



Draft s201 pricing guidance

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Executive Summary

Thank you for the opportunity to comment on submissions relating to the Commission's draft guidance on how it intends to apply s201 pricing requirements (**the guidelines**).

Section 201 provides important consumer and competition protections. Policy makers were conscious that the pure revenue cap and guaranteed return regulatory model that would be applied to Chorus left significant risks for end-users and competition. The purpose of s201 was to ensure prices across the markets served by regulated fibre networks remained comparable and to discourage anti-competitive "pocket pricing". Pocket pricing is where a regulated fibre provider could strategically and selectively drop prices on a location or market segment basis to undermine competition.

We support the Commission's proposed s201 approach that addresses both geographic and pocket pricing concerns and is consistent with the policy framework and words of s201.

However, Chorus has submitted that:

1. the Chorus connection incentive scheme, and discounts more generally, do not form part of a Chorus price; and
2. the prohibition on price differences relates only to price differences between "urban" and "rural" areas.

We disagree. We believe that Chorus' proposed approach, and potentially the draft guidance, risk bounding the s201 protections by focusing solely on one form of pricing structure (urban versus rural) and one level of geographic aggregation.

Discounts and rebates are a fundamental component of a price

Chorus's proposed approach would undermine the purpose of s201 and leave a key protection against pocket pricing redundant. Section 201 is clearly intended to mitigate both consumer and pocket pricing concerns, and the Act provides that price is the amount actually or effectively paid by access seekers. As the Commission's draft suggests, the reference to 'the same price' in the s201 context is to the price actually paid by access seekers once any adjustments, rebates or discounts have been accounted for. If components of the price sat outside s201, then the section would ultimately have no effect.

Chorus connection incentives are applied selectively on a geographic location-by-location basis in contravention of s201

Section 201 requires regulated providers to charge the same price for providing fibre fixed line access services ("FFLAS") regardless of the geographic location of the access seeker or end-user.

Chorus effectively proposes that the Commission should consider New Zealand to be made up of two distinct regional geographic locations: "urban" and "rural". But competition in the broadband market, and broadband technology, operates on a premises-by-premises basis. Further, the harm s201 is trying to protect end-users against – pocket pricing – exists at the micro, as well as macro, level of a market. End-users will not be protected from these harms if a broad, regional, interpretation is applied to s201's application. In our view, the assessment of whether a different price is being charged for the same service in different geographic locations must rightly be made at a more granular, premises-by-premises, level.

S201's use of the singular "the" ("the" location of "the" end-user) makes clear that its protections are intended to apply to all end-users and supports our position that the "geographic location" referenced

in s201 should be assessed at an individual end-user level. This position is also consistent with the Commission's determination that the "geographic areas" that make up a Specified Fibre Area should also be assessed on a premises-by-premises basis for the same reason:

...we will adopt a granular premises-by-premises approach that ... aligns with the end-user by end-user requirements and protections of the [Copper Withdrawal Code].¹

Chorus' connection incentives are applied on a premises-by-premises basis: if a location or premises is connected to a competing broadband technology, all of the Chorus incentives apply. If it is not, the majority of those incentives do not apply. In our view they therefore result in different prices based on the geographic location of an end-user in contravention of s201.

¹ Determining specified fibre areas: Framework and initial approach, pp21-23, Commerce Commission, 31 October 2019

Introduction

1. Thank you for the opportunity to comment on submissions relating to the Commission's draft guidance on how it intends to apply s201 pricing requirements (**the guidelines**).
2. Section 201 provides that:

201 Geographically consistent pricing

A regulated fibre service provider who is subject to price-quality regulation must, regardless of the geographic location of the access seeker or end-user, charge the same price for providing fibre fixed line access services that are, in all material respects, the same.

3. Policy makers were conscious that the pure revenue cap and guaranteed return regulatory model that would be applied to Chorus left significant risks for end-users and competition. The purpose of s201 was to ensure prices across regulated fibre networks remained comparable and to discourage anti-competitive pocket pricing².
4. We support the Commission's draft guidelines that set out how it intends to apply s201 in practice, ensuring the intended consumer and competition protections remain. Further, we support the Commission's observation that Chorus is expected to formulate services by reference to published service descriptions and standard terms³ and that it remain alive to potential gaming of the framework by, for example, formulating different services for different parts of the country to artificially create price differences.
5. Chorus has submitted that s 201 only relates to urban and rural differences and excludes discounts such as its current Connection Incentives, which have the effect of targeting low prices to specific segments. On its face that must be wrong. The obligation to charge the same price "*regardless of the geographic location of the ... end-user*" suggests on the plain meaning of the word that each end-user – all New Zealanders – should be offered the same price by Chorus. The use of the singular in s201 is, we believe, definitive. Our submission therefore is that section 201 requires that the price for the same service must be the same for all end-user premises connected to the FFLAS network "*regardless of geographic location*".

Comment

What pricing practices are addressed by s201

6. Chorus further submits that the pricing guidelines should be interpreted as being primarily aimed at ensuring that rural residential users pay the same for access services as their urban counterparts⁴.
7. We disagree. The Commission was right when it observed that the purposes of s201 is to ensure comparable pricing for all customers and to discourage pocket pricing.⁵

[33] By enacting s201, Parliament intended to ensure geographically consistent pricing between urban and rural areas and in particular to avoid end-users in more remote or sparsely populated parts of New Zealand paying a higher price for FFLAS than end-users in urban or densely populated areas. *Parliament also intended to prevent Chorus from selectively dropping prices in particular areas to*

² Policy makers also provided for declared price capped services to mitigate these concerns.

³ Draft at para 37

⁴ Chorus submission at page 2

⁵ Draft at para 33.

deter competition that might otherwise develop, in particular from competing technologies like fixed wireless access.

[emphasis added]

8. This follows the words of s201 and Officials' advice to the Select Committee setting out this purpose:⁶

Geographically consistent prices

[71] The legislation provides that Chorus must charge the same price for a fibre service regardless of the location of the customer. *This is to ensure comparable pricing for all customers, and to discourage "pocket pricing", where a regulated fibre provider could strategically drop prices in a geographic area to undermine competition.*

[emphasis added]

9. Section 201 is intended to prevent pocket pricing. Pocket pricing relates to differential pricing to geographic or customer segments by an incumbent operator in response to potential entry or expansion by a competitor⁷. As the Commission has noted, entry or expansion into a market could be constrained by an incumbent's differential customer pricing⁸.
10. Pocket pricing is a particular risk with a revenue cap model in that the regulated provider is guaranteed recoupment of any foregone revenues through the BBM, and it can check current wireless and cable competition for its copper-based services and future competition for its fibre services.
11. Section 201 is clearly intended to mitigate consumer and pocket pricing competition risk. This is reflected in the words of s201 that regulated providers must, regardless of the geographic location of the access seeker or end-user, charge the same price for providing fibre fixed line access services.
12. However, we are concerned that the Chorus submission, and potentially draft guidelines, are overly-focused on a specific form of differential pricing – i.e., urban and rural prices – and particular level of geographic aggregation when s201 is not limited in these ways.
13. In particular, we note that s201 – in seeking to mitigate urban/rural differences and pocket pricing – is not:
- Limited to a particular observable pricing structure. For example, s201 does not only relate to observable geographic pricing structures such as different urban and rural prices. It is differences in prices to access seekers and end-users (regardless of their location) that is the primary focus of the prohibition.
 - Filtered by a particular level of geographic aggregation. For example, the price differences do not need to be aggregated to a group of customers or to a suburb or region. It is the fact that *a/the* end-user faces a different price from a customer in any other location that is the concern.

What level of granularity should the Commission use to determine the relevant geographic location

⁶ Telecommunications (New Regulatory Framework) Amendment Bill, Departmental Report to the Economic Development, Science and Innovation Committee, 10 April 2018 at [71].

⁷ https://comcom.govt.nz/_data/assets/pdf_file/0023/61970/final.pdf

⁸ Referenced in the Enable and Ultrafast submission at para 3.2

14. The s201 requirement is to keep prices consistent between customers – and so is to be applied at a customer-by-customer level. Chorus and the Commission risk replacing the words of the Act with the idea that harmful pocket pricing only happens at a regional level. Just as rural price differences were a policy concern in the legislative drafting process, so too was pocket pricing, and s201 seeks to implement protections that mitigate *both* of these concerns.
15. A regional approach to interpreting the use of the words “geographic location” in s201 would not, therefore, satisfy the requirements of the Act. They would not protect every end-user against pocket pricing. S201 deliberately uses the singular (“the” geographic location of “the” end-user) to ensure that pocket pricing at a sub-regional level or at a premises-by-premises level, was also clearly prohibited. Not end-users, “the” end-user. Not locations, the “location”.
16. The Commission considered a very similar question – of whether the coarser term “geographic areas” should be interpreted in a broad or granular way - in its determination of Specified Fibre Areas in October 2019 and also formed the view that a premises-by-premises was the correct application of the Act given the way the Act was constructed, the particular harm the provision was protecting against, and the way telecommunications networks work. We encourage the Commission to make the same finding in this case.
17. At a minimum s201 requires the Commission to make an informed decision as to how “*the geographic location of the access seeker of end-user*” should be interpreted – in a broad or a granular way, just as it did in considering the meaning of the words “geographic areas” in s69AB.
18. In the case of S69AB, the Act required the Commission to determine “*the geographic areas in which a specified fibre service is available to end-users*”. The Commission considered whether this geographic delineation should be applied at a “general (broad) level or at a “more specific (granular) level” and concluded:

... we will adopt a granular premises-by-premises approach that aligns with how CIP assess the performance of Chorus and the LFC fibre network builds under the UFB agreements and aligns with the end-user by end-user requirements and protections of the [Copper Withdrawal Code].⁹
19. This logic applies equally to this case and to the harms s201 seeks to protect against, and the plain meaning of “geographic areas” is much wider than that of “the geographic location”. The Commission therefore should apply the same premises-by-premises approach to s201 as it took to s69AB.
20. These types of connection incentives harm end-users in a number of ways. They constrain competitive entry and expansion, which lessens competition with requisite poorer outcomes for end-users generally. They steer retailers to remove lower priced, entry-level, low-speed fibre services which potentially results in some end-users missing out on fibre broadband performance that might otherwise have been able to afford. And they have the potential to create a “two speed” retail market.
21. This is because the Chorus connection incentives are designed to reward end-users who self-identify as more open to switching through having taken up alternative (non-fibre) technologies at their address. The incentives lead Access Seekers to target competitive activity and offers selectively at those customers. And the corollary of that is they place commensurately less competitive focus on other customers. As the UK’s Competition and Markets Authority has

⁹ Determining specified fibre areas: Framework and initial approach, pp21-23, Commerce Commission, 31 October 2019

recently identified,¹⁰ this kind of pocket pricing can create a 'loyalty penalty' against inert customers.

22. Each of these harms affect end-users on a premises-by-premises basis and a regional approach to interpreting the geographic delineation in s201 will not address or prevent them.

What components form part of the "price"

23. The draft guidance notes that the reference to 'the same price' in the s201 context is to the price actually paid by access seekers once any adjustments, rebates or discounts have been accounted for¹¹. Such a formulation is uncontroversial and is consistent with the approach taken under the Commerce Act¹² and the practice of competition regulators generally.¹³ We agree, determining the price requires an assessment of the substance of the offer in aggregate and this includes all incentives, discounts and rebates that go to determining the effective price.

Determining price

24. Chorus argues that connection incentives do not form part of the price on the basis that:

- a. The Act defines price (at s5) as the consideration paid by access seekers for FFLAS, whereas the incentive is a separate payment from Chorus to the access seeker [15], and
- b. The Commission has interpreted incentives as a "related term of payment" as provided in the s164 definition of price. The Commission notes in the draft PQ decision that:¹⁴

Section 164(1)(b) defines price as including "any related terms of payment". We consider this broad definition includes incentive payments. Incentive payments must therefore meet the geographic consistency requirement under section 201.

- c. Chorus notes the incentives are not a "related term of payment" because:
 - i. The one-off incentive payments cannot be classified as a related term of payment because it cannot be applied as a discount to the monthly price, and is therefore are not discount off the price.¹⁵
 - ii. The incentives have a different accounting and PQR treatment as capex, and therefore must be treated as capex in the context of s201,¹⁶ and
 - iii. The incentive offers are made separately from the provision of the underlying service, can't be attributed to a single service, change from year to year, and require further RSP activity.

¹⁰ See Competition and Markets Authority *Loyalty penalty' super-complaint* <<https://www.gov.uk/cma-cases/loyalty-penalty-super-complaint>>, accessed on 5 July 2021.

¹¹ Draft Guidelines on s 201, footnote 18.

¹² For example, section 30A(2) of the Commerce Act 1986 where "price fixing" has long been defined with reference to the price, discount, allowance, rebate, or credit.

¹³ The Commission's guidance on price fixing is that price fixing includes not just the fixing of a specific price but any component of price or a pricing formula (See: <https://comcom.govt.nz/business/avoiding-anti-competitive-behaviour/what-is-a-cartel>).

¹⁴ Commerce Commission Draft Chorus PQ Decision at [G6].

¹⁵ Chorus submission at [16].

¹⁶ Chorus submission at [18]-[19].

25. We disagree, the Chorus argument makes no sense and prioritises form over substance. The Act is clear that price includes consideration in any form, whether direct or indirect,¹⁷ and can be 1 or more individual prices, aggregate prices, or revenues.
26. It is unclear why Chorus believes the Commission relied on “related term of payment” to define the price, but the definition of price simply clarifies that price includes (but is not limited to) related term of payment.
27. In practice, s201 relies on the effective price paid by the access seeker or end-user for s201 to perform its purpose. We agree with the Commission that this includes all relevant payments, discounts and incentive offers.

Does s201 apply in LFC areas

28. Section 201 applies to a regulated fibre service provider who is subject to price-quality regulation. The draft guidelines propose that s 201 should only apply to Chorus where it is subject to price-quality regulation, and not in areas where the LFCs operate. They say that s 201 is unambiguous, and so the restriction must apply to Chorus in all parts of New Zealand, including in areas where LFCs already operate.
29. Enable and Ultrafast note that the s201 obligation applies regardless of the geographic location of the access seeker or end-user, and this obligation is not qualified by the s226 regulations that state the person and describe the services which constitute the regulated fibre service provider.
30. We agree with the draft guidelines. Section 201 applies to regulated fibre service providers, and the regulations specify that this is Chorus and all fibre fixed line access services, except to the extent that a service is provided in a geographical area where a regulated fibre service provider (other than Chorus Limited) has installed a fibre network as part of the UFB initiative.
- 31.

[End]

¹⁷ Definition of price at s 5 of the Act.