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PUBLIC VERSION

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Geoff Thorn
Commerce Commission
PO Box 2351
WELLINGTON

Dear Geoff

Application to Vary Commerce Commission Determination Decision 580 – New Zealand Rugby Union Incorporated.

1. The Commerce Commission (the Commission) in its Decision 580 dated 2 June 2006 authorised the New Zealand Rugby Union (NZRU) to enter into a salary cap arrangement in accordance with the Collective Employment Agreement (CEA) between the NZRU and the New Zealand Rugby Players Association (NZRPA).
2. Since that decision there have been two developments that the NZRU and the NZRPA believe warrant some salary cap relief for the Provincial Unions involved in the 2007 Air New Zealand Cup competition. Both relate to the impact of the Rugby World Cup in 2007 and suggest the need for salary cap relief in just the 2007 year. The NZRU and NZRPA have now agreed to amend the CEA to provide some salary cap relief in the 2007 year subject to having that variation authorised by the Commerce Commission.
3. This letter therefore, is a request to the Commission to vary the authorisation in the ways set out below. We set out in this letter the recent developments referred to above, details of the variation sought and the NZRU's submissions in relation to the Commission's jurisdiction to grant a variation to the current authorisation.



4. The NZRU hereby requests that the Commission vary the current authorisation so as to permit the NZRU and the NZRPA to vary the CEA to provide salary cap relief to Provincial Unions for the 2007 Air New Zealand Cup competition (and for that year only) by:
 - (a) discounting the notional values of the players who are selected in Super 14 squads as replacements for the players who are on a conditioning programme to the notional values that the replacement players would otherwise have had in the absence of the conditioning programme; and
 - (b) providing a discount to each Provincial Union in respect of each of the 33 players (32 current All Blacks plus Greg Somerville) who are most likely to comprise the 30 players who will be absent for the whole of the 2007 Air New Zealand Cup of \$18,000 per player but only to the extent that a Provincial Union can show that they have incurred additional costs as a result of the All Blacks being away at the Rugby World Cup 2007.

Developments since Decision 580

5. There have been two developments since Decision 580 that affect the operation of the salary cap for 2007, namely:
 - (a) a decision by the NZRU Board to implement (on the recommendation of All Black coaching staff) a conditioning programme for 22 players who are expected to be part of the All Black squad for the Rugby World Cup 2007. This conditioning programme will take place at the beginning of the 2007 Rebel Sport Super 14 competition which will effectively mean that 22 players will be unavailable for the first seven rounds of the 2007 Rebel Sport Super 14 competition and need to be replaced in Rebel Sport Super 14 squads; and
 - (b) an agreement (subject to authorisation) with the NZRPA to vary the CEA to take account of the absence of All Blacks from the entire 2007 Air New Zealand Cup competition by reason of their selection to participate in the Rugby World Cup 2007.
6. In the absence of any change to the current salary cap rules, the first development would mean that at least 22 additions to the notional values would flow through to the salary cap calculation of Provincial Unions for the 2007 salary cap year. In respect of the second development Provincial Unions may also incur extra costs to replace All Blacks absent from the whole of the 2007 Air New Zealand Cup competition which would also add to the salary cap payments of each Provincial Union.

7. It is the view of both the NZRU and the NZRPA that these developments mean that the salary cap for the 2007 Air New Zealand Cup competition could operate in an unduly harsh or unfair manner and that some salary cap relief is warranted in the 2007 year due to these circumstances. To provide for such salary cap relief the NZRPA and NZRU have agreed (on a conditional basis) to amend the CEA between them to the effect that:
- (1) The notional values attributable to the 22 replacement players, and to additional players in the Wider Training Group for the Rebel Sport Super 14, be discounted; and
 - (2) A flat discount of \$18,000 per current All Black (as at the End of Year Tour 2006) plus Greg Somerville would be applied to the 2007 salary cap year, but only to the extent that a Provincial Union can show that they have incurred additional costs as a result of the contracted All Blacks being away at the Rugby World Cup 2007.

Is a variation to the current authorisation required?

8. The Commission granted authorisation to:

“(a) Enter into the Salary Cap arrangement in accordance with clauses 50, and 53 of the CEA; and....

(c) Give effect to the Salary Cap Arrangements by implementing and giving effect to salary cap regulations, such authorisation to apply only insofar as the salary cap regulations implement and give effect to clauses 53 to 59 of the CEA...”¹

9. Accordingly, what is authorised is quite specific and incorporates clause 54.5 of the CEA which provides for salary cap notional values for All Blacks and Rebel Sport Super 14 players and clause 54.3 which provides that all remuneration paid by a Provincial Union to rugby players be included in the salary cap. The proposed relief would mean that the NZRU would be operating outside the terms of authorisation if adopted as not all notional values would be included in the salary cap calculation, and not all remuneration paid to players would be included in the calculation. Accordingly, the NZRU has taken the view that a variation to the current authorisation is required.

Commerce Commission’s Jurisdiction to Vary

10. A preliminary issue is whether the Commission has jurisdiction to vary the existing authorisation. The NZRU submits that it does on the basis that the

¹ Decision 580 dated 2 June 2006, paragraph 851.

NZRU and NZRPA have agreed (conditionally) to amend the collective agreement in a way that takes the salary cap structure outside the scope of the existing authorisation. We elaborate on the Commission's jurisdiction to vary below.

Commerce Commission's Approach to Altering Existing Authorisations

11. Section 65 of the Commerce Act sets out the circumstances in which the Commission may alter, revoke or substitute authorisations made under section 58 of the Act. The Commission can amend an authorisation already granted by it under section 65(1)(b) where "*there has been a material change of circumstances since the authorisation was granted*".
12. The Commission considered the operation of section 65 in its recent determination concerning the proposed revocation of authorisation of arrangements to jointly market and sell Pohokura gas (the "Pohokura Revocation Determination"). In the Pohokura Revocation draft Determination the Commission held² that under the scheme of s 65, the Commission must first consider whether it has jurisdiction to vary or revoke an authorisation. If it considers it does have jurisdiction, it must then go on to consider whether to exercise its discretion to vary or revoke an authorisation or grant a substitute authorisation.
13. The Commission will have jurisdiction to amend an authorisation if it is satisfied that section 65(1)(b) has been fulfilled, namely that "*there has been a material change in circumstances since the authorisation was granted*".
14. It is submitted that the approach of the Commission must be different depending on whether it is deciding to revoke an authorisation altogether or to amend an authorisation. At paras 71-72 of the Pohokura Revocation Determination, the Commission noted that revocation was appropriate "*where it becomes apparent that the benefits of the conduct in question do not outweigh the detriments associated with the lessening in competition*" while an amendment to an authorisation was appropriate "*when all the basic elements of the facts and reasoning on which the determination was based are still in place, but some material detail or details should be altered.*"
15. The NZRU submits that the latter is the situation here.

Is there a material change in the NZRU's circumstances?

16. The decision by the NZRU to implement a conditioning programme which takes 22 prospective All Blacks out of the first half of the Rebel Sport Super 14

2.Commerce Commission "draft determination – proposed Revocation of Authorisation of Arrangements to Jointly market and Sell Pohokura Gas" (23 February 2005)

competition is a change in circumstance as the decision to do so was only taken on 21 July 2006 i.e. after the Commission's determination. The decision to take the 22 All Blacks out of the Rebel Sport Super 14 for about half of that competition means that the Rebel Sport Super 14 franchises will need replacement players for at least some of the Rebel Super 14 competition. Those replacement players will then, as a result of the operation of the CEA, carry over higher notional values for the Air New Zealand Cup than they otherwise would have.

17. Also, the proposed agreement by the NZRU and the NZRPA to conditionally vary the CEA to recognise the absence of the All Blacks for the whole of the Air New Zealand Cup in 2007 is a material change in circumstance.
18. Subsequent to the authorisation by the Commission, the NZRU and NZRPA have turned their minds to the impact of the Rugby World Cup on the salary cap and agreed that it is reasonable to seek some relief to cater for this eventuality. In other words the very decision by the NZRU and players that they wish to amend the salary cap structure (because they have formed the view that the structure will operate unfairly and harshly), is a "*change in circumstance*". Further, that change in circumstance is "*material*" because the amendment to the salary cap structure goes to the very question of whether the authorisation is operable or not.
19. If parties to an agreement that has been authorised by the Commission agree to vary that agreement in a way that takes the agreement outside the protection of the authorisation (because the authorisation does not on its face apply to the varied agreement) then clearly there has been a change in circumstances that is very material.
20. On this basis the NZRU submits that the Commission does have jurisdiction to vary the existing authorisation. Were that not the case the parties to an agreement that is authorised by the Commission would not be able to vary that agreement unless a completely new authorisation was applied for (and a completely new authorisation may not be possible if the counterfactual for the new authorisation application was taken to be the existing form of agreement, and the benefit/detriment analysis was essentially the same between the varied agreement and the counterfactual of the existing agreement so that the Commission could not be satisfied that there were additional benefits from the varied agreement when compared with the existing agreement).

Variation Sought

21. In essence the NZRU seeks a variation to the current authorisation to the effect that in the year 2007 only:

1. The additional portion of any notional values attributable to the 22 replacement players and Wider Training Group players who are selected in Rebel Sport Super 14 squads by reason only of the conditioning programme be discounted to what they would have been but for the conditioning programme; and
2. A flat discount of \$18,000 in respect of each of the 32 current All Blacks (as at the End of Year Tour 2006) plus Greg Somerville to each of the Provincial Unions they are contracted to would be applied but only to the extent that a Provincial Union can show that they have incurred additional costs as a result of their contracted All Blacks being away at the Rugby World Cup 2007.

Notional Values and the Conditioning Programme

22. Unless the additional notional values for replacement Rebel Sport Super 14 and Wider Training Group are removed, the salary cap calculation would be artificially high because more players will carry higher notional values for the year due to the conditioning programme than was envisaged at the time the salary cap architecture was finalised. Both the NZRU and the NZRPA regard this as being unfair to those Provincial Unions that are or may be hard up against the cap. The conditioning programme does not change the identity of who is playing in the Air New Zealand Cup. The same players are being selected for the Air New Zealand Cup. However, because the conditioning programme for the 2007 World Cup year requires additional players to be in Rebel Sport Super 14 squads as “cover” for players in the conditioning programme, a number of players will have higher notional values for the purpose of the salary cap calculation for the 2007 Air New Zealand Cup than they otherwise would have done. This is due to their status as Rebel Sport Super 14 players which status is only because they are temporary replacements for All Blacks who cannot play the whole Rebel Sport Super 14 tournament due to the conditioning programme.
23. To eliminate the unforeseen hardship of the artificially high salary cap calculation the NZRU and the NZRPA have agreed to conditionally amend the CEA. For the 2007 Air New Zealand Cup competition only, salary cap payments will exclude the notional values attributable to the additional notional values for the replacement players and extra Wider Training Group players created as a direct result of the conditioning programme. Appendix One of this letter sets out how the relief would be provided and also sets out the actual relief to be provided on a player by player and Provincial Union by Provincial Union basis.

Absence of All Blacks from the 2007 Air New Zealand Cup competition

24. The absence of the All Blacks from the 2007 Air New Zealand Cup is the second matter that gives rise to a need for salary cap relief. The CEA and the Salary Cap Regulations already provide a 60% discount for Current All Blacks which recognise that, on the one hand, All Blacks are valuable to Provincial Unions on and off the field (e.g. in a promotional capacity and because they can attract other players to the Provincial Union) but on the other hand their availability or lack of can be determined by the All Black coach and selectors in the interests of player welfare and other relevant matters. World Cup years are however different from normal years in the extent to which All Blacks are likely to be available for the Air New Zealand Cup. While in normal years All Blacks are available for part of the Air New Zealand Cup, in the 2007 World Cup year the All Blacks selected for the Rugby World Cup are likely to be absent from the entire Air New Zealand Cup.
25. The NZRU and the NZRPA believe that salary cap relief should be allowed in 2007 to the extent that Provincial Unions can show that they have or might incur additional contracting costs to replace those All Blacks included in the 2007 World Cup squad. We have set out in Appendix 2 how we have determined who the relief should apply to (32 current All Blacks plus Greg Somerville), the amount of relief (\$18,000 per All Black) and the total proposed relief for each Provincial Union.
26. Generally, these proposals seek to give relief on the basis that the relief matches as closely as possible the additional player salary cap costs a Provincial Union faces as a result of the absence of the All Blacks for the entire 2007 Air New Zealand Cup competition.
27. The Commission should note that we have adopted a conservative approach to relief in this instance with the \$18,000 being at the lower end of the Provincial Unions' estimates of the additional costs they will face. The NZRU has adopted this approach because it considers it is the best way of ensuring that the relief does not alter the balance of the Commission's previous assessment of the benefits and detriments arising from the salary cap. This is reflected in the conclusions of Brown Copeland & Co Ltd, as set out below:

In my opinion:

- *The All Blacks' conditioning programme and consequent salary cap implications were not explicitly or implicitly taken into account by the Commerce Commission in Decision 580. The NZRU proposed salary cap relief for the conditioning programme does not alter the Commission's assessment of the balance between competitive detriments and public benefits, since the proposed salary cap relief will have the effect of maintaining the status quo;*

- *The absence of the 2007 RWC All Blacks from the 2007 Air New Zealand Cup competition was not explicitly taken into account by the Commerce Commission in Decision 580. The NZRU proposed salary relief for the absence of RWC All Blacks from the 2007 Air New Zealand Cup competition does not alter the Commission's assessment of the balance between competitive detriments and public benefits, since it will only compensate provincial unions for the conservatively estimated additional salary costs they will incur due to the absence of the All Blacks; and*
- *Even if the Commerce Commission implicitly took into account the absence of RWC All Blacks from the 2007 Air New Zealand Cup competition, the salary cap relief proposed will not have a significant impact on the Commission's assessment of the balance between competitive detriments and public benefits. The salary cap relief proposed will not enable them to replace the absent All Blacks with players of similar calibre, in a year when the absence of the All Blacks will itself have a significant levelling effect on the evenness of the Air New Zealand Cup competition. Also the net effects of any hypothetical loosening of the salary cap in year 2 of the Commission's five-year quantitative analysis period will be very small, and not material in my opinion.*

Further Information

28. In support of this request for a variation to the authorisation in Decision 580 we have included additional information that may help the Commission form a view. Appendix 1 and 2 sets out the basis for the relief to be provided to Provincial Unions and also the actual relief to be provided on a player by player and Provincial Union by Provincial Unions basis. Appendix 3 sets out in full the Provincial Unions' views on the additional costs associated with the All Blacks being away for the 2007 Air New Zealand Cup competition. Appendix 4 sets out salary cap levels for 2006 and Appendix 5 sets out the views of Brown Copeland & Co Ltd on how the proposed relief is likely to affect the Commission's previous assessment of benefits and detriments associated with the authorisation. We have also agreed with the NZRPA changes to the Collective Employment Agreement and Salary Cap Regulations (subject to Commerce Commission authorisation) and have attached these changes as Appendix 6.

Conclusion

29. This matter is quite urgent as Provincial Unions are currently contracting players for the 2007 Air New Zealand Cup competition and need to know what salary cap relief (if any) will be available to them.
30. The NZRU submits that the Commission does have jurisdiction to consider this application and should vary the authorisation to allow the NZRU and the

NZRPA to agree to vary the CEA to provide salary cap relief to Provincial Unions for the 2007 Air New Zealand Cup competition on the following basis:

- (a) the additional portion of the notional value for those players selected in final Rebel Sport Super 14 squads as replacements for the prospective All Blacks who are conditioning plus the notional values for the additional Wider Training Group players who would not otherwise had been selected in the Wider Training Group should be discounted to what they would have been if they had not been selected in Rebel Sport Super 14 squads or Wider Training Groups respectively; and
 - (b) a flat discount of \$18,000 for each of the 32 current All Blacks plus Greg Somerville, who are most likely to comprise the 30 players selected in the Rugby World Cup squad contracted to each Provincial Union would be applied to the 2007 salary cap year but only to the extent that a Provincial Union can show that they have incurred additional costs as a result of the All Blacks being away at the Rugby World Cup 2007.
31. Should you want to further discuss this letter do not hesitate to call me, Keith Binnie (General Counsel) or Craig Neil (Salary Cap Manager) from this office.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Steve Tew', with a long horizontal stroke extending from the top left.

Steve Tew

Proposed Relief for Removing the Notional Values for the 22 Rebel Sport Super 14 Replacement Players

Under the Rebel Sport Super 14 Squad Selection Protocols each Super Rugby Franchise must identify the players selected as replacements for their conditioning players (Rebel Sport Super 14 Replacement Players). It is the additional notional value attributable to these replacement players and the Wider Training Group replacements that we are proposing is removed from the 2007 salary cap calculation, as follows:

- (1) As a result of the conditioning programme there will be 162 Final Super Rugby Squad members as opposed to 140 players in a normal year. This means that an extra 22 players will have notional values of either \$20,000, \$35,000 or even \$50,000 depending on their Rebel Sport Super 14 experience and All Blacks experience. It is proposed that the 22 designated replacement players **will not** be attributed a notional value of \$20,000, \$35,000 or \$50,000. In the absence of the conditioning programme these replacement players would likely be members of a Wider Training Group and would have had a notional value of \$10,000. For this reason it is proposed that all of the 22 replacement players **will** be attributed a Wider Training Group notional value of \$10,000; and
- (2) As a result of a Rebel Sport Super 14 Replacement Player being included in the Final Super Rugby Squad another replacement player will take his place in the Wider Training Group. The final step in the process would be to remove completely the notional value attributed to the Wider Training Group replacement player (unless the player is on a full NZRU Contract for 2007 in which case he will still have a \$10,000 notional value).

It follows that the proposal is that:

- The Agreed Provincial Union of each Super 14 Replacement Player would receive \$10,000 salary cap relief (if that player has a \$20,000 notional value) or \$25,000 salary cap relief (if that player has a \$35,000 notional value) or \$40,000 salary cap relief (if that player has a \$50,000 notional value per player); and
- The Agreed Provincial Union of each Wider Training Group Replacement Player would receive \$10,000 salary cap relief per player.

In this way there would be no **additional** notional value imposed as a result of the conditioning programme.

Notional Values - Specific Salary Cap Relief

This chart sets out the actual notional value relief to be provided on a Provincial Union by Provincial Union basis. The second chart in this Appendix sets out the notional value relief to be provided on a player by player basis.

Notional Value Relief on a Provincial Union by Provincial Union Basis

Notional Value Relief to be Provided on a Player by Player Basis

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Proposed Relief for Removing the Additional Costs Incurred by Provincial Unions as a Result of the Absence of the All Blacks from the Entire 2007 Air New Zealand Cup Competition

Any proposed salary cap relief would remove the additional salary cap costs associated with the absence of 30 All Blacks from the whole of the Air New Zealand Cup competition as opposed to some of it.

The aim of this approach is to put all Provincial Unions in the same position they would have been in had the All Blacks been available for some of the 2007 Air New Zealand Cup (as they would normally have been in a non World Cup year).

Providing Relief

Our original approach was to give Provincial Unions relief to compensate them for their additional costs in contracting replacement players for the *actual 30 All Blacks* going to the 2007 Rugby World Cup. However, in discussions with the NZRPA the point was made that this approach created too much uncertainty as the Air New Zealand Cup commences in July 2007 and the World Cup squad comprising the 30 All Blacks would not be announced until August 2007 which means that Provincial Unions would not know how much relief they were entitled to until after the start of the 2007 Air New Zealand Cup. This would adversely affect a number of the Provincial Union's contracting processes and also their ability to manage their salary cap.

Accordingly rather than provide relief in respect of the 30 All Blacks to be named in August 2007 we have identified 33 players who we consider to be the most likely to be selected in the 2007 World Cup squad and propose to provide relief to those Provincial Unions who have contracts with those players in the 2007 year. The 33 players comprise the 32 All Blacks who went on the 2006 end of year tour plus Greg Somerville who is in the conditioning programme and who would have gone on the end of year tour had he not been injured.

This approach provides Provincial Unions with the certainty of knowing now how much relief they will be entitled to and to plan and contract accordingly. We accept that the relief would apply to more players (33) than will actually be going to Rugby World Cup 2007 (30) but considered that the overriding fairness consideration was to give Provincial Unions certainty in respect of the proposed salary cap relief with any additional relief this may lead have to being dealt with through adjusting (if necessary) the amount of relief provided per player.

Having identified the players that the relief should apply to we then considered how the relief should be provided. Relief could be provided on:

- (1) a player by player basis whereby the additional cost of replacing each of the 33 players was determined and then that amount allocated to the player's Provincial Union; or

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- (2) an average basis whereby the additional cost of replacing each player is averaged across all those 33 players and that average amount allocated to the player's Provincial Union.

On balance the NZRU submits that the average approach should be adopted. The responses provided by the Provincial Unions (refer Appendix 3) show that it is extremely difficult (if not impossible) for Provincial Unions at this time to determine on a player by player basis the additional costs attributable to their absence from the 2007 Air New Zealand Cup. Moreover, the average approach is consistent with other aspects of the salary cap regulations namely the All Black and Veteran discounts and All Black Notional Values where an averaging approach is taken.

The Amount of Salary Cap Relief

The amount of salary cap relief has proved extremely difficult to quantify. However, two principles underpinned the NZRU's approach to determining the relevant amount:

- (1) Relief should be limited to the additional salary cap contracting costs associated with the absence of the All Blacks from the whole of the 2007 Air New Zealand Cup competition as opposed to some of it; and
- (2) Any proposed relief should not alter the balance of the Commission's previous assessment of the benefits and detriments arising from the salary cap. In particular, we should not provide for too much relief and, if anything, relief should be granted at the lower end of the scale.

To try and estimate the additional costs we asked all Air New Zealand Cup Provincial Unions to provide us with their best estimates of what their additional costs would be. Five Provincial Unions provided responses and these responses are set out in full in Appendix 3.

The information provided is mixed. Auckland indicates that they will simply upgrade Provincial Union Development contracts where appropriate. Waikato, Canterbury and Wellington have attempted to provide more specific information. Waikato indicates that they have had to spend on average [] to replace each potential World Cup All Black. Canterbury has indicated that their total additional costs will be somewhere around []. (Our estimates suggest that Canterbury will have around seven World Cup All Blacks so this averages out to [] per All Black.)

Wellington has tried to cost their additional costs out on a player-by-player basis which averages out to be [] per player. Taranaki has indicated that their cost for two players may be around [].

We have also looked at the average 2006 remuneration paid to the top 26 top players in each Provincial Union and the average remuneration per player across all teams was []. The average lowest 10 players (out of the 26) earned [] with the average lowest 5 players (out of the 26) earning [].

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It is extremely difficult to reach a definitive conclusion on what the actual cost per player will be with the evidence (such as there is) suggesting that the per All Black cost will be somewhere between [].

In reaching a final view there are a number of other factors that the NZRU has taken into account:

- Relief should only compensate Provincial Unions for the additional costs associated with their All Blacks being away for the Rugby World Cup;
- Not too much relief should be provided and any such relief should be at the lower end of Provincial Unions' estimates. This should ensure that the relief does not disturb the Commission's previous assessment of benefits and detriments associated with the authorisation;
- All the Franchise based Provincial Unions have some salary cap headroom so the NZRU should be careful not to provide too much relief as this could be used for future salary cap planning purposes; and
- The salary cap architecture already allows for Provincial Union remuneration to be discounted for current All Blacks (60%) and former All Blacks (40%) which reduces their remuneration for salary cap purposes and so reduces the impact on the Provincial Union of their availability or unavailability. The discounts were to recognise that, on the one hand All Blacks are valuable to Provincial Unions on the field and off the field but on the other hand their availability can be controlled by the All Black coach and selectors in the interests of player welfare and other relevant matters.

We believe that these additional factors lead to the conclusion that any relief should be at the lower end of the [] scale estimated by Provincial Unions. In determining a final figure within this range we have had close regard to the 2006 average amount paid to Provincial Union players – particularly at the lower end of the scale (e.g. the lowest 5 players in each Provincial Union earn on average []) as we believe that this is the level where Provincial Unions are most likely to contract replacement players.

Accordingly, we have conditionally agreed with the NZRPA that each Provincial Union be allowed to deduct \$18,000 from their Salary Cap Remuneration Payments for each of the 33 players listed in this Appendix. The \$18,000 is equivalent to \$19,800 if the relief had been provided to the 30 missing All Blacks.

However, the proposed relief is not automatically available to the Provincial Unions but is only available to the extent that a Provincial Union can show the NZRU Salary Cap Auditor that the Provincial Union has incurred additional costs as a result of the All Blacks being away at the Rugby World Cup 2007.

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33 Players of whom Relief is proposed for 2007 - Specific Salary Cap Relief on a Provincial Union Basis

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Appendix 3

[Responses Received from Provincial Unions on Proposed Salary Cap Relief

Canterbury

Hi Craig, I have been doing much thinking about this. It is quite difficult to do this with any real accuracy, but on the assumption the current EOYT players from here all make the RWC squad in 2007, I estimate the impact could be around [] without considering notional values.

This takes account of the fact that with the players out of our campaign completely, we have to contract players at a different level as their value goes up in the market place. [].

We also have issues at [], and if [] isn't to play for us at all next year I am assuming we will need to recruit. Again, it is more likely we will "make do" if we know [] is back shortly - we can't just make do if he's not coming back at all. The same logic applies to [], and to []. We have already made offers to [] and [] to cover players potentially away.

This estimate is not an exact science; however, there is no question the impact on contracting costs is upwards.

Cheers Hamish

Auckland

Hi Craig, Auckland Rugby have contracted a number of players on PU Development contracts as well as 2006 1st year ANZC players for at least one further year to cover for AB's that will be potentially away for the entire 2007 campaign.

This has been our main initiative in order to cover for AB's that will be missing.

Hopefully this assists.

Regards Warrick

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Waikato

Sorry to have missed the deadline for responding on this issue but for what it is worth here are my comments:

The players we are assuming will be missing from our PU squad next year because of the RWC2007 include:

[]

We have had to contract additional players to cover for each of these positions for the entire 2007 Air New Zealand Cup. These contracts are full PU contracts and range between [] each. The total additional cost is approximately []. Normally we would use PU Development players

In most cases we have been forced to contract them for two years because they wouldn't accept one year contracts for 2007 only given their caliber.

In addition the following players have an outside chance

[]

We anticipate contracting more players than we normally would under PU Development contracts to help provide cover should any of this second group make the RWC2007 squad.

Apart from the need for more players to cover for All Blacks being absent for all of the 2007 Air New Zealand Cup we haven't changed our contracting behaviour too much with regard to 2006 and 2007 All Blacks.

Give me a call if you need any further information.

Taranaki

Hi Craig, Assuming our two current All Blacks are selected in RWC 2007, we will cover [] from within what we have locally but will specifically be targeting a recruitment for []. Total cost of this could reach \$[]. Trust this is helpful information.

Regards Paul

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Wellington

*Craig Neil
Salary Cap Manager*

NZ Rugby Union
P O Box 2172
Wellington

Dear Craig

Relief Under Salary Cap for 2007

We are responding to your letter of 25 September 2006 on the above topic. We are pleased that the NZRU Board has approved in principle the granting of salary cap relief for 2007 subject to agreement with the NZRPA and authorization from the Commerce Commission.

Proposed Relief for the Conditioning Programme

The proposed method outlined in Appendix 1 of your letter seems to be unnecessarily complex. In our opinion the same result would be achieved more simply if:

- (a) The 28 first choice players in the Super 14 squads (including the 22 conditioning AB's) are assigned the relevant notional values as per the status quo
- (b) A further 8 players be classified as WTG members with a notional value of \$10,000. This will include a mixture of players who will directly replace the conditioning AB's for the first half of the competition and those who will still be in the WTG for their franchise.
- (c) A new classification be introduced "WTG Replacement Player" for the players who will need to be brought into each franchise to ensure there are a total of 36 players in each squad. These "WTG Replacement Players" would have a notional value of zero.

We believe that our suggested method reinforces a basic principle of the Salary Cap Regulations that, excluding those players on NZRU retainer contracts, there are only 180 players in NZ who want a notional value, comprising:

- (a) 140 Super 14 players with a notional value of \$20,000 or more, and
- (b) A further 40 WTG players with a notional value of \$10,000.

All other players are deemed to have a status too low to attract a notional value at all. The change in circumstances for a single year should not change this fact especially as they will only be part of the S14 squads for part of the season.

Proposed Relief for Absent All Blacks

We reiterate the comments in our letter of 24 July to Keith Binnie that it is inequitable that a PU should bear the cost of a player who will not play for them or be of any other benefit to the PU concerned at all during a season as a result of a direction by a third party. The unavailability of players due to injury is a normal business risk but frustration of a player's contract due to a decree from a third party is a most unusual, probably unique, business circumstance. It is the imposition of a restraint of trade on the PU's who are already supporting the NZRU in their goal to win the RWC by not seeking compensation from them for the 2007 salaries of the players involved. We expect this goodwill to be reciprocated by way of some relief under the Salary Cap.

Your proposal to give relief to the extent that PU's can show that they incur additional player costs as a result of the AB's absence from the whole of the ANZC (as opposed to a portion of it) ignores a very important point in that it does not recognize that the status quo salary cap amount enables Wellington to retain players of a certain standard. By stating that a PU should be compensated to the extent that its salary cap remuneration level is not increased, it ignores that fact that without the AB's, the standard of players available in 2007 must by definition be lower than the status quo. That is, we will be "paying" the same amount for an inferior product. PU's must get some compensation/relief for this.

In our opinion, the relief should recognize that the PU's will be receiving no value at all from their AB's in 2007 therefore the discount on the PU remuneration must be increased from 60% to 100% and the imposition of the notional value for each player must be removed. This matches the relief presently given under the Salary Cap Regulations in the circumstance where a player is injured or loaned for a full season. As well as being within the principles of the Regulations it will be far simpler to calculate and audit than the method proposed by NZRU.

As requested by you, we have assessed what the financial impact for Wellington will be of engaging replacements for those players who are likely to be in the RWC 2007 squad. This cost equates to \$[] — full details are shown in the attached appendix. We have assumed that there will be [] Wellington players in the RWC squad. In some cases we will be able to upgrade local players to fill the vacancies but in the areas of prop and half back it is quite likely we will need to recruit externally. A couple of positions will also be filled by players that we loaned to other PU's and for whom we got salary cap relief in 2006.

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Commerce Commission

You have stated that the Commerce Commission must be convinced that the proposed salary cap relief does not negatively impact on its previous assessment of the benefits and detriments arising from the salary cap.

Philosophically, we believe that our proposed solutions for relief under the Cap will increase the benefits of the salary cap because Wellington will be able to contract more players (albeit of a lower standard) who will obtain ANZC experience in 2007 which will make them better players. As a result they will be more marketable and available to transfer to other unions in 2008 and beyond. This should have the effect of making the ANZC more competitive in the future.

The Regulations have already restricted the number of players that we can contract. Without any relief from the Regulations, the lack of headroom in the Cap will make it extremely difficult for Wellington to contract additional players to replace seven RWC All Blacks. This, in turn, will place considerable restraints on our ability to field a competitive team in 2007. Surely such a constraint resulting from the decision of the NZRU to make the players unavailable for the ANZC is an uncompetitive practice and contrary to the Commerce Act.

We are available to discuss the contents of this letter with you if you wish.

Yours sincerely

Greg Peters
Chief Executive

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Appendix 4

2006 Salary Cap Levels

2006 Salary Cap Levels
Based on RugbyCap as at 26 October 2006

Letter from Mike Copeland – NZRU Economic Consultant

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1 December 2006

Mr Craig Neil
Salary Cap Manager
New Zealand Rugby Union
P O Box 2172
WELLINGTON 6140

Dear Craig

Application to Vary Commerce Commission Determination Decision 580

You have asked me to consider the implications in terms of public benefits and competitive detriments, as assessed by the Commerce Commission, of the relief proposed by the New Zealand Rugby Union in respect of

- The All Blacks conditioning programme and the discounting of notional values of the additional players therefore selected in Super 14 and wider training group squads as replacement players; and
- The absence of the All Black Rugby World Cup (RWC) squad from the 2007 Air New Zealand Cup competition and the salary cap \$18,000 discount for each of the nominated 33 All Black players.

I set out below my assessment for each of these forms of proposed relief.

Conditioning Programme Relief

- 1 The decision of the NZRU to implement a conditioning programme, which will exclude a squad of 22 All Blacks from the first 7 rounds of next year's Super 14 competition, was taken by the NZRU Board on 21 July 2006. This was after the Commerce Commission released its Decision 580, and therefore the impacts of the proposed conditioning programme were not taken into account by the Commission in its assessment of the balance between the salary cap competitive detriments and public benefits.
- 2 The relief proposed by the NZRU, in respect of the conditioning player All Blacks, has the effect of maintaining the status quo in terms of the tightness of the salary cap for provincial unions affected. To the extent that the conditioning programme requires provincial unions to contract players for the Air New Zealand Cup at higher notional values (for players who are now included within either Super 14 or wider training group squads), salary relief equivalent to those higher notional levels is to be granted.
- 3 It can also be noted that the relief proposed is only in respect of the 2007 season where the conditioning programme has an artificial impact on notional values of players.

- 4 Therefore in my opinion the conditioning programme relief proposed will have no impact on the balance between detriments and public benefits assessed by the Commerce Commission in its Decision 580.

RWC All Blacks Relief

- 5 The second aspect of relief proposed is in relation to the absence of All Blacks in the Air New Zealand Cup due to the 2007 Rugby World Cup. While All Blacks are normally expected to be absent from the Air New Zealand Cup for just part of the season, in 2007 they are expected to be absent for the whole season due to the World Cup. No recognition was given to this in submissions to the Commerce Commission or in the Commission's Decision itself.
- 6 Therefore in allowing a measure of relief to provincial unions that attempts to compensate them for the additional salary costs that will be imposed in replacing All Black RWC squad members is consistent with maintaining the balance between the salary cap's competitive detriments and public benefits as assessed by the Commerce Commission in its Decision 580.
- 7 It will always be difficult in advance to identify precisely the extra salary costs that will be incurred by a provincial union as a consequence of the probable loss of an All Black player. However on the basis of the material supplied by the five major provincial unions, I believe the \$18,000 per player is a reasonably conservative estimate.
- 8 Even if it was assumed that the Commerce Commission had in some way taken into account the absence of RWC All Blacks from the 2007 Air New Zealand Cup in its balancing of competitive detriments and public benefits, the relief proposed is unlikely to have a significant impact on the Commission's balancing of competitive detriments and public benefits. As already noted the proposed level of relief of \$18,000 for each of the 33 nominated All Blacks is towards the lower end of what the five wealthier provincial unions have estimated to be the additional costs they will incur.
- 9 More significantly, the \$18,000 per All Black will be insufficient for the provincial unions affected to fund replacement players with anything like the calibre of their lost All Blacks (even if such players were available in New Zealand or overseas). This will be in a year when the loss of the RWC All Blacks will itself have a significant levelling effect on the Air New Zealand Cup competition.
- 10 Furthermore 2007 is only year two of the five-year analysis period used by the Commerce Commission to calculate the quantified public benefits and competitive detriments. The Commission heavily discounted the public benefits it assumed would flow from the salary cap in the early years of this analysis period because of the time it expected would be required until the salary cap was fully effective in improving the evenness of the competition and the flow of benefits from this. Therefore even if the Commission took into account the absence of RWC players in 2007 and the proposed relief has the effect of a small loosening of the salary cap's effectiveness in 2007, any consequent impact on the Commission's estimate of public benefits would in my opinion be very small.
- 11 In addition any hypothetical loosening of the salary cap in 2007 as a consequence of the proposed relief for RWC All Blacks would also impact on the Commerce Commission's detriment calculations regarding loss of player talent and allocative

inefficiency.¹ Therefore the net effect in terms of the balancing of competitive detriments and public benefits would be even smaller. In my view there would not be a material impact on the difference between public benefits and detriments.

- 12 Again, it can be noted that the proposed salary cap relief would only apply in the 2007 year when the absence of the RWC All Blacks has a temporary impact on the expected salary costs of provincial unions.

Conclusions

- 13 In my opinion:

- The All Blacks' conditioning programme and consequent salary cap implications were not explicitly or implicitly taken into account by the Commerce Commission in Decision 580. The NZRU proposed salary cap relief for the conditioning programme does not alter the Commission's assessment of the balance between competitive detriments and public benefits, since the proposed salary cap relief will have the effect of maintaining the status quo;
- The absence of the 2007 RWC All Blacks from the 2007 Air New Zealand Cup competition was not explicitly taken into account by the Commerce Commission in Decision 580. The NZRU proposed salary relief for the absence of RWC All Blacks from the 2007 Air New Zealand Cup competition does not alter the Commission's assessment of the balance between competitive detriments and public benefits, since it will only compensate provincial unions for the conservatively estimated additional salary costs they will incur due to the absence of the All Blacks; and
- Even if the Commerce Commission implicitly took into account the absence of RWC All Blacks from the 2007 Air New Zealand Cup competition, the salary cap relief proposed will not have a significant impact on the Commission's assessment of the balance between competitive detriments and public benefits. The salary cap relief proposed will not enable them to replace the absent All Blacks with players of similar calibre, in a year when the absence of the All Blacks will itself have a significant levelling effect on the evenness of the Air New Zealand Cup competition. Also the net effects of any hypothetical loosening of the salary cap in year 2 of the Commission's five-year quantitative analysis period will be very small, and not material in my opinion.

Yours sincerely



M C Copeland

¹ Productive inefficiency losses relating to the salary cap's administration and policing costs are largely fixed and unaffected by whether the cap is tightened or loosened.

Changes to the Collective Employment Agreement and Salary Cap Regulations to give effect to Proposed Notional Value Relief

Clause 54.5 of the CEA

Clause 54.5 will be amended to include a proviso after clause 54.5 (e), being:

“Provided that for the Contract Year 2007 only:

“**Conditioning Player**” means a Player who has been identified by the All Blacks selectors as requiring a conditioning break prior to the Rugby World Cup 2007

“**Replacement Player**” means a player selected to replace a Conditioning Player in the Final Super Rugby Squad in accordance with the 2007 Rebel Sport Super 14 Squad Selection Protocols and Process

- a Player who is a Replacement Player will have a notional value of \$10,000; and
- a Player who would not have been in a Wider Training Group but for the conditioning programme will have a notional value of \$0 (unless that player is a De-Listed Player in which case the Player will have a notional value of \$10,000). The NZRU will determine the players who would not otherwise have been selected in the Wider Training Group and will notify the appropriate Provincial Unions.

Clause 42.2 of the Salary Cap Regulations

Insert the following definitions into the Regulations:

“**Conditioning Player**” means a Player who has been identified by the All Blacks selectors as requiring a conditioning break prior to the Rugby World Cup 2007.

“**Replacement Player**” means a player selected to replace a Conditioning Player in the Final Super Rugby Squad in accordance with the 2007 Rebel Sport Super 14 Squad Selection Protocols and Process.

“**De-Listed Player**” has the meaning set out in clause 40 of the CEA.

Clause 42 of the Salary Cap Regulations will be amended to include a proviso after clause 42.2 c. iii, being:

“Provided that for the Contract Year 2007 only:

- a Player who is a Replacement Player will have a notional value of \$10,000; and
- a Player who would not have been in a Wider Training Group but for the conditioning programme will have a notional value of \$0 (unless that player is a De-Listed Player in which case the Player will have a notional value of \$10,000). The NZRU will determine the players who would not otherwise have been selected in the Wider Training Group and will notify the appropriate Provincial Unions.

Changes to the Collective Employment Agreement and Salary Cap Regulations to give effect to the \$18,000 Relief

Collective Employment Agreement

Add a new definition:

“**Relief Player**” means one of the 33 players identified by the NZRU as qualifying the Provincial Union to whom they are contracted in 2007 for salary cap relief in accordance with the Salary Cap Regulations.

Clause 54.2 will be amended by adding a new bullet point after the 5th bullet point in paragraph (c):

- for the 2007 Contract Year only a Provincial Union will be entitled to subtract an amount of \$18,000 from their Salary Cap Payments in respect of each Relief Player contracted to that Provincial Union in 2007 to the extent that the Provincial Union can show that the amount was incurred by the Provincial Union to replace their Relief Players.

Clause 35A of the Salary Cap Regulations

Add a new definition:

“**Relief Player**” means one of the 33 players identified by the NZRU as qualifying the Provincial Union to whom they are contracted in 2007 for salary cap relief in accordance with these Cap Regulations.

Insert a new Clause 35A being:

For the 2007 Contract Year only a Provincial Union will be entitled to subtract an amount of up to \$18,000 from their Salary Cap Payments in respect of each Relief Player contracted to that Provincial Union in 2007 to the extent that the Provincial Union can show that the amount was incurred by the Provincial Union

to replace their Relief Players and the NZRU Salary Cap Auditor is satisfied that the additional costs were incurred to replace the Relief Players.

In considering whether additional costs were incurred to replace a Relief Player the NZRU Salary Cap Auditor may have regard to the following factors:

- a. whether a player was contracted specifically to replace a Relief Player;
- b. whether and to what extent a player received an upgraded contract in 2007 by reason of replacing a Relief Player;
- c. whether a player was a loan player in a previous year but was not loaned in the 2007 Contract Year to replace a Relief Player; and
- d. any other relevant factor.