

Clarification of the Vodafone New Zealand Rural Broadband Initiative Deed

Decision [2012] NZCC 19

Amendment to the Deed between Vodafone New Zealand Limited and the Crown made under s156AN of the Telecommunications Act 2001

The Commission:

Dr S Gale, Telecommunications Commissioner

A Mazzoleni

P Duignan

Date of Decision: 23 July 2012

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Overview

1. The Commission has agreed to clarify Vodafone's obligations regarding the discounts or other subsidies it gives when providing retail broadband services to rural customers. This decision sets out the nature of the amendment and the reasons for the Commission's decision.
2. Under this amendment, Vodafone must continue to recover any discount, credit, rebate or subsidy given to end-users purchasing its retail broadband services, but may do so within the actual retail mark-up over the lifetime of the service.
3. This amendment is made in accordance with s156AN of the Telecommunications Act 2001 (**Act**), which applies to Vodafone's Rural Broadband Initiative Deed through s156AZ of the Act.
4. The Commission considers that the clarification addresses an ambiguity within the text of the Deed and therefore is not material.

Background

Vodafone's participation in the rural broadband initiative

5. In 2011, the Government introduced its \$300 million rural broadband initiative (**RBI**), which provides for the roll-out of broadband services to rural communities throughout New Zealand. The purpose of the RBI is to improve the quality of broadband services for schools, enterprises, and households in hard-to-reach rural areas in which fibre is not likely to be deployed in the immediate future.
6. Vodafone New Zealand Limited (**Vodafone**) and Chorus New Zealand Limited (**Chorus**) were jointly awarded the tender to provide rural broadband coverage to much of rural New Zealand.¹
7. In return for Government funding, the Government has required that Vodafone and Chorus provide wholesale access services to other retail service providers. These wholesale access services include:
 - 7.1 A wholesale broadband service providing 5 Mbps peak speeds
 - 7.2 A wholesale "bundled" service of broadband together with a voice service
 - 7.3 A wholesale enhanced broadband service, with a higher prioritised speed than the (basic) broadband service.
8. These three wholesale access services allow the retail service providers to provide their own retail broadband (and voice) services to end-users.

¹ In addition, Chorus and Network Tasman will deploy fibre to provincial schools, rural hospitals, health centres, and public libraries and 57 remote schools and their surrounding communities will be connected by Inspire.net, Gisborne.net, Chorus, and Araneo.

9. The Government has required that Vodafone and Chorus provide these wholesale services on a non-discriminatory basis.

10. Non-discrimination –²

in relation to the supply of a relevant service, means that the service provider must not treat access seekers differently, or, where the service provider supplies itself with a relevant service, must not treat itself differently from other access seekers, except to the extent that a particular difference in treatment is objectively justifiable and does not harm, and is unlikely to harm, competition in any telecommunications market.

11. Vodafone’s non-discrimination obligations are governed by the terms of a Deed of Undertaking agreed between Vodafone and the Crown on 22 September 2011 (**Deed**).³

12. The Commission is given responsibility under the Telecommunications Act 2001, and the Deed, to monitor and enforce Vodafone’s obligations. In addition, the Act authorises the Commission to clarify Vodafone’s obligations under the Deed where the change is not material.

Vodafone’s non-discrimination obligations

13. The Deed sets out the enforceable non-discrimination undertakings in relation to the wholesale broadband services provided to access seekers. In order to ensure there is no discrimination for the wholesale price of the broadband services, the Deed sets limits on the retail price of the service, and on any discounts, rebates, credits, or other subsidies that Vodafone may offer.

14. First, the Deed requires that the average retail price at which Vodafone sells broadband to its customers must be at least 38% above the wholesale price:

6.21 Vodafone will not supply [retail broadband services] to Vodafone retail customers at a weighted average retail price, calculated over the average term of Vodafone’s retail customer lifetime, less than the aggregate of:

- (a) the wholesale price for the relevant [wholesale broadband service]; and
- (b) a retail margin adjustment mark up of 38% of the wholesale price of the relevant [wholesale broadband service] (“Retail Mark-Up”).

15. The Deed further provides that, when selling RBI retail broadband services to its end-users, Vodafone can offer discounts, rebates, or other subsidies in relation to the service, such as discounts on the cost of installation. However, Vodafone is required to ensure that any such discounts or similar offers will be recouped from the retail mark-up over the life of the service:

² See s156AB of the Act.

³ The Deed is required by subpart 4 of Part 4AA of the Act. A copy of the Deed is available on the following web page: <http://www.med.govt.nz/sectors-industries/technology-communication/communications/broadband-policy/ultra-fast-broadband-initiative/open-access-deeds>

- 6.29 Vodafone may enter into arrangements with third parties for the supply of goods or services related to the provision of Relevant Retail Services (for example installation services) and may supply those goods and services to end-users on any terms and conditions. *Should Vodafone choose to offer such goods and services to end-users at a discount, credit, rebate or subsidy then the quantum of the discount, credit, rebate or subsidy must be recovered within the Retail Mark-Up over the lifetime of the service.* (emphasis added)
16. The Retail Mark-Up is defined as “a retail margin adjustment mark up of 38% of the wholesale price”.⁴ The Deed sets a floor for the mark-up, not a ceiling – Vodafone can always charge at a retail price higher than that required by the mark-up. Clause 6.25 makes this clear for the avoidance of doubt:
- 6.25 To avoid doubt, Vodafone may set retail prices for [retail broadband services] at any level above the aggregate of:
- (a) the Retail Mark-Up; and
 - (b) the wholesale price of the [equivalent wholesale broadband service].
17. In other words, the difference between the price of Vodafone’s retail broadband services and its wholesale broadband services must be at least 38%.
18. This provision protects access seekers who purchase wholesale broadband services from Vodafone (to supply retail services to their own end-users) by ensuring that they can compete with Vodafone in the retail market. The 38% mark-up helps to ensure that Vodafone’s retail competitors are not faced with a price squeeze.

Vodafone’s requested clarification

19. Vodafone wrote to the Commission on 21 May 2012 requesting a clarification of how it may recover discounts within the retail mark-up specified in the Deed in accordance with the processes set out in s156AN of the Act. Section 156AN of the Act allows the Commission to make clarifications at the request of the LFC, provided the clarification is not material.
20. Specifically, Vodafone was concerned that clause 6.29 could be read two different ways. Under one reading, Vodafone would be entitled to recover any discounts within the actual retail mark-up offered for the service. If Vodafone raised the retail price of the service, it could in turn increase the size of the discount.
21. Under the other interpretation, Vodafone would be required to recover any discounts within the 38% minimum mark-up, regardless of whether Vodafone charged a higher retail price for the service. This would limit Vodafone’s ability to adjust the retail price to allow for larger up-front discounts or rebates.
22. Vodafone consequently requested a clarification so that it could introduce new discounts or rebate plans that allowed Vodafone to recover the costs with a higher retail mark-up.

⁴ Clause 6.21(b) of the Deed

23. Vodafone explained the reasons for the clarification in its letter:

Clause 6.29 was intended to protect RBI wholesalers from excessive discounting of upfront costs in Vodafone equivalent retail packages. However, the current drafting of clause 6.29 could be interpreted as limiting Vodafone's ability to discount upfront costs ... to the 38% Mark-Up defined in the Deed.

24. In Vodafone's view, this is contrary to their expectation (and 6.25 of the Deed) that the 38% mark-up in the Deed "is a price floor which Vodafone is prohibited from pricing its [retail broadband services] below."

Consultation

25. The Commission issued a consultation on the change on 8 June 2012.
26. Two submissions were received, one from Telecom Corporation of New Zealand Limited (**Telecom**), and one group response from Amuri.net on behalf of 5 wireless internet providers, including supplemental submissions from Rivernet Limited and Ultimate Mobile Limited.
27. Telecom supported the amendment.
28. Amuri.net and the other wireless internet providers, who purchase Vodafone's wholesale service in order to provide retail services, opposed the clarification.
29. Amuri.net and others noted that, if Vodafone raised its retail prices and offered a free installation, they might be required to make adjustments to their offers to compete with Vodafone.
30. Parties also considered that the current data caps, and the price of additional data above the cap, were prohibitive, and that this should be addressed or adjusted.

Discussion

Is the proposed amendment consistent with Vodafone's non-discrimination obligations?

31. The Commission considers that the clarification will promote the overall purposes of Part 4AA of the Act, and will not violate the non-discrimination obligations set out in the Deed.
32. As we explained in our draft decision:⁵
- The purpose of cl. 6.29 is to ensure that Vodafone does not price its retail broadband services in a way that undermines competition with access seekers purchasing Vodafone's wholesale broadband services, eg, a price squeeze.
33. The Deed clearly allows Vodafone to provide discounts if they can be recouped (along with any other costs incurred in providing the retail service) within the minimum average 38% discount. We consider that the Deed intended to allow Vodafone to offer larger discounts, provided these discounts were offset by a higher

⁵ Draft clarification of 8 June 2012, at para. 14.

retail price. This would allow Vodafone to create new, diverse offers in order to compete for retail customers. Other retail service providers also have the flexibility to take this approach.

34. We do not consider that this offer will constrain competition. Any discounts must be made within the overall retail mark-up for the service. Therefore, if Vodafone wants to give a discount on, for example, installation, then Vodafone may need to increase its margin (over and above the 38% minimum margin) by enough to recover the discount over the life of the service.

Guidance on the average lifetime of service

35. The Deed does not specify the timeframe in which any discount, credit, rebate, or other subsidy must be recovered. However, we consider some preliminary guidance will be helpful to Vodafone and other retail service providers.
36. In the interim deed signed by Vodafone on 20 April 2011, on which the final Deed of Undertaking was based, the average customer lifetime was “12 months (or such other time period as agreed with the Commission).”⁶
37. Under Vodafone’s current retail plans, customers who receive a discounted installation must sign up for a 24 month commitment,⁷ and therefore an effective minimum lifetime of 24 months after which they could change to another service provider – though in many cases this could be longer or shorter.
38. Looking more broadly at the telecommunications industry, contractual commitments, where used, tend to range from 12 to 36 months.
39. We consider that 24 months – Vodafone’s current contract term length – is a reasonable approximation of the expected lifetime of a typical customer relationship. Our view is therefore that Vodafone must recover any discounts or other subsidies within 24 months.

Is the proposed amendment material?

40. We do not consider that the proposed amendment changes the terms of the Deed, it only clarifies Vodafone’s obligation to meet any discounts or similar subsidies within its retail mark-up.
41. We therefore consider that the change is not material, and that it is appropriate to clarify the interrelationship of the retail mark-up and discounting provisions contained in the Deed.

Third party proposed amendments

42. Submissions recommended that the Commission re-assess the data caps and costs of Vodafone’s wholesale broadband service. These costs are unrelated to the

⁶ See clause 6.16 of the interim deed.

⁷ Customers may also enter into a 1 month contract, but must pay the full installation cost.

clarification proposed by Vodafone, and, consequently, cannot be considered under the clarification process set out in s156AN of the Act.

43. In addition, the proposed amendments would be material amendments, which can only be made by the Minister on recommendation of the Commission following a request from Vodafone. Therefore, we cannot consider the proposed amendments at this time.

Commission Decision

44. The Commission has agreed to amend the Deed by:

- 44.1 Deleting cl. 6.21(b) and replacing it with the following:

“(b) a minimum retail margin adjustment mark up of 38% of the wholesale price of the relevant Functionally Equivalent Broadband Service (“Minimum Retail Mark-Up”).”

- 44.2 Replacing the “Retail Mark-Up” in clauses 1 and 6.23(a)-(c) with “Minimum Retail Mark-Up”.

- 44.3 Replacing “Retail Mark-Up” in clause 6.29 with:

“actual retail-mark-up (being the difference between the wholesale price of the Relevant Functionally Equivalent Broadband Service and the actual retail price for the retail service for which the discount is being offered)”.

45. An updated copy of the Deed must be posted by Vodafone on a public website in accordance with s156AK of the Telecommunications Act 2001.



Dr. Stephen Gale, *Telecommunications Commissioner*

Dated at Wellington this 23rd day of July 2012.

COMMERCE COMMISSION