seem inevitable. Despite these intrinsic deficiencies, the concept arguably represents a "great advance on anything

40 Swann et al, supra n 21 at 103.

41 "Toward A Concept of Workable Competition" (1940) 30 American Economic Review 241.

42 See Asch, supra n 24 at 18.

43 "A Critique of Concepts of Workable Competition" (1958) 72 Quarterly Journal of Economics 380.

44 "An Alternative Approach to the Concept of Workable Competition" (1950) 40 American Economic Review 349.

45 See Clarkson and Miller, supra n 17 at 113; Scherer, supra n 6 at 42. Swann et al, supra n 21 at 109, suggest that "workable competition offers not so much empty economic boxes as a series of unrelated measuring rods of indeterminate length and with no units marked on them".

previously formulated"[46] in its recognition that competition is a fluid, multi-faceted notion.

III Interpreting Competition Under the Commerce Act

1 The Statutory Definition

Whilst the Long Title of the Commerce Act 1975 referred merely to "competition", the conception of competition envisaged under the Act was clarified by the objects clause, section 2A, which referred, inter alia, to the need to secure *effective competition* in industry and commerce in New Zealand.

Unambiguous confirmation of effective competition as the preferred statutory meaning of competition is found more recently in the new Commerce Act 1986 (the "Act"). Section 3 provides that

> (1) In this Act –
> "Competition", means workable or effective competition:
> "Market", means a market for goods or services within New Zealand that may be distinguished as a matter of fact and commercial common sense.
> (2) In this Act, unless the context otherwise requires, references to the lessening of competition include references to the hindering or preventing of competition.
> (3) For the purposes of this Act, the effect on competition in a market shall be determined by reference to all factors that affect competition in that market including competition from goods or services supplied or likely to be supplied by persons not resident or not carrying on business in New Zealand.

Competition is explicitly equated with effective competition. The defining of "market" within the same subsection highlights the closeness of these two concepts.[47] The Act consistently speaks of "competition within a market". Whilst each notion is conceptually distinct, both nevertheless ride intimately together in tandem throughout the Act.

Interestingly, the original draft Bill explicitly recognised the distinction between price and non-price competition. Unlike section 3(2) which merely includes "hindering or preventing of competition" within the ambit of "lessening of competition", the earlier draft went further including:

> The lessening, preventing, or hindering of price competition or any other single element of competition.

If the distinction is now to be purely implicit, its importance remains. As E T Sullivan recently urged:[48]

> In many markets, price competition may not be as important as other forms of competition . . . . If competition is directed away from price, competitors will engage in other competitive tactics. Rivalry may focus on quality, service or other promotional factors.

46 Swann et al, supra n 21 at 109.

47 See Norman and Williams, "The Analysis of Market and Competition under the Trade Practices Act: Towards the Resolution of Some Hitherto Unresolved Issues" (1983) 11 ABLR 396.

48 "On Nonprice Competition: An Economic and Marketing Analysis" (1984) 45 U Pitt L Rev 771 at 798, 799.

Specific reference in section 3(3) is made to the threat of import competition as a factor in determining competitive effect. This is particularly apposite given the Closer Economic Relations agreement together with a less protectionist trade policy by the current Labour administration. It recognises that the geographic market may extend beyond New Zealand to include, for example, Australia. This is so notwithstanding section 3(1) defining "market" to mean "a market for goods or services within New Zealand".

2 Visionhire Holdings/Sanyo Rentals

In what has now become a landmark decision in New Zealand antitrust jurisprudence, the Commerce Commission (the "Commission") in *Visionhire Holdings/Sanyo Rentals*[49] examined the meaning of "effective competition". Although it declined to give a detailed definition of the term, the Commission did however observe:[50]

> . . . [B]roadly it envisages a *market structure* in which there is an absence of power in any relevant market to raise and/or decrease services or to exclude entry by others to such a market. (emphasis added)

It then cited with approval criteria for determining whether such a market structure exists from the leading Australian decision upon the meaning of competition — *Re Queensland Co-operative Milling Association*:[51]

> Competition is a process rather than a situation. Nevertheless, whether firms compete is very much a matter of the structure of the markets in which they operate. The elements of market structure which we would stress as needing to be scanned in any case are these:
>
> (1) the number and size distribution of independent sellers, especially the degree of market concentration;
> (2) the height of barriers to entry, that is, the ease with which new firms may enter and secure a viable market;
> (3) the extent to which the products of the industry are characterised by extreme product differentiation and sales promotion;
> (4) the character of "vertical relationships" with customers and with suppliers and the extent of vertical integration; and
> (5) the nature of any formal, stable and fundamental arrangements between firms which restrict their ability to function as independent entities.

Although not cited by the Commission in *Visionhire*,[52] a further passage from the *QCMA* case merits mention. The Australian Trade Practices Tribunal went on to say:[53]

49 (1984) 4 NZAR 288.
50 Ibid at 290.
51 (1976) 8 ALR 481 at 516.
52 The present Chairman, Mr J G Collinge, has however stressed this passage in independent writings. See Collinge, "Mergers and Takeovers: Towards a Competition Policy in New Zealand" [1985] NZLJ 262 at 264-265.
53 Supra n 51 at 516.

> Of all these elements of market structure, no doubt the most important is (2), the condition of entry. For it is the ease with which firms may enter which establishes the possibilities of market concentration over time; and it is the threat of the entry of a new firm or a new plant which operates as the ultimate regulator of competitive conduct.

3 Post Visionhire Decisions

The formulation of effective competition in *Visionhire* has been affirmed by the Commission in later decisions.[55] For example, consent to the merger proposal in *Wattie Industries/Taylor Freezer Holdings* was refused because "there would not be effective competition (as defined in *Visionhire/Sanyo,* decision No 79) in the relevant market".[56] Similarly, consent to a merger proposal was declined by the majority of the Commission in *Air New Zealand/Mt Cook Group*:[57]

> In coming to this conclusion the Commission had regard to "effective competition" (as defined in *Visionhire/Sanyo,* decision No. 79) and finds that this proposal does not conform to the criteria stipulated in that decision as it does not result in a desirable market structure.

On appeal, Davison CJ cited the structural criteria for effective competition enunciated in *QCMA* (and incorporated in *Visionhire*) with approval.[58] He observed:[59]

> I find no reference to "market structure" in the Act but it may nevertheless if adequately defined be a useful tool to employ in considering questions of competition.

Clearly, the conception of effective competition which emerges is one which heavily emphasises market structure. This could hardly be otherwise given the Commission's adoption of the *QCMA* criteria. The fact that the overwhelming majority of decisions since *Visionhire* has been made

54 See generally Baumol, "Contestable Markets: An Uprising in the Theory of Industry Structure" (1982) 72 American Economic Review 1; Baumol, Panzar and Willig, *Contestable Markets and the Theory of Industry Structure* (Harcourt Brace Jovanich 1982).

55 See *Edmonds Food Industries/W F Tucker,* decision No. 84, 21 June 1984, at para 10; *Lion Breweries/Ballin Rattray,* decision No 86, 5 July 1984, at para 10; *Alex Harvey Industries/Smith & Smith* (1985) NZAR 36 at 39. Prior to this article being sent to the printers, the first decision under the Commerce Act 1986 (effective from 1 May 1986) has been given. In *News Ltd/Independent News Ltd,* decision No 164, 9 May 1986, at para 6 the Commission observed:

> Competition is . . . defined in s3(1) of the 1986 Act as workable or effective competition. This concept has been previously canvassed by the Commission in *Visionhire/Sanyo* (1984) 4 NZAR 288.

56 (1985) 5 NZAR 218 at 222.

57 Decision No 130, 6 June 1985, at para 31. The Chairman of the Commission dissented, taking a different view of the relevant market. His dissent was later upheld on appeal. Nevertheless the approach of the majority as to determining effective competition (not market definition) remains valid.

58 *Air New Zealand* v *Commerce Commission,* unreported, High Court (Administrative Division), Wellington, 18 July 1985, M 298/85, at 18-20.

59 Ibid at 19-20.

up of merger proposals also tends to reinforce the structural perspective.[60] Merger analysis invariably focuses primarily upon structural indicators of competition such as market shares and barriers to entry.

When applying the *Visionhire* test for determining effective competition, the predominant factors before the Commission have been first two *QCMA* criteria — the number and size distribution of independent sellers and the height of barriers to entry (or contestability).

(a) The number and size distribution of independent sellers

> . . . [T]he objective of the Commission must be to leave as many independent "heads" as possible in the market, in the expectation that this will promote effective competition.[61]

Where there are a large number of independent competitors (or "heads"), effective competition is usually presumed to exist in the relevant market notwithstanding the merger or other trade practice.[62] Without basic concentration data, the Commission has felt hindered in assessing effective competition.[63]

An inevitable criticism of this kind of approach is that it judges competition solely by counting the number of competitors. In *QCMA,* the Tribunal, anticipating this, commented:[64]

> While the equation of anti-competitive effect with enhanced concentration is tempting in its mechanical simplicity, there is much more to the idea of competition than this.

Similarly, the Chairman of the Commission has endeavoured to dispel misinterpretation of the Commission's approach:[65]

> The mere examination of market shares is criticised as "structuralist" and over-simplistic. But this is only the starting point of the inquiry and the Commission must then proceed to examine barriers to entry and contestability.

Notwithstanding examination of market shares, being described as a preliminary starting point (albeit an extremely important one), where the concentration data evince an adequate number of competitors, further

60 As at 25 February 1986 (decision No 155), the number of Commission decisions given since Visionhire (No 79) is seventy-six. Fifty of these decisions (nearly sixty-six percent) have been merger proposals.

61 *Air New Zealand/Mt Cook Group,* supra n 57 at para 25.

62 See eg *Brierley Investments/Winstone,* decision No 101, 8 November 1984, at para 4; *Brierley Investments/Consolidated Metal Industries,* decision No 124, 17 April 1985, at para 6(a); *John Fairfax/Fourth Estate Holdings* (1985) 5 NZAR 283 at 286; *Mair & Co/Astley Holdings,* decision No 138, 1 August 1985, at para 6.

63 See *Whitcoulls Group/Williamson Jeffery,* decision No 89, 2 August 1984, at para 9: "Unusually, no quantitative information was available . . . on market shares or market size, and it has therefore only been possible to evaluate whether there is effective competition in the markets in a general way."

64 Supra n 51.

65 Collinge, supra n 52 at 391.

analysis of entry (or other competitive characteristics) in reality becomes superfluous.[66]

(b) Barriers to entry/contestability

Focus upon entry conditions becomes important where the number of competitors is small. Moving from market share analysis, the inquiry then becomes whether despite high market concentration, the relevant market is nevertheless contestable, ie readily susceptible to potential entrants should the market incumbents abuse their dominant position. Unlike market share (a quantitative criterion), barriers to entry or contestability are qualitative factors in evaluating effective competition. In making the subjective assessment of contestability, the Chairman of the Commission has suggested a "practical commercial common sense [approach] based upon experience across a wide range of industries . . .".[67]

The threat of import competition will often arise when determining contestability. Assertions of potential import competition effectively disciplining domestic dominant firms have been viewed with suspicion by the Commission. Generally, where entry barriers are high (eg entrants face high capital costs or scarce technological requirements), the threat from imports is viewed as weak. Thus, in both *Fletcher Metals/Pacific Steel*[68] and *New Zealand Steel/Pacific Steel,*[69] the likelihood of import competition effectively constraining the market power of the dominant merged domestic producer was considered remote given the huge capital investment facing entrants to the steel-making industry. By contrast, the absence of substantial entry barriers facing foreign competitors favours an assessment of market contestability. In *Consolidated Metal Industries/Hurricane Wire Products*[70] entry costs were not prohibitive and the requisite technology was readily available. Accordingly, the Commission was satisfied that imports were able to offer "real and effective competition" to the merged firm in the domestic wire producing market.

Other factors such as the degree of product differentiation or vertical integration in an industry have been canvassed in the appropriate cases. However, they tend usually merely to buttress conclusions upon the level of effective competition arrived at using the predominant factors — market share and entry.

Certain conceptions of effective competition have been rejected by the Commission. It had little difficulty in dismissing the specious notion that inter-brand rivalry between divisions of the same company somehow constituted "effective competition" in terms of the Act.[71] In *Watties Industries/Taylor Freezer Holdings* the Commission said:[72]

66 See supra n 62.

67 Collinge, supra n 52 at 392.

68 Decision No 140, 27 September 1985, at para 15. (Presently on appeal to the High Court.)

69 Decision No 150, 21 November 1985, at paras 23-24. (Presently on appeal to the High Court.)

70 Decision No 154, 25 February 1986, at para 14.

71 See *Watties Industries/Taylor Freezer Holdings* (1985) 5 NZAR 218 at 221; *Air New Zealand/Mt Cook Group,* supra n 57 at para 31. The Chairman of the Commission has since remarked: "The Commission hopes it has heard the last of such an argument." See Collinge, supra n 52 at 394.

72 Ibid at 222.

> Competition, if any, between brands owned or controlled by one company or group is not competition in any real sense of the term and certainly not competition as we perceive was intended by Parliament in the Act.

The Commission has also rejected an "individualistic"[73] notion of competition, thereby mirroring a similar development in the interpretation of competition in the post-*QCMA* Australian case law. Underlining the close connection between "competition" and "market", the Commission has recognised that a restriction in rivalry between two competitors or upon an *individual* competitor does not necessarily signal a restriction in competition in the *market as a whole.*[74] Notwithstanding a reduction in rivalry between individual firms, effective competition may still exist in the relevant market. In *Associated Wholesalers*[75]the restriction in rivalry between members of a grocery store chain was viewed as actually enhancing competition. The resale price maintenance agreement strengthened the position of the smaller grocery retailers in the face of larger supermarkets and thereby served to encourage competition in the retail grocery market.

Approving the economic meaning of competition in *QCMA,*[76] the Federal Court of Australia has consistently rejected the fallacy that the competition test is concerned with the fate of individual competitors as opposed to the level of rival behaviour in the market. In *Outboard Marine Australia* v *Hecar Investments No 6,* Fitzgerald J said:[77]

> . . . [W]here there is a market which is generally competitive, it plainly does not follow that conduct which affects the balance of competition by advantaging or disadvantaging a particular dealer or dealers . . . necessarily lessens the competition in the market.

IV Conclusion

Economic theorists have developed various conceptions of competition usually emphasising one aspect of the SCP model. A hybrid conception – "effective competition" – has been preferred by the New Zealand Legislature as the definition of competition under the Commerce Act 1986.

Interpretation by the Commerce Commission of effective competition in *Visionhire Holdings/Sanyo Rentals* and subsequent decisions has witnessed the evolution of a notion of competition strongly emphasising market structure. Essentially, effective competition is equated with a desirable market structure, which in turn is evaluated primarily by examin-

73 This term is adopted by Norman and Williams, supra n 47 at 411.

74 See Collinge, supra n 52 at 263. In this context, the famous dictum of the US Supreme Court in *Brown Shoe* v *United States* 370 US 294 (1962) at 320, is recalled:

> Taken as a whole, the legislative history [of the Clayton Act] illuminates congressional concern with the protection of *competition,* not *competitors,* and its desire to restrain mergers only to the extent that such combinations may tend to lessen competition. (original emphasis)

75 Decision No 113, 20 February 1985, at para 5.

76 See *Trade Practices Commission* v *Ansett Transport Industries* (1978) 20 ALR 31 at 48; *Adamson* v *West Perth Football Club* (1980) 27 ALR 475 at 502; *Dandy Power Equipment* v *Mercury Marine* (1982) 44 ALR 173 at 191; *Outboard Marine Australia* v *Hecar Investments No. 6* (1982) 44 ALR 667 at 669; *Trade Practices Commission* v *TNT Management* (1985) 58 ALR 423 at 507.

77 44 ALR 667 at 679-680. Noted in (1983) 11 ABLR 145.

ing market concentration and entry conditions (or contestability). Although it might sacrifice some of the more subtle dimensions of competition, the Commission's approach is workable one.

Undoubtedly there is yet further light to be shed upon the meaning of competition in the New Zealand context. The broad parameters only have been scanned here. Beyond this, one faces the inevitable difficulties incumbent in seeking to define a rich, multifaceted concept in a more detailed, self-contained fashion.