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IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY
COMMERCIAL LIST

CIV 2008-404-4321

BETWEEN	THE COMMERCE COMMISSION Plaintiff
AND	NEW ZEALAND DIAGNOSTIC GROUP LTD First Defendant
AND	HAMILTON MEDICAL LABORATORY HOLDINGS LIMITED Second Defendant
AND	PATHOLOGY ASSOCIATES LIMITED Third Defendant

Hearing: 25 June 2010

Appearances: D J Goddard QC and B Hamlin for plaintiff
O J Meech for first and second defendants
J A Craig and M S C Harrison for third defendant

Judgment: 19 July 2010

JUDGMENT OF ALLAN J

In accordance with r 11.5 I direct that the Registrar endorse this judgment with the delivery time of 2 pm on Monday 19 July 2010

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[1] In this proceeding the Commission has alleged breaches by the defendants of s 27 of the Commerce Act 1986 (the Act). The defendants having admitted liability, the Court is asked to approve a penalty of $65,000 to be imposed jointly and severally on the first and second defendants (together the NZDG defendants) and $35,000 in respect of the third defendant (PAL).

[2] The defendants' admission appears in an agreed statement of facts in which the defendants support the Commission's approach to penalty assessment.

Agreed facts

[3] Between April 2004 and about June 2006 the defendants provided community pathology testing services in the Waikato Region. They were the two major suppliers; NZDG had a greater share of the market than PAL. Between February 2004 and late 2005, NZDG negotiated to acquire PAL. Towards the end of 2005, the Commission declined clearance for the merger of NZDG and another provider of pathology services on the basis that the Commission was not satisfied that the merger would not have had the likely effect of substantially lessening competition.

[4] Prices for the services were fixed by contract between each of the community laboratories (here NZDG and PAL) and the Health Funding Authority, and more recently the Waikato District Health Board (WDHB). The WDHB paid the defendants on a fee for service basis, calculated in accordance with a schedule of fees set out in the contract. Patients were not charged.

[5] NZDG and PAL negotiated arrangements with a number of GP practices for the provision of collection services. The defendants would organise the collection of samples from such practices.

[6] NZDG and PAL each held funding contracts with the WDHB for the provision of pathology services. In consequence, there was no price competition in

respect of sample testing. But there was competition between the defendants in respect of quality and the terms of service, including the terms upon which certain GP practices undertook sample collection services for the defendants.

[7] For a short period between January 2004 and 14 May 2004, the Waikato Hospital Laboratory (part of the WDHB) itself sought to enter the relevant markets by offering community testing services to certain general practitioners.

[8] In March 2004, representatives of the NZDG group and the WDHB (but not PAL) met and discussed potential changes to pathology services, including:

a) increased cooperation between the NZDG group and PAL;

b) the hospital laboratory's attempts to enter the relevant markets; and

c) the desirability of limiting competition in respect of collection payments.

[9] On or about 14 May 2004, the WDHB convened a meeting involving representatives of the NZDG group, PAL, the WDHB and the hospital laboratory. At that meeting the WDHB sought and obtained the agreement of the other parties to what was in effect a moratorium, the key terms of which were:

a) NZDG and PAL would not compete to win customers through the use of collection payments;

b) The WDHB (through the hospital laboratory) would refrain from seeking to provide community testing pathology services; and

c) NZDG and PAL would look at options for work that they may be able to direct to the hospital laboratory rather than elsewhere.

[10] It is common ground that the moratorium had as its likely effect and as its substantial purpose, the significant lessening of competition in the market for community pathology testing in the Waikato region because it:

a) Reduced the potential competitive constraint that the hospital laboratory could have imposed on NZDG and PAL in the relevant market:

b) Reduced the competitive constraint that NZDG and PAL imposed on each other in that market;

c) Reduced competition between NZDG and PAL on quality and terms of service, including terms relating to collection payments made to referrers, to the extent that these were permitted by the funding contracts with the WDHB.

[11] The parties to the moratorium duly carried it into effect. The WDHB immediately stopped seeking to provide community testing pathology services. The defendants refrained from competing for customers, and advised each other of prospective clients (although it must be said there is evidence that on the odd occasion limited competition continued).

Relevant statutory provisions

[12] The defendants accept that by entering into the moratorium they acted in breach of s 27 of the Act which relevantly provides:

> **27. Contracts, arrangements, or understandings substantially lessening competition prohibited**
>
> (1) No person shall enter into a contract or arrangement, or arrive at an understanding, containing a provision that has the purpose, or has or is likely to have the effect, of substantially lessening competition in a market.
>
> (2) No person shall give effect to a provision of a contract, arrangement, or understanding that has the purpose, or has or is likely to have the effect, of substantially lessening competition in a market.

[13] The defendants are accordingly liable to pay a pecuniary penalty by reason of the provisions of s 80 of the Act, which relevantly provides:

Pecuniary penalties

(1) If the Court is satisfied on the application of the Commission that a person—

(a) Has contravened any of the provisions of Part 2 of this Act

…

the Court may order the person to pay to the Crown such pecuniary penalty as the Court determines to be appropriate ….

(2A) In determining an appropriate penalty under this section, the Court must have regard to all relevant matters, in particular,—

(a) any exemplary damages awarded under section 82A; and

(b) in the case of a body corporate, the nature and extent of any commercial gain.

(2B) The amount of any pecuniary penalty must not, in respect of each act or omission, exceed,—

(a) in the case of an individual, $500,000; or

(b) in the case of a body corporate, the greater of—

(i) $10,000,000; or

(ii) either—

(A) if it can be readily ascertained and if the Court is satisfied that the contravention occurred in the course of producing a commercial gain, 3 times the value of any commercial gain resulting from the contravention; or

(B) if the commercial gain cannot be readily ascertained, 10% of the turnover of the body corporate and all of its interconnected bodies corporate (if any).

The Court's approach to penalty assessment

[14] It is not suggested that the Court should do other than apply ordinary sentencing principles to the assessment of an appropriate penalty. The Court is accordingly required to assess the seriousness of the offending, to identify relevant aggravating and mitigating factors, and then, having identified an appropriate starting point, to have regard to any factors specific to a defendant which might warrant an uplift or discount from the starting point.

[15] It is now well established that among the most important of the purposes and principles of sentencing in this area is that of deterrence, having regard in particular to the difficulty of detecting anti-competitive behaviour: *Commerce Commission v Koppers Wood Protection (NZ) Ltd*,[1] *Commerce Commission v Alstom Holdings SA*.[2] (See also *Commerce Commission v Koppers Arch Wood Protection (NZ) Ltd*[3] and *Commerce Commission v Koppers Arch Wood Protection (NZ) Ltd*[4]). In these cases, the Court has approached the question of penalty determination by:

a) assessing the level of penalty likely to be imposed in respect of the admitted conduct following a trial. In that regard the Court has considered penalties imposed in similar prior cases;

b) assessing the appropriate level of discount to reflect the admissions of liability by the defendants, their co-operation and a number of other mitigating factors.

[16] Formerly, s 80(2) of the Act required the Court, in determining an appropriate penalty, to have regard to all relevant matters, including:

a) The nature and extent of the act or omission;

b) The nature and extent of any loss or damage suffered by any person as a result of the act or omission;

c) The circumstances in which the act or omission took place;

d) Whether or not the person has previously been found by the Court in proceedings under the relevant part of the Act to have engaged in any similar conduct.

[17] That subsection has now been repealed. Section 80(2A) now simply requires the Court to consider "all relevant factors". It is however common ground that the

[1] (2006) 11 TCLR 581 (HC) at [30]
[2] HC Auckland CIV-2007-404-2165, 22 December 2008 at [17].
[3] HC Auckland CIV-2005-404-2080, 4 October 2006.

factors set out in the repealed s 80(2) will continue to be relevant, as will factors such as:

a) The duration of the contravening conduct;

b) The seniority of the employees or officers involved in the contravention;

c) The extent of any benefit derived from the contravening conduct;

d) The degree of market power held by the defendant;

e) The role of the defendant in the impugned conduct;

f) The size and resources of the defendant;

g) The degree of co-operation by the defendant with the Commission;

h) The fact that liability is admitted;

i) The extent to which a defendant has developed and implemented a compliance programme.

Quantum assessment

[18] Because the defendants derived very little (if any) commercial benefit from their admitted contraventions of the Act, the maximum penalty for each breach is $10 million: s 80(2B)(b)(i). Although in principle it would be possible to impose separate penalties in respect of each contravening act, it is common ground that separate penalties ought not to be imposed here because for each defendant the contravening behaviour is best seen as a single related course of conduct. Viewed in that light it is easier to determine a penalty which properly reflects the totality of the conduct concerned.

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[4] HC Auckland CIV-2005-404-2080, 8 February 2008.

[19] It is instructive to consider early New Zealand cases in which the Court has been obliged to assess an appropriate penalty for breaches of Part 2 of the Act. But care is needed in considering the first two cases cited in [15] above (which Mr Goddard calls the "*Wood Chemicals*" and "*Gas Insulated Switch Gear*" cases respectively). Significant penalties were imposed there in the context of hard core cartel activity. Mr Goddard submits, with support from other counsel, that cases such as the present ought to attract significantly lower penalties because they involve overt agreements. Indeed, the agreement in this case appears to have been voluntarily disclosed to the Commission: as to that see the observations of Miller J in *Commerce Commission v New Zealand Bus Ltd*[5].

[20] Mr Goddard refers by way of comparison (admittedly imperfect) to *Commerce Commission v Ophthalmological Society of New Zealand Inc*[6]. There the Society and a number of ophthalmologists entered into an arrangement in breach of s 27 of the Act, intending to lessen competition in the market for cataract surgery in Southland by attempting to exclude Australian surgeons. After a defended trial the High Court imposed a penalty of $100,000 on the Society, sufficient to exhaust its funds. The Society was subsequently wound up. It is to be noted that since that case, maximum penalties have doubled.

[21] But, as Mr Goddard observes, there are significant differences between that case and this. There, the arrangement was put into effect and vigorously monitored. There was an actual lessening of competition. The primary participant made a considerable gain of at least $300,000. The litigation itself was hard fought and there was no question of discounts for admissions of liability or co-operation. Moreover, there was a complete absence of remorse on the part of the principal offender. Lesser penalties were imposed on individual defendants.

[22] In my view, little assistance is to be gleaned from that case, although in a sense the scale of the activity (regional rather than national or international) provides a useful point of comparison. But a number of mitigating factors are relevant here which simply did not arise in that case.

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[5] HC Wellington CIV-2006-485-585, 29 September 2006 at [32].
[6] [2004] 3 NZLR 689 (HC).

[23] I turn to a brief consideration of those mitigating factors.

Discount for admission of liability and co-operation

[24] Mr Goddard accepts that a substantial discount is justified by reason of the defendants' admissions of liability, and their agreement to co-operate with the Commission. In previous cases discounts of between 20-50% have been allowed, depending on how early in the proceedings the admission of liability was made, and the level of assistance provided against other defendants, in particular.

[25] The Commission recommends a 33% discount. That figure is argued to be appropriate, having regard to the fact that the settlement was neither early nor late in the piece, the defendants offering to settle the proceeding after the completion of discovery but before the exchange of witness statements. The Court is also entitled to have regard to the degree of co-operation between the defendants and the Commission. Such co-operation is expressly accepted by the Commission, but has been of only limited value because there were near simultaneous settlements by both parties.

[26] Mr Goddard submits that a one-third discount is appropriate in the light of a similar discount allowed in the *Gas Insulated Switchgear* proceedings where settlement occurred at a similar stage in the litigation, and where, although assistance was proffered, it was of only limited value to the Commission.

[27] In the *Wood Chemicals* case a 50% discount was allowed, but there a very early admission of liability was made, and considerable assistance was obtained by the Commission against the remaining defendant.

[28] The Court is of course required, in assessing the discount for a liability admission, to take into account the recent judgment of the Court of Appeal in *R v Hessell*,[7] although cases under the Commerce Act have their complexities, and might not always be susceptible to a strict application of the *Hessell* tariff.

[7] [2010] 2 NZLR 298 at [15].

[29] In the present case, counsel for the defendants accept that a 33% discount is appropriate for admissions of liability and proffered co-operation, it being agreed that this is not a case for the allowance of a very substantial discount for co-operation of the sort discussed in *Hessell* at [23]. It is however appropriate to record here that the defendants:

a) Made their officers and employees available to the Commission for interview on a voluntary basis.

b) Complied with the Commission's requests for documents under s 98 of the Act and (in the case of the *NZDG* defendants) went to considerable effort and expense to recover electronic data;

c) Did not mislead or deceive the Commission during its investigations.

Impact of breaches

[30] It is agreed that the moratorium had the purpose and likely effect of substantially lessening competition in the relevant market. But in fact it did not have that effect. The Commission accepts that it is unlikely that any party suffered material loss or harm because:

a) The industry arrangements between the WDHB, the Ministry of Health and providers of pathology services (including the defendants) restricted the ability of the community laboratories to compete on price for testing services;

b) While the defendants purported to commit to and carry out the moratorium in their communications with each other, they in fact deviated from it (as noted earlier) and continued to compete in offering collection payments to referrers; and

c) The moratorium ceased once the parties were aware that the Commission had concerns about the relevant markets and was investigating the moratorium.

[31] The Commission accepts that no appreciable commercial gain was made by any party as a result of the moratorium, and that potential gains were at best limited.

[32] The imbalance in the penalties suggested by the Commission arises from the fact that the NZDG defendants enjoyed a greater market share than did PAL.

Previous contraventions

[33] No defendant has previously been found to have contravened the Act, and there have been no previous warnings by the Commission.

Compliance programmes

[34] Management of the NZDG defendants has changed substantially since the contraventions occurred. The Commission understands that the new owners are in the course of independently developing a competition or compliance programme, and in those circumstances has not sought a further commitment to any additional such programme.

[35] PAL has agreed to implement an internal competition law compliance programme to ensure future breaches of the Act do not occur. I accept that these are appropriate mitigating factors.

Resources

[36] Each defendant is a substantial company. Counsel for the defendants agree that they are in a position to pay the penalties recommended by the Commission.

Duration

[37] The contravening conduct did not continue for a significant period, and did not have a major effect on consumers in the relevant market.

Role of WDHB

[38] As earlier noted, there was nothing covert about these arrangements. Importantly for present purposes, the moratorium was not only known to the WDHB (the primary purchaser of the relevant services) but was initiated by it. I accept Mr Goddard's submission that the fact that the Board as a "major consumer" saw some benefits in limiting competition is a mitigating factor.

The Commission's submissions

[39] Against that background Mr Goddard submits that the penalty must be sufficient to ensure that the contravening conduct is unprofitable. He says that the penalties recommended by the Commission will achieve that objective, and in particular, they will substantially exceed any likely actual gain from the impugned conduct, and the likely gains from effective implementation from the moratorium.

[40] The penalty ultimately imposed by the Court should, he argues, take into account the prospect that implementation of the arrangements for any length of time could well have resulted in substantially reduced quality and service competition in the market, not only so affecting the WDHB but also patients and referrers. He accepts that the WDHB had itself a degree of countervailing market power but points out that the defendants together made up most of the relevant market.

[41] He also makes two further important points. First, it appears that the moratorium arose in the context of a possible merger. The Commission's position is that parties which propose to take steps towards merger must not in the meantime enter into anti-competitive arrangements or understandings. It is no answer to say that an eventual merger is likely to result in public benefits that exceed the anti-competitive detriments. Part 5 of the Act provides procedures designed to facilitate authorisation applications in the context of a transparent process which permits participation by affected parties.

[42] I accept Mr Goddard's submission on this issue.

[43] His second point concerns the role of the WDHB. It was not a defendant in the present proceeding, but in the light of the information available to the Court, it might well have been joined. Mr Goddard asks the Court to note the Commission's position which is that defendants in future cases, including government entities such as District Health Boards, should not expect lenient penalties by reason of the relatively limited penalties sought in this case. He asks the Court to note, as I do, that the Commission's approach to the involvement of the WDHB and indeed its approach to penalties generally in this case, are strongly grounded in the facts of this particular proceeding, which are somewhat unusual by reason of the very limited gains made by, or available to, the defendants, and the significant mitigating factors to which the defendants are able to refer.

Conclusion

[44] The Commission recommends penalties of $65,000 for NZDG and $35,000 for PAL. Counsel for the defendants support the imposition of those penalties as being appropriate in all the circumstances.

[45] The general approach of the Court is to accept and impose a penalty which has been agreed between the parties, so long as it is within the Court determined permissible range: *Australian Competition & Consumer Commission v ABB Power Transmission Pty Ltd;*[8] *NW Frozen Foods v Australian Competition & Consumer Commission*.[9] That approach is also adopted in this country. In the *Gas Insulated Switchgear* case Rodney Hansen J said at [18]:

> … there is a significant public benefit when corporations acknowledge wrongdoing, thereby avoiding time-consuming and costly investigation and litigation. The Court should play its part in promoting such resolutions by accepting a penalty within the proposed range. A defendant should not be deterred from a negotiated resolution by fears that a settlement will be rejected on insubstantial grounds, or because the proposed penalty does not precisely coincide with the penalty the Court might have imposed.

[8] (2004) ATPR 48,848 at 48,855.
[9] (1996) 71 FCR 285.

[46] I agree. In my judgment it is proper for the Court to accept appropriate penalties which have been negotiated between counsel and which plainly fall within the applicable range in all the circumstances of the case.

Result

[47] The recommended penalty is approved. There will be orders directing the first and second defendants (jointly and severally) to pay a penalty of $65,000 and the third defendant to pay a penalty of $35,000.

[48] Costs are also agreed. The NZDG defendants (jointly and severally) and PAL will each pay the Commission costs of $10,000.

C J Allan J