



Making sense of the numbers

**Protecting the consumer's interest in
the .nz domain name market**

Report to the Domain Name Commission

September 2021

Author: Mark Cox

Reviewer: Amanda Reid

All work is done, and services rendered at the request of, and for the purposes of the client only. Neither BERL nor any of its employees accepts any responsibility on any grounds whatsoever, including negligence, to any other person.

While every effort is made by BERL to ensure that the information, opinions and forecasts provided to the client are accurate and reliable, BERL shall not be liable for any adverse consequences of the client's decisions made in reliance of any report provided by BERL, nor shall BERL be held to have given or implied any warranty as to whether any report provided by BERL will assist in the performance of the client's functions.

Introduction

This report has been written with the intention that it should be comprehensible to most readers external to the Domain Name Commission (the Commission), rather than solely Commission insiders. It was prepared in response to a request from the Commission to Business and Economic Research Limited (BERL) for a report examining the Commission's work to protect consumers in the market for .nz domains. A particular issue was that the Commission has been seeing an increase in the common ownership of the entities that sell domain names to the public.

Following discussion, the Commission agreed that BERL should address three questions about the market for domain names in New Zealand, namely:

1. Is the concentration in the market harmful to consumers?
2. What other actual or potential harms are there, if any?
3. What information and data to measure and monitor harms should be collected and how should it be analysed?

It should be noted at the outset that the research focused only on the .nz domain name market and on the Commission's role in regulating that market. The research was based on an examination of: the report from a 2019 independent consultant's regulatory review of the Commission¹, data and information provided by the Commission; and further desk based research by BERL.

¹ David Pickens (2019) Domain Name Commission – Regulatory Review

About the Domain Name Commission

The Domain Name Commission was appointed by InternetNZ to develop and monitor a competitive registrar (i.e. domain name provider) market, as well as to create a fair environment for the registration and management of .nz domain names. The Commission helps individuals, businesses, and communities to have an online presence that is unique to Aotearoa New Zealand.

More specifically, the Commission's role is to:

- Enforce the rules and policies that apply to the .nz space and ensure they're being followed
- Ensure the market for .nz domain names and the space itself is equitable, safe, and trusted
- Provide services that enable people to report problems or submit complaints about .nz services.

In fulfilling its role, the Commission:

- Authorises and de-authorises providers
- Provides a .nz dispute resolution service
- Operates a contact centre for enquiries, questions and complaints about registrars
- Undertakes compliance work, including adjudication, mediation, and facilitation of disputes processes
- Validates registration information supplied for .nz domain names
- Carries out market regulation to deal with allegations of poor performance from service providers.

In the event of wrongdoing, the Commission ensures that the industry and consumers play by the rules and policies governing .nz. It investigates allegations of policy breaches and rules not being followed when consumers have evidence to substantiate the allegation. The Commission can impose sanctions and investigate complaints about performance and conduct, proportionate to the wrongdoing. It can also have a domain name registration cancelled if the registered information about the name is found to be incorrect.

About the domain name market

At least in the case of the .nz top level domain², there are three groups of actors in the market:

- The registry – Internet New Zealand, the parent of the Domain Name Commission, (the market regulator)
- The registrars – firms that sell .nz domain names (the providers)
- The registrants – individuals and businesses that buy domain names (the consumers).

The focus of this report is mainly on the providers and the consumers, and the relationship between them.

.nz has an approximately 80 percent share of the top level domain (TLD) market in New Zealand. There are approximately 80 providers in the market, although a number of them are in common ownership. The providers in common ownership are often based offshore. Based on June 2021 data, provided to BERL by the Commission, the average price for a domain name is just under \$40³. However, the consumers also have to pay an annual registration fee to the providers, and there are often extra costs for value added services alongside the domain name.

² A top level domain is the last part of an internet address, for example .nz, .com, .net

³ However, some names cost significantly more than \$100, and some desirable names can be re-sold for well over \$1,000.

Is the concentration in the market harmful to consumers?

A particular concern for the Commission is that there is increasing common ownership of providers. For example, one of the top 4 registrars in the .nz registrar market has been acquiring ownership of previously independent providers; and now accounts for roughly a 40 percent share of the .nz market. The question is, however, whether this is automatically a bad thing.

The test is whether providers are disadvantaging consumers, or might do so. It is generally assumed that highly concentrated markets, dominated by monopolists or oligopolists⁴, will lead to harm to consumers through higher prices and poorer quality service. Monopolists and oligopolists can also cause harms by impeding competitors from entering the market. But the existence of monopolistic or oligopolistic provision in a market will not automatically lead to these harms.

Whether or not the harms arise depends how monopolists or oligopolists behave. If the barriers to market entry by providers are low, then monopolists or oligopolists may be deterred from abusing their market position for fear that competition will arise. And, in the particular situation where a group of providers is in common ownership, the owner might see advantage in leaving the providers to compete with one another, as well as with providers it does not own. The logic here would be that competition drives efficiency and, hence, profitability.

The Commerce Commission has the stated central purpose of safeguarding the integrity of competitive markets to ensure businesses and consumers feel confident they are not being unfairly disadvantaged. It administers a voluntary clearance regime for mergers and acquisitions and can also take enforcement action to prevent anti-competitive transactions from going ahead, if prior clearance is not sought.

In making a determination, the Commerce Commission will often apply measures of market concentration to consider whether there is potential for disadvantage to consumers. The most commonly used measures of market concentration are the Herfindahl-Hirschman Index (HHI index) and the Concentration Ratio.

The HHI index is the sum of the squares of the market shares of each provider in a market, where the shares are expressed as whole percentages. The result is always a whole number from virtually zero up to a maximum 10,000. An HHI of less than 1,500 is generally considered to indicate a market where there is competitive supply; an HHI of 1,500 to 2,500 is generally considered to indicate a moderately concentrated market; and an HHI of greater than 2,500 is generally considered to be a highly concentrated market. For example, in a market where there is one provider with a 30 percent share, another with a 20 percent share and ten other providers each with a five percent share, the HHI would be $30^2 + 20^2 + (10 \times 5^2) = 1,500$, indicating a moderately concentrated market.

The Concentration Ratio is calculated as the sum of the market share percentage held by the largest specified number of firms, say five, in an industry. The concentration ratio ranges from zero percent to 100 percent, and an industry's concentration ratio indicates the degree of competition in the industry. A concentration ratio that ranges from zero percent to 50 percent may indicate that the industry is perfectly competitive, and is considered a low concentration. A rule of thumb is that an oligopoly exists when the top five firms in the market account for more than 60 percent of total market sales. If the concentration ratio of a single company is equal to 100 percent, this indicates that the industry is a monopoly.

⁴ Monopoly is where there is a single dominant provider in a market. Oligopoly is where there is a small group of equally strong providers.

The HHI and the Concentration Ratio are simple to calculate, but the HHI is generally preferred because it implicitly ascribes additional market power to larger providers. However, it should be noted that the HHI still has its drawbacks. A company could have only a modest market share overall, but a dominant share of a particular market segment. For example, the markets could be territorial, or related to a specialised product. However, these situations are unlikely to apply to the .nz market.

As was mentioned earlier, companies in one interconnected group have, in combination, a roughly 40 percent market share. This alone would give them an HHI of 1,600, and it would mean that the .nz market is moderately concentrated, even before the market shares of other providers are factored into the equation. However, taking into account .nz does not account for roughly 20 percent of the top level domain names in New Zealand, that interconnected group's HHI would be a little less than 1,300.

It should also be noted that measures of market concentration are far from being the sole consideration when the question of market power is assessed. If the Commerce Commission were to examine what is happening in the .nz market, it would also probably wish to know how an interconnected group with a large market share is behaving. If the Commission was satisfied that the interconnected providers were not acting in a coordinated fashion to disadvantage the consumers, it would not be concerned. On the other hand, if the interconnected companies were acting in a coordinated fashion, to the extent that they were taking improper advantage of their market power, they would be liable to prosecution under the Commerce Act.

What other actual or potential harms are there, if any?

The report by David Pickens referred to earlier, was partly focused on this question, so it will suffice to note the key findings and recommendations that relate specifically to the consumer's interests.

The report was partly focused on whether the Domain Name Commission's status and activities were supportive of the public interest. It found that there was a small risk of narrow self-interest, but it concluded that there were adequate safeguards to manage the risk. It also found that the Commission's status as a self-regulator is appropriate for the services it delivers. Nonetheless, the report recommended that the Commission should regard itself as a competitor against other top level domain administrators and regulators, with a view to being better than them at serving the needs of consumers.

In terms of market concentration, it found that competition risks for registrants in the .nz space were minimal and were likely to decline further as new top level domains were introduced. It also concluded that there appeared to be little opportunity for collusion between providers. Nevertheless, it recommended that the Commission should continue to collect and publish market concentration information, and other information, that might be useful to indicate whether there were any evolving issues.

The report also found that there are serious information deficiencies on the magnitude and nature of internet-related harm in New Zealand, and that only with good information would it be possible to target problems with effective strategies. The necessary information gathering would not, however, be the responsibility of the Commission alone.

BERL regards these particular findings and associated recommendations as being reasonable. But there was one aspect of the report where we would make a recommendation that differs from that in the report. The Pickens report found that there was the lack of the consumer's voice in the .nz market. To overcome this problem, it recommended that the providers should be required to disclose more information about their interactions with consumers. BERL doubts, however, whether an information disclosure approach would be useful, at least by itself. Our suggestions about what can be done to enable the consumer's voice to be heard are presented in the next section.

What information and data to measure and monitor harms should be collected, and how should it be analysed?

It is understandable that it is difficult for the consumer's voice to be heard, because many of them have no direct contact with providers. Rather, consumers obtain domain names and pay the associated fees through website hosts and IT service providers. In addition, especially for consumers operating a business, the cost of buying and keeping a domain name is likely to be a very small expenditure item, about which they may be disinclined to do, or say, much about.

Nonetheless, it would be remiss to treat the problems that consumers experience as generally being trivial. To hear the consumer's voice, even if only indirectly, the Commission could gather more information in the following ways:

- **Monitoring and analysis the subject matter of calls to its contact centre on a regular and ongoing basis.** BERL understands that the contact centre receives enquiries made up of over 1,850 emails and 570 phone calls a year, and that complaints from consumers mainly focus on difficulties in switching between providers and the pricing of add-on services. However, we also understand that there is only one year's worth of contact centre data. Consistent monitoring and analysis of the calls would have the potential to alert the Commission to the frequency and nature of harms to the consumer.
- **Surveying webhosting and IT service providers,** excluding any that are providers themselves, to discover what, if anything, they hear from consumers about the problems they have with providers.
- **Comparing itself with self-regulators in other industries** to see how they monitor the markets they regulate, especially to see how they capture the voice of the consumer.

All of these actions could inform decisions by the Commission about how to minimise or rectify the harms.

Conclusions

In considering the answers to the three questions shown in the Introduction, BERL did not find any egregious examples of consumer-related issues that should alarm the Commission.

On the face of it, the .nz domain name market is moderately concentrated, but this would only be of concern, and potentially a matter for the Commerce Commission, if all of the providers in common ownership of another entity were acting together in a coordinated fashion to disadvantage the consumers or their competitors.

The Pickens report identified actual and potential harms associated with the way the .nz domain name market operates and is regulated. However, BERL considers that all but one of the responses recommended by Pickens are reasonable.

Departing from what Pickens recommended about hearing the consumer's voice, BERL believes that there are three possible ways in which the Commission could endeavour to hear the consumer's voice better, other than by simply requiring providers to disclose more information.

The research leading to this report did not involve a deep dive into the question of how well the Commission is doing its job, but BERL's overall conclusion is that the Commission is being diligent. Naturally, however, it needs to remain vigilant in guarding against harms in the .nz market.