The near-collapse and pending recovery of regulatory governance in New Zealand

Presented to workshop on “Regulatory governance: models and dynamics”, Florence, 26-29 June 2022

Geoff Bertram
Institute for Governance and Policy Studies
Victoria University of Wellington

Abstract

Effective regulation of conduct in a market economy does not easily reduce to any single critical requirement. Rather, it flows from a constellation of mutually-supporting elements: appropriate legislation, clear codified criteria to measure compliance; smoothly-operating regulatory institutions with clear legitimacy, expert staff, and an enforcement mandate; and over all a political culture of recognition and respect for regulators. The breakdown of a pre-existing regulatory constellation lets loose familiar pathologies: abuse of monopoly power to price-gouge consumers and eliminate competitors; unbridled pursuit of self-interest degrading the quality of services and products; reduced health, safety and wages in workplaces; and unchecked environmental degradation.

The neoliberal revolution of the 1980s and 1990s had a particularly strong deregulatory impact in New Zealand, sweeping away established regulatory institutions and practices while converting national policy to a culture of non-regulation – what Feffer (2007) has called “the self-hating state”. Reconstruction of regulatory institutions and culture has been piecemeal, and has faced entrenched opposition from powerful vested interests consolidated during the unregulated decades. The paper reviews the impact on New Zealand’s regulatory institutions, and on their legislative foundations, of ideas from public-choice economics and the Chicago School of law and economics. Some case studies highlight key issues that have emerged, and an agenda is outlined for the revival of effective regulation tailored to New Zealand conditions.

1. Introduction: the New Zealand turn to neoliberalism

Between 1984 and 1995 New Zealand underwent a profound transformation of the character and structure of its government (Boston et al 1991; Easton 1997a, 1997b; Kelsey 1995) – a transformation that went significantly further than the better-known neoliberal programmes of Reagan in the USA and Thatcher in the UK on which the New Zealand experiment was based. As Smith and Montgomery (2004) noted,

> Where New Zealand stands out is in the speed, extent and apparent depth of the changes imposed. This was facilitated by the country’s small population and the absence of a second [parliamentary] chamber which might have put the brakes on the iconoclastic behaviour of a small, powerful group of elected politicians.

Lewis (2004 p.161) added

> In many ways, the New Zealand experience is a paradigm case of neo-liberal political reform… It is regarded as remarkable for the purity of its new state managerial design, the speed of its implementation, and the ideological certainty with which it was pursued.

In a number of papers over the past two decades (including Bertram 1999, 2004a, 2004b, 2006, 2010, 2014, 2020, 2021, 2022; Bertram and Chapple 2021; Bertram and Twaddle 2005) I have argued that the successful neoliberal crusade to free up markets and shrink the state, and the consequent near-elimination of regulatory will and capability in New Zealand state agencies, has had negative consequences for the economy and for ordinary people even as it carried New Zealand to the top of business-oriented measures such as "ease of doing business" (World Bank 2020 p.4)[1]. In this paper I pull together some themes and issues from those previous papers.

Over the century to 1984, New Zealand constructed and consolidated a mixed economy in which the public sector built and operated core infrastructure and services based on it – road, rail, ports, airports, telecommunications, electricity generation and distribution, gas and coal supply, health and education. Besides delivering these essential services to the population at officially-set prices, the state regulated, for example, bank lending, wages, prices when necessary, town planning and building standards. New Zealand was a politically stable democracy with a prosperous, relatively egalitarian economy, a highly educated and healthy population, and a deep-rooted regulatory culture operating through well-established institutions.

Insofar as there was an underlying "theory of government" it was that of pursuit of the common good by collective endeavour. If the public good was not being effectively advanced by the government of the day, the democratic remedy was to change the government, but without casting doubt on the fundamental legitimacy of the state itself, nor on the necessity of its regulatory functions.

Neoliberalism posed a challenge of a different order: a direct attack on the legitimacy of the modern state itself and a programme of stripping back its role and powers. The intellectual firepower behind this vision came from Hayek, Buchanan and Tullock, Stigler and Friedman and Bork, none of them familiar to

[1] The World Bank discontinued production of its *Doing Business Report* in 2021 after serious ethical issues were raised about the integrity of the survey and its results; see https://www.worldbank.org/en/news/statement/2021/09/16/world-bank-group-to-discontinue-doing-business-report and https://thedocs.worldbank.org/en/doc/84a922cc9273b7b120d49ad3b9e9d3f9-0090012021/original/DB-Investigation-Findings-and-Report-to-the-Board-of-Executive-Directors-September-15-2021.pdf . New Zealand was given the highest score out of 190 jurisdictions surveyed worldwide by the Bank in all four years 2015-2019; see data online at https://data.worldbank.org/indicator/IC.BUS.DFRN.XQ and https://www.doingbusiness.org/content/dam/doingBusiness/excel/db2020/Historical-data---COMPLETE-dataset-with-scores.xlsx .

the wider New Zealand public in the early 1980s. But a tight-knit group of young New Zealand officials, who had studied in the US and been exposed to libertarian thinking, brought those ideas directly to the top echelons of government and successfully captured a small cadre of elected politicians and key leaders in the rising financially-oriented business sector (Bertram 1993 pp.37-47; 2004a). Ideas about the magical properties of competition in markets were transplanted to a small economy where the space for competition was narrowly constrained and opportunities for the exercise of market power abounded.

Under attack from within, the state regulatory apparatus was dismantled, while publicly-owned utility operations in ports, airports, electricity, telecommunications, and gas pipelines were privatised or converted to profit-seeking corporations. Common-law restrictions on monopoly were suppressed, restraints on the financial sector were removed, organised labour broken, and the entire state sector subjected to wrenching changes to make it conform to the model of “New Public Management” (Boston et al 1991; Gregory 2003).

The outcome of this “internal coup d'etat within the State structure” (Bertram 1993 p.48) was a government apparatus designed and run by people who were deeply sceptical of the entire enterprise of government – what Feffer (2007) has termed the “self-hating state”. Officials and ministers proclaimed their own institution’s ineffectiveness and proneness to rent-seeking and capture, then used this as their excuse to abdicate from serious engagement with the core regulatory functions of government in a mixed capitalist economy. In place of an overarching concept of the public good, the new order enshrined the market as the ultimate arbiter of what was best. Indeed the whole idea of a common good was submerged beneath the vision of individual maximisation under competition, echoing Margaret Thatcher’s famous claim that “there is no such thing as society”. From relatively inclusive politics and strong regulatory enforcement, New Zealand shifted towards more extractive institutions and weaker regulation (Bertram 2021).

Three decades after the upheaval of the 1980s, the legislative pillars of neoliberalism in New Zealand – in particular the Commerce Act 1986, the State Owned Enterprises Act 1986, the State Sector Act 1988, the Public Finance Act 1989, and the Fiscal Responsibility Act 1994 – remain on the statute books and combine to trap New Zealand Governments of any party into an “iron cage” of restraints on state activism. Neo-liberal doctrines and attitudes remain embedded not only in the legislation but in the mindset of the state executive and the regulatory agencies.

This is not unique to New Zealand, of course. In the aftermath of the collapse of the Texas electricity grid in 2021, a critic commented that[2]

[2] https://www.politico.com/news/2021/02/19/texas-storm-response-cruz-abbott-perry-470109 .

> We shouldn't put people in charge of government who don't believe in government. They fail us every time.

New Zealand consistently ranks in the upper half of the OECD in that organisation's formal indicators of regulatory design, governance and performance (Arndt et al 2015; Gönenç et al 2001; OECD 2015). In addition it consistently scores highly in the OECD's "confidence in national government" rankings[3] as well as the World Bank's "ease of doing business" rankings[4] already mentioned. Both of these agencies were at the forefront of the neoliberal policy agenda (aka the Washington Consensus) and their regulatory prescriptions matched much of the narrative put forward by the New Zealand reformers. There is nevertheless some disconnect between the OECD's formal evaluations of New Zealand regulatory governance and the picture of New Zealand's regulatory culture and governance in this paper. New Zealand has gone further in a deregulatory direction than the OECD programme would have prescribed, and in a couple of respects has taken a completely different direction.

2. New Zealand and the OECD regulatory model

The OECD's regulatory reform agenda was summarised as follows in Gönenç et al (2001 p.12):

> Regulatory reforms have had three main dimensions: liberalisation, state retrenchment and new regulatory design. Liberalisation and state retrenchment were mainly concerned with:
>
> – Liberalising prices and access to markets which had previously been restricted by legal and regulatory barriers.
>
> – Handing or returning to the private sector activities that had been run directly by the government.
>
> New regulatory design was an essential element of regulatory reform to the extent that:
>
> – Rules had to be set in network industries to make access to the noncompetitive segments of the industry by a plurality of service providers possible and efficient.
>
> – In industries where liberalisation had involved the unbundling of vertically integrated monopolies, markets had to be created *ex novo* to replace transactions that were previously taking place within the firm.
>
> – In industries where (non-economic) public interest objectives were ensured within a regulated non-competitive environment, ways had to be found to achieve these objectives in a competitive framework.
>
> – Where firms had been privatised or activities had been contracted out, regulation through public ownership had to be replaced by arm's length regulation.

---

[3] https://stats.oecd.org, 'Government at a glance/Core government/Confidence in national government', accessed 27 May 2022.

[4] https://data.worldbank.org/indicator/IC.BUS.DFRN.XQ accessed 1 June 2022.

In addition, in the area of "new regulatory design" four basic principles were stated (Gönenç et al 2001 p.15):

> regulatory institutions should be designed to *i)* ensure independence of the regulator from the executive branch of the government; *ii)* impose constraints on the regulator's discretion (for example by allowing appeal procedures with general competition authorities); *iii)* enhance transparency of the regulatory process so as to limit information asymmetries and reduce regulatory discretion; and *iv)* ensure consistency of regulatory approaches across industries.

Public interest objectives dropped

The New Zealand Government enthusiastically went about corporatising and where possible privatising its activities in electricity, gas, coal, telecommunications, railways, banking, insurance, public works, and forestry (Jesson 1999 pp.161-181; Kelsey 1995). But far from finding ways to "achieve [public interest objectives] in a competitive environment" through action to mitigate the devastating impact of corporatisation and privatisation on the welfare of low-income households, the New Zealand Government moved in 1991 to sharply reduce the scope of welfare transfers and to destroy the union movement, opening the way for a driving-down of wages and conditions in a deregulated labour market within which employers retained unabated their oligopsonistic position (Bertram and Rosenberg 2022). As Taggart described it at the time (1990 pp.1-2)

> The formal separation of commercial and social objectives… has resulted, in practice, in the negation of social objectives.

Nor, Taggart went on to argue (1990 pp.7-8), was this an accidental oversight. On the contrary, it was a logical consequence of official adherence to the doctrines of "public choice theory" which denied the existence of any such thing as "the general welfare" or "the public good". The New Zealand Treasury, the lead government agency pushing the neoliberal agenda, strongly argued that public-good proponents were merely self-interested rent-seekers and that their concerns should therefore be set aside (NZ Treasury 1987; Bertram 2021).

Corporatisation removed from the scene a powerful group of *de facto* regulators – the managers of the old state-run service providers. They were replaced by (or converted into) commercial managers with a single-minded profit goal, as required by section 4 of the State-Owned Enterprises Act 1986[5] which blocks these companies from "exhibit[ing] a sense of social responsibility" unless doing so contributes to profitability.

Within a year of passage of the Act, the closure of 432 "uneconomic" Post Offices, withdrawing valued services from local communities, survived a High Court

[5] https://www.legislation.govt.nz/act/public/1986/0124/latest/096be8ed81bb974b.pdf accessed 7 June 2022.

challenge[6], with the court affirming the absolute primacy of the profit goal (see Taggart 1990 pp.9-10). Three and a half decades later the Act remains unchanged.

Competition overestimated

The OECD regulatory model drew a distinction between infrastructure/network activities (electricity and telecommunication lines, gas and water pipelines, rail networks, ports and airports, and so on) that were acknowledged to be natural monopolies, and all other activities that were treated as potentially competitive. The basis for drawing the distinction in this way was to lay the groundwork for treating all of the market economy apart from infrastructure monopolies as requiring no (or minimal) regulation, beyond measures to protect the process of competition itself[7].

This idea that monopoly pricing was of concern only in infrastructure facilities, with their large sunk costs and economies of scale, translated in New Zealand to wildly overoptimistic expectations for the effectiveness of competitive forces in all other sectors. New Zealand is a small economy in which the textbook conditions for natural monopoly – not to mention opportunities for exclusionary conduct - are by no means limited to infrastructure utilities. But blanket application of the OECD classification meant that no need for traditional regulation was acknowledged in other sectors, where market power has been left to run rampant without regulatory restraint.

This almost exclusive reliance on competition to curb the exercise of market power has left the way open for profiteering, especially by vertically-integrated companies. In a small market such as New Zealand, vertical integration is a powerful source of competitive advantage for large firms, and in the largely unregulated environment since the 1980s it has been taken full advantage of in a number of sectors. Notable examples are electricity generation and retailing, oil products wholesale and retail supply, building supplies, and supermarkets (which have used their control of upstream wholesale supply both to exclude new retail entry and to squeeze upstream suppliers – see Commerce Commission 2022).

In all of those sectors, vertical integration has gone beyond simple double-marginalisation to involve strategic dominance at the wholesale level of supply chains, with clear exclusionary consequences. Cartel-like arrangements at wholesale level have sustained strong vested interests which have been able, through their lobbying power, successfully to forestall any attempt at unbundling of their upstream operations.

---

[6] *The Wellington Regional Council v Post Office Bank Ltd,* High Court, Wellington, 22 December 1987, CP 720/87, Greig J.

[7] Later in New Zealand policy debates there were occasional appeals to "contestability theory" and "competition for the market" as sources of market discipline - even on natural monopolists - that might justify doing away with regulation altogether.

A law change in 2018 opened the way for the Commerce Commission to conduct "competition studies" when directed to do so by the Minister, and two such studies have been completed, into petroleum fuels and supermarkets (Commerce Commission 2019a, 2022). The first found that[8]

> an active wholesale market for fuel does not exist in New Zealand. The major fuel companies, Z Energy, BP and Mobil, share a joint infrastructure network which includes the Marsden Point refinery, coastal shipping operations and storage terminals at regional ports. They use this network to supply 90% of the nation's fuel through their own branded retail sites or via other distributors or resellers via exclusive long-term wholesale supply contracts. The only other fuel importer is Gull, with a terminal in Mt Maunganui… The combination of infrastructure sharing and restrictive supply relationships gives the major fuel companies an advantage. There is a reduced ability for importers to compete for customers of the majors and for distributors and dealers to obtain competitive wholesale supply terms.

The only remedies suggested were a mandatory posted-price regime for wholesale supply, and improved price information for retail customers. The Government response was the Fuel Industry Act 2020[9] which required retail prices to be displayed on roadside billboards and required all wholesalers to post spot prices at which supply would be available to independents. No enforceable industry code was legislated for, only a limited regulatory backstop was allowed for (section 20 of the Act), no unbundling was contemplated, and excess profits were not addressed. The major companies proceeded to close the single refinery in 2022, leaving New Zealand entirely dependent on petroleum products which (apart from Gull) must be imported through specialised port facilities owned by the majors on which no open-access requirements have been imposed.

The second market study, of supermarkets, found that (Commerce Commission 2022)[10]

> The major grocery retailers, Woolworths NZ and Foodstuffs, operate as a duopoly with a fringe of other competing grocery retailers… Under current market conditions, we see little prospect of new or expanding rivals being able to achieve the scale and geographic coverage required to compete effectively with the major grocery retailers. Competitors wanting to enter the market or expand face significant challenges, including a lack of suitable sites for store development[11] and

---

8 https://comcom.govt.nz/about-us/our-role/competition-studies/fuel-market-study/media-releases/retail-fuel-market-study-recommends-changes-to-benefit-competition-and-consumers accessed 2 June 2022.

9 https://www.legislation.govt.nz/act/public/2020/0060/latest/whole.html#LMS321426 accessed 2 June 2022.

10 https://comcom.govt.nz/__data/assets/pdf_file/0023/278402/Market-study-into-the-retail-grocery-sector-Executive-summary-8-March-2022.pdf accessed 2 June 2022.

11 A key reason for the lack of sites for new entrants was the fact that the duopoly had placed covenants on blocking any competitor from utilizing the site.

difficulties in sourcing wholesale supply of a comprehensive range of competitively priced grocery products.

The supermarkets were found to be securing a rate of return at least double their cost of capital. Translated into dollar terms, this implied excess profits amounting to $430 million per year[12] (Commerce Commission 2022 p.55). The Government response has been to threaten possible regulation in the hope of persuading the incumbent duopoly to lower its prices. One step in this direction was to ban the practice of placing restrictive covenants on sites for possible new entrant supermarket operationsa; a new law to this effect passed through Parliament in June 2022[13]. The Commission had identified 190 of these covenants across the country (2022 p.210).

Both the oil companies and the supermarket giants lobby strongly and publicly against any restriction on their conduct or prices, resulting in an ongoing “chicken game” with a Government that feels able to act only because of strong public pressure channelled through the media and opinion polls. Government loudly wishes for entry by some deep-pocketed “competitor for the market” – but in the small New Zealand market, any such successful entrant would struggle to make a profit unless it joins the incumbent cartels.

Politicisation of price regulation

In relation to restraint on monopoly profiteering the New Zealand model has had a crucial divergence from the OECD one. This is the politicisation of the actual decision to regulate, which was transferred in 1986 from the judicial to the executive branch of government.

Part IV of the Commerce Act 1986 reserved any decision even to consider price regulation, let alone actually regulate a monopolist’s pricing, to the minister, not the ostensible regulator. Only after a political decision is taken to declare a sector a “regulated good or service” can the Commerce Commission regulate an industry’s prices, and in doing so it is tightly constrained by prescriptive methodological procedures dictated from above[14]. To date price regulation has been applied to just three infrastructure sectors - electricity lines, gas pipelines, telecommunication networks – with a fourth, airports, subject only to “light handed” regulated information disclosure.

Prior to 1986, Section 54 of the old Commerce Act 1975 commenced with the provision: “(1) Every person commits an offence against this Act who whether as principal or agent, and whether by himself or his agent, sells or agrees or offers to

---

[12] To put this into perspective, the New Zealand economy’s Gross Domestic Product in the year to March 2021 was $328 billion, so supermarket excess profits were 0.13% of this.

[13] Commerce (Grocery Sector Covenants Amendment) Act, 2022/35.

[14] For example the “input methodologies” for price regulation set out in the Commerce Amendment Act 2008, and now included in Part 4 of the main Act.

sell any goods or services at a price which is unreasonably high.” The section then went on to lay out in detail the procedures to be followed by a court in assessing when a price was unreasonably high. Section 25 of the 1975 Act gave the Commerce Commission the power to hold an inquiry into pricing in any industry, and if appropriate to recommend that an offending industry be placed on the “Positive List” for price regulation (though the final decision of whether to act on the recommendation always lay with the Minister). The 1986 legislation removed this power from the Commission and vested it instead in the Minister.

The common-law role of the courts to sanction monopolistic pricing was also extinguished in 1986 (or rather, suppressed until Parliament might change its mind) (Taggart 2008; Court of Appeal of New Zealand 1999 paragraphs 52-54, 59).

From time to time regulatory agencies have recommended or taken action, only for the relevant minister (subject to the usual range of political and lobbying pressures from big business interests) to refuse to act, or even dismiss the regulator. Two examples follow.

- New Zealand’s electricity transmission grid Transpower is state-owned but corporatised. In 2001 an Electricity Commission was established “to regulate the operation of the electricity industry and markets”. But when the Commission withheld planning consent for a major new investment, Transpower quickly turned to its owner, the Government, for support. In September 2006 the Commission chair was dismissed and replaced with a political appointee who approved the new transmission line. The Commission itself was disestablished a couple of years later. (Bertram 2013 pp.657-658),

- New Zealand’s international airports were corporatised and part privatised in the 1980s, then left unregulated for ten years during which they freely used their market power to raise prices and asset values to monopoly levels (Lyon 2011, Bertram et al 2000). Strong lobbying by the major airlines eventually succeeded in persuading the Government in 1998 to refer airport landing charges to the Commerce Commission for a report on whether regulation might be appropriate. Following a four-year inquiry the Commission strongly recommended regulation of Auckland airport, including a write-down of its asset valuation to historic cost. The Minister flatly refused, saying “it is my responsibility as Minister of Commerce to look at the overall impact of my decision on the economy as a whole. That is where the net public benefit test comes in.”[15]

[15] “Airports to escape price curbs”, *New Zealand Herald* 24 May 2003.

Tolerance of monopoly profits

That "public benefit test", introduced under Treasury auspices in 1992 without legislative or publicly-announced justification, sets New Zealand apart from most other jurisdictions where a consumer surplus standard applies. New Zealand has adopted the so-called "total surplus standard" which says that any transfer of wealth from customers to a monopolist supplier of a good or service due to monopoly pricing has zero cost to the economy (Bertram 2004b).

Hence, as the Commerce Commission has noted (Commerce Commission 2009 p.6 paragraph ii, in relation to electricity supply)

> The exercise of market power to earn market power rents is not … a contravention of the Commerce Act, but is a lawful, rational exploitation of the ability and incentives available to the generators.

Similarly, in evaluating the "net public benefit" of mergers, so long as there is some "efficiency" gain the regulator does not ask whether acquirers of the good or service will be left worse off while the new monopoly's profits are increased. Wealth transfers within New Zealand are not an issue.

Failure to restrain anticompetitive conduct

The narrow focus of New Zealand's Commerce Act 1986 is stated as follows in its "purpose" section[16]:

> The purpose of this Act is to promote competition in markets for the long-term benefit of consumers within New Zealand.

The main regulatory agency under the Act – the Commerce Commission – is charged primarily with approval of mergers and with taking (or threatening to take) legal action against companies that are considered in breach of the Act's two main prohibitions: on collusion (sections 27 and 28) and on "taking advantage of market power" at the expense of competitors or would-be competitors (section 36).

Prior to 1986, part 1 of the Commerce Act 1975 provided for an independent Examiner of Trade Practices to report to the Commerce Commission any apparent monopolistic or anticompetitive conduct in any market, and for the Commission to conduct its own inquiry and make its own orders prohibiting or penalising the conduct, subject to appeal. An extensive list of illegal practices familiar from antitrust textbooks was set out, in explicit detail, in section 23 of that Act.

[16] The contrast with the previous legislation, the Commerce Act 1975, was stark (https://www.legislation.govt.nz/act/public/1986/0005/latest/096be8ed81c198d9.pdf accessed 3 June 2022 section 1A): the 1975 version was "an Act to assist in the orderly development of industry and commerce and to promote its efficiency, and the welfare of consumers, through the regulation, where desirable in the public interest, of trade practices, of monopolies, mergers, and takeovers, and of the prices of goods and services".

That explicit list was erased in the Commerce Act 1986 and replaced by a single generic sub-section 36(2). Until April 2022 this read as follows:

> A person that has a substantial degree of power in a market must not take advantage[17] of that power for the purpose of—
> (a) restricting the entry of a person into that or any other market; or
> (b) preventing or deterring a person from engaging in competitive conduct in that or any other market; or
> (c) eliminating a person from that or any other market.

To many observers at the time the Act was passed it seemed that this would still make illegal the exercise of market power against competitors, but it quickly turned out not to be so. Only where the proven "purpose" of the dominant firm was to erect barriers to entry was it subject to any penalty.

"Purpose" is subjective and not easily observable – and inferring purpose from actual conduct is not straightforward. The Act's requirement that "taking advantage of market power" had to be for an anti-competitive purpose, as distinct from merely a desire to compete vigorously as any firm is supposed to do, imposed a burden of proof that overwhelmed attempts by private parties and the Commerce Commission to rein in conduct that was transparently anticompetitive in its effects but could not be proven to flow from an anti-competitive purpose.

The courts' approach was to use a "counterfactual test"[18] which asked: would a firm that did not have market power do the same things in a competitive market? As the Privy Council put it in *Telecom Corporation of New Zealand Ltd v Clear Communications Ltd*[19]

> it cannot be said that a person in a dominant market position "uses" that position for the purposes of s36 if he acts in a way which a person not in a dominant position but otherwise in the same circumstances would have acted; … a monopolist is entitled, like everyone else, to compete with its competitors: if it is not permitted to do so it would be holding an umbrella over inefficient competitors.

This echoed a standard refrain in antitrust debates, that the goal is "protection of the process of competition, not of competitors". As Judge Learned Hand put it in 1945[20],

> The successful competitor, having been urged to compete, must not be turned upon when he wins.

In the hands of Chicago adherents this became the argument that any regulatory intervention that benefits any competitor or competitors at the expense of an

---

[17] The original wording was "use" of market power; the 2001 switch to "take advantage of" made no substantive difference. The same applies to the 2001 change of wording from the original "dominant position in a market" to "substantial degree of power in a market".

[18] A strong critique of the counterfactual test in the New Zealand context is Keene et al 2010.

[19] [1995] 1 NZLR 385.

[20] *United States v Aluminium C. of America*, 148 F.2nd 416 (2d Cir. 1945), at 430.

incumbent firm is a distortion of the optimal market outcome. (Hovenkamp 2019; Hovenkamp and Morton, 2020.) Whatever real-world firms were doing could, in Chicago terms, be characterised as just the normal process of competition at work. That in turn meant that virtually any conduct by a firm with power in a market could be defended. In 2019 a major law firm noted that "New Zealand is the only country with modern competition law that requires an anti-competitive purpose and does not consider the effects of the conduct" (MintnerEllisonRuddWatts, 2019).

In 2015, the manifest inadequacy of section 36 was highlighted at a Commerce Commission conference (Gavil, 2015, p.1046):

> Reliance on the counterfactual test … will fail to condemn conduct that warrants prohibition, precisely because it fails to attribute any significance to the dominant firm's market power.

. Finally in 2022 the New Zealand Parliament legislated to include an "effects test" in section 36[21].

Official reluctance to sanction monopolistic conduct has meant that vertical integration between wholesale and retail levels of supposedly "competitive" industries has been allowed to develop without regard to the powerfully anti-competitive and price-gouging consequences. Building hardware provides an example. In 2022, with a housing construction boom underway, the country's main manufacturer of the plaster wallboard used to line New Zealand houses restricted supply to independent builders while allowing its own affiliated company to stockpile the material. With 95% of the market in the hands of the dominant firm, and building regulations carefully tailored (under systematic lobbying from the dominant firm) to prevent the use of competing products including imports, many independent builders were forced out of business and pressure mounted on the Government to intervene.

This case is ongoing as of July 2022, but previous examples of similarly exclusionary conduct that avoided any sanctions were a 2013-14 Commerce Commission inquiry into plasterboard that cleared the dominant firm of any breach of section 36[22], and a 2004 court case in which the Commerce Commission suffered a particularly demoralising defeat over tied bundling[23]. An independent producer of building insulation entered the market in competition with Carter Holt Harvey's existing product ("Thick Pink Batts"). In response CHH moved to withhold all its numerous lines of building hardware from any retailer that carried

---

Commerce Amendment Act 2022, https://www.legislation.govt.nz/act/public/2022/0011/latest/096be8ed81bece42.pdf .

22 Winstone Wallboards Ltd Investigation Closure Report 22 December 2014, https://comcom.govt.nz/__data/assets/pdf_file/0028/94393/Winstone-Wallboards-Limited-Investigation-closure-report-22-December-2014.pdf .

23 *Carter Holt Harvey v Commerce Commission* [2006] 1 NZLR 145, [2004]UKPC 37, https://www.casemine.com/judgement/in/5779fc2fe561096c93131a3e .

the competitor's product. The Privy Council found this to be permissible under the counterfactual test (Bertram 2006a).

Merit appeals

The OECD's "constraints on the regulator's discretion" through appeals on merit to the courts was initially missing in the New Zealand legislation, but its introduction via a 2008 Commerce Act amendment – enthusiastically promoted by big business interests - has proved a powerful channel for industry capture, using the threat of dragging the regulator into expensive court cases that suck its litigation budget dry while establishing strongly pro-monopoly precedents.

A dramatic illustration was a 2013case[24] in which airports, gas pipeline companies and electricity generators challenged the Commerce Commission's first round of cost-based regulatory decisions, on grounds that traversed the entire miserable history of US Supreme Court litigation between *Smith v Ames*[25] in 1898 and *Hope Natural Gas*[26] in 1944.[27] The issue was the valuations attached to those companies' fixed assets, which had been massively revalued upwards during the preceding two decades of unregulated monopoly pricing. Having agreed, under remorseless industry and political pressure, to treat the resulting inflated asset values as deemed historic cost for regulatory purposes, the Commission found itself defending those valuations as a "line in the sand" against further upward revaluations. The court decision in favour of that line in the sand left the Commission thereafter fully committed to defence of the resulting network pricing, and reluctant to incur another round of legal warfare over asset valuations. Consequently the Commission now routinely allows network operators to raise prices in advance of new investment (enabling network operators to avoid the discipline of the capital market) and to recover in full the sunk cost of stranded assets.

---

24 *Wellington International Airport & Others v Commerce Commission* [2013] NZHC 3289 [11 December 2013] , https://forms.justice.govt.nz/search/Documents/pdf/jdo/53/alfresco/service/api/node/content/workspace/SpacesStore/1c117dea-b8ba-491e-ba1d-d4cd30dbe522/1c117dea-b8ba-491e-ba1d-d4cd30dbe522.pdf .

25 *Smyth v. Ames* 169 U.S. 466 (1898) https://supreme.justia.com/cases/federal/us/169/466/ .

26 *Federal Power Commission v Hope Natural Gas* 320 U.S. 591 (1944) https://supreme.justia.com/cases/federal/us/320/591/

27 In the USA under the 1890 Sherman Act and the 1914 Clayton Act, regulation to limit essential-facility pricing to reasonable levels was the subject of extensive litigation on the crucial issue of how a monopoly firm's fixed assets should be valued in calculating its reasonable costs. Central to the *Hope* decision was the proposition that regulated utility rates should be set on the basis of the historic cost of prudently-incurred investment. Investors in a monopoly business had the right to receive a "return on and of" what they actually spent to set up the business, but no more. The resulting pricing formula corresponds to Adam Smith's "natural price" and Alfred Marshall's "normal price".

Transparency

Transparency in the New Zealand regulatory context takes the form of "information disclosure", which has been massively counter-productive – partly because of the massive costs of achieving any discipline on monopolists because of assymetric information, and, equally important, because the anti-regulatory ideological colour of Governments throughout the 1980s, 1990s and 2000s meant that the disclosed information was not processed and disseminated in a way that might have made it accessible to the citizenry at large, so that the procedure was quickly discredited as a regulatory constraint on monopolists' behaviour (Bertram 1999, 2014; Bertram and Twaddle 2005). (It has, however, proved effective as a coordination device for emerging cartels in the utility sectors.) At first, in the almost completely deregulated 1990s and early 2000s, the detailed information disclosure requirements on electricity and gas companies revealed ample evidence of price-gouging and anticompetitive conduct, but this evidence was disregarded or discounted by officials and ministers. Then, as disclosure requirements became increasingly labrynthine (with enthusiastic industry encouragement) and the disclosed material ceased (after 2008) to be published in the *New Zealand Gazette*, it became impenetrable to all except the most committed analysts, virtually all of whom are employed by or contracted to the big industry players.

3. Conclusion

In 1993, commenting on the unfolding neoliberal policy regime in New Zealand, I suggested that (Bertram 1993 p.49)

> the growing conviction among key officials involved in economic management that the new classical models were correct, and that policy interventions would be ineffective, contributed to a decline in the competence of the State to undertake such interventions. The actual effects of any policy package, thus, depend upon the quality and attitudes of the policy agency as much as on the concrete measures contained in the package itself.

The fact that New Zealand's default position is non-regulation unless a politician determines otherwise has produced a strongly gun-shy mindset both in regulatory agencies and in the judiciary, echoing the persistent neoliberal culture within key departments of government. Regulation of monopoly profit-taking has become the subject of a "chicken game" between politicians and big business, with regulators on the sideline.

Effective regulation of conduct in a market economy does not easily reduce to any single critical requirement. Rather, it flows from a constellation of mutually-supporting elements: appropriate legislation, clear codified criteria to measure compliance; smoothly-operating regulatory institutions with clear legitimacy, expert staff, and an enforcement mandate; and over all a political culture of

recognition and respect for regulators. The breakdown of a pre-existing regulatory constellation lets loose familiar pathologies: abuse of monopoly power to price-gouge consumers and eliminate competitors; unbridled pursuit of self-interest degrading the quality of services and products; reduced health, safety and wages in workplaces; and unchecked environmental degradation.

Mazzucato (2021 pp.21 and 26) identifies a parallel problem in the UK:

> We live in an era in which … a flawed ideology about the role of government has infiltrated our expectations of what it can do … problematic theories about government lead to problematic practices that… get in the way of a mission-oriented approach.

The neoliberal revolution of the 1980s and 1990s had a particularly strong deregulatory impact in New Zealand, sweeping away established regulatory institutions and practices while converting national policy to a culture of non-regulation. Reconstruction of regulatory institutions and culture has been piecemeal, and has faced entrenched opposition from powerful vested interests consolidated during the unregulated decades.

In Bertram (2021 p.35) I have expanded on this point:

> With deregulation and a limited role of government written into [New Zealand] statutes and embodied in regulatory practice, the [rent-seeking and regulatory capture] pathologies identified and described by Buchanan, Tullock, Stigler and their collaborators became more, rather than less, prevalent in the New Zealand regulatory landscape. Privatisation opened the way for looting; the Commerce Act and new regulatory guidelines enabled rather than blocked anticompetitive practices and monopolistic rent taking; relaxed oversight meant that foreign direct investment became more extractive and less productive. From relatively inclusive politics and strong regulatory enforcement, New Zealand shifted towards more extractive institutions and weaker regulation. As a result, market power is exercised by the current business and financial elite in ways that have worsened wealth and income distributions, imposed deadweight burdens (both static and dynamic) on the economy, and now confront policymakers with roadblocks to achieving more inclusive institutions and pursuing a 'wellbeing' agenda.

Just as the original top-down imposition of a neoliberal regime was done without any clear mandate from the wider public, so the defence of deregulation continues to be undertaken by the Government and the high-level business lobbying organisations, while public opinion and the press have become increasingly impatient with regulatory inaction. The tide of public opinion may be flowing in favour of stronger antitrust action, but there is not yet any political party willing to seek a mandate accordingly. Until there is a shift at the top of the political system, full recovery of regulatory governance remains only "pending". Nevertheless, there have recently been tentative steps towards more regulatory restraint on the exercise of market power. These include the 2018 reintroduction of Commerce Commission "competition studies", the 2022 inclusion of an effects

test in section 36 of the Commerce Act, and the politically-explosive evidence of excessive margins and abuse of market power in the context of a sharp increase in inflationary pressure on household budgets during 2022.

References

Arndt C., A. C. Baker, T. Querbach and R. Schultz (2015) *2015 indicators of regulatory policy and governance: design, methodology and key results*, OECD Regulatory Policy Working Papers No. 1, http://www.oecd-ilibrary.org/governance/2015-indicators-of-regulatorypolicy-and-governance_5jrnwqm3zp43-en

Bertram G. (1993) Keynesianism, Neoclassicism and the State. Chapter 2 in C. Rudd and B. Roper, editors, *State and Economy in New Zealand*. Auckland: Oxford University Press, 1993.

Bertram G. (1999) Light Handed Disciplines on the Market power of Network Owners: New Zealand's Pipeline Access Code and Information Disclosure Regulations-. *Victoria Economic Commentaries*, pages 9-24, March. https://geoffbertram.files.wordpress.com/2021/12/light-handed_disciplines_on_gas_pipelines.pdf .

Bertram G. (2004a) The New Zealand Economy Since 1984: Elite Succession, Income Distribution and Economic Growth in a Small Trading Economy. *GeoJournal*, 59(2):93-106. https://geoffbertram.files.wordpress.com/2021/12/new_zealand_since_1984.pdf

Bertram G. (2004b) What's wrong with New Zealand's public benefit test? *New Zealand Economic Papers*, 38(2):265-277, December. [.pdf]

Bertram G. (2006a) Exclusionary bundling, predatory pricing, and section 36: Carter Holt Harvey Products Group Ltd v Commerce Commission. *Waikato Law Review* 14: 17-33. http://www.nzlii.org/nz/journals/WkoLawRw/2006/2.html .

Bertram G. (2006b) Restructuring of the New Zealand Electricity Sector, 1984-2005. In F.P. Sioshansi and W. Pfaffenberger (eds) *International Experience in Restructured Electricity Markets: What Works, What Does Not, and Why?* Amsterdam: Elsevier. https://geoffbertram.files.wordpress.com/2022/03/chapter-in-sioshansi-and-pfaffenberger-2006-scan.pdf .

Bertram G. (2009) The New Zealand Economy, 1900-2000", Chapter 22 in G. Byrnes (ed) *The New Oxford History of New Zealand*. Melbourne: Oxford University Press. https://geoffbertram.files.wordpress.com/2022/06/oxford-history-complete-1.pdf

Bertram G. (2010) Deregulatory Irresponsibility: Takings, Transfers and Transcendental Institutionalism. *Policy Quarterly*, 6(2):48-53, May. https://ojs.victoria.ac.nz/pq/article/view/4336/3838 .

Bertram G. (2011) A comparative world-systems analysis of settler colonies in the Hispanic and Anglo realms. *Journal of New Zealand Studies*, 11: 11-34. https://geoffbertram.files.wordpress.com/2021/12/settler-economies-jnzs-2011.pdf .

Bertram G. (2013) Weak regulation, rising margins, and asset revaluations: New Zealand's failing experiment in electricity reform. In Fereidoon Sioshansi, editor, *Evolution of Global Electricity Markets: new paradigms, new challenges, new approaches*, chapter 21, pages 645-628. Amsterdam: Elsevier. https://geoffbertram.files.wordpress.com/2021/12/weak-regulation-rising-margins-and-asset-revaluations.pdf .

Bertram G. (2014) Light-handed regulation of the energy sectors. In *Flawed theory, failed practice: light-handed regulation in New Zealand*. Welington: NZ Fabian Society, 2014, https://geoffbertram.files.wordpress.com/2021/12/fabians-book-chapter-2014.pdf

Bertram G. (2020) Why the Commerce Act 1986 is unfit for Purpose. *Policy Quarterly*, 16(3):80-87, August. https://ojs.victoria.ac.nz/pq/article/view/6561/5725 .

Bertram G. (2021) Regulatory capture in product markets and the power of business interests. *Policy Quarterly*, 17(2):35-44, May. https://ojs.victoria.ac.nz/pq/article/view/6821/5969 .

Bertram G. (2022) Shrinking the state 2.0. *Policy Quarterly* 18(1): 32-36.

Bertram G. and S. Chapple (2017) Getting consumer rights out from under the rug. *Newsroom Ideasroom*, December. https://geoffbertram.files.wordpress.com/2021/12/newsroom-dec-13-2017-commerce-act.pdf

Bertram, G and B. Rosenberg (2022) *How policy and institutions affect the shares of wages, profit, and rent in New Zealand* . Working paper, Institute for Governance and Policy Studies, Victoria University or Wellington.

Bertram G., I. Dempster and S. Terry (2000) *Rates of return at Auckland International Airport*, report prepared for Air New Zealand, August. https://geoffbertram.files.wordpress.com/2021/12/rates_of_return_at_auckland_airport.pdf .

Bertram G. and D. Twaddle (2005). Price-Cost Margins and Profit Rates in New Zealand Electricity Distribution Networks Since 1994: The Cost of Light-Handed Regulation. *Journal of Regulatory Economics*, 27(3):281-307. https://geoffbertram.files.wordpress.com/2021/12/price-cost-margins-and-profit-rates-in-new-zealand-electricity-distribution-networks-since-1994.pdf

Boston, J., J. Martin, J. Pallot and P. Walsh (eds) (1991) *Reshaping the State: New Zealand's bureaucratic revolution* Auckland: Oxford University Press.

Browne, O., S. Poletti, and D. Young (2012) Simulating market powering in the NZ electricity market. *New Zealand Economic Papers* 46(1),35–50.

Commerce Commission (2000) *Final Report: Part IV Inquiry into Airfield Activities at Auckland, Wellington, and Christchurch International Airports*, August, https://comcom.govt.nz/__data/assets/pdf_file/0024/90285/Part-4-inquiry-into-airfield-activities-at-Auckland,-Wellington,-and-Christchurch-international-airports-1-August-2002.pdf with executive summary at https://comcom.govt.nz/__data/assets/pdf_file/0024/90285/Part-4-inquiry-into-airfield-activities-at-Auckland,-Wellington,-and-Christchurch-international-airports-1-August-2002.pdf .

Commerce Commission (2009) *Investigation Report: Commerce Act 1986 s.27, s.30 and s.36 electricity investigation* https://comcom.govt.nz/s-uat/redirect?collection=comcom-www-meta&url=https%3A%2F%2Fcomcom.govt.nz%2F__data%2Fassets%2Fpdf_file%2F0025%2F219094%2FElectricity-investigation-Investigation-report-21-May-2009.PDF&auth=B7DrxGPD35zFGels55KzlQ&profile=noise&rank=2&query=Investigation+Report%3A+Commerce+Act+1986+s.27%2C+s.30+and+s.36+electricity+investigation .

Commerce Commission (2019a) *Market study into the retail fuel sector: Final report* December. https://comcom.govt.nz/__data/assets/pdf_file/0028/193915/Retail-fuel-market-study-Final-report-5-December-2019.PDF

Commerce Commission (2019b) 'Taking advantage of market power', https://comcom.govt.nz/business/avoiding-anti-competitive-behaviour/takingadvantage-of-market-power .

Commerce Commission (2022) Market study into the retail grocery sector: Final report, 8 March. https://comcom.govt.nz/__data/assets/pdf_file/0024/278403/Market-Study-into-the-retail-grocery-sector-Final-report-8-March-2022.pdf

Court of Appeal of New Zealand (1999) *Vector Ltd (formerly Mercury Energy Ltd) v Transpower New Zealand Ltd* [1999] NZCA 167; [1999] 3 NZLR 646; (1999) 6 NZBLC 102,908; (1999) 9 TCLR 238 (31 August 1999). http://www.nzlii.org/nz/cases/NZCA/1999/167.html .

Curtin, D. (2016) *Cross-submission on the Targeted Review of the Commerce Act* https://www.mbie.govt.nz/dmsdocument/2299-economics-new-zealand-targeted-review-commerce-act-phase-one-cross-submission-pdf .

Easton, B. (1997a) *In stormy seas: the post-war New Zealand economy* Dunedin: University of Otago Press.

Easton, B. (1997b) *The commercialisation of New Zealand* Auckland: Auckland University Press.

Feffer, J. (2007) The Self-Hating State. *Foreign Policy in Focus* 2(16), April. https://fpif.org/the_self-hating_state/ .

Gavil, A.I. (2015) 'Imagining a counterfactual section 36: rebalancing New Zealand's competition law framework', *Victoria University of Wellington Law Review*, 456 (4), December, pp.1043–80.

Gönenç R., M. Maher and G. Nicoletti (2001) "The implementation and the effects of regulatory reform: past experience and current issues" *OECD Economic Studies* No. 32, 2001/I, https://www.oecd-ilibrary.org/the-implementation-and-the-effects-of-regulatory-reform_5lgsjhvj8321.pdf?itemId=%2Fcontent%2Fpaper%2F413754754615&mimeType=pdf .

Gregory, R. (2003) 'All the king's horses and all the king's men: putting New Zealand's public sector back together again', *International Public Management Review*, 4 (2): 41-58. https://journals.sfu.ca/ipmr/index.php/ipmr/article/view/215/215 .

Hovenkamp, H.J. (2019) 'Is antitrust's consumer welfare principle imperilled?', *Journal of Corporate Law*, 45 (1), pp.65–94

Hovenkamp, H.J. and F.S. Morton (2020) 'Framing the Chicago School of antitrust analysis', *University of Pennsylvania Law Review* 168(7):1843-1878. . https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=3115&context=faculty_scholarship .

High Court of New Zealand (2013) *Wellington International Airport & Others v Commerce Commission* [2013] NZHC 3289 [11 December 2013] https://forms.justice.govt.nz/search/Documents/pdf/jdo/53/alfresco/service/api/node/content/workspace/SpacesStore/1c117dea-b8ba-491e-ba1d-d4cd30dbe522/1c117dea-b8ba-491e-ba1d-d4cd30dbe522.pdf .

Jesson, B. (1999) *Only Their Purpose is Mad: the money men take over New Zealand*, Palmerston North: Dunmore Press.

Keene, S., V. Irwin and A. Fincham (2010) *The 0867 case - death knell of the counterfactual?* Paper for BrightStar Competition Law and Regulatory Review Conference 22 - 23 February 2010, https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=&cad=rja&uact=8&ved=2ahUKEwi26IaNla74AhVFSGwGHepmCBUQFnoECAoQAQ&url=https%3A%2F%2Fwww.russellmcveagh.com%2Fgetmedia%2Fe88ee3f4-844f-460f-93e3-b6328bf68f7d%2FDeathKnellOftheCounterfactual-slides.pdf%2F&usg=AOvVaw2Dcz6eM0jxl56_72DHv01E

Kelsey, J. (1995) *The New Zealand experiment: a world model for structural adjustment* Wellington: Bridget Williams Books.

Lewis, N. (2004) Geographies of the New Zealand Experiment *Geojournal* 59(2): 161-166.

Lyon, D. (2011) *The development and performance of airports in New Zealand as commercial entities* Massey University PhD thesis, Palmerston North.

Mazzucato, M. (2021) *Mission economy: a moonshot guide to changing capitalism* Milton Keynes: Allen Lane.

MintnerEllisonRuddWatts (2019) 'Section 36 of the Commerce Act back in the spotlight', https://minterellison.co.nz/our-view/section-36-of-thecommerce-act-back-in-the-spotlight

New Zealand Treasury (1987) *Government Management: brief to the incoming government 1987* Vol.1. Wellington: Government Printing Office, https://www.treasury.govt.nz/publications/bim/government-management-brief-incoming-government-1987-volume-i

OECD (2021), *OECD Regulatory Policy Outlook 2021*, Paris: OECD Publishing.

Poletti, S. (2021) Market Power in the NZ wholesale market 2010-2016 *Energy Economics* 94, February.

Smith, A. (1759) *The theory of moral sentiments*. London: A. Kincaid.

Smith, W. and H. Montgomery (2004) Introduction: Reinventing Government – emerging geographies in the aftermath of the 1984 reforms in New Zealand. *Geojournal* 59(21): 91-92.

Taggart, M. (1990) *Corporatisation, privatisation and public law* Inaugural lecture, University of Auckland, New Zealand Legal Research Foundation Occasional Paper 31, September. http://www.nzlii.org/nz/journals/NZLRFOP/1990/31.html .

Taggart, M.(2008) "Common law price control, state-owned enterprises and the level playing field", in L. Pearson, C. Harlow and M. Taggart (eds) *Administrative Law in a Changing State: Essays in Honour of Mark Aronson*, Hart Publishing.

World Bank (2020) *Doing Business 2020: comparing business regulation in 190 countries*, https://openknowledge.worldbank.org/bitstream/handle/10986/32436/9781464814402.pdf .