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COMMERCE COMMISSION

DECISION NO. 356

Determination pursuant to the Commerce Act 1986 in the matter of an application for authorisation of restrictive trade practices. The application is made by:

Newcall Communications Limited
Teamtalk Limited
Telecom New Zealand Limited
Telstra New Zealand Limited
Vodafone New Zealand Limited

The Commission:

M N Berry
K M Brown
E M Coutts
P R Rebstock

Commission Staff:

R J Adam
S A Auva'a
J H Chilcott
P D Woolley
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**Summary of
Application:**

Five telecommunications companies have sought authorisation for the entry into and giving effect to a Number Administration Deed covering number administration and number portability.

Determination:

Pursuant to sections 58 and 61(1)(b) of the Commerce Act 1986, the Commission determines to decline the application for authorisation in relation to the entry into and giving effect to the Deed to the extent (if any) that section 27 of the Commerce Act 1986 would or might apply to the entry into and giving effect to the Deed.

Pursuant to sections 58 and 61(7) of the Commerce Act 1986, the Commission determines to grant an authorisation for the entry into and giving effect to the Deed to the extent (if any) that section 29 would or might apply to the entry into and giving effect to any provision in the Deed.

Date of Determination:

17 May 1999

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THE APPLICATION

- 1 On 22 January 1999, the Commission registered an application for authorisation of a restrictive trade practice, pursuant to section 58 of the Commerce Act 1986 (the Act), from five telecommunications companies (the Applicants):
 - Newcall Communications Limited (Newcall);
 - Teamtalk Limited (Teamtalk);
 - Telecom New Zealand Limited (Telecom);
 - Telstra New Zealand Limited (Telstra); and
 - Vodafone New Zealand Limited (Vodafone).

- 2 The Applicants have signed a Number Administration Deed (the Deed) dated 15 December 1998, and seek authorisation for the entry into and giving effect to the Deed:
 - under section 58(1) and (2) of the Act, to the extent (if any) that section 27 would or might apply to the entry into and giving effect to the Deed; and
 - under section 58(5) and (6) of the Act, to the extent (if any) that section 29 would or might apply to the entry into and giving effect to any provision in the Deed.

- 3 Section 58, which sets out the Commission’s powers to authorise restrictive trade practices, provides:
 - “(1) A person who wishes to enter into a contract or arrangement, or arrive at an understanding, to which that person considers section 27 of this Act would apply, or might apply, may apply to the Commission for an authorisation to do so ...;
 - (2) A person who wishes to give effect to a provision of a contract or arrangement or understanding to which that person considers section 27 of this Act would apply, or might apply, may apply to the Commission for an authorisation to do so ...;
 - ...
 - (5) A person who wishes to enter into a contract or arrangement, or arrive at an understanding to which that person considers section 29 of this Act would apply, or might apply, may apply to the Commission for an authorisation for that person to enter into the contract or arrangement or arrive at the understanding ...;
 - (6) A person who wishes to give effect to an exclusionary provision of a contract or arrangement or understanding to which that person considers section 29 of this Act would apply, or might apply, may apply to the Commission to do so”

- 4 The application states that the Applicants are applying for authorisation in the “interests of certainty”. The Applicants consider that the restrictive trade practice provisions of the Act do not apply, or should not apply, to the Deed. However, in the event that the Commission, or some other person, takes the view that the Act may apply, authorisation has been sought for protection from legal proceedings.

THE APPLICANTS

Newcall Communications Limited

- 5 Newcall is an Auckland based telecommunications company that provides national and international toll services and 0800 freephone services, primarily to business customers. Newcall also intends to provide internet services in the near future. Newcall commenced operations in June 1998.

Teamtalk Limited

- 6 Teamtalk is based in Wellington and commenced operations in August 1994. Teamtalk provides trunk mobile radio services to business customers, particularly those in the transport and contracting sectors.

Telecom New Zealand Limited

- 7 The New Zealand Post Office controlled telecommunications in New Zealand since the 1950s. In 1987 the Government separated telecommunications from the Post Office and formed Telecom, selling it in 1990. Current major market shareholders in Telecom are NZ Central Securities Depository Ltd, Bell Atlantic and NZ Guardian Trust Company.
- 8 Telecom provides a full range of telecommunication services including local call services, national and international toll services and a mobile network. Budde¹ reports that Telecom has 79% market share in the total voice market and 83% mobile market share.

Telstra New Zealand Limited

- 9 Telstra New Zealand Limited is a wholly owned subsidiary of Telstra Corporation Ltd (Australia) and is based in Auckland. Telstra commenced operations in New Zealand in 1996 and offers national and international toll services, 0800 freephone services, limited local services, data circuits and leased lines. Telstra markets its services to multinationals and New Zealand corporations, and particularly targets consumers who have offices in both New Zealand and Australia.

Vodafone New Zealand Limited

- 10 Vodafone is a wholly-owned subsidiary of Vodafone Australia. In August 1998 it acquired the business of BellSouth² which owned and operated New Zealand's second cellular network. BellSouth commenced operation in New Zealand in 1993. Vodafone

¹ Budde P, Communication, Telecommunications and Information Highways in New Zealand and South Pacific Islands, 1999, 2nd ed, p80.

² A trading partnership comprising BellSouth New Zealand Holdings Ltd, BellSouth Asia Pacific Enterprises Incorporated and S T Cellular (NZ) Pte Ltd.

has a fully digital GSM network and offers mobile communications, voice, data and advanced applications and value-added services.

COMMISSION PROCEDURES

- 11 Commission staff identified 19 parties as potentially having an interest in the authorisation application. The application and related material in support of the application was forwarded to those interested parties.
- 12 Pursuant to section 60(2) of the Act in relation to public notice of the application, the fact of the application was advertised in four metropolitan newspapers on 28 January 1999.
- 13 In the course of the Commission's consideration of the application, Commission staff have met with the following parties:
 - Clear Communications Ltd (Clear);
 - Compass Communications Ltd (Compass);
 - Ministry of Commerce;
 - Newcall;
 - Saturn Communications Ltd (Saturn);
 - Telecom;
 - Telstra;
 - Telecommunications Users Association of New Zealand (TUANZ);
 - Vodafone; and
 - WorldxChange Ltd (WorldxChange).
- 14 In addition, the Commission has sought and received further information from the individual Applicants.
- 15 The Commission has also received written submissions and comment from:
 - Clear;
 - Global One Communications Ltd (Global One);
 - Ministry of Commerce;
 - Teamtalk;
 - Telecom;
 - Telstra;
 - TUANZ;
 - Vodafone; and
 - WorldxChange.
- 16 On 22 March 1999, the Commission issued a Draft Determination giving its preliminary view that the public benefit from the Deed would outweigh the exclusionary provision, and that the Commission would grant an authorisation pursuant to section 61(7) of the Act.
- 17 The Commission also identified a number of issues in the Draft Determination for which further information and comment was sought.

- 18 Section 62(6) of the Act provides that the Commission may hold a conference prior to making a determination in respect of an application for an authorisation under section 58 of the Act. The Commission decided to hold a conference in Wellington on 20, 21 and 22 April 1999 to assist in its consideration of the application.
- 19 The following parties made oral submissions at the conference, and answered questions from Commissioners and staff:
- Clear;
 - Global One;
 - Ministry of Commerce;
 - Teamtalk;
 - Telecom;
 - TUANZ;
 - Vodafone; and
 - WorldxChange.

STATEMENT OF GOVERNMENT POLICY

- 20 In applying the relevant provisions of the Act, the Commission is required to have regard to the economic policies of the Government, transmitted to the Commission in accordance with section 26 of the Commerce Act. Specifically, section 26(1) provides that:
- “In the exercise of its powers under ... this Act, the Commission shall have regard to the economic policies of the Government as transmitted in writing from time to time to the Commission by the Minister.”
- 21 Pursuant to section 26 of the Commerce Act, the Minister for Enterprise and Commerce (the Minister) has transmitted a statement in writing to the Commission, dated 18 December 1998, of the economic policy of the Government in relation to telecommunications numbering (section 26 statement). A copy of the section 26 statement is attached in Appendix 1.
- 22 The Minister has stated that the Government’s overall policy objectives for telecommunications numbering are:
- to ensure the efficient administration of telecommunications numbering resources; and
 - to ensure the efficient provision of telecommunications number portability.
- 23 To achieve these policy objectives, the Government considers that the following outcomes are necessary:
- *Telecommunications Numbering Administration* - The Government states that telecommunications numbering resources must be independently administered and allocated. Furthermore; “... the allocation, use and ongoing planning of telecommunications numbering must be efficient, must be based on relevant principles, and must involve robust processes including binding dispute resolution to resolve any disputes that arise.”

- *Telecommunications Number Portability* - The Government states that telecommunications number portability must be available between telecommunications networks as "... number portability reduces customer switching costs and puts extra pressure on prices where relevant alternative services are available."

24 The Government considers that the form of number portability provision must be based on principles of economic efficiency.

25 The Minister has advised that the Government considers that a voluntary industry-based numbering arrangement covering number administration and number portability will best achieve its stated objectives for telecommunications numbering. Specifically, it is stated that:

"... the objectives and outcomes for telecommunications numbering will be best achieved by means of a voluntary industry-based numbering arrangement covering number administration and number portability, in preference to the status quo or a regulated numbering co-ordination mechanism."³

Consideration to be Given to Statements of the Economic Policies of Government

26 The implications of section 26 statements have previously been considered by the Commission and the High Court.⁴ The Commission has noted that:

"... having regard to the general policy discretion in the Act to promote competition section 26 may be used to advise the Commission of Government policy or policies or to be more specific in relation thereto. It is not to influence or determine the decisions which the Commission must make. Thus, fully preserving the discretions given to the Commission in the Act, the Commission is required only 'to have regard to' such statements in reaching its decisions."⁵

27 The High Court (Wylie J) has held that transmitting a section 26 statement to the Commission:⁶

"... is the exercise of a statutory right specifically conferred on {the Minister} by the Legislature for the very purpose of influencing the outcome of applications under the Act. That is not to say that the Commission ... is bound to apply the policy so transmitted to it. The statutory injunction of section 26 is no greater than that the Commission 'shall have regard to' the Government's policy."

28 Further:

"As with any other evidence it is for the tribunal to assess the weight to be given to each item of evidence and in the case of a statement of this kind, which in our view is simply an evidentiary statement of Government policy - it is certainly not a direction - it remains for the tribunal to assess the weight to be given to it as an expression of official perception of, in this case, public benefit. ...

The tribunal may not ignore the statement. It must be given genuine attention and thought, and such weight as the tribunal considers appropriate. But having done that, the tribunal is entitled to conclude it is not of sufficient significance either alone or together with other matters to outweigh other contrary considerations which it must take into account in accordance with its statutory function: ... In the end, however weighty the statement may be as an expression of

³ Section 26 statement.

⁴ *Re New Zealand Kiwifruit Exporters Associations (Inc) – New Zealand Kiwifruit Coolstorers Association (Inc)* (1989) 2 NZBLC (Com) 104,485.

⁵ Above n4, 104,494.

⁶ *New Zealand Co-operative Dairy Company Ltd & Anor v Commerce Commission* (1991) 3 NZBLC 102,067.

considered Government policy, it does not have any legislative effect to vary the nature of the duties which the tribunal must carry out.”⁷

- 29 The Commission has given the Statement of the Economic Policy of the Government in relation to telecommunications numbering careful consideration in reaching its decision as to whether or not to grant authorisation for the entry into and giving effect to the Deed. Where considered by the Commission to be necessary, issues raised by the section 26 statement are dealt with in the body of the Determination.

BACKGROUND

The Development of the New Zealand Telecommunications Industry

- 30 The telecommunications industry is dynamic, characterised by high levels of innovation, investment and rapidly developing technology. Additionally, the telecommunications industry provides services that are crucial to almost all New Zealand businesses and households.
- 31 The Electric Telegraph Act 1865 established the Telegraphic Department as a monopoly with the ability to construct, establish, maintain and regulate telegraphic communications. The Telegraphic Department, and its successor, the Post Office, continued to provide nearly all telecommunications services (other than television and radio broadcasting) until 1987 when a Government commissioned review of the Post Office resulted in the establishment of Telecom, a state owned enterprise.⁸ Telecommunications policy advice was placed under the responsibility of the Ministry of Commerce.
- 32 In October 1986, customer premises equipment was gradually opened up to competition. New players entered the market almost immediately. From 1 April 1989, New Zealand opened its telecommunications market to full, unlicensed competition. In 1990, the Government privatised Telecom.
- 33 Following the deregulation of the telecommunications industry, competition has emerged in most markets, including local and international toll services, mobile services and, in some areas, the local loop.
- 34 Competition has had some effect on prices, with the prices for long distance calls falling dramatically over the ten year period ending in March 1998.⁹ However, over the same period, the Consumer Price Index for residential telephone rental, purchase and connection has increased steadily even though a 1996 study by Boles de Boer and Evans¹⁰ estimated that Telecom’s productivity improved by an annual compound average of 5.6% over the period 1987-1993.

⁷ Above n6, 102,067-102,068.

⁸ State Owned Enterprises Act, 1986.

⁹ Todd Communications Consortium, New Zealand Telecommunications: the State of Competition; November 1998, p13.

¹⁰ Boles de Boer D and Evans, L; Government Department for Public Corporation in a Deregulated Economy: The Economic Efficiency of New Zealand Telecommunications” 1996, Manuscript.

- 35 Competition, evolving since deregulation, has eroded the market share of the incumbent operator, Telecom. The Budde report estimates that Telecom has 79% market share in the voice market (including mobile) over the period 1997-1998. Budde also estimates that Clear has 10% market share, BellSouth 3% and other service providers have 8% market share.

Telecommunications Regulatory Environment

- 36 The Government has stated that the objective of the telecommunications regulatory framework is to promote sustainable, economically efficient outcomes within the industry. Competition is regarded as the means to achieve this outcome. There are four key components to the regulatory environment: the Commerce Act 1986, the telecommunications disclosure regime, the Kiwi Share Obligation and the Government's threat to take further regulatory action if necessary.

The Commerce Act 1986

- 37 The Commerce Act is an Act to promote competition in markets in New Zealand. Part II of the Commerce Act prohibits contracts, arrangements and understandings that substantially lessen competition or contain exclusionary provisions, price fixing, resale price maintenance, and the use of a dominant position in a market for the purpose of restricting, preventing or deterring entry or eliminating a person from the market.
- 38 The Commerce Act is relied on to ensure competition in the telecommunications industry and is the principal legal mechanism for ensuring that competitors have access to critical telecommunications facilities and resources.

The Telecommunications (Disclosure) Regulations 1990

- 39 The Telecommunications (Disclosure) Regulations 1990 (Disclosure Regulations) impose certain information disclosure requirements on Telecom Corporation of New Zealand Limited (Telecom Corp) and its subsidiaries. The Disclosure Regulations require Telecom Corp to publish information about the prices and terms and conditions under which certain prescribed services are supplied. Telecom Corp is also required to disclose interconnection agreements with other parties, including its subsidiaries, and publish separate financial statements for its principal operating subsidiary, Telecom.
- 40 The objectives of the requirements placed on Telecom Corp include:
- ensuring that relevant telecommunications service pricing and interconnect agreement information is available to other telecommunications operators; and
 - assisting in the detection of anti-competitive behaviour and any excess profits in any monopoly components of Telecom's business.

Kiwi Share Obligation

- 41 On the sale of its shareholding in Telecom, the Government retained a Kiwi (or golden) Share which provided special voting rights and created certain obligations that:

- control the maximum shareholdings of any single foreign party;
- control the transfers of blocks of shares among parties; and
- ensure Telecom's compliance with the following residential service pledges:
 - the local free calling tariff option is to remain available to all residential customers;
 - the Standard Residential Rental for a phone line is not to rise faster than Consumer Price Index movements unless the profits of Telecom's Regional Operating Companies are unreasonably impaired; and
 - phone line rentals for residential customers in rural areas must not be higher than in the cities, and the residential service will remain as widely available as it is at present.

The Threat of Government Regulation

- 42 In December 1991, the Government issued a policy statement towards the development of competition in New Zealand telecommunications markets. After identifying the key aspects of existing policy, the Government stated:
- “... if it proves to be necessary, the Government will consider the introduction of other statutory measures or regulation. It will take particular care to ensure that it is not seen to be acting merely to enhance the commercial position of one firm or group within society at the expense of another.”
- 43 The Government also stated that interconnection was the critical competition issue and it expected all parties to act in good faith; to expedite negotiations and any court actions and to recognise the unique regulatory features of New Zealand's telecommunications markets.
- 44 The most recent threat of government regulation was in August 1998 when the Minister of Communications, Mr Maurice Williamson, threatened a regulatory solution to develop number allocation and portability rules if telecommunication companies did not develop by 30 November 1998 the following:
- an appropriate set of principles for number allocation and administration;
 - establishment and funding of an independent number administrator;
 - a dispute resolution mechanism; and
 - a legal framework within which such an approach would operate.

Number Administration

- 45 To date the administration of numbers has been the responsibility of Telecom.
- 46 Initially, the Commerce Act was the primary means by which to resolve numbering disputes. However, in 1991 a review of access to numbers resulted in the formation of the New Zealand Telecommunications Numbering Advisory Group (NZTNAG). NZTNAG was established by the Government in February 1993 as a consultative body and its terms of reference were:

“... to discuss and seek consensus on switched telecommunication networks numbering issues in New Zealand, with the objectives of facilitating competition and improving the benefits to users of telecommunications services.”

- 47 NZTNAG membership is voluntary and consists of telecommunications service providers, Government officials and user representatives. NZTNAG is chaired and convened by the Ministry of Commerce with all decisions requiring consensus. NZTNAG has no particular powers other than the provision of views to the Minister of Communications.
- 48 In NZTNAG’s first years of operation, the majority of number allocation principles were determined with subsequent revisions as required. These principles were then used by Telecom to develop the Telecom Numbering Plan. The Telecom Numbering Plan sets out the rules by which codes and numbers are allocated and includes all codes and numbers required by the Telecom network to provide services to customers, including those elements allocated to other telecommunications service providers to facilitate interconnection.
- 49 Telecommunications service providers apply for number allocations from Telecom according to the rules of the Telecom Numbering Plan with Telecom then accepting or rejecting the application. Initial allocations of numbers remain confidential until the earlier of the public disclosure of the relevant interconnection agreement or the activation of the code in the Telecom network. Telecom publishes a record of allocations in its network every three months.
- 50 Some telecommunications service providers have expressed concern over this method of number allocation and administration. The concerns relate, in part, to Telecom’s claim of ownership of the numbers allocated and administered under the Telecom Numbering Plan. Telecom considers that the numbers were part of the assets sold by the Government in 1987. Telecommunications service providers also have concerns about the sometimes lengthy process of resolving issues by consensus. NZTNAG members have called for the introduction of a timely dispute resolution process. However, Telecom’s position has been that it would not voluntarily agree to such a process.
- 51 NZTNAG members have also been unable to agree on a mutually acceptable and independent number administration process.
- 52 In early 1998, BellSouth withdrew from NZTNAG participation, stating that NZTNAG was ineffective in resolving numbering issues.¹¹ NZTNAG agreed to keep BellSouth fully informed and to continue to consult with BellSouth.

Portability

Types of Portability

- 53 Portability is the ability of telephone subscribers to retain a telephone number if they change telecommunications service provider (service provider portability), change telecommunication services (service portability) or change physical locations

¹¹ BellSouth media release, 6 May 1998.

(geographic portability), without impairing quality, reliability or convenience of use of that number. The processes in the Deed relating to number portability address the issue of service provider portability only. The following background information briefly explains the different types of portability.

Service Provider Portability

- 54 Service provider portability enables a telephone subscriber to change telecommunications service provider while remaining at the same physical location, and retaining the same telephone number. Service provider portability is also known as inter-carrier portability.
- 55 Service provider portability is regarded by many as critical to the development of competition in the local telephony market, as subscribers, particularly business customers, place importance on the ability to retain the same telephone number. An OFTEL Report¹² stated that the Director General of Telecommunications and his predecessors
- “... have long been convinced that the absence of number portability is a major barrier to customers changing operator, and hence to the development of effective competition here in the UK.”
- 56 An American survey found that 90% of businesses were unlikely to switch local service providers at a reduced price, if they had to change telephone numbers.¹³ The same survey found that 80% of residential customers considered that changing telephone numbers when changing carriers would be a significant impediment.
- 57 A New Zealand survey¹⁴ commissioned by Clear found that 71% of residential customers and 85% of business customers were unlikely to change their local service telecommunications supplier if they had to change their telephone number. The same survey found that if customers were able to retain their telephone number, 52% of residential customers and 53% of business customers would be unlikely to change their local service telecommunications supplier.¹⁵
- 58 It should be noted that if customers are able to obtain a discount, they are more likely to change local service telecommunications suppliers, even if they have to change their telephone number. The Clear commissioned survey found that if customers were offered a 10% discount, 44% of residential customers and 73% of business customers would be unlikely to change their local telecommunications supplier. If customers were offered a 10% discount and able to retain their telephone number, 18% of residential customers and 24% of business customers would be unlikely to change their local telecommunications supplier.
- 59 The results of these surveys suggest that if service provider portability is not available, it is more difficult for new entrants to win customers from the incumbent telecommunications service provider. As a result, lack of service provider portability

¹² Office of Telecommunications, Inquiry by the Monopolies and Mergers Commission into Telephone Number Portability: Explanatory Statement from the Director General of Communications, 1995, p2.

¹³ T H Reinke, Local Number Portability, Telecommunications Policy, Vol. 22, No 1, pp73-87, 74, 1998.

¹⁴ Research Solutions Ltd, Number Portability Research, November 1996.

¹⁵ Assuming the new supplier does not offer a discount.

may deter new entrants and mean that any new entrants to the market are not able to compete on a 'level playing field' with the incumbent operator.

60 The Australian Competition and Consumer Commission has stated:¹⁶

"The provision of number portability can potentially lower the costs incurred by customers when changing from one carriage service provider to another and thereby promote competition. In the absence of number portability, competing service providers may have to offer significantly lower prices and/or provide significantly higher quality services than the customer's existing service provider in order to compete effectively. This disincentive may discourage efficient entry and retard the promotion of competition more generally. Number portability, by reducing the costs to customers associated with changing carriage service providers, may therefore promote competition."

61 Service provider portability in New Zealand is generally considered in terms of:

- local number portability which refers to portability of fixed line telephone numbers;
- cellular portability which refers to the portability of mobile telephone numbers; and
- 0800 portability which refers to the portability of 0800/0508 (or free-to-caller) numbers.

Service Portability

62 Service portability allows subscribers to change the types of service which they receive from a telecommunications carrier while retaining the same telephone number. For example, a subscriber may change from a fixed telephone line to a mobile telephone service, but retain the same number. Lack of service portability is considered a potential impediment to the substitution of cellular mobile services for wire-line based telecommunications services.¹⁷

Geographic Portability

63 Geographic portability enables a subscriber to shift to a new physical location but retain the same telephone number without the need to pay a premium for the service. It is also known as location portability.

Portability Methods

64 The Commission has no view as to which portability method would be most efficient in the New Zealand telecommunications environment. The following information is provided by way of background information, and to briefly identify the distinguishing factors of the portability methods advocated by the various parties.

65 There are two primary types of methods for implementing number portability: non-database methods and database methods.

¹⁶ Australian Competition and Consumer Commission, ACCC Directions to the Australian Communications Authority on Number Portability – Commission's Reasoning, September 1997.

¹⁷ Above n9, p74.

Non-Database Methods

- 66 Non-database methods include call forwarding, direct inward dialling, and their derivatives.
- 67 Common criticisms of non-database methods include:
- the strain they place on number plan administration and their contribution to area code exhaustion (as they use two telephone numbers);
 - their inability to support functions such as caller identification;
 - their ability to only handle a limited number of simultaneous calls to a particular service provider;
 - occasionally longer call set-up times;
 - that the incumbent local exchange service provider's network is required to route calls;
 - that they may provide the incumbent local exchange service provider with access to competitor's proprietary information; and
 - they can impose substantial costs on new entrants.
- 68 The Commission notes that not all of these criticisms are applicable to all non-data base methods.
- 69 At the conference, Telecom stated that it considers the current form of portability is sufficient for the levels of demand evident in the market today. The form of portability currently in use in New Zealand is call forwarding, a non-database method.

Database Methods

- 70 Database methods use intelligent network or advanced intelligent network capabilities to route (or port) calls to their correct terminating locations. Hence they are sometimes known as "intelligent network solutions". Some of the parties to the Deed and some of the parties opposed to the Deed advocate the implementation of an intelligent network solution in New Zealand.
- 71 Database methods are sometimes considered long term solutions as they can significantly reduce the limitations of non-database methods. Database methods use either single number or dual number solutions to port numbers.
- 72 Single number solutions use only one number (the number dialled by the calling party) to identify the customer in the serving switch. For each call, the database is 'dipped' and digits added to the dialled number are used by the intelligent network to direct the call to the appropriate caller and switch.
- 73 Dual number solutions use a 'dual number domain' by assigning a second identity number to every subscriber whose telephone number has been ported. However, as each subscriber with a ported number requires two numbers, this is a less efficient use of numbers.
- 74 Triggering mechanisms can be used in conjunction with some database methods to determine whether or not it is necessary to check the database.

Local Number Portability

NZTNAG Negotiations

- 75 Pressure within NZTNAG to resolve number portability issues first emerged in 1995.¹⁸ Progress was slow and concerns were expressed about the ability of NZTNAG to deal with numbering issues. These concerns arose in part due to the NZTNAG's consensus voting structure.¹⁹
- 76 In November 1996, NZTNAG members agreed that number portability should first be introduced through call forwarding, in particular Telecom's remote call forwarding product, "Customer Link". However members could not agree over pricing issues and in December 1996 Telecom's opening offer was rejected. A revised offer from Telecom in March 1996 was also rejected.

Bilateral Negotiations

- 77 In March 1997, the Ministry of Commerce announced that it would co-ordinate bilateral "briefings between the carriers to attempt to resolve number portability issues." The Ministry said it was not acting as a mediator but providing
 "... the opportunity for the two parties to state their positions in front of the Ministry, both to keep the Ministry informed and clear up any misconceptions that have been going on."
- 78 Eventually, local number portability agreements providing for local number portability via call forwarding were signed and the incumbent operator, Telecom, has advised that it has reciprocal local number portability agreements with all carriers offering or intending to offer, local telephone services.
- 79 Entrants to the telecommunications market would generally prefer that portability was conducted via an intelligent network solution.²⁰ However there has been debate between the telecommunications service providers as to how and when an intelligent network solution should be introduced, if at all. Intelligent network solutions are more expensive than call forwarding options, therefore the issue of cost allocation has compounded the issue.

Cellular Portability

- 80 Currently, cellular portability is not available in New Zealand. There have been lengthy negotiations between the major cellular service providers.

0800 Portability

New Zealand Telecommunications Numbering Advisory Group Discussions

- 81 In September 1994, NZTNAG set up an 0800 freephone service number portability sub-committee to investigate and advise on the practicability, technical implementation

¹⁸ Summary record for the 18th meeting of NZTNAG, 29 June 1995.

¹⁹ Hosking, Bob; Portability Squabbles Costing; Management Technology Briefing, September 1996.

²⁰ Annex, entitled "Background: Telecommunications Numbering Issues in New Zealand", to letter dated 30 July 1998 from Ministry of Commerce and the Treasury to the Ministers of Finance, Enterprise and Commerce, and Communications.

and possible costs of 0800 number portability. Any commercial issues were to be dealt with on a bilateral basis.

- 82 In August 1995, a technical sub-committee was established to define and design an 0800 portability solution. Additionally, BellSouth, Clear, Telecom and Telstra undertook to work to develop an 0800 number portability administration agreement.
- 83 Progress in the NZTNAG forum was slow and participants alleged that Telecom was deliberately delaying negotiations. It is not clear where the blame lies in relation to the delays that have occurred. However some progress was made with the parties designing an 0800 number portability technical solution and commencing planning for operational procedures and equipment.
- 84 In early 1998, the parties reached an impasse concerning the procedures to be followed when porting an 0800 number between service providers.

1998 Bilateral Negotiations

- 85 Following the breakdown of the multilateral negotiations, Telecom commenced bilateral negotiations with some parties.

1998 Joint Venture Arrangement

- 86 As Telecom conducted its bilateral negotiations, six of the parties which had participated in the original 0800 joint venture agreement decided to form a new joint venture and then ask Telecom to participate once the six parties were in agreement.
- 87 The parties, including Telecom, have now prepared a draft Joint Venture Agreement for the purpose of introducing free-to-caller number portability into New Zealand, co-ordinating the operation of a system for the continued portability of free-to-caller numbers and the continued administration of a free-to-caller number allocation system.
- 88 The Commission understand that the parties are currently in the process of signing, or are close to signing, the Joint Venture Agreement.

Government Intervention in Number Portability

- 89 In June 1998, the Minister of Communications initiated a review of telecommunications numbering issues and, as part of that review, sought comment from major telecommunications service providers. The resulting report identified continuing issues in:
- setting up an independent process for allocating and resolving disputes on number allocation;
 - introducing 0800 number portability; and
 - making progress on considering long term solutions for number portability.
- 90 The report noted a range of options for resolving these issues and concluded that:
- “... voluntary independent number administration with access to dispute resolution ... has the potential to efficiently resolve numbering issues provided that:
- satisfactory principles and procedures, including dispute resolution, can be agreed in a timely manner; and

- the arrangements include number portability.”

- 91 The Minister of Communications directed Ministry of Commerce officials to commence developing a voluntary solution, in discussion with Telecom and other telecommunications service providers. The Minister advised parties that, if satisfactory arrangements were not developed by 30 November 1998, he would recommend that the Government develop a regulatory solution that set allocation and portability rules, established an industry-funded administrator, and provided for compulsory arbitration of disputes.
- 92 Therefore, in late August 1998, telecommunications industry participants were invited to work with Government officials and other industry participants to develop:
- an appropriate set of principles for number administration and allocation;
 - the establishment and industry funding of an independent number administrator;
 - a dispute resolution mechanism; and
 - a legal framework within which such an approach would operate.
- 93 In mid-November, the Ministry of Commerce submitted a draft deed for negotiation to the prospective parties. Clear, Compass, Newcall, Saturn, Teamtalk, Telecom, Telstra, Vodafone and WorldxChange all participated in the negotiations.
- 94 The Deed, which is the subject of the Application, is the outcome of those discussions. However, of those who participated in negotiations, Clear, Compass, Saturn and WorldxChange have not signed the Deed.

THE NUMBER ADMINISTRATION DEED

- 95 The Deed intends to establish a telecommunications industry-based mechanism for the centralised and independent administration of the parties’ telecommunications numbering resources, and to facilitate the provision of number portability.
- 96 Principally, the numbering mechanism will comprise an industry body (Management Committee) to oversee number administration and number portability, and an independent Number Administrator.
- 97 The Management Committee will consist of one voting representative from each party to the Deed, with an Independent Chair. Each party shall have only one voting representative on the Management Committee, and a single vote as to each decision of the Management Committee.
- 98 Every person who is providing public switched telecommunications services in New Zealand is entitled to become a party to the Deed, and the parties’ public switched telecommunications numbering resources will be under the administration of the Number Administrator. Only parties to the Deed will be eligible for number allocations in accordance with the Number Allocation Rules established under the Deed.

Numbering Principles

- 99 The Deed sets out numbering principles (the Principles) which all persons exercising functions, powers and responsibilities under the Deed must be consistent, and with which the Number Allocation Rules must be consistent.
- 100 The Principles provide for:
- the economically efficient, non-discriminatory allocation of numbering resources;
 - the economically efficient use of numbering resources;
 - the economically efficient planning and implementation of numbering;
 - the portability of allocated numbers;
 - the provision of economically efficient number portability arrangements;
 - existing number allocations to stand, except in specific circumstances;
 - existing number ownership not to be affected, although ownership rights will not prevent or limit the operation of the Deed;
 - network freedom in that the parties' rights to implement network changes, which are consistent with the Deed, are not limited; and
 - dispute resolution for disputes over numbering issues.

Number Allocation

- 101 The Deed provides that any person providing public switched telecommunication services can become a party to the Deed, and that becoming a party is a prerequisite to being allocated numbers. Persons intending to provide public switched telecommunications services may request number allocations, providing certain requirements as to Deed participation and the implementation of telecommunications services are met.
- 102 The Deed provides for the appointment of a Number Administrator, and the parties must place their numbering plans under the control of the Number Administrator. The Number Administrator will be responsible for allocating numbers in accordance with the Number Allocation Rules. The allocation of numbering resources is required to be economically efficient.
- 103 Provision is made for dispute resolution in relation to disputes arising from number allocation decisions.
- 104 The Deed does not affect interconnection agreements, or the ownership of numbers and numbering plans brought within the mechanism created by the Deed. However, as stated earlier, ownership rights cannot be relied on to override the scheme established by the Deed.

Number Portability

- 105 The Deed provides for the Management Committee (by majority) to commission an independent expert to report on whether there are positive net economic benefits to

society from the implementation and operation of proposed preferred number portability²¹ solutions.

- 106 The Management Committee has specific time frames within which to agree on the terms of reference for the independent expert, the method for allocating costs of the independent expert, and for the selection of a suitable independent expert. It is noted that there is provision for these matters to be referred to arbitration, which would lengthen the time frames.
- 107 Further, the independent expert's report is required to be produced within 6 months of being commissioned. The report is required to determine whether or not there are net economic benefits to the implementation of one or more preferred number portability solutions.
- 108 Number portability arrangements, including pricing and operational matters, are to be economically efficient.
- 109 The Management Committee has a stated time frame within which to agree on the report's conclusion. The Management Committee will decide (by consensus) whether to proceed with the preferred number portability option, and if so, the timing of implementation and the allocation of implementation costs. There is provision for these issues to be referred to arbitration if the Management Committee fails to reach a consensus (which again would necessarily lengthen the time frame).
- 110 If a preferred number portability solution is to be implemented, all parties are bound to meet their share of the costs of implementation and operation of that solution.
- 111 The independent expert is to assess the total costs to society of the implementation and operation of the proposed preferred number portability solution, including the net costs of the implementation and operation of number portability in the parties' networks. The net costs are those costs arising from network enhancements required for the provision of number portability less benefits arising from those network enhancements that do not solely relate to the provision of number portability.
- 112 It is noted that the Deed's number portability provisions do not apply to free-to-caller number portability development.

Management Committee

- 113 The Deed establishes the Management Committee which comprises one representative from each party to the Deed, with an Independent Chair. Each voting representative has a single vote in relation to Management Committee decisions. The Independent Chair may investigate breaches and impose certain sanctions where parties breach the Deed.
- 114 The Management Committee decision to commission an independent study into whether there are positive net economic benefits to society from the implementation and operation of proposed preferred number portability solutions requires a majority

²¹ The term "preferred number portability" is used to describe the method of portability selected by the Management Committee in accordance with the Deed's procedures.

decision. Other decisions of the Management Committee require consensus. For example:

- the decision of the Management Committee to require or not to require a prospective party to pay or make an irrevocable commitment to pay, a share of the costs of implementing and operating the preferred number portability solution;
- agreement by the parties to have more than one voting representative on the Management Committee;
- appointment of the Independent Chair and his/her terms of appointment;
- Management Committee decisions relating to changes to the Telecommunications Numbering Plan;
- Management Committee decisions relating to the establishment of or changes to the Number Allocation Rules;
- appointment of the Number Administrator and his/her terms of appointment;
- number portability development, other than the decision to commission the independent expert;
- appointment of Management Committee sub-committees; and
- revision of the initial Number Allocation Rules (the number allocation principles of NZTNAG) by the Management Committee.

Dispute Resolution

- 115 The Deed provides for dispute resolution which can be invoked in a wide range of circumstances including, the Applicants note, “circumstances which would not normally be subject to a dispute resolution process.”
- 116 Decisions of the Management Committee, the Number Administrator and the Independent Chair are subject to dispute resolution.
- 117 All matters requiring a consensus decision of the Management Committee are referable to dispute resolution. Any party affected by the matter in dispute may give notice referring the matter to arbitration.
- 118 Unless otherwise agreed, and subject to a number of exceptions, arbitration is to be conducted in accordance with the Arbitration Act 1996. Further, the arbitrator shall adopt, wherever practicable, a simplified and expedited procedure.

Operational Costs

- 119 The Deed provides that each party shall pay an annual fee of \$10,000 for the operational costs of administering the Deed, and the balance of any operational costs shall be apportioned on the basis of number allocations made in that year.

Confidentiality

- 120 The Deed is stated to be a public document, but provides that no party shall make any public announcements relating to the affairs of the Management Committee, or to the Deed, without the prior approval of the Management Committee.

Effect of Deed

- 121 The Deed provides for the parties to investigate and decide on whether an application for authorisation, pursuant to section 58 of the Act, is required. The provisions of the Deed in respect of which authorisation is required will not come into force until authorisation is granted.
- 122 The Deed will not affect or limit the terms and provisions of any interconnection agreements between any of the parties.

On-Sale of Numbers

- 123 There is some debate as to whether the Deed allows for the on-sale of numbers by parties to the Deed to service providers which are not carriers to the Deed.
- 124 Telecom considers that service providers that are not party to the Deed can obtain numbers by resale. Telecom suggests service providers are able to use their own 05XY or 02XY codes to resell network services to other service providers, and as such, service providers can compete in the toll and mobile markets without having to enter the Deed. With respect to local services, Telecom suggests that service providers that are party to the Deed can resell local network services (and possibly number portability services) to service providers that are not party to the Deed. Telecom suggests that a service provider that is a party to the Deed could apply for local numbers on behalf of the service provider that is not a party, and handle all local calls on behalf of that carrier.
- 125 Teamtalk notes that it can see no reason why resellers cannot access number groups under the guise of reselling services provided by parties to the Deed.
- 126 The Ministry of Commerce considers that the Deed does not prohibit the on-selling of numbers and notes that while the Deed provides that a party may not assign its rights under the Deed it does not prohibit the assignment of benefits received under the Deed. However the Ministry notes that the initial number allocation rules will be those of NZTNAG and as such on-selling will not always be possible, initially at least. The Ministry has stated:

“In the Ministry’s view these provisions do not prohibit on-selling taking place. However, the Deed also provides that the Number Allocation Rules which apply to the allocation of numbers shall be the number allocation principles of NZTNAG, until such time as they are revised (clause 6.3). The NZTNAG number allocation principles provide that for various short access codes, such as 1XYZ and 01XY, an allocated code shall not be reallocated by a carrier to any other person. However, the NZTNAG principles are not comprehensive in their coverage of the numbering resources subject to the Deed. Accordingly on-selling will be prohibited in some cases and, depending on what the new allocation rules provide, may or may not prohibit on-selling for future allocations.

For existing short access codes that have been allocated by Telecom from its numbering plan, Telecom's number allocation rules consistently state that a code allocation may not be transferred to another person. Accordingly, numbers currently allocated by Telecom under its numbering plan, are unable to be on-sold."

Effect of Authorisation

127 The Deed provides a mechanism for independent number administration and the provision of number portability. The Commission must determine whether or not to grant authorisation to the entry into and giving effect to this mechanism. Subsequent decisions of the Management Committee, Number Administrator, or other office holders, in implementing the mechanism will themselves continue to be subject to the provisions of Part II of the Commerce Act (unless authorised).

APPLICATION OF THE ACT

128 In terms of section 58 of the Act, a person may apply for authorisation for arrangements to which sections 27, 28, 29, 37 or 38 may apply.

129 The Applicants have sought an authorisation under:

- sections 58(1) and 58(2) of the Act to the extent (if any) that section 27 would or might apply to the entry into and giving effect to the Deed; and
- sections 58(5) and 58(6) of the Act to the extent (if any) that section 29 would or might apply to the entry into and giving effect to any provision in the Deed.

130 The Applicants consider that sections 27, 29 and 30 of the Act do not apply (or should not apply) to the Deed. However, they state in the application that they recognise that the Commission, or some other person, may take the view that these sections *may* apply to some aspects of the arrangements contemplated by the Deed, and they consider that given the importance of the arrangements to the whole telecommunications sector, there is the need to ensure, so far as practicable, that they are immune from legal challenge by any disaffected party before they are given effect to. The Applicants state that they are applying in the interests of certainty.

131 In respect of any application under sections 58(1) and 58(2) (to the extent, if any, that section 27 of the Act would apply, or might apply), the Commission must consider whether the practice in question has the purpose or effect or likely effect of lessening competition in a market, or will result in a deemed lessening of competition in a market (in terms of section 30). If it concludes that the practice does not have such a purpose or effect, the Commission must decline to authorise the practice under section 61(6).

132 The Applicants have applied for authorisation, not only under sections 58(1) and 58(2), but also under sections 58(5) and 58(6) (to the extent, if any, that section 29 would or might apply). Accordingly, even if the Commission declines to authorise the practice under section 61(6), it may still consider the practice for authorisation under section 61(7) if it considers section 29 applies.

Constitutional and Administrative Law Matters

- 133 Clear presented a late submission to the Commission at the conference on the constitutional and administrative law aspects arising from the authorisation application. Clear made its submission on the premise that the Deed prevented the allocation of numbers to a provider that did not sign the Deed. The corollary of that was seen to be that a provider had to sign the Deed in order to avoid being constrained in the future by an inability to obtain new numbers.
- 134 Clear made wide-ranging submissions on various constitutional and administrative law issues. The issues raised included the improper use of Ministerial influence, matters of “constitutional objectionability” and proper procedure, the right to freedom of association and so on. Having considered all of the matters addressed in this submission, the Commission considers that Clear essentially made three main points:
- i The Deed does by private arrangement what could constitutionally be done by enactment because of the corollary, and the Commission should not assist in achieving that arrangement.

Section 61(7) confers upon the Commission a power to authorise a provision that has the effect of excluding non-parties from a market properly defined. This follows from the principle of statutory interpretation whereby the words in which section 61(7) is expressed are given their natural and ordinary meaning. Given Parliament’s sovereignty, there is no general principle of interpretation that would prevent it from conferring power of the width indicated by the words of section 61(7).

- ii An enactment to the effect of the Deed provides safeguards absent from a private agreement.

Clear submits that, because of the corollary, the mechanism for the Deed should be state regulation. It also suggests that the Deed should be considered as if it were privately established state regulation. Absent the procedural process for state regulation, Clear submits that the process of agreeing the Deed, and subjecting it to the authorisation process under the Commerce Act, amounts to a denial of proper process.

The Commission is not persuaded by these arguments. Significant factors are not properly addressed in Clear's submissions. For example, the submission fails to take into account the counterbalancing factors of negotiation between the parties, the quasi-judicial character of the Commission's proceedings and the prospect of judicial review. Further, the express and limited nature of the Commission's statutory powers to grant authorisation are relevant. The Commission has power to authorise provisions which may otherwise be in breach of sections 27 and 29. However, it will only do so after a detailed consideration of detriments and benefits as required under the Commerce Act. Any authorisation is limited to the provision in question.

In this case all that is being considered for authorisation is the process or mechanism to be set up under the Deed. In this decision the Commission emphasises that if the Management Committee adopts an allocation

methodology which is likely to substantially lessen competition, then this authorisation will not preclude the application of Part II of the Commerce Act to such methodology. Any other anti-competitive outcomes not covered by the authorisation will also be subject to the application of these restrictive trade practices provisions.

- iii An enactment would not be made because it would be contrary to the New Zealand Bill of Rights Act 1990 as would authorisation.

The Commission accepts that section 17 of the New Zealand Bill of Rights Act 1990 (freedom of association) is relevant to this decision. However, the freedoms set out in sections 8-27 of the New Zealand Bill of Rights Act 1990 are not absolutes. There are justified limitations by virtue of section 5 which provides that the rights and freedoms of the Bill of Rights are subject to “reasonable limits prescribed by law as can be demonstrably justified in a free and democratic society.” The subject matter of the Commerce Act relates to arrangements of both behavioural and structural kinds which necessarily restrict freedom of association. The Commerce Act only restricts freedom to associate in an anti-competitive way. It follows that the policy and application of the Commerce Act contemplate certain limits on freedom of association, and that these limits are prescribed by law as reasonable in terms of section 5. If authority is needed for this proposition, it lies in *Alex Couture Inc v Attorney-General of Canada* (1991) 81 DLR (4th) 577 (Que, CA) and *Royal Le Page Real Estate Services Ltd v R* (1993) 105 DLR (4th) 556 (Alta, QB) and implicitly in *Lewis v Real Estate Institute of New Zealand Inc* (1995) 3 HRNZ 436, 446.

- 135 For the above reasons, the Commission rejects the arguments made in Clear's submissions on constitutional and administrative law issues.

MARKET DEFINITION

- 136 Analysis of a trade practice in terms of the Act requires that the activities affected by the practice in question are placed within market boundaries which most clearly highlight the competitive implications of the practice.
- 137 The Commerce Act defines the term “market” as being a market in New Zealand for goods and services as well as for other goods or services that, as a matter of fact and commercial common sense, are substitutable for them.
- 138 Market definition principles have been set out by the High Court in *Telecom Corporation of NZ Ltd v Commerce Commission* (the AMPS A case):²²

“First, and most generally, we seek to identify the area or areas of close competition of relevance for the application(s). In other words, we seek to identify the constraints upon the price and production policies of firms whose conduct is of relevance for the matters litigated. In this matter it is of especial importance to highlight the constraints upon Telecom’s price and production policies.

Secondly, competition may proceed both through substitution in demand and substitution in supply in response to changing prices or, more comprehensively, the changing price-product-

²² (1991) 4 TCLR 473, 502; 3 NZBLC 102,340, 102,362.

service packages offered The mental test that prompts a summary evaluation of the evidence is to ask how buyers and sellers would likely react to a notional small percentage increase in price of the products of interest, eg the standard telephone service, the cellular service (the 'price elevation test'). ...

Thirdly, the market is a multi-dimensional concept – with dimensions of product, space, functional level, and time. Here we need to give special attention to the principles that should govern the isolation of the dimensions of function and time.

If we ask what functional divisions are appropriate in any market definition exercise the answer, plainly enough, must be whatever will best expose the play of market forces, actual and potential, upon buyers and sellers.”

139 In a report on the application which was commissioned by Telecom,²³ Mr Alex Sundakov of NZ Institute of Economic Research, suggested that the relevant markets were:

- markets for various telecommunications services;
- a market for telephone numbers; and
- a market for the portability of numbers among competing telecommunications service providers.

140 The Commission has considered the relevance of each of these separately.

Various Telecommunications Services

141 The interested parties contacted during the Commission’s investigation of the application agreed that access to numbers on a competitively neutral basis, and the ability for numbers to be ported, are important factors which impact on competition in a range of telecommunications services. Telecom has suggested that these services fall within the following markets:

- the provision of access to telephony networks and local telephone calling service to residential customers;
- the provision of Access/Local Service to business customers which are located outside the CBD areas of Auckland, Wellington and Christchurch;
- the provision of Access/Local Service to very large customers located outside the CBD areas;
- the provision of Access/Local Service to business and very large business (corporate) customers located in the CBD areas;
- the provision of mobile telecommunications services to residential customers; and

²³ Telephone Number Administration – Economic Comment on the Number Administration Deed, Alex Sundakov, NZ Institute of Economic Research (Inc) January 1999.

In a covering letter with Mr Sundakov’s report, Chapman Tripp (solicitors for Telecom) have stated: “Although the report was commissioned by only one of the Applicants, Telecom New Zealand Limited, Mr Sundakov also spoke with several of the other Applicants in obtaining the information on which the conclusions in the report are based. Those conclusions (and other statements contained in the report) are solely the work of Mr Sundakov and the Institute and should not necessarily be attributed to Telecom or the other Applicants.”

- the provision of mobile telecommunications services to customers other than residential customers.

142 The Commission considers that there is no great utility in considering the impact of the proposal separately in each of these markets. The way the Deed impacts on each is similar. The parties at the conference accepted that this is the case. Accordingly it is proposed to use the market definition of “the market for various telecommunications services” in the analysis below.

Telephone Numbers

143 At present telephone numbers are allocated to users free of charge. Further, with the exception of some 0800/0508 numbers with premium alpha-numeric combinations (which are not subject to the Deed), it is understood that users do not trade numbers among themselves to any significant extent. Nevertheless, Mr Sundakov, in his report for Telecom on the application, has submitted that some users at least place value on particular numbers, and that there are economic consequences flowing from the allocation process. It has been pointed out that OFTEL has recently sought submissions on whether it would be desirable to permit what could be called a secondary market for numbers in the United Kingdom.

144 Mr Sundakov has concluded that because there are users who would, in principle, be willing to exchange money for access to particular telephone numbers, and there are potential suppliers of those numbers, there exists a market for telephone numbers.

145 The Commission considers that the trading of telephone numbers is unlikely to be materially affected by the proposed Deed, and is unlikely to be more than a minor activity in any event. To the extent that competition issues are raised in respect of the trading of numbers, it is considered that they can be addressed in the context of the broad market for telecommunication services.

Portability of Numbers Among Competing Service Providers

146 None of the interested parties identified how a market defined as that for “the portability of numbers among competing telecommunications service providers” would assist in identifying or highlighting competition issues raised by the Deed.

147 It appears to the Commission that while such a definition identifies the matter of principal concern to service providers, it is not necessary to use this definition to analyse the case adequately.

Conclusion on Market Definition

148 The Commission concludes that the relevant markets for the consideration of the application are the markets for the provision of various telecommunications services. The principal parties at the conference agreed with this conclusion.

149 The markets are national in scope.

THE COUNTERFACTUAL

Introduction

- 150 In carrying out an assessment of an application under section 58 of the Act, the Commission must assess the likely competitive effects of the proposal, and any public benefits and detriments likely to result. This requires the Commission to determine a benchmark against which to measure the effects of changes arising from the proposal. As the Commission has noted in previous decisions, the benchmark is the counterfactual; that is, the likely situation in the absence of the proposed arrangement. Thus the Commission undertakes a with and without comparison rather than a before and after comparison.
- 151 The counterfactual is not necessarily the arrangement which might be preferred by the Commission or by others with an interest in the telecommunications sector. The Commission does not have the mandate, nor the expertise, to be a market designer. The counterfactual is simply the Commission's pragmatic and commercial assessment of what is likely to occur in the absence of the proposal.

Views of the Parties

- 152 Most interested parties have suggested counterfactuals which fall within two broad categories. First, there is what is described as a continuation of the 'status quo'. Second, there is the 'regulated solution' (with variations).
- 153 In his report for Telecom on the application, Mr Alex Sundakov has commented separately on the counterfactual for number allocation and the counterfactual for number portability. In respect of number allocation he said:
- “In the absence of the Deed, the existing practice for number allocation is likely to remain in place. Again from a policy perspective, the anticipated concern is that the incumbent network operator may have an incentive to push its advantage as far as it can go without triggering an adverse legal or regulatory response. However, those who believe that Telecom is substantially constrained by external pressure, point out that as market participants become better established in the New Zealand market, and given the attention from regulatory authorities, Telecom would have increasingly fewer degrees of freedom to behave differently from how a disinterested third-party administrator would behave.
- An alternative view is that Telecom is not sufficiently constrained by external pressure, such as the threat of regulation, and that over time, in the absence of the Deed, Telecom would increasingly use the number allocation process for its own competitive advantage. According to this view, that could result in number shortages and would deter new entry into the industry. The sustainability of this counterfactual would depend on the likely response of the Government to an obvious breakdown in the market.”
- 154 In respect of number portability, Mr Sundakov has said that in the absence of compulsory participation by all service providers in the development of long term number portability (such as would be the case with the Deed) the investment required to implement portability does not appear likely to take place. Consequently he suggests that the counterfactual to the Deed is a situation where there is no long term number portability in New Zealand under the foreseeable technology. Mr Sundakov notes however, that the Government policy statement suggests an alternative counterfactual is that the Government would regulate to ensure compulsory participation in the number

portability regime, in a format that is likely to resemble closely the provisions of the Deed.

155 Telecom has subsequently confirmed that it agrees with this view. That is, it considers that in the counterfactual, the Government would be likely to regulate for compulsory participation along the lines envisaged by the Deed. Others who have signed the Deed have expressed similar views.

156 Vodafone has said it considers a status quo counterfactual is the more likely outcome in the absence of the Deed. At the conference, its counsel said:

“Vodafone does not see a real prospect of Government intervention if the Deed is not implemented or is delayed. Vodafone considers regulation to be unlikely because of the difficulty in designing and implementing workable and appropriate regulation, because over the 13 year history of the Commerce Act the Government has maintained a clear position that it believes competition, and not regulation, to deliver efficiencies, lower costs and provide for new customer services ...”

157 In support of the status quo counterfactual Vodafone also referred to:

- the potential for further industry negotiation;
- the difficulty in regulating an industry in which competitors are different sizes and not all competitors offer an extensive range of telecommunication services;
- the difficulty in regulating an area of rapidly changing technology; and
- the Minister’s statement subsequent to the signing of the Deed that the Government would not now need to regulate.

158 Parties opposed to the Deed have, in the main, suggested that the appropriate counterfactual is a number allocation regime which is similar to that proposed in the Deed, but importantly, is not linked to the number portability regime. Participation in a number portability regime would be voluntary. One party suggested that Telecom would be required to make the necessary enhancements to its network to make number portability possible as the capacity of the call forwarding option would be exhausted within 2 years. Other parties suggested that Telecom would be required by the Government to invest in an intelligent network solution without further analysis being undertaken.

159 Among the parties approached for comment on the counterfactual was the Ministry of Commerce. It was asked about the advice it would be likely to give to the Government in the absence of the Deed. The Ministry replied as follows:

“When the Minister of Communications invited telecommunications companies to work toward a numbering agreement in late August 1998, he advised them to reach agreement by 30 November 1998 or face regulation. Subsequently, in his press statement dated 14 December 1998, the Minister said ‘because an agreement now exists which I consider enables all substantive numbering issues to be effectively addressed in the best interests of New Zealand as a whole, I see no need for the Government to regulate in this area’.

It is our view that if the Deed were not able to proceed, an agreement has in effect not been able to be reached. In this case the Ministry of Commerce’s advice to the Minister of Communications is likely to be that the Government should pass empowering legislation to

enable a numbering mechanism with the characteristics of the Number Administration Deed to be established by regulation.”²⁴

160 The Ministry’s advice appears to match the views of the Government. In a letter to Clear on 11 February 1999, the Minister of Communications said:

“I can only advise you that, consistent with my earlier statements to the industry, if the Deed were not able to proceed, it is likely that the Government would regulate to enable a numbering mechanism with the characteristics of the Deed to be established.”²⁵

Factors Influencing the Choice of Counterfactual

161 The Commission is required to identify the counterfactual which, having regard to matters, is the most likely outcome in the absence of the Deed. This requires consideration of such matters as the commercial incentives of the parties and, of particular importance, likely Government actions. The following matters are considered relevant:

- there is unanimous belief from new service providers that independent number administration in the manner proposed by the Deed is desirable irrespective of the type of number portability regime which is adopted;
- there is strong support for number portability from new service providers, from telecommunication users and other consumer groups, from the Government, and from political parties. All consider that efficient number portability would enhance competition in telecommunications markets;
- all parties, with the possible exception of Telecom, regard the call forwarding method of number portability as being less efficient than, and technically inferior to, other possible options;
- there is agreement by most that it is appropriate to assess the benefits of different portability options against their costs before a decision is made on the introduction of a particular option. (What should count as benefits and costs remains a matter of dispute.) However the view of Global One is that international evidence clearly demonstrates that there are major net benefits from implementing an alternative to the call forwarding option, and this view appears to be shared by most of the other parties opposed to the Deed;
- Telecom has stated that it was persuaded to agree to some elements of the Deed because it wished to avoid the regulatory alternative, which it considered was very real;
- Telecom considers the Deed as being part of a package. It has stated that it would not be likely to agree to a voluntary alternative package which imposed greater costs or risks on Telecom. At the conference Telecom’s General Manager Interconnect advised:

“The Deed was negotiated from the outset as a package and a number of concessions were made in relation to number administration by Telecom to try ... meet the Government’s objective and produce a satisfactory Deed covering both administration and the process of portability. It’s not our view that we would be prepared to sign up to simply the administration part of the Deed absent the portability provisions.”

²⁴ Letter from Mike Lear, Ministry of Commerce to Dick Adam, Commerce Commission dated 3 February 1999.

²⁵ Letter from Minister of Communications to Rosanne Graham, Clear Communications dated 11 February 1999.

- Vodafone has informed the Commission that it would not voluntarily enter an arrangement for determining and paying for an appropriate number portability solution unless all other service providers were similarly committed;
- the industry is characterised by rapid technological change, which would make a prescriptive regulatory regime difficult to draw up and administer;
- the present Government has indicated a preference to rely on the Commerce Act, rather than industry specific regulations to address competition concerns; and
- any regulation would require empowering legislation, and that there is little opportunity for this legislation to be passed in 1999.

162 In addition the Government has made it clear that it considers that a continuation of the status quo is unacceptable. As outlined in the section 26 statement, it considers that telecommunications numbering resources must be independently administered and allocated, that number portability must be available where required, and that the form of number portability must be based on principles of economic efficiency.

163 Government Ministers have stated often that if the numbering issues cannot be resolved by industry participants, the Government would impose a regulatory solution. In his statement on 28 August 1998, the Minister of Communications said in respect of elements in the regulatory solution:

“These are likely to include:

- Setting allocation and portability rules and procedures;
- Establishing an independent number administrator, funded by industry;
- Providing access to compulsory arbitration.”

164 The Minister of Communications has stated his expectation is that the provisions of the regulations would be very similar to provisions in the Deed.

The Choice of Counterfactual

165 In its Draft Determination, the Commission sought comments on the counterfactual. It went into the conference with the view that the most likely counterfactual was either a regulated scenario or the status quo scenario. The parties were questioned closely on the subject.

Status Quo Scenario

166 The one party which indicated a view that the status quo scenario was the appropriate counterfactual was Vodafone. It indicated that its view is based on the difficulty of designing and implementing an appropriate regulatory regime, the cost of administering regulations, and the distaste which governments have expressed towards regulations since the Commerce Act was passed 13 years ago. In the absence of the Deed, Vodafone considers bilateral negotiations will take place.

167 The Commission accepts that the points made by Vodafone are important, and considers that there is some possibility of the status quo continuing in the absence of the Deed. However, it has concluded that the status quo is unlikely to achieve the goals of major industry participants and the Government to introduce independent number

administration and efficient number portability. For this reason the Commission considers that the status quo scenario will be unlikely to continue in the absence of the Deed, and consequently rejects this counterfactual for further analysis.

Regulated Solution Scenario

168 In the absence of the Deed, the Commission considers that there will continue to be strong pressure for independent number administration and for a more efficient number portability method than the current call forwarding system. It also considers that this will not be achieved on a voluntary basis. At the conference Telecom's General Manager Interconnect stated:

"Telecom's position is, and has been, that the current form of portability is sufficient for the levels of demand evident in the market today So until that situation changes in our perception, our view would be that it would be that the need for a bilateral process arrangement is unnecessary, because we have a form of existing portability that is sufficient for current demand in the market."

169 Nothing provided to the Commission has suggested that independent number administration and a more efficient number portability method will be achieved in the absence of the Deed except by Government intervention. Based on the advice of Government officials, the Commission considers that such intervention is likely to be by way of regulation. It is recognised that such regulations would impose costs on the economy. However the Commission is of the view that the Government is likely to consider that the benefits which can be achieved from the stated goals will justify these costs.

170 The Commission also considers that it is likely that the regulations would mirror the provisions of the Deed. In part this view has been derived from the expressed views of the Government and Government officials. The letter from the Minister of Communications to Clear on 11 February 1999 which is quoted in paragraph 160 is one example.

Conclusion on Counterfactual

171 The Commission has concluded, therefore, that the appropriate counterfactual is a regulated solution with the regulations substantially mirroring the provisions of the Deed. The Commission accepts the advice of the Ministry of Commerce that any regulated solution would require enabling legislation be passed by Parliament.

COMPETITION ANALYSIS

The Application of Section 27

172 Section 27 of the Act prohibits the entering into of contracts, arrangements or understandings which have the purpose or effect of substantially lessening competition in a market. The Applicants have stated that they believe that the Deed is an arrangement which some persons may consider substantially lessens competition in a market and accordingly have applied for authorisation under sections 58(1) and 58(2).

(As discussed elsewhere, they have also applied for authorisation under sections 58(5) and 58(6) as they consider that some persons may consider that section 29 applies to the Deed.) For the Commission to consider an authorisation under sections 58(1) and 58(2), it is necessary for it to be satisfied that the Deed lessens competition in a market. Without a lessening of competition the Commission must decline to authorise the Deed.

173 The principal emphasis of many of the submissions made to the Commission on the application was the importance to competition in the telecommunications sector of an independent number administration regime and an efficient number portability mechanism. Global One, for instance, stated:

“... there seems to be universal acceptance that the realisation of the goal of competitively neutral and efficient numbering allocation and portability arrangements, in multi-carrier environments, is essential for the development and maintenance of sustainable telecommunications competition.”

174 Further, as made clear in the section 26 statement, the Government has said that the objective of New Zealand’s regulatory environment for telecommunications is to promote economic efficiency and that competition is seen as the best means of achieving this objective. In this respect the Government has emphasised that it wishes to ensure the efficient administration of telecommunications numbering resources and the efficient provision of telecommunications number portability.

175 The view that number portability and independent number administration greatly facilitate competition in the markets for various telecommunications services coincides with the findings of all major overseas reports the Commission has seen on this topic. The Commission accepts that the implementation of both in an efficient manner is likely to enhance competition significantly in New Zealand.

176 However, when assessing the competitive impact of the Deed for the purpose of determining whether the Commission can grant an authorisation in terms of section 61(6) of the Act, the Commission is not required to assess the extent to which competition is enhanced through independent number administration and through preferred number portability *per se*. Rather it is required to assess the difference in the competitive outcomes between the scenario under the Deed and the counterfactual scenario.

177 In undertaking this task, the Commission has considered competition issues arising from each principal provision in the Deed, and from the Deed as a whole.

178 The Deed:

- outlines numbering principles to be followed by all persons exercising functions, powers and responsibilities under the Deed;
- limits the entitlement to be a party to the Deed to providers of public switched telecommunications services;
- precludes persons who are not parties to the Deed from being allocated numbers under the Deed;
- provides for the establishment of a Management Committee to administer the Deed, an Independent Chair, the right for each party to exercise one vote, and majority or consensus decisions depending on the matter before the Management Committee;

- provides a means by which costs are recovered from the parties;
- provides for the commissioning of an independent expert to analyse whether there are net economic benefits to society from the implementation and operation of proposed preferred number portability solutions, and a time frame for the study;
- provides for the drawing up of a time frame for the implementation of a preferred number portability solution which has net economic benefits;
- provides for establishing how and to what extent the costs of implementation are to be allocated between parties;
- provides for the appointment of an independent Number Administrator, and for determining rules which shall apply to number allocation;
- provides for dispute resolution, including by referring the matter in dispute to arbitration; and
- notes that the Deed is a public document and that none of its provisions is confidential or commercially sensitive, although commercially sensitive material made available by parties shall be treated as confidential unless it is necessary to enable obligations to be fulfilled under the Deed.

The Competitive Impacts in the Markets for Various Telecommunications Services

179 The assessment of the competitive impact of the Deed in these markets has been undertaken by considering separately the provisions of the Deed (and the Deed as a whole), and where appropriate making comparisons with the counterfactual scenario adopted by the Commission (the regulated solution).

Numbering Principles

180 The numbering principles which are set out in clause 2 of the Deed and described above emphasise efficient non-discriminatory allocation of numbers and provide that all numbers shall be capable of being ported.

181 The Commission is satisfied that these principles do not have an anti-competitive purpose or effect. Further it considers that the principles closely mirror the principles which would be found in the counterfactual.

182 Accordingly the Commission does not consider that the numbering principles in the Deed lessen competition.

Entitlement of Telecom to be a Full Party

183 The Deed entitles any person providing public switched telecommunications services to become a party to the Deed.

184 Global One has argued in its written submission and at the conference that because Telecom, as the incumbent, has every reason to resist, delay or restrict “true competitive number portability”, its involvement in the number portability process should be confined to implementation of a competitively-neutral process, not its

formulation. Global One considers that the mere fact of Telecom's involvement in the formulation of portability principles violates the key principle of competitive neutrality.

- 185 The Commission accepts that it is likely that different parties to the Deed will have different incentives to argue for different types of portability and different timeframes for their introduction. However each party to the Deed has the same voting rights. Telecom, for instance, would have the same ability under the Deed as other parties to use its vote to achieve its favoured option and timing. The Deed requires the arbitrator to adopt, wherever practicable, a simplified and expedited procedure.
- 186 The Commission considers that the entitlement Telecom would have to be a party to the Deed does not lessen competition in a market.

Tying Access to Numbers to the Signing of the Deed

- 187 As noted above, a provision in the Deed provides that only parties to the Deed are eligible for allocations of numbers under the Deed.
- 188 In his report for Telecom, Mr Sundakov stated that this provision and the need to have numbers meant that "it is not practical for any provider of public switched services to stay outside the Deed for any significant period of time."
- 189 At the conference, Vodafone stated that it considered the provision in the Deed which links access to numbers with participation in the Deed to be crucial to the Deed's ability to deliver the rewards from number portability. Telecom argued that the provision plays a crucial role in reconciling the various incentives in operation in the telecommunications industry in relation to number portability, particularly the incentives to avoid incurring costs. Professor Ergas, one of Telecom's economic experts, argued that the provision was necessary to prevent free-riding, and was not unreasonable.
- 190 Both Telecom and Vodafone stated that the tie between access to numbers and participation in the Deed is crucial to their participation in the number portability solution contained in the Deed.
- 191 On the other hand, Clear stated in its submissions that the tie:
 "... serves no legitimate objective, is unnecessary and has severely anti-competitive effects by either foreclosing local service competition or coercing signatures to the Deed from parties which have legitimate objections to doing so."
- 192 However the Commission accepts Vodafone's submission at the conference that number portability is an inherent part of number administration. Vodafone considers that the transfer of numbers between service providers is an element of "administration" in the same way as the initial allocation of numbers is an "administration" matter.
- 193 The Commission does not consider that it is necessarily anti-competitive for the Deed to be concerned with both the initial allocation of numbers and with determining the appropriate means by which numbers are ported. In addition the Commission considers that it is not necessarily anti-competitive for the Deed to establish common principles to

apply to all functions undertaken under the Deed. Both situations are also likely in the counterfactual scenario.

- 194 The Commission acknowledges that it is possible that the functions provided for under the Deed may be performed in a way which creates entry barriers or substantially lessens competition in a market. However, if that is the case, remedies are available under the Commerce Act. The Commission's authorisation of the Deed would not give protection from the Act to the Management Committee or other parties engaging in anti-competitive behaviour.
- 195 It is the view of the Commission that tying in itself is not necessarily harmful, although it can be if tying unlawfully imposes costs on competitors or raises the cost of new competitors entering the market. The Commission considers that what is principally relevant is whether costs are allocated in a way which would result in an anti-competitive impact. This aspect is considered below.

Governance Arrangements

- 196 There has been concern expressed that, under the Deed, Telecom will be able to exert an undue influence on the decisions of the Management Committee. The Commission recognises that Telecom, with its resources and expertise, may be in a stronger position to influence the Committee than smaller parties. However, as noted above, each party to the Deed has only one vote. All parties will be represented on the Management Committee including Vodafone and Telstra who are also very well resourced. The Commission is of the view that the governance arrangements in the Deed are not anti-competitive.

Recovery of Administrative Costs

- 197 The Deed provides that the operational costs of administering the Deed shall be recovered from each party in part by way of fixed fee (\$10,000 per annum) with the remainder being apportioned to each party according to the party's share of total number allocations made in that year.
- 198 The Commission does not consider that the cost recovery methodology in the Deed imposes a material barrier to entry into the relevant markets. In any event, the proposal is likely to match the method of cost recovery in the counterfactual scenario.

Commissioning the Independent Expert to Report on Preferred Number Portability Solutions

- 199 In a written submission to the Commission and at the conference, Global One criticised the Deed for being equivocal about selecting Global One's preferred number portability option. It considers that a need for this option has already been clearly demonstrated by overseas practice.
- 200 Clear also expressed the view that the public interest, especially that of consumers, overwhelmingly favours the introduction of an intelligent network solution as soon as possible. It suggested that economic efficiency was too imprecise a concept to base a decision on which number portability option should be adopted. At the conference,

Clear's economic expert, Dr McEwin, expressed opposition to a cost-benefit analysis being undertaken. He said:

"... my predisposition is against cost-benefit analysis in practice, simply because I believe you are promoting competition, you're going to end up with a much better outcome than you can ever possibly plan via a cost-benefit analysis. ..."

I find it very difficult to understand why a cost-benefit study would be needed to be undertaken at all in the first place, given the fact that the figures that we have just quoted from the OECD seem to suggest to me that it's not a particularly efficient telecommunications network here, given the lagging in technology well beyond world best practice; ..."

201 However, the Commission is of the opinion that it is appropriate for a study to be undertaken to determine what form of number portability is appropriate for New Zealand conditions. Mr Lear of the Ministry of Commerce said at the conference:

"... we already have number portability in New Zealand through the call forwarding mechanism. There are arguments that that is not entirely satisfactory, from a technical point of view in the long term, and there are a number of alternatives available, and other alternatives will develop over time. And obviously the Government, because it sees number portability as being important to the provision of competition, the Government would want to see those options examined to see whether or not they do provide net benefits, and that will change over time as the technology changes and its costs change and the like.

So, the Deed provide a process for looking at that, and making a determination at particular points in time as to whether particular number portability solutions – more advanced number portability solutions – do in fact provide for net benefits and, if they do, it's compulsory that those are implemented."

202 The Commission considers a study by an independent expert is a normal and reasonable safeguard against an inefficient investment decision. An expert study is even more appropriate because there will be an element of compulsion in the investment.

203 The Commission is satisfied that the provisions of the Deed relating to the independent expert's report on preferred number portability solutions do not lessen competition.

Time Frame for Implementation

204 In the view of the Commission the provision in the Deed requiring the Management Committee to establish a time frame for implementation of any new portability solution is practical and not anti-competitive.

Allocation of the Cost of Implementing the Preferred Number Portability Option

205 Clear and others have argued that the owner of each network should be required to meet any upgrade costs required on its network to implement the chosen option. They have suggested that any other outcome would be anti-competitive. Given the relative size and age of the various networks, their proposed cost allocation would mean that the great bulk of the cost of any new portability system would fall on Telecom.

206 The Deed is silent on how these costs should be allocated. It states at clause 5.10:

"All Parties shall be bound to meet their share of costs of implementing and operating a long term number portability solution as determined by the Management Committee by Consensus or by the arbitrator based on the Numbering Principles."

- 207 The Numbering Principles require that number portability arrangements, including pricing and operational matters, are to be efficient. The drafters of the Deed have not attempted to pre-judge the findings of the Management Committee or the arbitrator as to what may be efficient.
- 208 The Commission is satisfied that the Deed is not anti-competitive because it requires an efficient cost allocation outcome, or because it fails to impose a particular cost allocation methodology on the Management Committee or the arbitrator.
- 209 The Commission emphasises that it is being asked to authorise a process, and not a particular cost allocation methodology. If the Management Committee adopts an allocation methodology which is likely to substantially lessen competition, it will not be protected by the Commission's authorisation of the Deed from prosecution under Part II of the Commerce Act.
- 210 The Commission accepts that some, mainly small, parties currently have a genuine concern that if they sign the Deed they may face unacceptably high costs relating to a new number portability arrangement. They have argued that this would prevent them from entering the Deed, but as non-signatories they will not have access to numbers in the future and therefore may not be able to compete in the market.
- 211 The Commission considers that these parties' concern may be overstated. Some of these parties currently have surplus numbers to allow them to compete for the medium term. In addition they will be able to sign the Deed, obtain access to new numbers, and then withdraw from the Deed before they would be eligible to meet the cost of any new portability arrangements. In addition the Commission considers that the Deed's efficiency principles would be unlikely to allow an unduly high proportion of these costs to be imposed on small parties. Further, as noted, any method of allocating costs which results in a substantial lessening of competition would be likely to be the subject of action under the Commerce Act.
- 212 The Commission accepts that the implementation of a new number portability system will place additional costs on firms operating in the market. However if the costs are allocated in a way which results in an anti-competitive impact, remedies are available under the Commerce Act.

Rules for Number Administration

- 213 The number administration rules in the Deed have not been raised by any party as being contentious. The Commission has not identified any anti-competitive issues arising in relation to these rules.

Dispute Resolution

- 214 The Commission has not identified any anti-competitive issues arising from those parts of the Deed dealing with dispute resolution. It considers that similar provisions are likely in the counterfactual.

Confidentiality

215 TUANZ has stated that the Deed allows for the Management Committee to conduct its affairs in private with virtually unrestricted confidentiality provisions, and that this is not in the users' interests. At the conference, the Chief Executive for TUANZ stated:

“... the Deed allows for the Management Committee to conduct its affairs in private with a virtually unrestricted confidentiality provision. The way is open for the communication to be little more than a periodical progress report sent out with telephone accounts and heavily sanitised by the signatories' PR departments, and we don't see that as being in the user interest.”

216 The Commission considers that the confidentiality provisions do not appear unreasonable having regard to the commercially sensitive material which will be handled by the Management Committee. It considers that it is likely that the provisions will be replicated in the counterfactual. The Commission considers that they are unlikely to lessen competition.

Potential for Collusion

217 TUANZ has expressed concern that an industry arrangement such as envisaged by the Deed increases the possibility of anti-competitive collusion between competitors.

218 While the Commission considers that any industry grouping can prove a useful meeting point for those with collusive intentions, it does not consider that such groupings are necessarily anti-competitive. Further, the Commission concurs with the point made by Vodafone at the conference when it noted that any anti-competitive conduct arising from the Deed will be subject to the Commerce Act. The Commission's authorisation of the Deed would not protect parties engaging in collusive conduct from legal action under the restrictive trade practices provisions of the Act .

Conclusion on the Competitive Effects of the Deed

219 Having regard to the above matters, the Commission has concluded that the provisions of the Deed would not lessen competition in a market.

The Application of Section 29

220 In addition to seeking Commission authorisation for the Deed under sections 58(1) and 58(2) to the extent (if any) that section 27 would or might apply, the Applicants have also sought authorisation of the Deed under sections 58(5) and 58(6) of the Act, to the extent (if any) that section 29 would or might apply.

221 Section 29 states (inter alia):

- (1) For the purpose of this Act, a provision of a contract, arrangement, or understanding is an exclusionary provision if –
 - (a) It is a provision of a contract or arrangement entered into, or understanding arrived at, between persons of whom any 2 or more are in competition with each other; and
 - (b) It has the purpose of preventing, restricting, or limiting the supply of goods or services to, or the acquisition of goods or services from, any particular person, or class of persons, either generally or in particular circumstances or on particular conditions, by all or any of the parties to the contract, arrangement or understanding,

or if a party is a body corporate, by a body corporate that is interconnected with that party; and

- (c) The particular person or the class of person to which the provision relates is in competition with one or more of the parties to the contract, arrangement or understanding in relation to the supply or acquisition of those goods or services.

...

- (3) No person shall enter into a contract, or arrangement, or arrive at an understanding, that contains an exclusionary provision.
- (4) No person shall give effect to an exclusionary provision of a contract, arrangement or understanding.

222 The Applicants suggested that section 29 does not apply to the Deed, but the application was submitted in the interests of certainty. However in their subsequent submissions both Telecom and Vodafone appeared to agree with the Commission's conclusion in the Draft Determination that the provisions of the Deed came within the ambit of section 29.

223 In essence section 29 applies to the Deed if it has the purpose of preventing the supply of goods or services from any person, and the parties to the Deed are in competition with each other.

224 The Commission considers that the parties to the Deed are clearly in competition with each other. The Deed (at clause 3.1) requires all parties to be providers of public switched telecommunications services. While these services can fall within various markets, the Commission is satisfied in this instance that the parties compete with each other.

225 The Deed (also at clause 3.1) specifies that (subject to clause 3.3) no person other than a party to the Deed is eligible for allocations of numbers under the Deed. Clause 3.3 permits numbers to be allocated to new entrants but permits those new entrants to use the numbers only if they become a party to the Deed.

226 In the view of the Commission the exclusionary purpose provision of section 29 is also met. The purpose of clause 3.1 is to prevent those telecommunications service providers who do not commit to the preferred number portability provisions of the Deed from being supplied numbers. The fact that the exclusionary provision may have, in the words of Mr Sundakov in his NZIER report, an ultimate aim of reducing "the incentives and opportunities for industry participants to game against one another to the detriment of efficiency in number administration and of efficient solutions to long term number portability"²⁶ does not exempt the Deed from section 29.

227 Accordingly the Commission concludes that the Deed is an arrangement which falls within the ambit of section 29 of the Act.

ASSESSING BENEFIT TO THE PUBLIC

228 Having concluded that the Deed is a contract, arrangement or understanding to which section 29 applies, the Commission is required to make a determination in terms of section 61(7) of the Act.

²⁶ Above n23.

229 Section 61(7) of the Act states:

“The Commission shall not make a determination granting an authorisation pursuant to an application under section 58(5) or (6) of this Act unless it is satisfied that-

- (a) The entering into of the contract or arrangement or the arriving at the understanding; or
- (b) The giving effect to the exclusionary provision of the contract or arrangement or the arriving at the understanding;

as the case may be, to which the application relates, will in all the circumstances result, or be likely to result, in such a benefit to the public that-

- (c) The contract or arrangement or understanding should be permitted to be entered into or arrived at; or
- (d) The exclusionary provision should be permitted to be given effect to.”

230 In assessing whether the Deed results in such a benefit to the public that it should be allowed, the Commission is required to take into account both gains and losses to the public of New Zealand, arising from the Deed.

Detriments

231 Losses, or detriments, relevant to this exercise usually arise from a lessening in competition. These detriments typically fall within the category of productive inefficiency, allocative inefficiency and innovative inefficiency. The Commission can also take into account other types of detriments where they occur, such as negative impact on health and the environment.

232 The Commission does not consider that any of the components of the Deed would lessen competition. Accordingly it does not consider that the Deed would result in any loss of productive, allocative or innovative efficiency from a change in the competitive situation.

233 The Commission has concluded that the Deed falls within the ambit of section 29 of the Act. Clear has argued that section 29 is a *per se* offence as it does not contain a competition test. Clear has suggested that Parliament regards practices which fall within the ambit of section 29 as being inherently anti-competitive and, in the view of one of Clear’s economists, only in the most exceptional circumstances should such practices be capable of being authorised.

234 The Commission does not agree that this is the approach required by the Act. There is nothing in the Act which suggests that the mere fact that a practice falls within sections of the Act which may be characterised as a *per se* offence requires the Commission automatically to attribute an especially high level of detriment to the practice. Rather the Act requires the Commission to assess the benefits and detriments on the facts of each case. This approach is consistent with past decisions of the Commission. In Decision No 277 of 30 January 1996, for instance, the Commission concluded that the Interim Pricing Mechanism in the rules for the New Zealand Electricity Market fell within the ambit of section 30 and was therefore deemed to substantially lessen competition. That is, without authorisation it would be a *per se* offence. In that case the Commission, in the weighing of benefits and detriments, concluded that the detriments were not significant. It went on to authorise the Interim Pricing Mechanism.

- 235 During the course of the consideration of the current application, those opposed to the Deed have suggested a range of detriments. The principal ones are considered below.
- 236 It has been claimed that the Deed would reduce competition through restriction on access to numbers, delays in the introduction of the optimal means of number portability, and implementation of inappropriate means of cost recovery. It is maintained that this reduction of competition would have a detrimental impact on productive and innovative efficiency.
- 237 As noted above, the Commission has concluded that the Deed would not lessen competition. Accordingly it does not consider that it would have a detrimental impact on productive and innovative efficiency arising from a change in the competitive state of the market.
- 238 It has been suggested that the Deed would have an institutionalising effect, cause unnecessary delays, and give rise to uncertainties. However, the Commission considers that these effects are more likely with the counterfactual, because of its attendant regulations, than with the Deed.
- 239 Another suggestion has been that the Deed would lead to collusive behaviour because it would bring competitors together to discuss industry issues. However the Commission notes that the provisions of the Deed do not promote collusive behaviour. If anti-competitive collusive behaviour occurred, the parties involved would be subject to enforcement action under the Commerce Act.
- 240 TUANZ has suggested that the confidentiality provisions of the Deed are not in consumers' interests. The Commission is satisfied that the provisions are reasonable considering the commercially sensitive nature of much of the material which will come before the Management Committee. The Commission considers that they would be likely to be found in the counterfactual and, in any event, their presence would not lead to anti-competitive detriment.
- 241 At the conference, counsel for Clear stated during his discussion of detriments:
"This arrangement is an arrangement which represents, if it is authorised, the successful attempt by the dominant firm to impose its preferred solution on its competitors."
- 242 The Commission does not accept this characterisation. The evidence provided indicates that the Ministry of Commerce had a leading role in facilitating the Deed, and that all major parties, including Telecom (and Clear), had an influence on its final shape. Further the Commission is satisfied that the governance arrangements in the Deed do not give any single party the ability to impose particular outcomes on the industry as a whole.
- 243 One aspect of the Deed which gives the Commission concern is the predominant influence of existing market participants on the Management Committee. The Commission accepts that, in itself, this is not unreasonable and does not lessen competition. However the Commission is concerned that the Committee may have an incentive to make decisions which make it more difficult for new players to enter the market. The Commission has the ability to take enforcement action if the Committee seeks to raise entry barriers to new entrants.

Conclusion on Detriments

244 The Commission has not identified any detriments arising from the Deed.

Benefit to the Public

245 It is emphasised again that what is relevant to the application is the benefit to the public from the Deed (compared to the counterfactual) and **not** the benefit to the public from independent number administration and/or number portability *per se*.

246 In its Public Benefit Guidelines,²⁷ the Commission states that it encourages applicants to quantify projected efficiency gains as far as possible. This is in line with statements made by the Courts. For instance in the AMPS A case,²⁸ Richardson J, sitting as one of the five judges in the Court of Appeal, remarked on the:

“... responsibility on a regulatory body to attempt so far as possible to quantify detriments and benefits rather than rely on a purely intuitive judgment to justify a conclusion that detriments in fact exceed quantified benefits.”

247 The Applicants were unable to provide to the Commission a precise quantification of the size of the benefits they claimed would occur under the Deed, but rather concentrated on a description of the benefits.

248 In relation to the difficulties in quantifying the benefits and detriments, Professor Ergas, on behalf of Telecom stated:

“I accept the difficulty that the lack of quantification creates. I would note that that is not the difficulty that has solely confronted the applicants; those who do not support authorisation of the Deed have not quantified any detriments. ...

I really wonder whether the costs of quantification in this specific case would be such that they would not greatly swamp any benefits that it might provide you with in terms of improved decision-making.”

249 Mr Sundakov, on behalf of Telecom, went on to state:

“We would dearly love to find a workable way of quantifying this, and we have made, in various submissions to the Commission, a stab at trying to identify some of the more obvious differences in costs relating to, for example, personnel that would be required for the Government to undertake its regulatory work. But these are probably marginal and pale in terms of significance with the real economic costs and benefits of an arrangement such as this Deed; and would be loathe to see spurious values attached when the economic welfare, of the effect of the Deed on economic welfare, is really about bringing forward, and bringing forward more rapidly and more simply, the consideration of the introduction of long term number portability. But we can only know what the economic effect of that is once the cost-benefit analysis of long term number portability is undertaken.”

250 Equally other parties were unable to quantify claimed benefits and costs. The Commission recognises that in this instance it would have been very difficult and costly to undertake quantification with any precision.

251 The principal benefits claimed were those arising from the earlier introduction than would otherwise be the case of efficient number portability and independent number

²⁷ *Guidelines to the Analysis of Public Benefits and Detriments in the Context of the Commerce Act*, Commerce Commission, October 1994.

²⁸ *Telecom Corporation of New Zealand Ltd v Commerce Commission* {1992} 3 NZLR 429, 447.

administration, and the advantage of industry self regulation over government regulation.

Timing

252 The Commission accepts that a regulated solution will require legislation. At the conference Sir Geoffrey Palmer, who appeared on behalf of Clear, stated:

“It is my view that a very simple legislative amendment can be made quite quickly here, and indeed the legislative amendment can, by no stretch of the imagination, be regarded as major.”

However the Ministry of Commerce has suggested that it could be 18 months to 2 years before regulations could be promulgated. Further it considers that such new legislation would be unlikely to be passed this year, and that there may be further delays next year as the election may alter legislative priorities.

253 The Commission considers that the Ministry of Commerce is well positioned to advise upon current legislative priorities, and as such considers that the time frame of 18 months to 2 years is the more likely scenario.

254 After the enactment of the legislation the Commission considers that the processes and therefore the timing would be the same as for the Deed itself. Therefore the difference in timing between the regulated solution and the Deed would be the time taken to pass the new legislation and give effect to the regulations - approximately 18 months to 2 years.

255 Clear’s counsel identified a number of stages in the Deed’s processes that may result in delays. However, the Commission notes that these delays have the potential to arise under both the Deed and the counterfactual.

256 The Commission concludes that the Deed will result in the commencement of the process leading to the independent administration of numbers and the study to determine the efficient number portability method taking place 18 months to 2 years earlier under the Deed than under the counterfactual.

257 Further, the Commission considers that there are significant benefits arising from this time saving. All parties considered that the independent administration of numbers was desirable and would reduce transaction costs. Also reaching a decision as to the preferred number portability solution for New Zealand was seen as enhancing competition and efficiencies. The Commission accepts these views.

258 At the conference Professor Ergas, speaking on behalf of Telecom, identified several detriments that would arise from any delay. Professor Ergas noted:

“...the opportunity cost associated with delay is that once you’ve delayed something , you are, at the subsequent stage in time ... not where you could otherwise have been. And if, by doing the action, undertaking the conduct, during that period of time you learn more and expand your possibility set in one way or another, then the delay will have this possibly high opportunity cost. So, the more important is learning by doing, the more important is the accumulation of skills as a result of actually engaging in the process, the more the delay may be costly.”

Professor Ergas also commented that delay can cause uncertainty. This uncertainty can affect investment decisions by existing market participants and entry decisions by potential new market entrants.

259 However, it is also relevant to note that the speed of technological development is such that current technology and any steps taken towards implementation of that technology may be overtaken. Mr Sundakov, speaking on behalf of Telecom, stated:

“... the critical nature of this industry is that time is extremely valuable, because the technology is changing so quickly. ... The period of time could be quite valuable in anticipation of this new technology evolving.”

260 Overall the Commission considers therefore that the earlier commencement of processes leading to the independent administration of numbers and the study to determine the efficient number portability method provides a public benefit.

Advantages of Industry Self-regulation over Government Regulation

261 Professor Ergas and Mr Sundakov, on behalf of Telecom, emphasised to the Commission the advantages of industry self-regulation over government regulation. Costs can be expected to be lower, incentives to improve efficiency to be greater, and flexibility to be enhanced with the former. The Commission accepts these benefits and has given weight to them in its assessment of the benefit to the public arising from the Deed.

Conclusion on Benefit to the Public

262 The Commission concludes that the Deed is likely to lead to a significant benefit compared with the counterfactual. It also concludes that there is unlikely to be any detriment arising from the Deed. On balance the Commission concludes that the Deed will be likely to bring about such a benefit to the public that it should be allowed. It concludes that this benefit is such that it is satisfied that the Deed should be authorised in terms of section 61(7) of the Act

OVERALL CONCLUSION

263 The Commission has considered whether the Deed should receive authorisation under section 58(1) and 58(2) of the Act. The Commission finds that the Deed does not lessen competition and therefore declines to grant an authorisation under those provisions.

264 The Commission has concluded that the public benefit from the Deed is such that it determines to grant an authorisation pursuant to sections 58(5), 58(6) and 61(7) of the Act.

DETERMINATION

Pursuant to sections 58 and 61(1)(b) of the Commerce Act 1986, the Commission determines to decline the application by Newcall Communications Limited, Teamtalk Limited, Telecom New Zealand Limited, Telstra New Zealand Limited and Vodafone New Zealand Limited, for authorisation in relation to the entry into and giving effect to the Deed dated 15 December 1998 to the extent (if any) that section 27 would or might apply to the entry into and giving effect to the Deed dated 15 December 1998.

Pursuant to sections 58 and 61(7) of the Commerce Act 1986, the Commission determines to grant an authorisation to Newcall Communications Limited, Teamtalk Limited, Telecom New Zealand Limited, Telstra New Zealand Limited and Vodafone New Zealand Limited, for the entry into and giving effect to the Deed dated 15 December 1998 to the extent (if any) that section 29 would or might apply to the entry into and giving effect to any provision in the Deed dated 15 December 1998.

Dated this 17th day of May 1999

M N Berry

Acting Chairman

APPENDIX 1: SECTION 26 STATEMENT