IN THE COURT OF APPEAL OF NEW ZEALAND

CA75/05

UNDER	**The Judicature Act 1908**
AND UNDER	**The Declaratory Judgments Act 1908**
IN THE MATTER	**of the Telecommunications Act 2001**
BETWEEN	**TELECOM NEW ZEALAND LIMITED**
	Appellant
AND	**THE COMMERCE COMMISSION**
	First Respondent
AND	**TELSTRACLEAR LIMITED**
	Second Respondent

SUBMISSIONS OF THE FIRST RESPONDENT DATED 1 FEBRUARY 2006

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A. INTRODUCTION AND SUMMARY

1. The appellant ("Telecom") sought declaratory relief intended to confine the jurisdiction of the first respondent ("the Commission") relating to pricing review determinations made by the Commission pursuant to the Telecommunications Act 2001 (the "Act").

2. The Commission contends for outcomes to the opposite effect of those sought by Telecom, and supports the High Court judgment which upheld its view on the scope of its jurisdiction, namely:

   2.1 that a pricing review determination relating to a designated service and made under s 51 of the Act after an earlier s 27 determination which includes provision for the price payable for the designated service, can include a commencement date earlier than the date of public notice of the making at the pricing review determination.

   2.2 that a pricing review determination relating to a designated service made under s 51, after an earlier s 27 determination which includes provision for the price payable for the designated service, can amend the expiry date of the s 27 determination or include an expiry date other than that included in the s 27 determination.

   2.3 that a pricing review determination relating to a designated service can be made under s 51 after the expiry date included in an earlier s 27 determination which includes provision for the price payable for the designated service.

3. The Commission agrees that these jurisdictional issues remain relevant notwithstanding that the second respondent ("TelstraClear") and Telecom have recently withdrawn all of their extant applications for review of those parts of determinations made by the Commission under s 27 that relate to the price to be paid for the service.

4. Telecom contends for a closely confined and purportedly literal interpretation of the Act. Whilst seeking to rely on the principle of achieving certainty in the law and praying in aid an alleged detrimental effect on business planning, this

view is not sustainable on its own terms and would have the consequence of rendering subpart 4 of Part 2 of the Act unworkable.

5. The Commission submits that a "practical and realistic" interpretation of the Act is required (*R v Salmond* [1992] 2 NZLR 8 (CA) per Cooke P at 13) and that this end is best served by the relevant statutory provisions being given a purposive interpretation that is alive to the realities of the statutory regime within which they operate.

6. The Commission says in summary:

6.1 A pricing review determination applies a *final* pricing principle. It is a fresh look, using a different technical approach, and the relevant provisions contemplate the substitution of the review determination for what had been stipulated in the initial determination. It is in a very real sense a review of what was done before, applying a more sophisticated approach to determine the appropriate price. (Paragraph 27, below).

6.2 The aims of subpart 4 of Part 2 of the Act will be substantially frustrated if the more thoroughly analysed proxy for the efficient price determined on review does not apply to the period in respect of which the original application was made. Otherwise, a review of the initial price designed to create efficient pricing is neutered by rendering the outcome a purely academic and theoretical contract, likely to be articulated only after it could have any commercial effect. (Paragraphs 35 – 40).

6.3 The rationale for a presumption against retrospective operation of statutory provisions does not apply here. All parties to an initial pricing determination will know within 15 days of it being delivered whether it is being reviewed, and the Commission, in the context of this statutory regime, performs an analogous role to that which the High Court does on judicial review. (Paragraphs 52 – 66).

6.4 The allegation that backdating the commencement of pricing review determinations would have a detrimental effect on business planning

and certainty is overstated and not supported by the factual background to this case. (Paragraphs 75 – 80).

6.5 The Commission is expressly empowered by ss 49(f) and 52(f) to determine the expiry date of its pricing review determination. This is unconditional. This is consistent with power to make a determination on matters "that *relate* to the price to be paid for the service" (s 42(1) or "to the price payable" (s 48(b)) and must include the ability to stipulate an expiry date other than that included in the s 27 determination. (Paragraphs 81 – 93).

B. THE JUDGMENT UNDER APPEAL

7. His Honour Justice Harrison dismissed Telecom's application for declaratory relief. In particular, His Honour held:

7.1 The Courts have long adopted a purposive approach to interpreting legislation, to avoid an absurd result: judgment, paragraph [23], **Case 1 – 27;**

7.2 The statutory scheme suggests that the Commission can provide for both determinations [initial and review] to take effect from the same date, that date being the date set by the s 27 determination: judgment, paragraph [27], **Case 1 – 28;**

7.3 The pricing review determination extinguishes and replaces the s 27 determination on price and related terms because, pursuant to s 42(1), it reviews the amount of 'the price' [initially fixed] to be paid for the service: judgment, paragraph [29], **Case 1 – 29;**

7.4 There would be no legal sense in applying different commencement dates for two determinations where one is a process of reviewing the price fixed by the other for a specified period of service: judgment, paragraph [30], **Case 1 – 29;**

7.5 The statute's silence on recovery mechanisms [for under or overpayments arising out of a difference between the pricing review determination and the initial determination] may reflect a legislative

presumption that common and commercial sense would prevail: judgment, paragraph [38], **Case 1 – 32;**

7.6 The statutory appeal process against the s 27 determination is not rendered redundant because of a pricing review determination: judgment, paragraph [40], **Case 1 – 33;**

7.7 Providing any action is within the decision-maker's statutory power, the fact that it takes effect from a date earlier than the date of the decision does not of itself lead to invalidity: judgment, paragraph [42], **Case 1 – 33;**

7.8 The deterrent effect (in terms of competitive behaviour in the market) of making a pricing review determination operative from an earlier date is not immediately apparent: judgment, paragraph [46], **Case 1 – 35**;

7.9 The Commission is expressly empowered to fix the expiry date of its pricing review determination pursuant to ss 49(f) and 52(f). This power is unconditional and the Act does not stipulate that the expiry date must be the expiry date of the s 27 determination: judgment, paragraph [50], **Case 1 – 36**;

7.10 The Commission's power to make a determination on matters that are related to the price to be paid for the service (s 42(1)) or to the price payable (s 45(b)) are not to be read subject to a gloss of relating directly to the price: judgment, paragraph [52], **Case 1 – 37**;

7.11 The third declaration follows as a matter of application from the second and, as the second fails, so does the third: judgment, paragraph [55], **Case 1 – 77;**

C. THE SCHEME OF THE TELECOMMUNICATIONS ACT 2001

8. The Act was passed into law on 19 December 2001. Its enactment followed publication of a final report from a Ministerial Inquiry into Telecommunications published on 27 September 2000 (the Fletcher Report).

9. Section 3 of the Act defines its main purpose as "to regulate the supply of telecommunication services".

10. The Act provides the Commission with jurisdiction to determine all or some of the terms by which regulated services much be supplied by access providers to access seekers. The paragraphs numbered 2 in Telecom's written submissions for this appeal ("Telecom's submissions") purport to put the interpretation issue in the context of the background to the Act, the commercial expectations of it, and its terms. Many of the nuances or inferences suggested are not accepted, so it is appropriate to put the relevant parts of the Act in their own context.

11. The purpose of Part 2 of the Act is defined in s 18 which state:

> "**18. Purpose—**
>
> (1) The purpose of this Part and Schedules 1 to 3 is to promote competition in telecommunications markets for the long-term benefit of end-users of telecommunications services within New Zealand by regulating, and providing for the regulation of, the supply of certain telecommunications services between service providers.
>
> (2) In determining whether or not, or the extent to which, any act or omission will result, or will be likely to result, in competition in telecommunications markets for the long-term benefit of end-users of telecommunications services within New Zealand, the efficiencies that will result, or will be likely to result, from that act or omission must be considered.
>
> (3) Except as otherwise expressly provided, nothing in this Act limits the application of this section.
>
> (4) Subsection (3) is for the avoidance of doubt.

12. Section 19, among other things, requires the Commission when making any determination to:

> "(a) consider the purpose set out in section 18; and
>
> (b) if applicable, consider the additional matters set out in Schedule 1 regarding the application of section 18; and

(c) make the recommendation, determination, or decision that the Commissioner or Minister considers best gives, or is likely to best give, effect to the purpose set out in section 18."

13. Accordingly, s 18 sets out the requirements by which Part 2 of the Act is to be interpreted and applied. Section 19 of the Act sets the boundaries of the Commission's discretion under Part 2 of the Act, by requiring the Commission to make the decision that "best gives, or is most likely to best give, effect to the purpose set out in s 18".

14. Part 2 of the Act details the process that applies where a party applies for a determination in respect of the designated access services and specified services subject to possible regulatory control:

14.1 Designated access services – subject to possible control as to terms on which they are to be supplied, including price: s 20(2)(a). The scope of such services is defined in Schedule 1, Part 2;

14.2 Specified services – subject to possible control as to terms for supply, excluding price: s 20(2)(b). The scope of such services is defined in Schedule 1, Part 3.

15. The status as designated access services or specified services lasts for 5 years, subject to extension: s 65.

16. Applications for determinations cannot be made unless reasonable attempts have been made to negotiate the terms for supply of the service, or where the parties have an agreement for the supply of the service for part or all of the period to which the application relates: s 22(a) and (c).

17. Where a determination is sought in respect of a designated access service (ie, including as to price), then it must be in accordance with the applicable initial pricing principle: s 29(c).

18. Benchmarking by comparison with the cost of such services in comparable jurisdictions was envisaged from the outset: see Ministerial Inquiry into Telecommunications, pp 47, 68-9.

19. The Commission is obliged to consult or hold conferences in respect of a proposed determination (s 26), and is required to make reasonable efforts to prepare the determination not later than 50 working days after the Commission has decided to investigate in relation to a determination that includes the price payable for the supply of the service (cf. 40 working days, where the determination does not address price): s 28(1).

20. The determination is to be copied to the parties, and publicly notified: s 27. It must include, inter alia, the terms on which the service is to be supplied, the Commission 's reasons, and the expiry date for the determination: s 30.

21. By way of example, for the determination in Decision No. 477, which was arguably the one most relevant to Telecom's concerns, (described further in paragraph 28.1 below), the parties indicated in advance to the Commission their agreement on a one-year term.

22. Any party to a s 27 determination may apply for a review of that part of it relating to the price to be paid for the service. The s 27 determination continues to have effect and is enforceable pending the making of a pricing review determination: s 42(1) and (2).

An application for review must be given to the Commission no later than 15 working days after receipt of the determination. The Commission must, on receiving an application, notify the parties in writing of its receipt: ss 43, 44. The price review in respect of Decision 477 was to apply the applicable final pricing principle – TSLRIC, which involves a calculation of what ought to be the costs of an efficient service provider's costs: ss 45(2), 49(a), (see Ministerial Inquiry report, p 68).

23. A more thorough process is provided for, requiring the Commission to issue a draft and consult: ss 49, 50. The statute imposes no time limits.

24. Both draft and final determinations are required to include the same elements, these include the terms and conditions (if any) on which the pricing review determination is made and any review of matters that were included in the s 27 determination that relate to price and the expiry date of the determination: ss 49, 52.

25. The s 27 determination continues to have effect and is enforceable to the extent that it has not been altered by a pricing review determination: s 51(2).

26. Appeals to the High Court may be pursued on a question of law (s 60(1)(b)) and a determination is enforceable by a party to it, by filing in the High Court: s 61.

27. Salient points to note about this statutory regime are:

27.1 The initial determination and the review determination proceed on entirely different bases. The Commission is required to make reasonable efforts to prepare the initial determination within specified time periods, s 28. The review determination is far more detailed and accurate, requiring analysis and modelling of the efficient costs of a notional provider of the service. The Commission, whilst having to provide the determination timeously, ("as soon as practicable" – section 47) is not bound to any defined time period, s 51. Telecom's submissions (paragraph 2.38) concede that final pricing principles produce "a more accurate fulfilment of the long term s 18 purpose – a closer proxy for competitive and efficient prices".

27.2 The parties to the determination are aware that the s 27 initial determination is just that. Until such time as either a review application is not filed within time or the Commission reaches a final review determination, that initial price is not final.

27.3 Whilst the Telecommunications Commissioner is empowered to produce an initial pricing decision on his own, a final pricing determination has to be produced by a division of three Commerce Commissioners, including the Telecommunications Commissioner: see sections 10(1)(c) and 10(1)(a)(ii).

27.4 There is no provision in the Act that the review is not to have effect for a period that coincides with all or part of the initial determination of which it is a review. To the contrary, the Commission submits that the scheme and purpose of the Act contemplate that the review will operate in respect of the period covered by the initial determination. This is subject to an exception where the pricing review arises as an

original application under s 21:- there, the Commission is not constrained as to commencement date.

D. THE RELEVANT FACTS

28. Telecom's application for declaratory relief attached no particular decision of the Commission or particular factual matrix. Notwithstanding that, the initial determinations made by the Commission that are described below formed a backdrop to the High Court proceeding. The statutory time periods involved are instructive in determining the scope of the Commission's powers pursuant to Part 2 of the Act.

29. The Commission released four initial pricing determinations relevant to this proceeding:

29.1 Decision No. 477: The determination on TelstraClear's application for determination of the designated access services of "interconnection with Telecom's fixed PSTN" and "interconnection with fixed PSTN other than Telecom's", released on 5 November 2002, **Case 2 - 49**;

29.2 Decision No. 497: The determination on TelstraClear's application for determination in regard to the designated access service of "retail services offered by means of Telecom's fixed telecommunications network" (the "wholesale" designated access service)~~s~~, released on 12 May 2003, **Case 2 - 86**;

29.3 Decision No. 525: The determination on TelstraClear's application for determination in regard to designated access services including the "wholesale" designated access services, released on 14 June 2004, **Case 2 – 111**; and (since the High Court judgment)

29.4 Decision No. 563: The determination on TelstraClear's application for determination in regard to the wholesale designated access service (including private office networking) released on 9 December 2005.

30. In respect of each of these decisions, one or other, and sometimes both, of the commercial parties to this proceeding applied for a review of those parts of the

determinations relating to the price to be paid for the services. In summary, the Commission received the following applications:

30.1 In respect of Decision No. 477, TelstraClear filed its application for a pricing review determination in regard to interconnection with Telecom's PSTN pursuant to s 42 on 15 November 2002, **Case 2 - 77**. Telecom filed its two applications for a pricing review determination in regard to interconnection with Telecom's PSTN and interconnection with Telstra Clear's PSTN on 26 November 2002, **Case 2 - 80**.

30.2 In respect of Decision No. 497, TelstraClear filed its application for a pricing review determination pursuant to s 42 on 30 May 2003, **Case 2 - 105**. Telecom filed its application for a pricing review determination on 3 June 2003, **Case 2 - 108**.

30.3 In respect of Decision No. 525, TelstraClear filed its application for a pricing review determination pursuant to s 42 on 2 July 2004, **Case 2 - 127**. Telecom filed its application for a pricing review determination on 5 July 2004, **Case 2 - 135**.

30.4 In respect of Decision No. 563, TelstraClear filed its application for a pricing review determination pursuant to s 42 on 22 December 2005. Telecom filed its application for a pricing review determination pursuant to s 42 on 9 January 2006.

31. On 13 January 2006, as a result of a commercial settlement between them, Telecom and TelstraClear withdrew their respective applications for review.

32. As the parties have withdrawn their pricing review applications, and the Commission notified the parties of the withdrawal under section 54(2) and ceased preparation of the determinations under section 54(2)(b), the Commission will not be required to release determinations in respect of the above pricing review applications. A draft of the Commission's analysis on the review of Decision 477 had been released in accordance with the process contemplated for all such reviews.

E. DECLARATION A: CAN A PRICING REVIEW DETERMINATION TAKE EFFECT PRIOR TO THE DATE OF PUBLIC NOTIFICATION OF THAT DETERMINATION?

33. The Commission submits that the dating of a pricing review determination to cover the same period as the initial pricing review is consistent with the statutory scheme, and not unlawful. The ability to relate to the same period is intrinsic to the notion of a review, even if there were no indications in the statute that this was what was intended. Tellingly, Telecom's submissions, whilst deconstructing the meaning of the word "initial", undertake no such exercise in respect of the word "review".

34. However, in this case, both the extrinsic indications of legislative purpose and the Act itself indicate the way that a pricing review determination is intended to work, and both indicate that it is permissible for the Commission to provide that pricing review determinations are to have effect from the (earlier) date of the initial determination.

Extrinsic indications of legislative purpose

35. The Government's characterisation of the Bill on its first reading included:

> "The contents of this bill reflect the Government's overall objective to ensure delivery of cost-efficient, timely, and innovative telecommunications services on an ongoing fair and equitable basis to all existing and potential users…
>
> The dispute resolution process for designated services allowed a relatively quick decision to be taken on a pricing dispute in which the commissioner applies initial pricing principles. A party to the dispute may seek a pricing review of this initial decision by the Telecommunications Commissioner, plus two other commissioners, but the initial decision will stand pending the outcome of a pricing review."

36. The report back to the House from the Commerce Committee included:

> "A person may apply for a determination in respect of a designated access service or a specified service. An initial determination is made, which is a binding ruling from the Commission on matters in dispute. Initial determinations continue to apply pending any pricing review determination. The determination is made in accordance with the applicable access or pricing principles…"
>
> "A party to an initial determination on the price payable for a designated access service may apply to the Commission for a pricing review determination." (Commentary, p9) **Appellant's Bundle Tab 11**

37. These comments suggest an expectation that the review will revisit the price initially determined under s 27. Given the time required, a serious lacuna arises unless the review applies to the period that is reviewed.

38. The scheme of Part 2 of the Act, and the limited circumstances in which a pricing review determination will be made, means that the aims of that Part of the Act are substantially frustrated if the efficient price determined on review does not apply to the period in respect of which the original application was made. The object is to determine terms and conditions for designated services, when the contracting parties cannot agree them. The party advantaged by the determination should not be deprived of the benefits by virtue of delays that are beyond its control, including the pressure of other legitimate commitments on the Commission. If it had been intended to confine the effect of a pricing review determination to apply prospectively, then timing provisions to give it that utility would have been included. In particular, the notion of a "review" acting prospectively only is so antithetical to the meaning of that word that it would reasonably be expected that Parliament, if it had intended such an unusual result, would have expressly stated that the "review" was only prospective.

39. The practical reality reinforcing the approach the Commission has adopted to its jurisdiction is that a pricing review determination represents a very significant commitment of resources both for the parties, and for the Commission . It is unrealistic to suggest that such an exercise be entirely or largely academic, in the sense of producing an outcome that is not applied to regulate the contractual dealings it has focussed upon. For the process to have utility, consistently with the legislative aim, it has to be a review in the genuine sense of amending (if that is the outcome) the price that was imposed by the initial determination.

40. In practical terms, the work on a review applying the TSLRIC method depends on detailed information demanded from the access provider. It would incentivise Telecom to delay the provision of such information if it knew that such delays avoided the earlier application of a more accurately calculated price, by reference to a notional, efficient provider of the service.

Section 18 Purpose

41. The s 18 aim of promoting competition for the long-term benefit of end-users will be advanced if the efficient price is actually imposed, at a minimum, for the period of the initial determination. Telecom prefers a restrictive view of the scope of s 18 that plays down the relationship between competition and efficiency. In determining the promotion of "competition in telecommunications markets for the long-term benefit of end users of telecommunications services within New Zealand" the Commission must consider the efficiencies that will result from any decision. "Efficiencies" is not defined but, as noted by Telecom at paragraph 2.24 of its submissions, embraces a variety of considerations (dynamic, allocative and productive). Telecom itself notes that a s 51 determination will produce a more accurate fulfilment of the long term s 18 purpose (submissions, paragraph 2.38). In light of this, it is difficult to see why such a statutory process should be minimised in its effectiveness just because the cost of services, once provided, should not be revisited. This is no different to any other industry and, as noted by Telecom (submissions, paragraph 2.22) this is a carefully targeted regulatory jurisdiction. Such "targeting" is a good indication that parliament would have intended the statutory processes put in place to ensure the aims of the Act are given full effect and not read down in an artificial way.

42. The light-handed regulatory regime is intended to incentivise the participants in the industry to conclude arrangements commercially, and to resort to the regulator more or less as a last resort. In that context, it ought to be a fully effective, and not merely an academic exercise.

43. Telecom is wrong to say (paragraph 3.40) that the section 18 purpose has very largely been achieved, when access is procured on initial pricing terms. The legislation recognises that either party may see the benchmarking exercise applied to get the initial price as materially wrong, so that the basis for regulatory intervention can at that point be revisited, by a method that models the costs for a notional efficient provider of the service.

44. There would be significant frustration of the statutory scheme if reviews were only prospective. Access seekers would press for initial determinations to be made for longer periods than would otherwise be appropriate, to maximise the

utility of a subsequent review on price, and the Commission would be likely to accede to such requests, even though longer periods might not otherwise best achieve the statutory aims. Access seekers would also pressure the Commission to accord urgency to completion of a review, when the statute does not suggest that is warranted. Such long lead times in endeavouring to agree terms several years in advance would also create artificiality in parties satisfying the s 22(c) requirement for reasonable attempts to negotiate terms, before making an application.

What is a review?

45. A pricing review determination is a "review", ie per Oxford English Dictionary:

- A formal assessment of something with the intention of instituting change if necessary.
- A reconsideration of a judgment or sentence by a higher court or authority.

46. Black's Legal Dictionary [citation to come] defines review as:

> "**1.** Consideration, inspection, or re-examination of a subject or thing. **2.** Plenary power to direct and instruct an agent or subordinate, including the right to amend, modify, or vacate any action by the agent or subordinate, or to act directly in place of the agent or subordinate".

47. *Words and Phrases Legally Defined* cites the *Shorter Oxford English Dictionary* defining "review" as: "the act of looking over something (again), with a view to correction or improvement". The meaning in law is also given: "Revision of a sentence, etc, by some other court or authority".

48. Here, it is a revisiting of an earlier decision applying a different methodology to the same issue – ie, price of the service. It is correct, as Telecom asserts at paragraph 2.34 of its submissions, that the initial benchmarking work may involve analysis of considerable sophistication. However, it is also true that the s 51 determination is more accurate and more complex. The second process is intended to be more thorough, involve more work for the service provider and the Commission. It requires consultation on a draft and reasons for a decision on the same subject matter as determined in the earlier process.

49. The price set under the initial determination is reviewed under the TSLRIC final pricing principle and the initial determination continues to have effect pending the making of a pricing review determination: s 42(2). To the extent that the pricing review determination does not alter the initial determination, the latter continues to have effect: s 51(2).

50. Given the usual nature of a review, these provisions contemplate the substituted application of the review determination for what had been stipulated in the earlier determination.

51. Consistently with that, the technical approach used at the different stages requires a fresh look, or review, of what had been considered before: initial pricing principle, cf, final pricing principle.

52. A review applying the final pricing principle connotes an outcome after the completion of a process, while the former ("initial pricing"…)infers it may be provisional, or open to revision under a later process. A review in such circumstances is not achieved unless it covers the ground previously traversed. Either party may request it, and either may be advantaged or disadvantaged.

Alleged "retrospectivity"

53. The Commission respectfully adopts the High Court reasoning on alleged retrospectively in paragraphs [41] to [43] of the Judgment, **Case 1 – 33/ 34**. It submits that this is not a case where it could properly be said that the Commission acts "retrospectively". Telecom's concerns are less about fairness in that sense, then they are about the existence of a review causing commercial uncertainty. However, the scheme and purpose of the Act support an operative review, with all participants knowing of the prospect that an adjustment may occur, whilst a review is pending.

54. First, a pricing review contemplates the Commission reviewing the initial determination with a view to changing, or confirming, the price for the entire term of the initial Determination in accordance with the final pricing principle. Just as a reviewing court is required to address the process and procedures of decision-making and ask whether the decision should be allowed to stand, so too the Commission's role under a pricing review is to address whether the initial

price (determined under the initial pricing principle) should be altered, when assessed under the final pricing principle.

55. Telecom characterises the s 27 and s 51 determinations as sequential. The Commission's view is that they are not sequential, in the sense of being successive in their effect. There is not one decision and then an entirely new decision that only operates moving forward. There is an initial decision, with the prospect of a review as to a part of that original decision that, as s 51 stipulates, "alters" the original decision, which is exactly what is expected from a review.

56. Telecom suggests (submissions paragraph 3.13) that a s 51 determination may be expected to apply to a significant part of the period prior to a s 27 determination expiry date. That has not been borne out by experience thus far, and is seen as most unlikely by the Commission. The greater complexity involved in a s 51 determination means that the Commission depends on information being provided by the access provider and then undertaking and testing complex modelling to reflect the efficient costs for provision of the service.

57. Secondly, the processes for pricing reviews and initial determinations contrast with each other, which suggests that the legislature designed them in a manner which takes into account the different objectives and processes for initial determinations and reviews applied to the same subject matter.

58. The process for initial determinations requires the Commission and the disputing parties to meet tight statutory deadlines. Whilst the framework for pricing reviews also includes deadlines, the entire process is open ended in terms of timing restraints: initial determinations should be completed not later than 50 working days after giving notice to investigate the matter, cf, no deadline for draft pricing review determinations. This difference reflects the need for initial determinations to be completed promptly as the access seeker requires timely access to the network to satisfy business needs. In contrast, completion of the review within tight timeframes is not an issue as the access seeker already has had access to the network, and far more work is contemplated in producing a review determination.

59. Thirdly, the parties are aware from the outset that the initial price determination may change. There can be no suggestion that the rule of law is infringed or that unfairness results from any application of a review determination to a period before the determination is made. Until either the period for filing an application for review has elapsed, or a final pricing review determination is issued by the Commission, the initial pricing determination can only sensibly be seen as an interim finding pending the more detailed assessment pursuant to the final pricing principle. The Commission does not accept Telecom's submissions (paragraphs 3.18 to 3.23) that the use of the phrase "initial" as opposed to, for example, interim or provisional, gives any statutory indication that a pricing review determination will only apply prospectively. The use of the word "initial" simply reflects that it is a decision that may or may not be reviewed at the initiative of one of the parties. It would not be correct to say that it is interim or provisional because those words connote that a final decision will definitely be made and, in the context of this statutory regime that may not be the case.

60. Telecom contrasts the use of the word "initial" in this context with the use of the word "provisional" in Part 5 the Commerce Act 1986 (submissions, paragraph 3.22). However, that regime is completely different because there the statute requires progression from "provisional" to "final" determinations in every case, and the whole process remains under the Commission's control. In contrast, the Commission cannot initiate a s 51 review determination.

61. Fourthly, if a pricing review could not review the entire period that was subject to the initial determination, the review process would fail to meet the object of the access regime under which the Commission must determine the terms and conditions for access when the contracting parties cannot agree them.

62. Fifthly, if reviews do not have operative effect from the initial determination date, then the party that is likely to benefit from a higher (or lower) price will be disadvantaged in circumstances where the Commission is unable to expedite the pricing review process for any of a range of legitimate reasons.

63. Sixthly, where the reviewed price is lower than the initial price and is not backdated, the access seeker would be unfairly disadvantaged by having to pay substantial additional amounts (above cost) for the delivery of services which were provided in the past. Further, in that situation the access provider might

be unfairly advantaged by recouping access prices which are substantially above cost for the period subject to the initial determination. Backdating the pricing review ensures that a party does not make any windfall gain from contractual provisions determined for the parties under the Act, and pursuant to which they are compelled to deal, but subject to either party being entitled to have the regulator revisit the accuracy of the price initially determined. A windfall from the non-application of a reviewed price is a situation that would clearly offend against the purposes of this part of the Act, set out in s 18. The converse also applies if benchmarking has set the initial price too low, and the service provider establishes on a TSLRIC assessment, that the efficient price should be higher.

64. Telecom submits (paragraph 3.7(e)) that backdating s 51 determinations does not provide for the s 18 purpose because efficiency is not served by altering the cost of the service after it has been consumed and paid for. The Commission submits that the commercial reality is that the providers of telecommunications services are aware that they provide these services in a regulated environment where the prospect exists that the regulator may impose price terms that are retrospective. Similarly, it enhances the Part 2 regulatory regime by providing a price that is, in Telecom's own words; "a more accurate fulfilment of the long term section 18 purpose". It is difficult to understand why a process that allows the regulator to give best effect to the purpose of the Act should be given a restrictive meaning.

65. The Commission disagrees with Telecom's assertion (submissions, paragraph 3.7(e)(ii)) that a review determination does not improve early access to designated services provided by a s 27 determination for the simple reason that it does improve it by ensuring that that early access takes place with, in Telecom's words, a "closer proxy for competitive and efficient prices".

66. The Commission submits that the fact that a review replaces the original decision to the extent required does not undermine the statutory scheme of Part 2 of the Act but gives effect to the requirement that the pricing review, being a review of the initial determination, gives effect to the final pricing principle.

67. Telecom now argues for a construction of the pricing review determination scheme that is prospective essentially on the basis of two points. Each will be discussed in turn below.

The Absence of a Statutory Mechanism for Over and Under Payments Following a Pricing Review Determination (submissions, paragraphs 3.24 ff.)

68. There is no explicit legislative power for the recovery of either under or overpayment made in respect of an initial pricing determination that is subsequently altered by a pricing review determination. However, given the way the "light handed" regulatory framework interfaces with the course of commercial dealings between access providers and access seekers, it was reasonable for Parliament to anticipate that the consequences of a revised price in a final determination would be resolved in the ongoing dealings those parties will necessarily need to have with each other. Certainly, the absence of a statutory provision mandating recovery of under or over payments does not assist Telecom in asserting that pricing review determinations can only be prospective.

69. In any event, the Commission could, when delivering its pricing review determination pursuant to s 52(b) of the Act, impose a condition for repayment by the party advantaged by the initial price. It is relatively unlikely that this would be necessary, as the High Court noted at paragraph [37] of its judgment, **Case 1 - 32**, commercial parties like Telecom and TelstraClear would probably agree on a mechanism for this purpose. The recent settlement bears this out. Such an expectation is entirely in keeping with the statute's emphasis on ongoing dialogue: For example, a party is prohibited from making application for a determination unless it has made reasonable efforts to negotiate the terms of supply of the service with the other party pursuant to s 22(b).

70. The High Court found at paragraph [38] **Case 1 – 32** that the statute's silence on any recovery mechanism may reflect a legislative presumption that common and commercial sense would prevail. That is respectfully adopted and the point that other regimes may have to provide an overpayment/underpayment mechanism does not mean that its absence in this case is significant.

The Statutory Provision for Appeal of the Price Terms Under a Section 27 Determination While an Application for a Pricing Review Determination is Under Way (submissions 3.31 ff.)

71. Telecom sees the prospect for an appeal from an initial determination coexisting with the review determination as indicating that the review determination should have no retrospective effect.

72. The legislative history of the Act indicates that Parliament intended complementary remedies, without restricting the practical outcome of a pricing review: The report back to the House from the Commerce Committee commented on a change to permit appeals (on a question of law) where an application for a pricing review determination has been lodged:

> "**Appeals from determinations:**
>
> The committee recommends the bill be amended to allow parties to appeal an initial determination even though a price review determination may be pending, and vice versa. This change is intended to ensure that an initial determination can be reviewed on points of law while a pricing review determination is being undertaken. The potential complexity of a pricing review determination means that it may take a long time to resolve. It would be appropriate for the initial determination (which may set a price) to be reviewed during this time, as one party may be paying a higher (or lower) price for the service than they should be (due to an error of law) until such time as the pricing review determination is completed." (Commentary, p10), **Appellant's Bundle Tab 11.**

73. This acknowledges the prospect that a party to an initial determination may have discrete concerns, first as to an alleged error of law affecting the outcome, and secondly, as to the initial outcome on price. The latter may be no more than a view that benchmarking has not achieved the best outcome, and that the TSLRIC modelling of the costs of a provider of such services will better reflect the efficient costs of providing that service. The Select Committee contemplated that both initiatives (appeal on question of law, review applying different methodology) could lead to a correction. Just as a successful appeal would lead to adjustment, so it was contemplated that a review would achieve the same outcome.

74. As noted by the High Court at paragraph [40], **Case 1 - 32**, the right of appeal applies to questions of law on all terms and conditions of a s 27 determination. A party may both appeal and apply to review a s 27 determination on price. For instance, the High Court might find that the price is excessive due to an

error of law and in that event an adjustment will take place from the date of the s 27 determination, whatever is the outcome of the pricing review determination. It may or may not later be altered by the pricing review determination. A backdated pricing review determination does not render the appeal right redundant and again does not suggest that the legislature intended that pricing review determinations can only apply prospectively.

Certainty and predictability

75. Each statutory regime must be assessed on its own terms, reflecting what it is that the regime is attempting to accomplish. Telecom's concerns about certainty and predictability, even if valid, are not the only values that the law recognises and should not be regarded as an end in themselves. There is no more than an example of a typical statutory regime that allows reviews or appeals to take place from an original decision. If certainty and predictability were regarded as all important then there would only be provision for one decision.

76. The Commission submits there is no material difference between a pricing review determination looking once more at the initial pricing determination, and determining a different figure, and a successful judicial review application that comes to a different conclusion. As explained earlier, the initial pricing determination is a snapshot designed to promptly facilitate provision of services. A pricing review determination is far more complicated and more accurate and will, accordingly, be far more time consuming. On the issue that it covers, the pricing review determination replaces the initial pricing determination.

77. It is speculative on Telecom's part to contend that any significant detrimental effects on business planning and certainty would flow from having to adjust prices for a prior period, as a consequence of a pricing review determination (e.g. submissions, paragraph 3.49). It is also inaccurate to suggest an expectation that services will be provided on terms established in advance (submissions, para 2.26). Telecom operates in an environment where at least part of its services are regulated and where, accordingly, there may be decisions made by that regulator, or by a reviewing Court that have material impact on its costs or revenues. An obvious example is the retrospective adjustment to

the identified cost of Telecom complying with its uncommercial service obligations (the "TSO") under Part 3 of the Act. The quantification of that, and the contributions to it by other liable persons necessarily occurs a significant period after the end of the financial period to which it relates. For the year to 30 June 2003, other liable persons were required to pay some $17.3 million to Telecom. More generally, it is unrealistic to expect that a business such as Telecom's can operate without potentially significant items of revenue and costs only being ascertained after the time at which the services are provided.

78. As to the contingencies a pricing review creates in financial reporting terms, the magnitude of any variation is not beyond the scale of other contingencies such entities have to provide for (e.g. significant litigation), and is easily understood by the market.

79. Further, the submissions implicitly overstate the effect of a pricing review determination on Telecom's business as a whole. Telecom agreed to pay TelstraClear $17.5 million as a settlement for matters including the pricing reviews that originally provided the background to this proceeding. The backdating applied from 1 June 2002 to early 2006. – Assuming 3½ years, that would mean a maximum adjustment of $5 million p.a. Even assuming that the settlement did not include any interest component (which seems unlikely), then it is a small fraction of Telecom's reported annual profit before tax for 2005 of $1.3 billion on revenues of $5.7 billion. During that year Telecom reported over $200 million of abnormal expenses including $31 million for inter-carrier adjustments. On 20 January 2006 Telecom announced a write off on its Australian investment in AAPT of approximately $700 million.

80. Similarly Telecom's complaint that pricing review determinations only result in a transfer of funds between ISPs without promoting the s 18 purpose of the Act (e.g. submissions, paragraphs 3.7(f), 3.37) misconstrues the scope of that section. There is nothing in the wording of section 18 to indicate that the Commission is restricted to considering only the short term effects of any determination, or for example, that the Commission has to see any regulation translating into immediate measurable benefits for consumers. If a competitor's behaviour is regulated/constrained by the existence, or even the

prospect of, a detailed price review determination it does not matter that any adjustment is not immediately passed onto the consumer. The existence of a pricing review that is an effective proxy for efficient and competitive pricing will influence more competitive behaviour and fulfil the s18 purpose of this part of the Act. Access seekers will be incentivised to compete, or compete more vigorously, if they know that they will ultimately get the service at an efficient price by regulatory intervention, if commercial negotiations fail.

F. DECLARATION B: THE COMMISSION'S POWER TO AMEND THE EXPIRY DATE PROVIDED FOR IN A SECTION 27 DETERMNIATION

81. As well as challenging the ability of the Commission to set a commencement date from which pricing review determinations take effect, Telecom also challenges the ability of the Commission to amend the expiry date provided for in a s 27 determination.

82. Section 52(f) of the Act provides that a pricing review determination must include "the expiry date of the determination". Accordingly, as part of every pricing review determination, the Commission must turn its mind to the expiry date that it wishes to apply and stipulate that in its determination. This is not to say that, in any given case, the Commission will exercise that power by deciding on a date other than the expiry date of the initial pricing determination. However, the Commission takes the view that the consistent provisions in ss 49(f) and 52(f) create the jurisdiction to determine an expiry date of a price review determination and that, to be a meaningful power, this must extend to a date different from the expiry date of the initial determination.

83. Had it been the legislative intent that the review determination could only pertain to the term of the initial pricing determination then ss 49(f) and 52(f) would not have been specified in that form. Instead, the Act would have specified that each s 52 determination in respect of a s 27 determination would have effect until the expiry date or the earlier determination.

84. Telecom argues that the Commission is confined to reviewing only price (s 42(1)), and the term during which a determined price is applied does not stipulate the price, and is therefore beyond the Commission 's jurisdiction.

85. The Commission's response is that:

85.1 The terms of the statute contemplate matters in relation to price going beyond simply the price itself: s 48(b) permits the Commission to consider any matters included in the s 27 determination "that relate to the price payable …" and that includes the price itself, and contemplates matters other than the price, but which relate to it.

85.2 Telecom argues that this would be too open-ended, as all terms would have some bearing on price. However, many terms will have no influence on what the price should be and an arbiter of price will be indifferent to their inclusion or exclusion.

85.3 Consistently, in ss 49(b) and (c), an 52(b) and (c), if the Commission has undertaken any s 48(b) considerations, both the draft and final review determinations are to include determinations on those points, and the reasons for them.

85.4 The recognition in the context of a price review of the potential relevance of matters that relate to price is sensible and uncontroversial. In practical terms the price may be different depending on the period for which it is determined to apply. The Commission could well fix a different price if it was for 18 months than if it was for five years.

86. Accordingly, the Commission submits that the characterisation of the price review as limited solely to the price for the service is not supported by the scheme of those provisions and would frustrate the purpose of making the best determination of the efficient price.

87. Telecom also argues that the provisions in ss 49(f) and 52(f) do not apply to a review of a s 27 determination but are included only to meet a requirement for an expiry date in applications made under s 21, where the pricing issue is being considered for the first time, without any earlier determination (including an expiry date) that is being reviewed.

88. That approach necessarily recognises that applications under s 21, being treated as if under s 42, would extend beyond just "price" to which they would

otherwise be confined, on account of the necessity to provide for a termination date.

89. If Telecom were correct, in that the term to which a price was to apply had independent status as a term that was not "related to price", then a s 21 application could only proceed when the term was agreed, in which case sections 49 and 52 would not need to make provision for the Commission to stipulate the term that was to apply.

90. Further, if ss 49(f) and 52(f) were to be confined to s 21 applications, it is reasonable to expect that the sections would have said so. The Commission submits that the period to which all price reviews will relate is a matter sufficiently related to price for logic to require that it be positively considered and determined.

91. The Commission respectfully adopts the reasoning of the High Court at paragraph [52] of its judgment, **Case 1 - 37**. The Commission's power to make a determination on matters "that *relate* to the price to be paid for the service" (s 42(i)) or to "the price payable" (s 48(b)) should not be read subject to a gloss of relating *directly* to price. This is simply not what the Act says.

92. There is absolutely no justification for Telecom's submissions (paragraphs 4.16 and 4.17) raising the spectre of the Commission disregarding parties' earlier agreements and enjoying an "unfettered" view of what "related matters" means when applying section 52 of the Act means. The simple answer to this is that this is not how the Commission has indicated it will behave, and there is no basis for slanting an argument on interpretation by a fanciful implication – see e.g. Commission letter, **Case 2 – 176**.

93. Should the Commission not have the ability to extend the expiry date of a determination in the circumstances where it considers that appropriate, the substantial extent of work applying the final pricing principle could be frustrated because parties will need to revert to the Commission to start the process over again to get a decision that actually has some commercial application.

G DECLARATION C: THE COMMISSION CAN MAKE A PRICING REVIEW AFTER THE EXPIRY DATE OF THE INITIAL DETERMINATION

94. The Commission submits that it can make a pricing review under section 51 of the Act after the expiry date included in the earlier section 27 determination to which the review relates.

95. The Commission respectfully agrees with the view of the High Court at paragraph [55] of its judgment, **Case 1 - 37** that as the second declaration failed, the third declaration must also fail.

96. The Commission requires flexibility to determine a new expiry date to address the specific circumstances of the initial determination under review and as the matter develops in the course of each particular pricing review. The Commission may be required to determine an expiry date which differs from the initial determination. For example, a new expiry date may be required where the effect of an initial determination has carried on by default after the expiry date of the initial determination pursuant to a term which is enforceable as an element of the determination. The Commission is empowered to determine an expiry date different from the expiry date of the initial determination under section 52(f) of the Act and that this may occur does not depend on the characterisation of the expiry date as a price or non-price term.

Conclusions

97. Accordingly the Commission respectfully contends for confirmation of the law as being to the opposite effect to the declarations sought by Telecom:

    97.1 As to Declaration A, that a price review determination can include a commencement date earlier than the date for public notice of the making of the pricing review determination;

    97.2 As to Declaration B, that the Commission can, under s 52(f), amend the expiry date of the earlier s 27 determination and a pricing review determination and can include an expiry date other than that included in the s 27 determination;

97.3 As to Declaration C, (essentially consequential on A and B), that the constraint Telecom contends for does not apply, so that a s 51 determination can be made after the expiry date of the s 27 determination which it reviews as to price.

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