Internet New Zealand (Inc)

Submission to the Commerce Commission

on the

Draft Requirements for disclosure by Telecom
and the
Draft Companion Paper

23 March 2009

Public Version

(There is no confidential version)

1. Introduction

1.1 InternetNZ welcomes and strongly supports the draft Requirements and the draft Companion paper, with the reservations noted below.

1.2 Among other things, InternetNZ wishes to assist the Commission by identifying reviewable error in the Companion paper. This applies to the approach of not requiring disclosure of information relating to price squeeze and bundling issues. This in our submission is not a matter that can be left to a review in a year or two's time. The currently proposed approach, in addition, does not align with the Commission's views expressed elsewhere, as we note in the final paragraph of this submission.

1.3 However, InternetNZ suggests that finalising the remainder of the Requirements should not be held up while the price squeeze and bundling issues are considered. InternetNZ proposes that the Commission address the price squeeze and bundling issues soon after the rest of the requirements are finalised (relying on the ability to do so under the Act and also as specifically provided for under the Requirements document[1]).

1.4 This will rectify the problems we identify, and benefit end users. The Commission can readily remedy the position by a simple change to Para 260-263, by stating that what, if anything, is to be done about price squeeze/bundling information disclosure is to be considered separately. In this way, the draft Companion Paper and Requirements can be finalised immediately.

1.5 Additionally, in taking this approach, the Commission will have the benefit of a new and significant report that came out after the draft Companion Paper and draft requirements were finalised. This is the March 2009 European Regulators Group *Report on the Discussion on the application of margin squeeze tests to bundles*. Significantly, this is a report dedicated only to *ex ante* regulation not *ex post* competition remedies.

1.6 This new paper shows, as we note in the final paragraph of these submissions, an approach to obtain positive outcomes for the market, where the Court's current interpretation of Section 36 of the Commerce Act (based on *Telecom v Clear* and *Carter Holt*) may not permit this.

1.7 In this submission, we will refer to "price squeeze/bundling information disclosure", for ease of reference, to cover the various options available to the Commission. In doing so, we are not suggesting an assumption that there is anti-competitive bundling or price squeeze. For example, one of the benefits of disclosure is that Telecom can more readily demonstrate compliance in a transparent way. The Commission has available an array of options ranging from requiring Telecom to provide worked-up imputation tests, through to simply providing the underlying data to enable others (or just the Commission depending on confidentiality issues) to undertake their own assessment.

1.8 Circumstances that may constitute anti-competitive price squeeze and/or bundling are internationally affecting competition and investment in telecommunications. As the Commission will know, this is a major issue domestically and internationally. There is good reason why it is important to consider information disclosure in this area.

[1] At Para 2.3 of the Requirements

1.9 Bundling for example is dominating the nature of services offered to consumers, often where one or more of the components in the bundle is available only from the upstream supplier (or the upstream supplier has some form of SMP).

1.10 In its draft Companion Paper, the Commission recognises underlying relevant issues, at Para 31-46.

1.11 These are particularly difficult issues for regulators and stakeholders to deal with. The time taken to deal with price squeeze and bundling concerns is just an example: several years for the Telecom bundling review and over 7 years for the data tails litigation. There is an opportunity to proactively deal with these serious challenges to competition in advance. For example, imputation test disclosure is likely to provide incentives for the incumbent to avoid anti-competitive price squeeze and/or bundling from the outset. Transparency will be powerful. Additionally, it is a means by which Telecom can reassure stakeholders that there is compliance, so there is benefit for them too.

2. The Commission's approach in relation to price squeeze/bundling information disclosure

2.1 This is dealt with briefly, along with other issues, under the heading, *Non-financial information*, at Paras 260-263 of the draft Companion Paper. The Commission, in this draft paper, gives 3 reasons for not requiring disclosure (we will deal with each in turn):

(a) Raises questions about confidentiality;

(b) Adds unreasonably to Telecom's current requirements;

(c) The product statements will allow the wide audience to perform imputation tests and form a view on price squeeze.

3. Disclosure is said to raise questions of confidentiality

3.1 There is an error in approach here. Two steps are conflated into one. This is an invalid reason for there to be no price squeeze/bundling information disclosure.

3.2 The first of the two steps to take is to determine whether there should be information disclosure. This does not raise issues as to confidentiality.

3.3 The second step is: if there should be information disclosure, should the information that is disclosed be made available outside the Commission (or outside people within a "Restricted Information" umbrella). Applying the confidentiality regime in the draft Requirements, if price squeeze/bundling information is deemed to be confidential, then only the Commission (or a narrow group if the material is equivalent to Restricted Information) sees the information. The information disclosure would be valuable nonetheless.

3.4 Confidentiality concern is not a reason for there to be no information disclosure.

4. Disclosure is said to add unreasonably to Telecom's requirements

4.1 Even if Telecom had to do materially additional work to fulfil the requirements, this is both minor, and considerably outweighed by the benefits.

4.2 However, it is almost inevitable that Telecom does these tests internally anyway, to check compliance. (If they don't do them, then that would be more reason to require disclosure.) The Commission is able to verify this by enquiry of Telecom. It would not be correct to conclude that price squeeze/bundling information disclosure adds unreasonably to Telecom's requirements.

4.3 If, contrary to our submission, stakeholders receive enough information anyway to do the tests themselves, it makes sense for Telecom to take those additional steps.

5. The product statements are said to provide sufficient information and allow imputation testing

5.1 There are threshold issues here including (a) not all relevant products (in relation to price squeeze and bundles) are included in the product statements, and (b) the product statements are produced well after new products and pricing are introduced (i.e. too late).

5.2 However, the product statements do not contain all the information required to do a 'first order' imputation test. That is so for vertical price squeeze but is even more apparent for horizontal bundling issues.

5.3 The product statements are a long way removed from what is sufficient for imputation tests, as the Commission's own imputation tests on Telecom bundles (reported on by the Commission in December 2007) show. This is also shown by:

(a) The new ERG report, and the approaches of national regulatory authorities referred to in that report;

(b) The work done by Oxera for the Irish regulator, Comreg, namely, *Bundling and retail minus regulation – Developing an Imputation Test*[2].

6. Price squeeze/bundling information disclosure is within the Act

6.1 It is accepted by the Commission that disclosure in relation to price squeeze and bundles is available under Part 2B[3], a view that we agree is correct as we have already submitted.[4]

6.2 The March 2009 ERG report identifies a further reason for this, which we deal with below: price squeeze and bundle information disclosure is also necessary for regulatory purposes (i.e. under the Telecommunications Act). It appears that the Commission

[2] http://www.comreg.ie/publications/oxera_s_report_on_bundling.597.102914.p.html

[3] Pages 11-13 of Draft Companion Paper. Additionally the draft Companion Paper proceeds on the basis that price squeeze/bundle information is not excluded because it is outside the Act. Rather, it is excluded for other reasons: confidentiality; unreasonable addition to Telecom's obligations; and existing availability of sufficient information (Page 45 Draft Companion Paper)

[4] For the reasons outlined in Paras 2 and 3 of our 21 July 2008 submission

accepts that there can be information disclosure for Commerce Act and other purposes outside the Telecommunications Act itself. But, to avoid any doubt about this, we outline below reasons why there should be price squeeze/bundle information disclosure for purposes fully within the Telecommunications Act regime.

7. Price squeeze/bundling information disclosure for the purposes of the Telecommunications Act

7.1 *Ex Ante* regulatory (as opposed to *ex post* competition) treatment of price squeeze and disclosure is comprehensively discussed in the March 2009 ERG report. We submit that the Commission should consider this new and significant report, available after the drafts were finalised.

7.2 We illustrate this in a New Zealand context with an example which is of concern to many stakeholders: the relative pricing of the wholesale UBA input and Xtra broadband retail pricing. Stakeholders are concerned about potential price (margin) squeezes between the upstream input price and the downstream retail price. However, it is generally too difficult for them to do anything about this.

7.3 UBA is priced on a retail-minus basis. Retail-minus does not provide a solution to price squeeze, as the UK Competition Appeal Authority concluded in *Albion v Water Services Regulatory Authority and Dwr Cymru.* [5]

7.4 The Commerce Commission has the same view. The Commission stated (as to UBS: the retail-minus model has not changed for UBA):[6]

> *"The existing retail minus mechanism in its current format does not prevent potential price squeezes by the incumbent. As explained [in this paper], in countries where retail minus is in place, it is generally complemented by additional safeguards, including imputation requirements, to ensure compliance with the control on an ex ante basis and to prevent gaming by the incumbent".*

7.5 In that paper, the Commission has earlier identified the problem. The paper goes into some detail on the seriousness of the problems with retail minus pricing (and therefore suggests the safeguards quoted above). This Commission paper preceded the important Competition Appeal Tribunal decision in *Albion* (noted above) which outlined the issues with retail minus even more clearly.

7.6 Against that background, the Commission is now presented with a significant solution to the problem (in a regulatory *ex ante* context). The Commission can achieve now what it proposed should be done in the quoted paper. We submit that the Commission should take the opportunity to do what it suggested should happen in the paper noted above, to deal with a major problem with retail-minus. For the Commission to do otherwise is, to use its own words quoted above, to choose to go against what is generally done in other countries: "*in countries where retail minus is in place, it is generally complemented by additional safeguards, including imputation requirements, to ensure compliance with the control on an ex ante basis and to prevent gaming by the incumbent".*[7]

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[5] [2006] CAT 23 and 36. The decision was upheld by the Court of Appeal but the appeal only considered other points.
[6] Para 44, Commerce Commission 2006 submission to the Finance and Expenditure Select Committee.
[7] Para 44, Commerce Commission 2006 submission to the Finance and Expenditure Select Committee.

7.7 In this UBA/Xtra retail pricing example, if information disclosure demonstrates a price squeeze issue, then, from a regulatory perspective, the Commission can instigate a Schedule 3 investigation (for example to add an imputation test compliance requirement, as Ireland has done, or to change the pricing model). This is within the Telecommunications Act framework.

7.8 Particularly given the Court's interpretation of Section 36 of the Commerce Act, the Commission is presented with the opportunity to remedy a market failure by way of regulation, if it ascertains the problem exists. That is regulation fulfilling an appropriate role. If general competition law cannot solve market failure, regulation is, correctly, available.

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