



COMMERCE COMMISSION

**CONSULTATION ON THE NON-DISCRIMINATION AND EOI
OBLIGATIONS UNDER THE TELECOM SEPARATION
UNDERTAKING REQUIREMENTS WITH RESPECT TO THE
COMPLAINTS CONCERNING THE TELECOM WHOLESALE
LOYALTY OFFERS**

**THE TELECOMMUNICATIONS ACT 2001
AND TELECOM SEPARATION UNDERTAKINGS**

PUBLIC VERSION

16 October 2009

Confidential material in this consultation document is contained in square brackets.

I. BACKGROUND

A. Overview

1. The Commerce Commission (“**Commission**”) is investigating whether three “loyalty offers” launched by Telecom Wholesale in December 2008 (the “**Auckland Offer**”), March 2009 (the “**All of NZ Offer**”), and July 2009 (the “**Regions Offer**”), respectively, constitute *prima facie* breaches of the Telecom Separation Undertakings¹ (the “**Undertakings**”), and, if so, whether enforcement proceedings are appropriate.
2. This draft decision considers two related investigations undertaken by the Commission: one commenced under the Commission’s discretionary monitoring and enforcement powers, and the other arising from complaints received by Vodafone and Kordia.
3. Under its general investigation, the Commission must decide whether the Telecom Wholesale Loyalty Offers are likely to have breached the non-discrimination and/or the EOI provisions of the Undertakings.
4. Clause 56 of the Undertakings sets out Telecom Wholesale’s non-discrimination obligation:

56 Wholesale Unit will not discriminate

56.1 When doing or omitting to do anything in respect of the provision of a Relevant Wholesale Service, the Wholesale Unit (including its Employees, agents and contractors) will not discriminate between Service Providers and Retail Units or between Service Providers.

56.2 For the avoidance of doubt:

- (a) clause 56.1 does not prevent the Wholesale Unit from doing or omitting to do something in respect of the provision of a Relevant Wholesale Service that is different for different recipients of that service where those differences reflect the different requirements of the recipients;
- (b) clause 56.1 is subject to clause 6; and
- (c) this clause does not limit clauses 47 to 49.

5. The particular provisions of the EOI obligations are the December 2009 Requirements, which most relevantly state:²

December 2009 Requirements means, in relation to a particular Relevant Service:

- (a) the following requirements:
 - (i) Telecom Business Units and Service Providers are provided with the same service on the same terms (including price);

6. If the Commission identifies a *prima facie* breach of the Undertakings in its general investigation, the Commission may decide whether to issue enforcement proceedings. The Commission may seek:

- orders and other injunctive relief under s69R of the Act,
- pecuniary penalties under s156L, and/or

¹ The Telecom Separation Undertakings, as provided to the Minister of Communications on 25 March 2008 in accordance with section 69K(2)(c) of the Telecommunications Act 2001, as amended. The Undertakings were varied by agreement between Telecom and the Minister of Communications on 10 June 2009 in accordance with s69U of the Act (the “First Variation”).

² Undertakings, Schedule 1, clause 1.1.

- pecuniary penalties and other damages under ss156P-156R of the Act.
7. In relation to the complaints submitted by Vodafone and Kordia under the Commission's process for handling complaints under s156O of the Act *Complaints (Operational Separation) Handling Under Part 4A of the Telecommunications Act 2001*, published July 2008 (the "**Operational Separation Complaints Guidelines**" or "**Guidelines**"),³ the Commission must decide whether to take, or join the complainants in taking, enforcement action under section 156P of the Act, taking into consideration:
 - (a) the purpose of section 18, and
 - (b) the financial means of the complainant(s).
 8. The Commission will consider what enforcement action is appropriate in the event the Commission determines Telecom is likely to have breached the Undertakings. It will not consult on what enforcement action, if any, to take.

B. The Separation Undertakings

9. In December 2006 the Government passed a number of amendments to the Telecommunications Act 2001 (the "**Act**"). A key component of the changes to the Act was Part 2A, which set out the requirement for the Operational Separation of Telecom Corporation of New Zealand ("**Telecom**"). The Act states that the purpose of operational separation is to:⁴
 - promote competition in telecommunications markets for the long-term benefit of end-users of telecommunications services in New Zealand;
 - require transparency, non-discrimination, and equivalence of supply in relation to certain telecommunications services; and
 - facilitate efficient investment in telecommunications infrastructure and services.
10. The operational separation of Telecom was negotiated between Telecom and the Minister of Communications with substantial input from the Commission, and implemented as a deed from Telecom to the Crown. The Undertakings were provided to the Minister of Communications on 25 March 2008 in accordance with section 69k(2)(c) of the Telecommunications Act 2001; and came into effect progressively commencing on 31 March 2008.
11. The Undertakings required Telecom to create and adequately fund an internal Independent Oversight Group (the "**IOG**") to monitor Telecom's compliance with the Undertakings and report findings to the Telecom Board and the Commission. The functions of the IOG include processing complaints concerning Telecom's compliance with the Undertakings, and carrying out investigations to assess compliance.⁵ It can issue reports, but has no enforcement powers.
12. The Commission has the overall role of monitoring the broader effects of the separation arrangements, as well as the explicit role of taking enforcement action in respect of the Undertakings. Only the Commission may seek pecuniary penalties from the High Court

³ At <http://www.comcom.govt.nz/IndustryRegulation/Telecommunications/Guidelines/guidelines.aspx>.

⁴ Telecommunications Act 2001, s69A.

⁵ See Undertakings, clause 79. The IOG has no role in monitoring or investigating potential Commerce Act 1986 breaches.

for breaches of the Undertakings. It can also recommend to the Minister if it considers variations and exemptions to the Undertakings are required.

13. Under the Commission's Guidelines for handling operational separation complaints, the Commission first requests consideration of the complaints by the IOG. If complaints are received prior to consideration by the IOG, the Commission will forward the complaints to the IOG unless there is a strong justification for immediate Commission investigation or intervention.

C. The Telecom Wholesale "Loyalty Offers"

14. On 19 December 2008, Telecom Wholesale launched the first of three "Loyalty Offers", the "**Auckland Offer**", which related solely to nominated Auckland exchanges and provided discounted pricing of three separate \$50 wholesale broadband and phone line bundles (UBA or UBS and PSTN access and UBR Backhaul)⁶. To accept the offer, wholesale customers had to agree to use only Telecom Wholesale services to provide service to:
 - 100% of end-users in Auckland currently served using Telecom Wholesale services, and
 - 100% of all new end-users in Auckland.
15. The offer was open until 31 March 2009.
16. On 24 March 2009 Telecom announced the second offer (the "**All of NZ Offer**"). It repeated the discounts of the Auckland Offer of \$50 wholesale broadband and phone line service bundles, the stand-alone \$33 PSTN product for Auckland end-users, and added new stand-alone broadband products discounted to \$23.02 (for full speed service) and \$20.51 for broadband service with a slower upstream speed in the rest of New Zealand (that is, outside Auckland). To accept this offer, wholesale customers had to agree to use only Telecom Wholesale services to provide retail services to:
 - 90% of end-users in Auckland currently served using Telecom Wholesale services
 - 90% of all new end-users in Auckland
 - 90% of end-users in the rest of New Zealand currently served using Telecom Wholesale services, and
 - 90% of all new end-users in the rest of New Zealand.
17. The offer was made available through to 24 April 2009.
18. On 1 July 2009, Telecom introduced a third loyalty offer (the "**Regions Offer**"). The Regions Offer made available discounted wholesale broadband and phone line bundles at \$56, and the other stand-alone broadband products described in the All of New Zealand Offer, in specific regions (Hamilton, Palmerston North, Rotorua, Tauranga, and Hibiscus Coast). To accept the offer, wholesale customers had to agree to use Telecom Wholesale services to provide retail services to 90% of all current end-users currently served using Telecom Wholesale services outside of Auckland, and 90% of all future end-users outside of Auckland. Acceptance of the offer was required by 31 July 2009.

⁶ The offer also included a residential PSTN product at the discounted price of \$33.

19. All the offers consisted of a package of services, including UBA, a Relevant Wholesale Service under the Undertakings.

D. Complaints to Telecom Wholesale and the IOG

20. On 9th April 2009, Vodafone complained to Telecom Wholesale that the loyalty offers breached the Commerce Act 1986 (the “**Commerce Act**”), and discriminated against service providers who had made LLU investments. Vodafone requested that the discriminatory conditions be removed.
21. On 15th April 2009, Kordia complained to Telecom Wholesale that the loyalty pricing was a breach of the EOI and non-discrimination provisions of the Undertakings, and asked that the pricing be made available to all service providers without condition. It also alleged that the offers breached s27 and s36 of the Commerce Act.
22. Telecom briefed the Commission on the offer on 20 April. The Commission sought views from industry, and Vodafone and TelstraClear provided responses which were forwarded to Telecom Wholesale and the IOG.⁷
23. Vodafone’s response reiterated the points made in its earlier letter to Telecom Wholesale. TelstraClear stated that, in its view, the offers were a breach of the EOI requirements (clause 1.2 and 47) of the Undertakings, and did not fall within any of the exceptions provided under clause 1.2(b) to the EOI standard.
24. Telecom Wholesale first considered the complaints as a part of its internal “Honesty Box” process. The Honesty Box report, released 14 May 2009, concluded that Telecom was compliant and there was no breach of the Undertakings on the basis that the offers had been made available to all service providers. In Telecom’s view, the fact that the offers were unattractive to some did not amount to discrimination:⁸
- Wholesale cannot be expected to second guess every service providers business requirements in order to create generic offers that are appealing in every respect to all service providers.
25. For the same reason it concluded the loyalty offers were consistent with the EOI requirements, while noting those requirement had not yet come into effect.⁹

E. The IOG investigation

26. The Independent Oversight Group (the “**IOG**”) commenced an investigation into the Loyalty Offers following completion of Telecom Wholesale’s “Honesty Box” investigation report.
27. In its preliminary determination of 12th June 2009, the IOG agreed with the Honesty Box conclusions and identified no breach under the non-discrimination clause of the Undertakings.¹⁰ It reached no preliminary view as to whether there would be a breach of

⁷ The Vodafone Complaint was submitted by letter to the Commission on 1 May 2009, and the TelstraClear Complaint was submitted on 8 May 2009. The Commission wrote to Telecom on 14 May 2009; see para. 38, below.

⁸ Telecom Honesty Box Report, para. 12.

⁹ Ibid, para. 24.

¹⁰ *Preliminary Determination of the IOG in the matter of Vodafone New Zealand and Kordia Group Limited v. Telecom Wholesale*, 12 June 2009, para. 20.

the EOI obligations.¹¹ The IOG asked for submissions from parties prior to reaching a final decision.

28. Vodafone argued in its submission that an offer can be discriminatory-¹²
if its terms and conditions are offered in such a way that a service provider would be severely disadvantaged (whether technically, operationally or commercially) if it were to accept it.
29. In addition, Vodafone argued that clause 56.2 could not provide an excuse or exception for Telecom Wholesale's offer, as it was "primarily intended to allow Telecom to offer different non-price terms to different service providers."¹³ In so concluding, Vodafone noted that exceptions are permitted under 56.2 only where they:¹⁴
reflect the different requirements of the recipients. It is not stipulated to be an entitlement which exists and arises based on anything in relation to Telecom itself.
30. In Vodafone's view, as the offers could not be justified by the different *requirements* of Vodafone, the offers constituted a breach of the Undertakings.¹⁵
31. Kordia stated in its submission that:¹⁶
To "discriminate" under Clause 56(1) is to treat any Service Provider (or Telecom Retail) differently in any way (or any material way) unless the exceptional circumstances in Clause 56(2) apply. It is not correct to use a strained interpretation so that discrimination requires unfair or prejudicial treatment.
32. Kordia noted that while Telecom Wholesale may compete (such as by dropping prices), "it may not do so on a non-equivalent or discriminatory basis."¹⁷
33. In addition to the non-discrimination breach, Kordia argued that the offers constituted an anticipatory breach of the EOI standard because they were offered on different price and non-price terms.¹⁸ In addition, they noted that Telecom would be in breach when Telecom Retail would be required to consume the UBA service on the same terms and conditions as other service providers.¹⁹
34. Telecom said that the offers were not discriminatory because the same terms and conditions were offered to all service providers, and that the differential treatment is permitted under the Undertakings.²⁰
35. The IOG announced its decision on 27 August 2009, concluding that Telecom's wholesale loyalty offers were "non-trivial breaches" of Telecom's operational separation undertakings as they:
- Breached the non-discrimination obligations imposed on Telecom Wholesale by clause 56.1 of the Undertakings, and

¹¹ Ibid., para. 29.

¹² Vodafone's *Submission in response to the Preliminary Determination of the IOG dated 12th June 2009*, 26 June 2009, page 2.

¹³ Ibid, page 3.

¹⁴ Ibid.

¹⁵ Ibid.

¹⁶ Kordia submission on the *Preliminary Determination in the matter of a complaint under the Undertakings Given by Telecom to the Crown under Section 69K(2)(c) of the Telecommunications Act 2001*, dated 26 June 2009, para. 1.10.

¹⁷ Ibid, para. 1.14.

¹⁸ Ibid, para. 1.17; 5.2.

¹⁹ Ibid., paras. 5.13, 5.14.

²⁰ Telecom submission to the IOG, 26 June 2009.

- Would be in breach of the EOI obligations on 30 September 2009 as UBA services would be supplied on different terms and conditions
36. The IOG found that the loyalty offers discriminated against parties that had participated in unbundling. The IOG referred in its written reasons to a Telecom Wholesale executive paper (pertaining to the Auckland Offer) which contained-
- comments which in the IOG's views establish that the offers were constructed in a manner to prevent those utilising UCLL²¹ services from accepting them... The paper was concerned at competition which was emerging in the wholesale market.
37. In response to the IOG's decision, Telecom announced on 27 August 2009 that it would terminate all Loyalty Offer agreements with effect from the end of September. It has removed the Loyalty Offers from the market.

F. The Commission investigation

38. On 14 May 2009, the Commission advised Telecom that it was considering whether to open an investigation into whether the offers were likely to be a breach under the Commerce Act 1986 (the "**Commerce Act**"). With respect to the potential breach of the Undertakings, the Commission advised it was deferring consideration pending a decision from the IOG. It advised that it would monitor the progress of the IOG investigation closely.
39. On 18 August 2009, Vodafone New Zealand Limited ("**Vodafone**") submitted a formal complaint to the Commission under s156O of the Telecommunications Act 2001.
40. On 31 August 2009,²² following receipt of the IOG decision, the Commission commenced an investigation into Vodafone's complaint consistent with its Guidelines, and at the same time commenced its own investigation into the Loyalty Offers under its Undertakings enforcement powers as set out in the Telecommunications Act 2001.
41. On 2nd October 2009, Kordia transmitted a formal complaint to the Commission under section 156O of the Act. Telecom and Kordia agreed to consider that complaint as part of the Commission's on-going investigation.
42. The Vodafone and Kordia investigation is to determine whether the Auckland or All of NZ Offers are likely to have breached the Undertakings and, if so, whether to take, or join Vodafone and/or Kordia in taking, enforcement action under section 156P of the Act, and, in particular, whether to seek pecuniary penalties under s156Q.
43. The Commission investigation is to determine whether any of the offers constitute a likely breach of the Undertakings, and, if a likely breach is identified, what enforcement action (if any) to seek in the High Court.

G. Scope of Consultation

44. The issues before the Commission concern two core components of the Undertakings, the Arm's-Length Rules,²³ and the Equivalence of Input ("**EOI**") obligations.²⁴

²¹ Unbundled copper local loop.

²² The Commission delayed its decision as to whether to commence its own investigation pending the outcome of the IOG's investigation process.

²³ Defined in clause 1.1 of the Undertakings.

²⁴ See the Undertakings, clauses 47-49, 1.2, and Schedule 1.

45. The Arm's-Length Rules impose a number of behavioural controls on Telecom. Telecom Wholesale, for example, is obligated to act independently and at arm's-length from the retail business units,²⁵ to maintain separate management and reporting lines,²⁶ to formulate its own commercial policies,²⁷ to limit the disclosure of its commercial information,²⁸ and not to discriminate²⁹ in the provision of certain specified services defined in clause 45 of the Undertakings (the "**Relevant Wholesale Services**").
46. In the current matter, the critical Arm's-Length Rule at issue is the **non-discrimination clause** obligations in clause 56 of the Undertakings.
47. The EOI obligations consist of two parts: the EOI standards³⁰ and the transition to equivalence process.³¹ The EOI obligations (relevantly) require Telecom to provide and deliver certain enumerated services to itself and other service providers on the same terms and conditions. Unlike the Arm's-Length Rules, the EOI obligations are imposed on a transitional basis, with the majority of services not required to be supplied on a full EOI basis until 2011.
48. Relevant to the present matter are the *December 2009 Requirements*, which are effectively a half-way point in the implementation of the transition to equivalence process for some of the services. Under the *December 2009 Requirements*, Telecom must supply the UBA service to itself and others on the same terms and conditions (including price) after 30 September 2009.³²

H. Request for submissions

49. The Commission's preliminary view with respect to these requirements are set out in Part II, below. Confidential Commission-only information is marked in the attached in square brackets []COI.
50. The Commission seeks submissions on the preliminary views reached by the Commission regarding the Undertakings requirements with respect to the non-discrimination obligation, and regarding the EOI standard and the Transition to Equivalence, particularly the December 2009 Requirements.
51. Submissions should be provided to the Commission no later than **5 p.m., Friday, 30th October 2009**. Submissions should be forwarded to telco@comcom.govt.nz.

²⁵ Undertakings, clause 52.

²⁶ Ibid, clause 53.

²⁷ Ibid, clause 55.

²⁸ Ibid, clause 59.

²⁹ Ibid, clause 56.

³⁰ Ibid, clause 1.2.

³¹ The process for transition to equivalence is set out in Schedule 1 of the Undertakings.

³² Prior to the First Variation to the Undertakings, Telecom Retail was not obligated to consumer basic UBA for new customers until 31 December 2009.

II. RELEVANT REQUIREMENTS OF THE UNDERTAKINGS

A. The Non-Discrimination Obligation

52. Clause 56.1 provides:

56 **Wholesale Unit will not discriminate**

56.1 When doing or omitting to do anything in respect of the provision of a Relevant Wholesale Service, the Wholesale Unit (including its Employees, agents and contractors) will not discriminate between Service Providers and Retail Units or between Service Providers.

Discussion

53. The *Shorter Oxford English Dictionary* defines “discriminate” as meaning to “make or constitute a difference in or between; distinguish, differentiate.”³³ “Discrimination” is the “action or an act of discriminating or distinguishing; the fact or condition of being discriminated or distinguished; or a distinction made.”³⁴ More concisely, the *Pocket Oxford Dictionary* provides “(often foll. by between) make or see a distinction.”³⁵
54. It is the Commission’s preliminary view that the meaning of this clause is clear: the existence of any non-trivial difference in the provision of a Relevant Wholesale Service between service providers constitutes discrimination under this clause – there is no requirement that there has been any unjust or prejudicial treatment (which would require some form of express or implied intent).
55. “Provision” is the “act of providing”.³⁶ “Provision”, therefore means the act of actually supplying or delivering a service. The prohibition on discrimination extends to “doing or omitting to do anything in respect of the provision”; this extends the scope of the term to include all steps related to the supply of a service, including planning, designing, and making an offer to supply or deliver the service.
56. It is the Commission’s preliminary view that the correct reading of clause 56.1 is that, unless otherwise permitted by the Undertakings (and with respect only to Relevant Wholesale Services):
- Telecom cannot plan or design an offer that has the *intent* of treating service providers differently;
 - Telecom cannot make an offer that has the *effect* of treating service providers differently; and
 - Telecom cannot supply or deliver a service on different terms (including price) as between services providers.

³³ *Shorter Oxford English Dictionary*, Oxford University Press (2002), page 697.

³⁴ *Ibid.*

³⁵ *Pocket Oxford English Dictionary*, pg. 246. This entry also notes that the unjust or prejudicial use of the word, “to treat unfavourably or favourably, esp. on the basis of race, gender, etc.” is “usu. foll. by *against or in favour of.*” Similarly, clause 56.2 uses the word “different” as a synonym for “discriminate”.

³⁶ See the *Pocket Oxford English Dictionary*, pg. 722. It is not, as Telecom has suggested in Telecom Submission, Annex C, para. 24., simply to “make available.” To “make available” is to offer; if the Undertakings had intended to limit the scope of the non-discrimination provision to simply offering a service on non-discriminatory terms, it would have used the word “offer” instead.

Differences permitted under the Undertakings

57. Clause 56.2 clarifies the non-discrimination obligation. It provides:

56.2 For the avoidance of doubt:

- (a) clause 56.1 does not prevent the Wholesale Unit from doing or omitting to do something in respect of the provision of a Relevant Wholesale Service that is different for different recipients of that service where those differences reflect the different requirements of the recipients;
 - (b) clause 56.1 is subject to clause 6; and
 - (c) this clause does not limit clauses 47 to 49.
58. The use of the phrase “For the avoidance of doubt” indicates that clause 56.2 does not provide any exceptions to the non-discrimination obligation in clause 56.1. It merely clarifies the scope of Telecom Wholesale’s non-discrimination obligation, and its interaction with other provisions of the Undertakings.
59. Clause 56.2(a) accommodates differences in the provision of a service where required by the service provider. Telecom argues that a service provider may request that a service be provided on loyalty offer-type terms.³⁷ It is hard to imagine a service provider insisting that a loyalty obligation be imposed upon it, but in any event, a service which “reflects the different *requirements* of the recipients” must reflect requirements of the service provider that are *necessitated* by some condition or specific need of the service provider.
60. Therefore, in the Commission’s view, “requirements” in clause 56.2(a) must be limited to those of a technical, operational, or similar nature. Any other view would suggest that Telecom could, in effect, negotiate discriminatory provisions by conditioning the service on a “request” from the service provider that a loyalty obligation be imposed upon it so as to justify differential pricing.
61. Clause 56.2(b) makes clear that when Telecom is not required to provide a service, it will not be in breach of its non-discrimination obligation by providing that service solely to itself.³⁸
62. Clause 56.2(c) acknowledges that the limited exceptions permitted under the EOI obligations, including, in particular, the gradual transition to the EOI standard as set out in Schedule 1 to the Undertakings, will not breach the non-discrimination obligation. Under clauses 47 to 49, Telecom Wholesale commits to transitioning various Relevant Wholesale Services (though not all) to the EOI standard by a certain date, and to commence consuming those services on or before the effective date of the EOI standard.³⁹ During that transition period, the EOI standard permits some differences.

³⁷ Telecom Submission, Annex C., para. 28.

³⁸ However, clause 51 requires that, if Telecom chooses to provide a Relevant Wholesale Service it is not obligated to provide, then it must do so in a manner consistent with the non-discrimination obligation.

³⁹ This is discussed more fully in the discussion of Equivalence of Inputs (EOI), below. These exceptions are set out in clause 1.2 of the Undertakings. When Telecom is providing “the same” Relevant Service, then the Service must be exactly the same, subject only to:

- Trivial differences

63. In relation to clause 56.2, the Commission's preliminary view is the same as that reached by the IOG:⁴⁰

{Clause 56.2} cannot in the view of the IOG be used to justify making different offers to different groups of service providers. Service providers will offer different products and have different means of delivery. The standard conditions of an offer may not apply to the particular circumstances of a service provider. Clause 56.1 allows TW to adjust its offer to take into account the different requirements, which would presumably normally be technical, of the recipient service provider. It does not permit TW to frame its offers in a way which discriminate between service providers .

64. In summary, the language of clause 56.2 makes it clear that the range of differences permitted in delivering a Relevant Wholesale Service is very narrow. The provision of the same service to service providers at different prices is not contemplated by clause 56.2.

Undertakings negotiation history

65. Telecom argues that clause 56.2 of the Undertakings expressly recognises that there will be material distinctions between customers:⁴¹

It is also self-evident from the very nature of telecommunications which is an industry characterised by economies of scale and scope.

...

Volume and term discounts based on economies of scale help secure the investment and infrastructure necessary to provide services.... Volume discounts, for example, reflect the economies of scale in service provision, and therefore apply differentially to high and low consuming service providers.

66. It concludes that:⁴²

The Act's requirement for non-discrimination simply prevents Telecom Wholesale from choosing between service providers....as to the terms and conditions on which it provides services.

67. Telecom explains that the clarification in 56.2 was closely negotiated between Telecom and the Crown with a direct involvement of Telecom CEO Paul Reynolds:⁴³

the particular form of the non-discrimination undertaking was closely negotiated between Telecom and the Crown, with the direct involvement of Telecom CEO, Paul Reynolds. Dr Reynolds' UK experience - in which the corresponding prohibition is against "undue discrimination" meaning

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- Differences relating to some specific security and performance related provisions (described in 1.2(b)(ii))
 - Differences agreed by the Commission
 - Differences requested in writing by a service provider
 - Differences expressly required or authorised elsewhere by the Undertakings
 - Differences required by an applicable Part 2 residua terms determination

⁴⁰ IOG decision, para. 20.

⁴¹ Telecom Submission, Annex C, para. 7, 8.

⁴² Telecom Submission, Annex C, para. 15.

⁴³ Telecom Submission, Annex C, para. 4.

differential treatment without objective justification – led him to press hard for clarification as to non-discrimination’s intended scope.

68. It is acknowledged that the circumstances surrounding the negotiation of the Undertakings are relevant only in the case of ambiguity, and in the Commission’s view there is no ambiguity in this case. Putting that aside, the Commission was also involved in the discussion in relation to the drafting of the non-discrimination obligation, and considers that the negotiation of clause 56.2 is consistent with the Commission’s interpretation.
69. [

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70. This is consistent with the Commission’s view that, using an example put forward in Telecom’s submission, volume discounts for Relevant Wholesale Services are not permitted under clause 56.2(a) of the non-discrimination obligation. The Commission would note, however, that exceptions may be granted by written agreement with the Commission under clause 1.2(b)(iii).

International Precedent

71. Telecom cites international precedent in support of its interpretation of the Undertakings, in particular focusing on the “undue discrimination” standards used in the UK and EU. Telecom refers to the undue discrimination test in the UK Act, and suggests this provides guidance in that “it does not intend or wish to rule out all differentiation”.⁴⁴ Telecom refers to the Ofcom guidelines which “acknowledge that in some cases customers can be treated differently, independently of the circumstances, in a manner that is consistent with effective competition, and that benefits consumers.”⁴⁵
72. As a preliminary point, it is noted that, where the language in the Undertakings is different from that used in other jurisdictions, decisions from those overseas jurisdictions are unlikely to be a sound source of guidance. If the Undertakings were intended to adopt the same standard, they would have used the same language.
73. In addition, as discussed above, the interpretation put forward by Telecom aligning the non-discrimination obligation with the UK’s “undue discrimination” standard is not supported by the negotiation history.

⁴⁴ Telecom Submission, Annex B, para. 18.

⁴⁵ Telecom Submission, Annex B, para. 19.

74. It is the Commission’s preliminary view that Telecom’s analogy to the English Court of Appeal decision in *R v Secretary of State for Trade and Industry*⁴⁶ is tenuous. In any event, the type of differentiation described in that proceeding would be permitted under the Undertakings (as clause 1.2 authorises differences in payment procedures) without the need to give “non-discrimination” the limited meaning advanced by Telecom.⁴⁷
75. In *Albion Water*,⁴⁸ it should be noted that the Court accepted only that different prices *might* not constitute undue discrimination *where the differences were based on the cost of supply*.⁴⁹ The plain language of the Undertakings, particularly the description of the limited exceptions permitted by clause 1.2, and the equivalence obligations, indicate that the costs of supply by Telecom are not a relevant factor. Quite the contrary, the equivalence obligations in particular make it quite clear that services must be provided on the same terms and conditions – *including price*.

Availability of offers

76. Telecom submits that the non-discrimination obligation requires nothing more than that Telecom Wholesale make available services to all service providers on the same terms and conditions.⁵⁰ In Telecom’s view:⁵¹

Not every offer is going to be perfectly suited to everyone. If the complaint is upheld then non-discrimination would mean that Telecom Wholesale would be unable to deliver nuanced commercial offerings responding to a range of customers’ needs.

77. Telecom’s internal Honesty Box report concluded that Telecom Wholesale’s offers were compliant:⁵²

Wholesale has treated all service providers in the same way. This is because the loyalty offers were made available on the same basis to all service providers – no service providers were treated differently by Wholesale, but some service providers chose not to take advantage of the offer.

78. In particular, in Telecom’s view, the fact that an offer is “unattractive” to UCLL service providers does not make that offer discriminatory:⁵³

Wholesale cannot be expected to second guess every service providers business requirements in order to create generic offers that are appealing in every respect to all service providers.

79. Telecom advances this view even in circumstances where it acknowledges that the offer is intentionally less desirable for particular service providers because of their investment decisions:⁵⁴

⁴⁶ *R v Secretary of State for Trade and Industry* {2001}EWCA Civ 1448.

⁴⁷ See clause 1.2(b)(ii)(B) of the Undertakings.

⁴⁸ Telecom Submission, Annex C, para. 13 and footnote 14.

⁴⁹ We would also emphasise that the Court did not conclude that discrimination based on the cost of supply was always justifiable under the non-discrimination language at issue in this case. Indeed, its language makes it clear that this would be the exception rather than the rule.

⁵⁰ Telecom Submission, pg. 1, bullet point 2.

⁵¹ *Ibid.*, para. 1, page 3.

⁵² Telecom Wholesale Honesty Box Report, para. 11.

⁵³ *Ibid.*, para. 12.

⁵⁴ Telecom Cross-submission, 2nd October 2009, para. 10 (emphasis in original).

The more unbundling you do, the less attractive are the offers put forward by Telecom Wholesale. The real point is that both the All of New Zealand and regions offers were capable of being accepted by **all** of Telecom Wholesale's customers.

Commission view

80. It is the Commission's preliminary view that whether an offer has been made on non-discriminatory terms must be determined on a case by case basis. An offer that is made available to all, but contains extraneous terms and conditions that are not necessary for making the offer should be subjected to additional scrutiny for any discriminatory effect.
81. The Commission's preliminary view is that any terms and conditions that have the effect of limiting the parties to whom the offer is acceptable is likely to be discriminatory unless consistent with clause 56.2.
82. It is the Commission's preliminary view that the non-discrimination obligation prohibits Telecom Wholesale from designing, offering, or supplying a Relevant Wholesale Service on terms and conditions (including price) that are different between any two service providers, unless:
 - The difference is required by, and necessary for, addressing the specific needs of the service provider; or
 - The difference is consistent with Telecom's EOI obligations set out in clauses 47 through 49.
83. Where Telecom is not required to offer a Relevant Wholesale Service to service providers under clause 6, but chooses to do so, that service must be designed, offered, and supplied on non-discriminatory terms and conditions (including price).

B. Equivalence of Inputs (EOI)

The EOI standard

84. Under the operational separation plan adopted under Part 2A, Telecom must migrate most relevant services to an "Equivalence of Inputs" basis by 2011.⁵⁵
85. The definition of Equivalence of Inputs states that when the "same services" are supplied under the EOI standard, "same" means "*exactly* the same"⁵⁶ except where the differences are requested in writing by the service provider or agreed to by the Commission.

The December 2009 Requirements

86. There are several milestones along the migratory path to the Equivalence of Inputs for these services, but the most significant milestone is the December 2009 Requirements, effectively a mid-way point in the migration to equivalency.

⁵⁵ See, generally, Undertakings, clause 47.1 and Schedule 1, which provides the milestones for various relevant services.

⁵⁶ *Ibid.*, cl. 1.2(b).

87. Telecom must ensure that it provides services to the standards set by the December 2009 Requirements by the date indicated in the Transition to the Equivalence schedule for that service. Those requirements state:⁵⁷

December 2009 Requirements means, in relation to a particular Relevant Service:

- (a) the following requirements:
 - (i) Telecom Business Units and Service Providers are provided with the same service on the same terms (including price);
 - (ii) Telecom Business Units and Service Providers are able to use the same:
 - (A) B2B Gateway; or
 - (B) Online Portal that meets the reasonable needs of those Service Providers or other Telecom Business Units who do not require or are not capable of using B2B Gateway;
 - (iii) Telecom Business Units use only the B2B Gateway or Online Portal referred to in (ii) above for ordering, provisioning; and faulting management of the service;
 - (iv) Telecom Business Units and Service Providers receive the same service level reporting for the service; and
- (b) The following EOI capability building blocks are completed for the ANS Unit or the Wholesale Unit (as relevant) for the Relevant Service:
 - ...

Telecom's view

88. Telecom argues that the requirement that the same service be “provided” means only that it be “made available”, and therefore under the December 2009 Requirements, where Telecom must provide the same service on the same terms (including price), Telecom must only make available the service on these terms.⁵⁹ According to Telecom, if service providers choose not to accept the terms of supply, and it supplies the service to those who accept the terms at one price, and to those who do not accept the terms at another price, then it is not in breach of the Undertakings.⁶⁰
89. Telecom argues that the foregoing view must be correct, as the December 2009 Requirements require Telecom to “provide”, while the EOI standard requires Telecom to “deliver”.⁶¹

Discussion

90. It is the Commission’s preliminary view that there is no material difference between the meaning of “provide” and “deliver”. To “provide” means to

⁵⁷ Undertakings, Schedule 1, clause 1.1.

⁵⁸ Full list omitted. The list of EOI capability building blocks include: Management EOI Building Block, the Channels EOI Building Block, the Order Management (Sales Order Management Component Only) EOI Building Block, the Customer Information Management EOI Building Block, and the Service Management (Service Desk Component Only) EOI Building Block.

⁵⁹ See *Telecom Submission*, Annex C, para. 24.

⁶⁰ Ibid.

⁶¹ Ibid. See, generally, Annex C, paras. 20-24.

“supply, furnish”.⁶² “Provide” in the definition of the December 2009 Requirements includes to offer to supply, and to actually supply.

91. It is the Commission’s preliminary view that all parties – including Telecom business units and all other service providers – must be provided with (i.e., supplied with) relevant services on the same terms and conditions, including price. With respect to relevant services, such as Basic UBA, Telecom is not permitted to supply the service at a lower price to one group of service providers, and at a higher price to another group of service providers after the date on which Telecom retail units must be supplied with the service under the transition to equivalence schedule.
92. As mentioned above, there is no material distinction between the use of “provide” in the December 2009 Requirements and “deliver” in the EOI standard. To “deliver” means to “distribute (letters, goods, etc.) to their destination(s)”, to “hand over”.⁶³ The term “deliver” in clause 1.2 is used in lieu of the word “provide” where Telecom is required to use mechanical ordering and billing systems or follow particular processes (including service level commitments). Where reference is made solely to the supply of a service, rather than the process by which it is supplied, the word “provide” is used in its stead.

Relationship between the December 2009 Requirements and EOI standard

93. As noted above, the December 2009 Requirements are merely a half-way point in the delivery of full EOI. The proper view of the interrelationship of the December 2009 Requirements and the EOI standards is relatively straightforward. Where Telecom business units and service providers are being provided with the *same* service, the December 2009 Requirements obligate Telecom to, with respect to the service to which the requirement applies:
 - supply that service on the same terms and conditions, including price;
 - ensure Telecom business units and service providers are able to use the B2B Gateway and Online Portal systems, and receive the same level of service reporting; and
 - complete five EOI building blocks
94. The EOI standard, which takes full effect for most services on 31 December 2011,⁶⁴ expands the equivalency requirements (as one would expect with a gradual milestone-based implementation process). The EOI standard requires Telecom, in addition to providing the service on the same terms and conditions (including price), to:
 - ensure Telecom business units and service providers use all of the same systems;
 - ensure Telecom business units and other service providers receive the same level of service; and

⁶² *Pocket English Dictionary*, Oxford University Press, 1992, pg. 721.

⁶³ *Pocket English Dictionary*, pg. 226.

⁶⁴ The transitional arrangements that govern the EOI migration process state when the Telecom business units are required to commence consuming the same services. See Schedule 1 of the Undertakings.

- provide itself and service providers with the same commercial information regarding the services.

Commission view

95. The Commission agrees with Telecom’s view that Telecom business units and other service providers are not obligated to consume the same service by the December 2009 Requirements.⁶⁵ The December 2009 Requirements require only that when Telecom supplies service to itself and other service providers, it must supply the same service on the same terms and conditions, including price.
96. It is the Commission’s preliminary view that on the effective date of the December 2009 Requirements, Telecom is forbidden from supplying the services set out in Schedule 1 of the Undertakings on different terms and conditions (including price) to itself and to other service providers unless:
- The difference is trivial;
 - The difference falls within the class of listed differences relating to security, payment, and termination of supply, et. al., enumerated in 1.2(b)(ii)
 - The difference is agreed by the Commission in writing;
 - The difference is requested by a service provider, and is required for technical or other operational necessities;
 - The difference is specified by the Undertakings;
 - The difference arises from a residual terms determination.

C. The relationship between the non-discrimination obligations and the December 2009 Requirements

Telecom’s view

97. Telecom argues that the EOI standard is effectively meaningless if the non-discrimination provision is interpreted too broadly:⁶⁶
15. The Act’s requirement for non-discrimination simply prevents Telecom Wholesale from choosing between service providers (including Telecom Retail) as to the terms and conditions on which it provides services. Any other interpretation of the requirement will necessarily impinge on the intended operation of other more closely specified obligations.
 16. The scope of the non-discrimination provision is instructive in this respect. It applies to all “Relevant Wholesale Services”, which is a term of substantial breadth extending well beyond services Telecom Wholesale may be required by regulation to provide. However ... only a subset of those services are subject to the EOI standard, which requires provision to both Telecom and service providers of exactly the same service. There is no room for that standard, if non-discrimination is to be interpreted as meaning the same thing. Yet the Undertakings clearly anticipate that the EOI standard is *superior* to non-discrimination, because the prohibition on discrimination is

⁶⁵ Telecom Submission, Annex C, para. 24.

⁶⁶ Telecom Submission, Annex C, paras. 15, 16; citations omitted.

expressly stated not to limit equivalence, despite the EOI standard applying to a lesser range of wholesale services.

Discussion

98. Clause 56 is part of the Arm's-Length Rules, which apply to all relevant services and is concerned with the behaviour of Telecom. The December 2009 Requirements, in contrast, are a milestone in the implementation of the EOI requirements. The "superiority" of EOI arises from Telecom's ultimate obligation under the Transition to Equivalence schedules to consume the limited number of Relevant Wholesale Services on the same terms as its competitors.
99. EOI imposes a number of additional requirements beyond a general non-discrimination obligation, including obligations to:
- provide that service to itself and service providers using the same billing and ordering systems;
 - provide itself and service with the same level of service;
 - provide itself and service providers with the same commercial information regarding the services.
100. As previously noted, the EOI Standard cannot be considered in isolation from the obligation to supply the services to itself under Schedule 1 – they are both part and parcel of the Transition to Equivalence process. In that light, the limited distinction between "provide" and "deliver" becomes clear. Prior to EOI, there is no obligation for Telecom to supply the same service to its own business units. And if Telecom does supply the same service at a date earlier than set forth in the Schedule, it is not subject to the EOI Standard – it is subject only to the non-discrimination obligation.

Commission view

101. It is the Commission's preliminary view that non-discrimination is a broad obligation applicable across all Relevant Wholesale Services provided by Telecom Wholesale.
102. The EOI obligation, on the other hand, while applicable to a smaller subset of services, imposes substantially greater obligations on Telecom in relation to those services, specifically, the obligation to supply the service to itself on the same terms and conditions as it supplies that service to other service providers.

D. Regulatory considerations

Telecom's view

103. In Telecom's view, a decision favouring service provider investments into local loop unbundling would amount to a:⁶⁷
- fundamental bias against robust competition in favour of certain policy goals around UCLL penetration that do not exist in the New Zealand framework.
104. Telecom expressed this view in its criticism of the IOG decision, stating that the-⁶⁸

⁶⁷ Telecom Cross-submission, para. 3.

25. IOG was clearly motivated by a concern to make LLU work, potentially at the expense of service providers purchasing UBA off Telecom Wholesale.
 26. While the policy discussion on the introduction of operational separation included reference to concepts like the ladder of investment, this was always intended to be neutral and facilitative rather than biased in favour of any particular access products. The government intended to make available a ladder, not an escalator.
 - ...
 28. In fact, a potential criticism of our policy framework is that had we developed a clearer policy and explicitly backed either LLU/SLU or UBA then we might have avoided considerable regulatory expense, uncertainty and costly market experimentation and potential stranded investment. But the fact remains that the New Zealand policy is neutral and we have not backed a particular access product.
105. Telecom also argues that the non-discrimination obligation was “primarily directed at preventing Chorus and Telecom Wholesale from favouring Telecom Retail”,⁶⁹ and that “in the Minister’s Determination this was extended to discrimination between service providers, but there was no policy discussion of the concerns as between providers.”⁷⁰

⁶⁸ Telecom Submission, Annex B para. 25, 26, and 28.

⁶⁹ Telecom Submission, Annex B, para. 16.

⁷⁰ Ibid.

Discussion

106. The Commission notes that the Cabinet Policy Paper⁷¹ makes it clear that LLU and SLU, introduced along with other changes to Schedule 1 of the Act, were key components in delivering a competitive wholesale market. As the policy minute explained, the purpose of the amendments were to:⁷²

Introduce a local loop unbundling service (LLU) in Telecom exchanges (full loop unbundling - UCLL) and cabinets (sub-loop unbundling - SLU) with forward-looking cost-based pricing;

Amend the existing regulated unbundled bitstream services (UBS) to remove the constraint on the upstream speed and the prohibition on supporting any function that relies on real-time network capability;

Amend the existing regulated UBS to clarify that the existing regulated service can be purchased (as “naked DSL”) without a requirement to purchase an analogue telephone service, with the pricing principle being “retail minus”;

Introduce a regulated co-location of equipment service and two backhaul services for the LLU service⁷³.

107. The Cabinet paper explained the policy basis for the changes was the furtherance of the “ladder of investment” model (emphasis added):⁷⁴

A commonly adopted approach in the EU and other jurisdictions that attempts to find a balance to increase overall investment levels is the so-called “ladder of investment” **that drives wholesale competitors toward investment in their own infrastructure**. Commencing at lower rungs of the ladder with basic resale and intermediate wholesale of services while building a customer base, this concept envisages movement via LLU to eventual investment in alternative network infrastructure investment⁷⁵. The long-run aim of such policies is competition on level terms among operators, **and it is important to price wholesale access products appropriately so as to maintain incentives for progressive alternative infrastructure investment**.

108. The Cabinet paper that introduced the 2006 amendments noted that-⁷⁶

...the overall net effect of introducing a more competitive environment is considered to be positive for overall investment levels ... As LLU is one of a number of wholesale broadband products (the others being UBS and resale of retail broadband plans) the pricing relativities between these products should be carefully set by the Commission to maintain incentives for both Telecom and entrants to invest in infrastructure and service provision.

109. In the Commission’s December 2007 determination on the new UBA service (replacing UBS), the Commission said on the question of relativity:⁷⁷

⁷¹ Cabinet Policy Paper introducing the 2006 Amendments to the Telecommunication Act 2001, para. 99.

⁷² Cabinet Policy Committee Minute of Decision POL Min (06) 7/9, para. 7.

⁷³ Cabinet Policy Committee Minute (06) 7/9, paras. 7.1-7.4.

⁷⁴ Cabinet Policy Paper which introduced the 2006 Amendment to the Telecommunication Act 2001, para. 99.

⁷⁵ Ibid.

⁷⁶ Cabinet paper introducing the 2006 Amendments to the Telecommunications Act 2001, para. 98 and para. 115.

An Access Seeker will be more willing to access the UCLL service and incur the upfront costs of investment in equipment at an exchange where it has a larger customer base over which to spread those costs. In contrast an Access Seeker with a small number of customers at an exchange is more likely to prefer the UBA service. This allows the Access Seeker to take advantage of economies of density where they exist.

...

The Commission also notes that the UBA price is set according to a retail-minus pricing principle, whereas the UCLL price is cost-based. UBA prices will therefore equal or more likely exceed the costs of providing a UBA service. One consequence of this is that Access Seekers will face an incentive to invest in their own infrastructure to the extent that such investment minimises their cost of providing retail services.

Commission view

110. In the Commission's preliminary view the policy objectives in relation to LLU/SLU and UBA, and the requirement of non-discrimination between service providers, are clear from the Cabinet Policy paper that introduced the 2006 reforms, and are implicit in the ladder of investment theory which underpinned the 2006 Amendment.
111. The policy setting between UBA and UCLL is not "neutral" as Telecom suggests. In the current context, service provider investment in local loop unbundling is seen as a desirable outcome, and the policy framework seeks to "maintain incentives for progressing alternative infrastructure investment."
112. In the Commission's preliminary view, this also explains the policy reasons for a prohibition against discriminating *between* service providers. In its absence the pricing of wholesale access products so as to maintain incentives for progressive alternative infrastructure investment could be undermined.