Wigley & Company
BARRISTERS and SOLICITORS

Comments on the Commission's Consultation on Telecom's Non-Discrimination Obligations under the Separation Undertakings

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1. Summary and Introduction

1.1 The Commission's well-intentioned endeavour to clarify application of the non-discrimination provisions has the benefit of teasing out how hard and risky this is to do. For example, if the Court applied the proposed tests in the Loyalty litigation (an unlikely scenario), it is likely that the Commission's case would fail. In any event, the scope of the litigation, in using that approach, would be unwieldy.

P O Box 10842 • Level 7 • 107 Customhouse Quay • Wellington • New Zealand • Ph. + 64 (4) 472 3023 • Fax. + 64 (4) 471 1833
also at Auckland Ph. + 64 (9) 307 5957 • www.wigleylaw.com

1.2 Having usefully teased out the issues, the best path may be to have no guidelines at all, or guidelines that are substantially changed. Like much law, it may be best to allow interpretation of the provision to evolve naturally.

1.3 We wish to emphasise the value of these draft guidelines in bringing issues to the surface, even though we take a different view. That is a real benefit of the approach.

Two key questions

1.4 While the draft guidelines are not clear on the point, their purpose can only be guidelines on one or both of the following:

(a) What do the two provisions (and "not discriminate" in particular) mean, taking into account relevant material?

(b) If, based on that interpretation, the Commission considers there is a breach, how will it exercise its discretion to take action such as to issue proceedings?

1.5 It is possible that the reason why, in our view, the tests in the draft Guidelines depart substantially from answering that first question correctly, is that the two questions have been conflated into one.

First question: breach of Undertakings

1.6 The first question is relevant, because, under the Act, the Commission will be deciding whether or not there may a breach of the undertakings. Ultimately it is for the Court to decide whether there has in fact been a breach (just as it does in relation to, for example, Section 36 Commerce Act claims, where the Commission makes the initial decision to sue). Thus the Commission's initial step is to decide, by using the same analytical method as the Court would apply, whether there may have been a breach.

1.7 If there may be a breach, the Commission then has a second question: does it exercise its discretion in favour of, for example, suing Telecom. These two questions need to be clearly delineated.

1.8 The first question involves interpretation of the provisions, using the interpretation tools developed by the courts.

1.9 The draft Guidelines do apply some of those interpretation tools. But they do not use an explicit framework, as the Courts use, based squarely on interpreting the provisions. Further, the matters referred to in the draft Guidelines stray outside issues to be taken into account in a standard interpretation of such a provision.

Difference between draft loyalty decision and draft guidelines

1.10 We note in particular that the draft Guidelines depart radically from the Commission's draft decision on the loyalty offer (which has not been converted into a final publicly available decision). Yet virtually no reasons are given for this change of tack, nor are reasons fully articulated generally in the draft Guidelines for the proposed approach. The December 2009 draft guidelines on non-discrimination should be re-issued for comment. In a de facto sense the draft guidelines become the equivalent, as to non-discrimination, of a final report, in

relation to that draft Loyalty decision. This creates problems for all, including the Commission, as we note below.

Return to anti-trust and regulatory murky waters

1.11 Some of the tests proposed in the draft guidelines take issues back into the murky waters of ex post (Commerce Act) and ex ante (Pre-operational separation Telecommunications Act) seas. They introduce a test (which seems to have little relationship to the wording of the provisions) based on adequacy of competition in a particular market. That is a notoriously difficult area. What is or are the markets? What constitutes adequate competition? Those questions occupy reams of paper and weeks of Court and Commission time. The very sort of problem the undertakings are designed to avoid, among other things. Likewise as to another test: impact on investment incentives. Whose incentives to invest, for example, and what is the relevant degree of impact? A complex question.

1.12 Telecom, based on those two proposed principles, would seek to argue, in the Loyalty case, issues that are appropriate in a full blown anti-trust case. Some sort of "lite" market definition and competition analysis also doesn't seem workable. How can a different "lite" approach be justified? Where is the line drawn? This begs many questions and anyway is irrelevant to the key question: has Telecom breached the undertakings based on a proper interpretation of the provision. It is to be hoped that the Commission can run the Loyalty litigation in a manner that allows the court to draw its conclusions in ways different than the 4-step test.

Delineate symptoms and ingredients

1.13 Significantly, competition problems as a consequence of the breach of the non-discrimination provisions are a possible (but not inevitable) **symptom** of the breach. They are not an **ingredient** in the breach. Similarly as to the investment limb of the test. Our impression is that the underlying problem in the draft would be solved if the symptoms are decoupled from the ingredients, even though the symptoms are among the reasons why the non-discrimination provisions are there in the first place.

Policy underlying operational separation

1.14 Operational separation was introduced because the traditional anti-trust and regulatory remedies had failed. The draft guidelines take matters back into those troubled waters. A strength of operational separation is its relative simplicity and the clear delineation of acceptable conduct:

1.15 Further the undertakings are designed to create a level and transparent playing field for all wholesale customers including Telecom. This is a particularly important point. The undertakings, including the non-discrimination provisions, are designed to create that level playing field. The complex 4 step approach departs from that fundamental policy and legislative objective.

Interpretation: overview

1.16 Stating the position outlined in more detail below:

(a) The ingredients in "Not discriminating" in the clauses do not involve considerations of anti-competitive activity or whether discrimination is "good or bad". It is about differences and distinctions such as price and

non-price components. The clarifier around changes to suit specific circumstances supports this view.

(b) In normal language, and also from an economist's perspective, discrimination does not mean discrimination that is anti-competitive or "bad". Discrimination can be pro or anti-competitive. It can be" good" or "bad" discrimination. The draft guidelines however incorporate competition issues in the test, incorrectly.

(c) If issues such as competition or investment were to be included, the clause would have said so. In contrast, that is what happens in relation to the UK situation where the test is undue discrimination, that is, "discrimination" which is "undue". Here, we have just "discrimination". Contrary to Telecom's reliance on the UK approach, to show our "discrimination" should be interpreted similarly to the UK (and the EU), the position is the opposite. The parties to the deed chose not to include words like "undue" in the undertakings. They choose not to go down the UK path as to treatment of discrimination (and the UK operational separation is the model on which the New Zealand solution is based). The strong implication is that "discrimination" has its normal language meaning (whether as understood by an economist, or by someone else).

1.17 Interpreting the clauses has some challenges, particularly where a wholesale customer has a genuine and reasonable need to have different aspects to the service. But none of this requires the detailed gloss proposed to be added (that is, it is not appropriate to add materially to the plain meaning of the language in the undertakings). Non-discrimination is a more straightforward concept.

1.18 To interpret the provisions, as proposed by Telecom in, for example, their response to the Loyalty draft decision, would be to render those provisions ineffective. Many of the problems they identify are not problematic, or, if they are, they are a by-product on the way to achieving larger objectives. No solution is perfect in telecommunications. Additionally, Telecom can apply for exemptions (a variation application to the Minister, terms in an STD, etc).

Future guidance, and Sub-loop extension service

1.19 In light of the matters raised in this paper, the sub-loop extension service (SLES) guidance last year is therefore based on incorrect and judicially reviewable grounds. The decision should be reversed and rectified.

1.20 Additionally, there was no consultation. Implicit in that guidance, and the draft guidelines, is that consultation with affected parties is not required in all instances. Leaving aside public law duties to consult, the points in this paper confirm that consulting in all instances would be prudent. One of the most important times to consult is when the wholesale customer does not know about the matter. Yet the SLES decision, and the guidelines make it clear it is not intended when other parties do not know of the issues.

1.21 The difficulties in giving guidance may outweigh the benefits: it may be best to allow the position to evolve.

UFB

1.22 These submissions address the specifics of the undertakings: they do not address the important issue of non-discrimination in relation to the proposed

UFB network. While there are common themes, the immediate question is undertaking-specific.

2. Principles for interpretation of the non-discrimination provisions

2.1 As noted above, the Commission's primary task is to determine whether, applying principles used by the Courts, there may be a breach of the undertakings. Ultimately it is for the Court to decide whether there has in fact been a breach. The guidelines should follow and apply the framework likely to be adopted by the Courts. It is therefore necessary to analyse the court's likely approach.

Which interpretation rules apply?

2.2 The undertakings raise interesting questions as to what specific interpretation rules apply:

(a) The undertakings take effect as if they are a deed (so, deed interpretation rules apply).[1]

(b) However, the undertakings are also an instrument by which an Act is implemented. This may impact the approach, either:

(i) Generally (as a matter of the Court's approach in a statutory context); or

(ii) Specifically, if the Court concludes that the definition of "regulation", in the Acts Interpretation Act 1999 extends to these undertakings. If that is so, then the undertakings are an "enactment" under the Interpretation Act 1999, and the purpose test in Section 5 of that Act may apply:

> The meaning of an enactment [the undertakings] must be ascertained from its text and in light of its purpose

2.3 However, which approach (or both) applies does not appear to need to be resolved now (unless the Commission continues to provide advance guidance, in which event this issue may need to be resolved now). At a high level, there are broad similarities between interpreting legislation, deeds and contracts:

(a) Deeds are interpreted using the same principles as for interpretation of contracts[2]

(b) Interpretation of all three (deeds, contract and legislation) takes, among other things, a purposive approach. For contracts (and therefore deeds) that is articulated in the classic approach (including as to the matrix of facts) adopted in *Boat Park v Hutchinson*[3], applying *Investors Compensation Scheme v West Brunswick Building Society.*[4]

[1] Section 69N Telecommunications Act
[2] McNeel, The Construction of Contracts: Interpretation, Implication and Rectification (Oxford University Press) at Page 15
[3] [1999] 2 NZLR 74; see also Burrows et al, Law of Contract in New Zealand (3rd edition) (Lexis Nexis) at page 161
[4] [1998] 1 WLR 896.

Key facts and implications for interpretation

2.4 Of importance when interpreting the non-discrimination provisions is that:

(a) The undertakings are heavily negotiated, heavily lawyered, and formally documented

(b) Telecom, a large and experienced company, has agreed to the wording.

(c) The model is based on the UK model with its associated "undue discrimination" provision. That is entirely different from a clause that does not qualify discrimination with words like "undue". The NZ undertakings are based on the UK model. Telecom incorrectly states that the UK approach should be followed (with its interpretation by the Courts based on "undue discrimination". To the contrary, the parties in New Zealand can be taken to have chosen a different path: "discrimination" without any qualifier such as "undue". This strengthens the position that discrimination means just that, without any qualifier, other than the specifically stated matters.[5]

2.5 This means that there should not be a departure from the normal meaning of the words (or a small range of reasonable meanings), or some sort of gloss added to the words, unless the context clearly justifies that. As Lord Hoffman noted in part of the key passage from *Investors Compensation Scheme,* which is quoted in most contract interpretation cases:[6]

> The "rule" that words should be given their natural and ordinary meaning' reflects the commonsense proposition that we do not easily accept that people have made linguistic mistakes, particularly in formal documents. On the other hand, if one would nevertheless conclude from the background that something must have gone wrong with the language, the law does not require judges to attribute to the parties an intention which they plainly could not have had.

2.6 While context, such as the purpose statement and underlying policy, are relevant, this should not be used to distort natural meanings (or a natural range of meanings) where that is not necessary. This is the more so in such a carefully crafted and formal document.

2.7 The same passage from the *Investors* judgment states:

> Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.

2.8 It is not clear whether the Courts would decide that the "reasonable person" in this context is:

(a) A specialist: Someone with telecoms regulatory and economic knowledge, given the focus of the undertaking, and the cohort of typical readers; or

[5] We agree with Telecom, based on the authorities they cite, that the Commission must disregard the content of negotiations when coming to a view, as the Court must disregard those negotiations.
[6] At page 913

(b) A generalist: someone who is not familiar with economic concepts, given that this is a document ultimately intended for the benefit of a wider community.

2.9 It would be prudent to assume the latter not the former, pending clarification by the Court, on this issue. Like all issues covered by the draft Guidelines, it may be best to allow the approach to evolve on a case by case basis.

What does "not discriminate" mean?

2.10 However, whether the generalist or the specialist is the benchmark, the outcome may be the same, for the following reasons:

(a) The first step, in interpreting the clauses, is to look at the meaning of non-discrimination (or, more accurately, "not discriminate"). This should be done before turning to the qualifications and the broader context. As noted above, plain and ordinary meanings apply unless something plainly went wrong in the drafting.

(b) The Commission did this in its draft Loyalty decision:

> 53. The *Shorter Oxford English Dictionary* defines "discriminate" as meaning to "make or constitute a difference in or between; distinguish, differentiate." "Discrimination" is the "action or an act of discriminating or distinguishing; the fact or condition of being discriminated or distinguished; or a distinction made." More concisely, the Pocket Oxford Dictionary provides "(*often foll. By* between) make or see a distinction."
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> 54. It is the Commission's preliminary view that the meaning of this clause is clear**: the existence of any non-trivial difference in the provision of a Relevant Wholesale Service between service providers constitutes discrimination under this clause – there is no requirement that there has been any unjust or prejudicial treatment** (which would require some form of express or implied intent). [bold added]

(c) The Commission in the rest of the draft decision, did not materially change the conclusion above that discrimination (subject to the clarifiers):

(i) Is "any no-trivial difference"

(ii) Does not include a requirement that there has been unjust or prejudicial treatment.

(d) No reasons are given in the draft Guidelines for the substantial change of approach from that adopted in the draft Loyalty report.

Economist's approach

(e) If the economist's view of discrimination is relevant, discrimination is about differences, whether or not they are anti- or pro- competitive ("unjust or prejudicial", "good" or "bad"). Selling economy seats on a plane at different prices is discriminatory. But it is – usually – pro-competitive. So, discrimination per se can be pro- or anti-competitive. Discrimination can be "good "and "bad".

(f) The clauses make no distinction between the two ("good" and "bad"). So "not discriminate" does not connote the quality of that discrimination (whether pro or anti-competitive, "good" or "bad").

(g) Whether the specialist or the generalist is interpreting this, "not discriminate" means that there will not be differences or distinctions (or maybe non-trivial differences as the Commission notes in the draft loyalty decision). This does not involve value judgments as to whether the discrimination is anti-competitive or not.

(h) As noted above, Telecom incorrectly conflates the UK and EU "undue discrimination" with the simpler "discrimination" (more specifically, "not discriminate"). The Commission draft Guidance does not deal with the concept that discrimination can be "good" or "bad", pro- or anti-competitive.

Policy

(i) The conclusions above are consistent with, and fulfil, the policy underlying the undertakings, as outlined in the legislation, the MED discussion papers, the UK experience, etc. The undertaking regime was introduced because the anti-trust (Commerce Act) and regulatory (Telecommunications Act) regimes had failed. The undertakings provided more transparency and bright line certainty (when anti-trust in particular involved highly complex assessment and approach). Having a non-discrimination regime is, like the EOI structure, a way to have that level of simplicity.

(j) Importantly, the policy underlying the legislation is to create a level playing field. All wholesale customers get the services on the same basis as the Telecom customers. The level playing field facilitates competition between competitors downstream of Chorus and Telecom Wholesale respectively (including downstream Telecom units). Those two entities (Chorus and Telecom Wholesale respectively) can compete by changing their services for all their customers, thereby preserving the level playing field. For example, if a competitor at the wholesale level puts pressure on Telecom Wholesale in relation to one of its products, Telecom Wholesale can drop its prices (including below regulated prices where applicable) for all of its customers. Telecom Wholesale and Chorus have choices to compete, constrained by the broader policy objectives of having a level playing field and avoiding the quagmire of the failed anti-trust and regulatory regime, which underpins why there is operational separation.

EOI

(k) Non-discrimination is a twin requirement with EOI, both designed to achieve similar outcomes; equivalence, transparency and non-discrimination. The non-discrimination provisions cover broader territory than the services covered by EOI. The EOI regime does not point away from the conclusion that discrimination means, in this context, any price or non-price differences. To have an approach that differs from a simple one (and one that supports the level playing field approach) runs counter to underlying policy, and also violates the use of the words in the clauses.

(l) Commercial services like sub-loop extension underlie why the non-discrimination provisions co-exist with EOI which doesn't cover commercial services. It is a generic approach. It meets concerns

identified by us in our submissions to the Minister, around the restriction of the undertakings to only regulated services.

Effect of the clarifying words ("for the avoidance of doubt")

(m) Thus far, in this discussion, the simpler bright line approach applies the plain and natural meaning of the words, and is consistent with underlying policy and objectives. The clarifiers (differences that reflect different requirements, and so on) do not change this approach. They confirm it. They allow for pragmatic exceptions such as specific and justifiable individual needs.

Too soon to draw the discrimination line

(n) It would be premature to draw a line now: it should be done on a case by case basis, with the Commission indicating that it will seek to argue, in future cases, that only the differences and distinctions in the clarifiers allow for differences in price and non-price components in services.

3. The purpose statement and other surrounding material

3.1 The draft Guidelines correctly note the Section 69A purpose statement, which should be considered, taking a purposive approach, when interpreting the provisions. However, such surrounding material cannot be used to change use of the plainly available range of meanings where it cannot be shown that something has gone wrong. (We have dealt with this above).

3.2 The approach noted above, by which discrimination is not based on whether the differences are anti-competitive, does not change due to the purpose statement. To the contrary, the purpose statement supports that approach:

(a) The three purposes in the purpose statement are, in summary:

(i) Promote competition

(ii) **Require** transparency, non-discrimination, and equivalence

(iii) Facilitate efficient investment.

(b) As noted above, the operational separation undertakings were introduced as the existing anti-trust and regulatory regimes were not working in relation to competition and investment. The first and third purposes (competition and investment) are best achieved by implementing the second purpose (which **requires** transparency, non-discrimination, and equivalence of supply). Competition (and maybe investment) problems are **symptoms** which are allayed by non-discrimination: they are not **components** of the non-discrimination definition, contrary to the approach in the draft guidelines.

4. Limited reasons justifying competition and investment as factors

4.1 If the Commission intends to rely on the various components in its approach to defining non-discrimination, further reasons for doing so should be given, and opportunity given to comment. Anti-competitive problems such as margin

squeeze seem inextricably linked with the approach in the draft.[7] But it is important to delineate them.

4.2 The draft has an anti-trust flavour which appears to impact the approach. See for example, the approach under the competition limb of the 4-step test at Para 28- 30 of the draft Guidelines. It is necessary to clearly delineate the approach in the undertakings from reliance (except where clearly justified) on anti-trust and other principles.

4.3 As noted above, no justification is given for the marked change between the draft Loyalty decision and the draft Guidelines. This surely calls for clear articulation of the reasons for the conclusions in the Guidelines, and also the reasons why there is such a radical change from the Loyalty draft. Then parties can comment. We note also that the draft Guidelines go considerably further than even Telecom contended for in their loyalty submissions (in terms of the detail and the scope).

5. Commission guidance to stakeholders

5.1 It follows from the above that, in our view, the Commission should be cautious about giving future-looking guidance to stakeholders on the application of the undertakings, despite the benefits of getting some clarity. There are too many moving parts. The Commission is not the final arbiter. The court is. Advance guidance by the Commission may make it harder for other affected parties to succeed in a claim under the undertakings, based on the Contracts (Privity) Act.

Sub-loop extension service

5.2 It also follows that we do not agree with the Commission's reliance, in the sub-loop extension service letter of 24 November, on the relevance of lack of harm to competition, and lack of negative impact on investment. We have not reviewed the other aspects of that letter as to the tests but this alone is enough for a conclusion that:

(a) The Commission has adopted the wrong approach, which means that it is not correctly applying the law (that is a judicially reviewable issue);

(b) It should withdraw the SLES approval as it does not have the correct legal basis;

(c) If the Commission is minded to provide guidelines, it should then reopen the matter and go out to consultation.

Consultation

5.3 The 24 November letter indicates that there was no consultation with stakeholders before the guidance was given. It appears from the draft Guidelines that there will not be consultation in some instances, particularly where a wholesale customer has not raised the issue.

5.4 In addition to public law duties to consult, the Commission should always consult when such guidance is given:

[7] See for example Paras 13 and 14 of the draft Guidelines, albeit that such problems are noted as a consequence of discrimination.

(a) There will always be affected parties including wholesale customers, the ultimate retail customers, etc;

(b) The situations that wholesale customers don't know about are the very situations where there should be disclosure and transparency;

(c) The contents of this report indicate the desirability of consultation, including to protect the Commission.

6. Loyalty litigation

6.1 It is suggested that the pleadings and case should be framed widely enough to cover the prospect that the correct test is not as outlined in the draft Guidelines.

6.2 We also note the impact of extensive discovery, and other procedural steps if the guidelines approach is contended for, even if the court ultimately rejects the approach. Telecom would surely argue the case based upon the approach in the guidelines that is so favourable to them.

6.3 Additionally, taking the line in the guidelines may be used by Telecom to lock the Commission down to a position in Court (in practice anyway, even if no sort of estoppel or the like is raised).

6.4 The worst case scenario would be that the pleadings are such that the court is stuck with an unsustainable cause of action.

6.5 Therefore, the way in which this case is framed and pursued should be revisited.

7. The third limb: differences objectively justifiable, etc

7.1 On the surface this seems a convenient way to deal with the need to have differences in services. But, again, the endeavour to get clarity highlights the risks. It is hard to see how this fits with an appropriate interpretation of the provisions.

7.2 For example, Para 36 notes: "Differences are likely to be reasonable if they are an appropriate means of accommodating the service provider's requirements". It is relatively simple however, for Telecom to create required differences, which are not available to others (for example, differences in non-price aspects due to their size, which cannot be matched). The excellent idea of the default position against Telecom does not overcome such openings to game or otherwise take advantage of this "rule". In any event, such a default rule would not be applied by the Court in its assessment, as it does not follow rules of evidence and proof.

7.3 It is better to deal with this on a case-by-case basis, if necessary with some guidelines where they are clearly supported by appropriate interpretation and application of the Undertakings.

8. Telecom submissions on draft Loyalty paper

8.1 We have dealt with many of Telecom's points above.

8.2 Telecom point to a number of examples in support of their submissions. However:

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(a) The ability for Chorus and Telecom Wholesale to provide different services to different customers (including downstream Telecom customers) is deliberately constrained. That is pro-competitive overall as the level playing field thereby created encourages competition between retailers. To achieve the broader objective, there are restraints at the wholesale and network levels;

(b) Chorus and Telecom Wholesale can react to competition at their respective levels by changing the services available to all their customers (for example, by dropping the price of a particular service (even if it is regulated) across the board.

(c) Therefore, Telecom can react to competition at both the network, wholesale and retail levels. This is pro-competitive overall. The regime can also encourage innovation overall.

(d) No regulatory solution is perfect: some of the examples given by Telecom are simply a symptom of achieving broader and better outcomes.

(e) However, many of the examples are not problematic when the approach noted in this paper is taken. For example, the clarifying statements in each of the provisions will often give the appropriate solution. Often there will be issues specific to the customer that are appropriate to take into account. Where there is a regulated service, the STD can deal with the issue.

(f) Application of the provisions will sometimes raise issues at the edges, which need to be worked through. That is one reason why it may be better to allow interpretation to evolve naturally over time.

(g) Telecom can, if necessary, in specific situations, seek variation of the undertakings.

(h) If Telecom's approach was accepted, the non-discrimination provision would be largely ineffective. There is a "thin end of the wedge" aspect to this.

9. The discretion to act

9.1 As we noted above, the Commission, if it finds there has been a breach, has discretion to decide what to do. In our view, guidelines on this aspect should not be issued. But if they are issued, they should be changed substantially from the nature of the approach in the draft.