Submission

By

THE NEW ZEALAND INITIATIVE

to the Economic Development, Science and Innovation Committee

on the

Commerce (Criminalisation of Cartels) Amendment Bill

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1. INTRODUCTION AND SUMMARY

1.1 This submission on the Commerce (Criminalisation of Cartels) Amendment Bill (**the Bill**) is made by The New Zealand Initiative, a think tank supported primarily by chief executives of major New Zealand businesses. In combination, our members' revenues account for one third of New Zealand's economy and provide employment to more than 150,000 people in New Zealand. The Initiative undertakes research that contributes to the development of sound public policies in New Zealand which help create a competitive, open and dynamic economy and a free, prosperous, fair, and cohesive society.

1.2 We oppose the amendment to the Commerce Act 1986 (**the Act)** proposed in the Bill for three reasons:

(a) There is no compelling evidence that the benefits of cartel criminalisation outweigh the costs or, indeed, that criminalising cartel conduct will promote the objectives of the Commerce Act;
(b) There are insufficient checks and balances in the Bill on the Commerce Commission's (**the Commission**) power to launch a criminal prosecution for cartel conduct; and
(c) There is evidence of substantial shortcomings in the behaviour and performance of the Commission which should be addressed before arming the Commission with further powers.

2. CRIMINALISING CARTEL CONDUCT UNLIKELY TO PROMOTE OBJECTIVES OF ACT AND MAY ADVERSELY AFFECT THEM

2.1 We accept that cartels may harm consumers and reduce welfare by enabling firms to raise prices above competitive levels. We also accept that cartels are difficult to detect.

2.2 However, we agree with the views expressed by Treasury set out in the 2011 Cabinet Paper preceding the introduction of the Commerce (Cartels and other matters) Bill 2011 (**the 2011 Bill**) that:[1]

(a) It is not clear that New Zealand has levels of cartel behaviour that warrant criminalisation. As at 2011, only 16 alleged price fixing cartels had been the subject of civil decisions by the New Zealand courts during the preceding 25 years, and the maximum civil penalties have never been imposed.

(b) Given the civil penalties already available, criminalisation is unlikely to significantly increase either the deterrence or detection of cartel behaviour.

(c) The primary benefit claimed to arise from criminalisation is improved alignment of New Zealand's competition regulatory regime with other jurisdictions. However, increased international cooperation can be achieved through other means.

(d) Any marginal benefits from criminalisation are likely to be significantly outweighed by the costs. These include:

[1] Cabinet Paper, Proposed Amendments to the Commerce Act in relation to cartels, Ministry of Economic Development, MED1256329.

I. The costs faced by businesses exposed to risk of criminal prosecution. Despite the clearance regime for collaborative arrangements, there is a risk criminalisation will have a chilling effect on pro-competitive behaviour.

II. The Commission and the Courts would also face increased costs, as a higher standard of proof would be required to pursue criminal cases.

2.3 In 2011 Treasury concluded:[2]

> "On balance, it is difficult to see how the likely benefits of cartel criminalisation in terms of international cooperation would exceed the likely costs imposed on businesses, the Commerce Commission, and the Courts. The benefits from clarifying the laws around cartel behaviour can be achieved without the introduction of criminal penalties."

2.4 We agree. And as the clarifications referred to by Treasury were made to the Commerce Act following the enactment of the 2011 Bill, there is no compelling case for legislative reform.

2.5 The Cabinet paper supporting the new Bill states that Treasury has now reached a different view and "on balance is supportive" – though noting that Treasury states "there will be fiscal implications from the policy change which are currently unknown."[3] The Cabinet paper does not disclose what has caused Treasury's change of heart and, unfortunately, the balance of the paragraph dealing with Treasury's view has been withheld under the Official Information Act.

2.6 Despite Treasury's apparent change of view, we consider the reservations expressed by Treasury in relation to the 2011 Bill still stand.

2.7 The position might be different if new analysis had been presented making the case that the benefits of cartel criminalisation exceeded the costs. But no such new analysis accompanied the Cabinet paper recommending the introduction of the Bill.[4] Instead, the Cabinet paper relied on the Regulatory Impact Statement (**the RIS**)[5] prepared for the Cabinet decision in 2011 for the introduction of the 2011 Bill recommending cartel criminalisation – a decision subsequently resiled from by Cabinet in December 2015.[6]

2.8 For the reasons expressed by Treasury in relation to the 2011 Bill, we consider there is no compelling case to criminalise cartels, and no persuasive evidence that the benefits of cartel criminalisation will exceed the costs.

3 THE BILL HAS INSUFFICIENT CHECKS AND BALANCES

3.1 We have two reservations in relation to the lack of checks and balances in the Bill, one substantive, and one procedural.

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[2] *Ibid,* paragraph 64.
[3] Cabinet Paper, *Amending the Commerce Act to criminalise cartel conduct*, Hon Kris Faafoi, 15 February 2018, paragraph 32.
[4] Cabinet Paper, *Amending the Commerce Act to criminalise cartel conduct*, Hon Kris Faafoi, 15 February 2018.
[5] Regulatory Impact Statement, Ministry of Business, Innovation and Employment, 26 August 2011.
[6] Cabinet Paper, Removal of the criminal offence for cartels from the Commerce (Cartels and Other Matters) Amendment Bill, Hon Paul Goldsmith, December 2015.

Mental Element of Proposed Cartel Offence Too Broad

3.2 Our substantive concern relates to the mental element of the proposed new offence relating to cartel prohibition in new section 82B. The difficulties designing the mental element of cartel offences are notorious. Is it enough that a person merely *intends* to do the act that is ultimately found to have the effect of fixing price, restricting output, or allocating markets (**the prohibited effects**), or must this be done *dishonestly* or at least *knowingly* (in the sense that the person is aware that the conduct is unlawful)?

3.3 It is a fundamental principle of the rule of law that a person convicted of a serious crime should have a culpable state of mind when committing the acts resulting in his or her conviction. The principle was expressed by Lord Bingham in Regina v.G:[7]

> "[I]t is a salutary principle that conviction of serious crime should depend on proof not simply that the defendant caused (by act or omission) an injurious result to another but that his state of mind when so acting was culpable. This, after all, is the meaning of the familiar rule *actus non facit reum nisi mens sit rea*. The most obviously culpable state of mind is no doubt an intention to cause the injurious result, but knowing disregard of an appreciated and unacceptable risk of causing an injurious result or a deliberate closing of the mind to such risk would be readily accepted as culpable also. It is clearly blameworthy to take an obvious and significant risk of causing injury to another. But it is not clearly blameworthy to do something involving a risk of injury to another if ... one genuinely does not perceive the risk. Such a person may fairly be accused of stupidity or lack of imagination, but neither of those failings should expose him to conviction of serious crime or the risk of punishment."

3.4 The Bill is intended to catch so-called "hard core cartels", and the penalty prescribed clearly places the new offence within the category of "serious crimes". Yet the proposed mental element of the offence requires only that a person commits the offence if the person "intends… to engage in price fixing, restricting output, or market allocation". There is no requirement for dishonesty (in the sense of knowledge of wrongdoing).

3.5 Consequently, it is possible that a person might commit the offence by the simple act of entering into a contract, neither knowing that the contract had one of the prohibited effects or intending the contract to have this effect. In other words, the person might not have the "culpable mind" – or be "blameworthy" in the words of Lord Bingham.

3.1 This concern is not merely an abstract one. In cartel cases, it is often only after analysis by a lawyer or economist that what may appear to be an ordinary commercial arrangement proves to have the prohibited effect of fixing price, restricting output, or allocating markets.

Example:

If doctors in a low decile community were to get together and agree a maximum price for doctors' consultations for the benefit of the community, that would constitute price fixing. This is because, under the Commerce Act, an agreement that controls price – like an agreement setting a maximum price – falls within the definition of price fixing. As the doctors would have intended to control the maximum price of consultations, the mental element of the cartel offence would be met, and the offence as drafted in the Bill would be made out. All that would

[7] [2004]1 AC 1034, at para 34.

stand between the doctors and a criminal prosecution would be the discretion of the prosecutor as to whether or not to charge them.

3.2 It is highly unsatisfactory – and offends the rule of law – for criminal offences to be cast more widely than necessary, as this leaves potential defendants on the mercy of the prosecuting agency.

3.3 To guard against this risk, new section 82B should not be enacted unless it is amended to include the element of dishonesty – in the sense that a person will only commit the cartel offence if they know that their allegedly infringing activity will have one of the prohibited effects.

Commission should not be both Investigator and Prosecutor

3.4 Prosecutorial independence is a cornerstone of the rule of law. Yet the Bill contains no safe guards to ensure that the decision to prosecute is made independently of those tasked with investigating an alleged cartel.

3.5 As it is the Commission that is tasked with the investigative function also decides on any prosecution. The Bill should specify a mechanism for independent prosecutorial decision-making.

3.6 The need for prosecutorial independence is likely to be more acute in relation to cartel inquiries because of the increased risk of a lack of objectivity following the type of lengthy investigations that are a characteristic of cartel inquiries internationally.

3.7 Jurisdictions where this separation is legislated in relation to cartel offences include Canada (where decisions on prosecutions are referred to the Attorney General), Australia and Ireland (in these latter two jurisdictions the decision is made by an independent Director of Public Prosecutions). In New Zealand, the Solicitor General – in whose name prosecutions are brought – should be required to perform this role.

4 COMMISSION'S GOVERENANCE AND ACCOUNTABILITY MECHANISMS SHOULD BE STRENGTHENED BEFORE COMMISSION IS GIVEN FURTHER POWERS

4.1 On 13 April next week, The New Zealand Initiative will publish the results of a major research project examining the performance, accountabilities and governance of New Zealand's regulatory agencies. Our research included extensive interviews with the leadership of many of New Zealand's leading regulators, interviews with consumer organisations and major businesses, discussions with a wide range of public officials, and an extensive survey of New Zealand's 200 largest businesses.

4.2 Our research also drew on a significant 2014 report of the Productivity Commission into New Zealand's *Regulatory Institutions and Practices.*[8] That report found a litany of shortcomings with regulatory agencies in New Zealand. It concluded that governance structures of regulators were *ad hoc* rather than based on sound governance principles.

[8] Productivity Commission, "Regulatory Institutions and Practices", (Wellington: Productivity Commission, 2014).

4.3 Our research disclosed serious concerns with the performance, behaviours and governance of several regulatory agencies, including, in particular, the Commission. The concerns relate to consistency and predictability of decision-making, accountability and commercial expertise.

4.4 In many respects, these concerns mirror those of the former Securities Commission, which lacked an effective internal accountability mechanism as a result of governance and executive functions being rolled up within the "commissioner" role.

4.5 The "commissioner" model of the Commission (and the former Securities Commission) stands in stark contrast to the board governance model of the Securities Commission's successor, the Financial Markets Authority (FMA). Under the FMA's board governance model, the FMA's non-executive board is able to exercise oversight over the regulator's executive and hold them accountable for regulatory decision-making.

4.6 We submit that the issues relating to the governance and accountabilities of the Commission should be resolved before the Commission is equipped with any further enforcement powers, including the very significant powers proposed in the Bill.

The New Zealand Initiative

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