International developments

From New Zealand

New Zealand's Commerce Commission enforces both the Commerce Act 1986, which contains restrictive trade practices provisions, and the Fair Trading Act 1986, which deals with consumer protection matters.

The following items were extracted from the November 1996 issue of the Commerce Commission's new newsletter, Compliance, *and the December 1996/January 1997 issue of* Fair's Fair. *The first deals with the Fair Trading Act in relation to franchising, an area that the ACCC is currently addressing through, for example, its submission to the fair trading inquiry.*

Franchising breaches under the Fair Trading Act

Section 22 of the Fair Trading Act creates two offences relating to franchise operations. The first relates to franchises carried out from home. The second relates to any franchise operation no matter where it originates as long as the franchise is to be run in New Zealand. Both offences deal with false or misleading representations made by the franchise seller about the profitability, risk or any other material aspects of the franchise. It is possible following a successful criminal prosecution undertaken by the Commerce Commission, or civil claim taken by the purchaser of a franchise, for compensation to be sought under s. 43 of the Act.

To succeed under s. 22 of the Act, it is necessary to establish that the seller of the franchise made a false or misleading representation, that the representation relates to a key part of the franchise operation, and that at the time the representation was made the basis for making it was flawed.

It is not enough to prove that what the franchise seller said has not happened. For example, if the franchise seller said you will make $100 000 profit in the first year, and only $5000 was made, this is not sufficient for a case under s. 22. To be successful it is necessary to ascertain the basis on which the representation was made, and prove that the basis does not support the representation. If the seller made the representation on reasonable material that they had obtained either themselves or from independent sources, then that representation can neither be misleading nor false.

If part of the franchise sale is to offer training, backup, support, a hot line or other facilities, it is necessary to ascertain whether the seller of the franchise has the ability to provide these facilities. If at the time the seller made these representations, they had both the infrastructure and support staff enabling them to offer the facilities, then there is unlikely to be a contravention of s. 22.

If the seller of the franchise based his or her representation on faulty research, faulty methodology and faulty analysis of the potential markets for operating the franchise in, but could reasonably base the representation on this basis, there is unlikely to be a false or misleading representation in terms of s. 22 of the Act. However, if no reasonable person could have based their representation on this data, that would equate to a false or misleading representation for the purposes of s. 22.

The leading case in this area is the case of *Commerce Commission v Chalmers* (1990) 3

TCLR 522. The defendants in this case were officers of a company which attempted to set up a franchise operation to distribute video tapes. The company issued a prospectus to potential franchise purchasers stating that training would be given, and that a van containing a 'comprehensive range of the latest movies' would be provided. The company also stated that new releases would be made available for purchase, and included projected earning figures.

The evidence presented in Court by the Commission was that those who had purchased the franchise had received no training, and had been unable to obtain the projected income. The main reasons were that the video tapes which were provided were second rate, and that the franchise purchasers were not provided with new releases.

Judge Inglis QC said at p. 553 of the report:

> ... the real effect of such cases is to provide a warning against being too ready to infer that because a representation as to future events has turned out to be wrong it must therefore, and for that reason alone, have been false or misleading ... It is not in my opinion a simple matter of saying that when a representation is a forecast or prediction as to the future it has to be proved that the representor 'did not believe that the forecast or predictions would be satisfied or was recklessly indifferent concerning them' before it can be held that the representation was false or misleading ... for the representation may not in fact be merely a forecast or prediction; it may also be a representation as to the representor's state of mind, state of knowledge, expertise, that he had no proper basis for making the representation, that he had the present intention to make good the forecast, that he had the means to make good — in other words his representation needs to be evaluated in light of all the surrounding circumstances in order to determine its true content and character.

Therefore to put together a successful prosecution, or indeed a successful civil claim for damages, it is necessary to look behind the representations that were made by the seller of the franchise to ascertain the basis for those representations. If the basis for those representations is itself so corrupt, or the basis does not support the representations which were made, then it is possible to have judgment entered against the seller of the franchise under s. 22 of the Act. However, if the representations logically flow from that basis, and that basis is itself relatively firm and robust, then there can be no success under s. 22 of the Act.

A message to government organisations

The Commission believes that an important message to all government bodies in trade that enter into agreements to control competition, or have the power to grant concessions, licences or other rights, has come out of an investigation into a possible breach of the Commerce Act.

It has told the Department of Conservation (DOC) and two tourist launch operators at Milford Sound that they cannot restrict competition by using DOC's power to grant concession licences. The Commission is aware that organisations other than DOC control similar rights, and it is keen to prevent breaches of the Act from occurring in other situations.

The problems at Milford Sound arose through formal agreements made between the Minister of Conservation and Milford Sound Development Authority Limited (MDA) at a time when Milford Sound was being developed to handle increasing numbers of visitors.

The agreements were in the form of a Deed and a variation to that Deed, and were signed respectively in 1990 and 1992.

The effect of the agreements was that the two existing tourist launch operators, Fiordland Travel Ltd and Tourism Milford Ltd (which, together with Southland District Council, own MDA), could operate without restriction, but that DOC would place restrictions on other tourist launch operators so they:

- could not run the popular short sightseeing trips;
- could not carry more than 50 passengers each trip;
- could not sell food, drinks and souvenirs from the visitor centre;
- had to operate for 365 days each year; and

- had to operate from a 'development zone' where the facilities were controlled by MDA.

The agreements also allowed that, if anybody applied to DOC for a concession licence to operate at Milford Sound, DOC would first give Fiordland Travel and Tourism Milford the option to increase their own services. If neither did so, a concession licence could be given to a competitor.

The Commission's view was that these restrictions had the effect of substantially lessening competition in the market for the provision of sightseeing tourist activities in Fiordland National Park.

The matter was resolved through settlements with the parties.

The message to government bodies is that unless they are specifically authorised by other legislation to regulate competition they could risk breaching the Commerce Act by entering into agreements which substantially lessen competition in a market or which aim to do so.

In addition, an organisation which dominates a market for the granting of concessions, licences or other rights must be aware that it should not use that dominance to restrict entry to a market, prevent or deter competitive conduct, or eliminate any person from a market.

Product safety settlements

In two separate settlements the Commission received undertakings in relation to breaches of the Children's Night Clothes Product Safety Standard.

Nelson company, Maruia Nature Company, undertook to recall a children's Birds of the Night night shirt because it failed flame spread tests, with the flames spreading through the night shirts almost twice as quickly as the standard allows.

The test showed that the night shirt was made from flammable fabric and did not meet the measurements set in the standard for form fitting styles. The shirts were 100 per cent cotton.

Maruia undertook to recall and stop selling the shirts, to establish a compliance program and to report to the Commission on the recall.

Deka NZ Ltd undertook to remove fire safety labelling and to relabel nearly 5000 items of children's Ladybird range night clothing after the Commission raised concerns.

It has removed labels from size 000 infant gowns that are not covered by the safety standard because the standard does not cover clothing for babies who cannot yet crawl. It applies to night clothes for children aged between six months and 14 years and the Commission was concerned that customers and retailers would be confused about what the standard covers.

Deka attached correct fire safety labels to 4456 romper suits which had none. It also destroyed 500 size 00 infant gowns because there was concern that these might be covered by the standard yet not comply with it.

Deka undertook also to establish a compliance system and report on the numbers of garments relabelled or removed from sale.

Power acquisition cleared

In November 1996 the Commission cleared CentralPower to acquire 100 per cent of the shares in Electro Power.

The Commission concluded that the proposed merger would not result in any person acquiring or strengthening a dominant position in any market.

Its view is that the merger would result in limited aggregation in the competitive national retail electricity market and a minimal loss of cross-border competition in the merged entity's electricity distribution market. However, that loss of competition is not such that it would give rise to dominance concerns.

The Commission also concluded that the competitive constraints currently faced by the companies would not be significantly changed.

From Canada

The following items are based on press releases from the Competition Bureau, Canada.

Amendments to the Competition Act

Amendments to the Competition Act were introduced on 7 November 1996 in the House of Commons by Industry Minister, John Manley. This initiative aims to help promote a healthier marketplace, one of the key features of the government's jobs and growth agenda, by providing more effective tools for competition law enforcement. The amendments are intended to provide significant benefits to consumers and businesses.

The proposed amendments are in the areas of notifiable transactions, prohibition orders, misleading advertising, deceptive telemarketing and regular price claims.

Notifiable transactions

In the case of large merger transactions, the parties are required to provide the Competition Bureau with advance notification of the proposed transaction, and wait a prescribed period of time before completing it, thereby giving the Bureau an opportunity to examine the transaction and determine whether it will have a harmful impact on competition.

The amendments will more clearly identify the parties required to pre-notify and supply information to the Bureau, and will clarify when the acquisition of interests in a combination is subject to pre-notification. The information to be submitted will be more relevant and more clearly outlined in the regulations.

Waiting periods will be lengthened, and authority to shorten the waiting periods will be delegated to a person authorised by the Director. Conditions for obtaining interim orders will be relaxed so that the Director may, while conducting reviews, delay the closing of a merger that gives rise to serious concerns. Failure to pre-notify will no longer be punishable by imprisonment, but the fine will be raised to a maximum of CND$50 000.

Prohibition orders

Section 34 of the Competition Act provides that a court may issue an order prohibiting a person from continuing or repeating an offence, or from doing any act or thing directed toward the continuation or repetition of an offence. These orders may also be obtained without securing a conviction.

The Bureau said that, although prohibition orders have been widely used and are very useful in prohibiting certain conduct, they do not authorise the issuance of prescriptive terms which would require that the accused take positive steps or engage in certain conduct. Currently, also, there are no provisions in the Act that allow for a prohibition order to be varied or rescinded.

The proposed amendments will allow a prescriptive term to be included in an order if all parties to the order consent. The Act will provide the courts with the power to vary or rescind any order.

Misleading advertising and deceptive marketing practices

Proposed amendments will change the focus of the misleading advertising and deceptive marketing practices provisions, from punishment to quick and efficient compliance, through the creation of a criminal/civil regime.

A criminal sanction, with a subjective mental element, will remain in place to deal with the most serious cases of misleading advertising. However, most of the existing misleading advertising and deceptive marketing practices provisions would be treated as reviewable matters under a new civil regime.

The Director of Investigation and Research, who is responsible for the administration and enforcement of the Competition Act, could refer reviewable matters to a single judicial member of the Competition Tribunal, the Federal Court of Canada, the trial division of the Federal Court of Canada, or a provincial superior court. These adjudicators would have access to a range of remedies, including cease and desist orders, interim cease and desist orders, administrative monetary penalties, information notices and consent orders.

Deceptive telemarketing

The amendments include a new criminal offence provision to deal with deceptive telemarketing. It will apply to situations involving the practice of using interactive telephone communications for the purpose of promoting the supply of a product or a business interest. Telemarketers will be required to disclose certain types of information during the telephone call.

Special provisions will be enacted to expand the responsibility of corporations, and their officers and directors, for ensuring compliance with the law.

The law will also be amended to make it easier for courts to issue interim injunctions to stop the operations of alleged fraudulent telemarketers.

Regular price claims

The amendments will revise and clarify the law regarding comparative price advertisers by retailers. Retailers as well as some consumer groups had expressed concern that the existing law did not clearly specify the circumstances under which ordinary price claims could be made.

Under the amendments, misleading regular price representations will be made reviewable matters under the Act. The legitimacy of regular price claims will be determined according to two alternative tests: the price or prices at which a substantial volume of recent sales has occurred; and the price or prices at which the product was recently offered for sale in good faith for a substantial period of time prior to the sale.

Joint Canada–US task force on deceptive marketing practices

On 10 September 1996 the Acting Director of Investigation and Research under the Competition Act announced that the Competition Bureau and the United States Federal Trade Commission had signed an agreement establishing a joint task force on cross-border deceptive marketing practices.

The task force is intended to provide a framework to promote cooperation between law enforcement agencies in Canada and the US with respect to deceptive marketing practices with a transborder component. The task force will operate within the laws, policies and practices of each country. It will focus on operations based in either country which target the residents of the other country.

The agreement follows on from the Canada–US Competition Policy Agreement signed on 3 August 1995 by the governments of the two countries. That agreement established a framework for closer relations between Canada and the US regarding the enforcement of their competition and deceptive marketing practices laws.

From the USA

The following update on the ADM matter is based on a news release from the US Department of Justice dated 3 December 1996.

Former ADM executives indicted

On 3 December 1996 a Chicago federal grand jury indicted three former top Archer Daniels Midland Co. executives and one Japanese executive for conspiring to fix prices and allocate sales in the lysine market worldwide. A Korean company also agreed to plead guilty to separate charges and pay a $1.25 million fine for its role in the conspiracy.

This is the third round of charges brought as a result of the Department's investigation into the food and feed additives industry. In October 1996 ADM pleaded guilty and was sentenced to pay a $100 million criminal fine for its role in two international conspiracies to fix prices and allocate sales in the lysine and citric acid markets worldwide. Lysine, a $600 million a year industry, is used by farmers as a feed additive to ensure the proper growth of swine and poultry.

The defendants will be arraigned at a later date in the federal court in Chicago.

The Department's investigation into the lysine, citric acid and high fructose corn syrup markets continues.