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IN THE COURT OF APPEAL OF NEW ZEALAND

CA700/2009
[2012] NZCA 278

BETWEEN	TELECOM CORPORATION OF NEW ZEALAND LIMITED First Appellant
AND	TELECOM NEW ZEALAND LIMITED Second Appellant
AND	COMMERCE COMMISSION Respondent

Hearing: 26, 27, 28, 29 September and 3 October 2011

Court: Glazebrook, Chambers and Ellen France JJ

Counsel: D Shavin QC, J E Hodder SC, P Jagose and T Smith for First and Second Appellants
J A Farmer QC, G M Coumbe and J S McHerron for Respondent

Judgment: 27 June 2012 at 11.00 am

JUDGMENT OF THE COURT

A The appeal is dismissed.

B The cross-appeal is allowed.

C The declaration made in the High Court is amended to read as follows:

> **The plaintiff is granted a declaration that Telecom used and/or took advantage of its dominant position/market power from 1 February 1999 until late 2004 (when Telecom introduced a UPC service) for the purposes of deterring potential or existing competitors in the wholesale market for backbone transmission**

services and the retail market for end-to-end high speed data transmission services.

D The appellants must pay the respondent costs for a complex appeal on a band B basis and usual disbursements. We certify for three counsel.

REASONS

Glazebrook and Ellen France JJ	[1]
Chambers J	[281]

GLAZEBROOK AND ELLEN FRANCE JJ

(Given by Glazebrook J)

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Introduction

[1] Telecom inherited its telecommunications network from the Post Office when the telecommunications industry was privatised in 1989. The telecommunications network is used to transmit information that has been converted into digital format. During the 1990s, rival telecommunications service providers (TSPs)[1] sought access to Telecom's network in order to provide their own data transmission services. This access was achieved by TSPs utilising data tails, which are the connection between an end customer's premises and the point where a rival TSP can take delivery of data signals from Telecom.[2] This appeal concerns Telecom's pricing of those data tails.

[2] In the High Court, the Commerce Commission alleged that, over the period from 1 December 1998 until late 2004,[3] the wholesale price charged by Telecom to other TSPs for access to data tails was so high relative to Telecom's retail price that it caused a price squeeze. A price squeeze occurs when a dominant vertically integrated supplier sets prices in the upstream wholesale market in a manner that prevents equally or more efficient competitors from profitably operating in the downstream retail market.

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1 As pointed out by the High Court, the telecommunications industry makes frequent use of acronyms. For the convenience of readers, we attach as an Appendix the glossary of acronyms and abbreviations prepared by the High Court.

2 This is discussed further at [33] below.

3 The Commission says Telecom's anti-competitive pricing policies for data tails did not come to an end until June 2004, when Telecom gave undertakings that it would introduce an Unbundled Partial Circuit (UPC) service to telecommunications service providers (TSPs) at cost-based pricing by 30 September 2004. This led soon afterwards to UPC pricing agreements with TelstraClear and others.

[3] In particular, it was alleged by the Commission that Telecom's pricing breached the Efficient Component Pricing Rule (ECPR) endorsed by the Privy Council in *Telecom v Clear*[4] as the appropriate pricing model where there is a dominant vertically integrated provider of network infrastructure and services. Under ECPR the price of an input equals its average-incremental cost as well as a sum sufficient to compensate the incumbent for its opportunity costs. "Opportunity cost" refers to all potential earnings that the supplying firm foregoes, either by providing inputs of its own rather than purchasing them, or by offering services to competitors that force it to relinquish business to those rivals and thus to forego the profits on that lost business.[5]

[4] In a judgment delivered on 9 October 2009 (we will refer to this as the Liability Judgment),[6] Rodney Hansen J and Professor Martin Richardson held that Telecom's pricing was above ECPR in virtually all cases where Telecom provided all the tails in a TSP's customer network, whether two or more, and the TSP did not self-provide any tails (the "two-tail" scenario). The Court did not consider that Telecom's pricing breached ECPR in cases where a TSP self-provided one or more tails and Telecom supplied the remainder (the "one-tail" scenario).

[5] On the basis of those findings, it was held that Telecom had used and/or taken advantage of its dominant position/market power from 18 March 2001 until late 2004 for the purpose of deterring potential or existing competitors in the wholesale market for backbone transmission services and the retail market for end-to-end high speed data transmission (HSDT) services.[7]

[6] Telecom had therefore breached s 36 of the Commerce Act 1986. The High Court concluded that the Commission was entitled to relief (both declaratory and pecuniary) in respect of Telecom's conduct in that period. The Court granted the

4 *Telecom Corporation of New Zealand Ltd v Clear Communication Ltd* [1995] 1 NZLR 385 (PC) [*Telecom v Clear* (PC)].

5 William J Baumol and J Gregory Sidak "The Pricing of Inputs Sold to Competitors" (1994) 11 Yale Journal on Regulation 171 at 178.

6 *Commerce Commission v Telecom Corporation of New Zealand Ltd* HC Auckland CIV-2004-404-1333, 9 October 2009 ["Liability Judgment"].

7 High speed data transmission (HSDT) services permit customers to transmit data from one site to another at speeds of above 64 kilobits per second (kbps). An HSDT service is a fixed connection between two sites only (unlike telephony services).

Commission declaratory relief with respect to Telecom's conduct between 18 March 2001 until late 2004, but not with respect to Telecom's conduct prior to 18 March 2001.

[7] Telecom appeals against the Liability Judgment. There is a cross-appeal by the Commission, asserting that declaratory relief should have been available for the period prior to 18 March 2001.[8] The Commission also seeks to challenge the Liability Judgment on the basis that the High Court should have found that Telecom's pricing in the one-tail scenario breached ECPR.[9]

[8] The issue of the quantum of the remedy by way of pecuniary penalty was dealt with in a separate judgment.[10] Telecom also appeals against that decision.[11] We will deal with that appeal in a separate judgment.

[9] Before we turn to the issues in the appeal against the Liability Judgment,[12] we set out the legislative background,[13] explain the technical background in more detail[14] and describe Telecom's pricing structure.[15] We then summarise the High Court decision[16] and, as it was pivotal to the reasoning of the High Court, summarise the course of the *Telecom v Clear* litigation.[17] We also set out a description of ECPR.[18]

The legislation

[10] As noted above, the High Court held that Telecom's conduct contravened s 36 of the Commerce Act. That section now provides that a person who has a substantial degree of power in a market must not take advantage of that power for a

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8 This issue is dealt with in Chambers J's judgment, starting at [281] below.
9 We deal with this issue at [226] below.
10 *Commerce Commission v Telecom Corporation of New Zealand Ltd* HC Auckland CIV-2004-404-1333, 19 April 2011 ["Penalty Judgment"]. In that judgment, Rodney Hansen J ordered that Telecom pay a pecuniary penalty of $12 million.
11 CA313/2011.
12 Set out at [74] below.
13 At [10] below.
14 At [13] below.
15 At [21] below.
16 At [39] below.
17 At [56] below.
18 At [64] below.

proscribed purpose. One of the proscribed purposes is preventing or deterring a person from engaging in competitive conduct in that or any other market. In relevant part that section provides:

> **36 Taking advantage of market power**
>
> …
>
> (2) A person that has a substantial degree of power in a market must not take advantage of that power for the purpose of—
>
> (a) restricting the entry of a person into that or any other market; or
>
> (b) preventing or deterring a person from engaging in competitive conduct in that or any other market; or
>
> (c) eliminating a person from that or any other market.
>
> …

[11] Before 26 May 2001, s 36 provided that a person who has a dominant position in a market must not use that position for a proscribed purpose:

> **36 Use of dominant position in a market**
>
> (1) No person who has a dominant position in a market shall use that position for the purpose of—
>
> (a) Restricting the entry of any person into that or any other market; or
>
> (b) Preventing or deterring any person from engaging in competitive conduct in that or any other market; or
>
> (c) Eliminating any person from that or any other market.

[12] The High Court for convenience used the term "dominance" to encompass a firm possessing a substantial degree of market power unless it was necessary to distinguish between the concepts by the replacement of "use" with "take advantage of". We shall do the same in this judgment.[19]

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[19] It was also accepted that no change to the meaning of s 36 resulted from the replacement of the word "use" with "take advantage of". References to "use" of dominance accordingly are to be read if necessary as including taking advantage of a substantial degree of market power.

Technical background

[13] The transmission of data between geographically remote locations has been achieved by modifications to Telecom's Public Switched Telephone Network (PSTN).[20] The PSTN has two main elements. The core or backbone of the system comprises the exchanges and the trunk lines that connect them. The connection of the core with customers' premises is the access component, known as the local access network or local loop. Historically the local network comprised pairs of copper wires. Fibre optic cable has now replaced copper in many of the local access lines. They are linked to an exchange where, for the purpose of voice calls, switches enable a call from one telephone number to be connected to another number for the duration of the call.

[14] The PSTN was used for the transmission of basic data services such as telex and fax, but the speedy and efficient transmission of high volumes of data by converting the data into digital format required additional technology. The basic components are:

(a) A network terminating unit (NTU) located at the customer's premises. The NTU converts and transfers data into digital format and receives and converts data transmitted in digital format.

(b) Multiplexers, which are sited at selected exchanges (or at a roadside cabinet). They aggregate individual data circuits. The aggregated stream is then transmitted to switches at telephone exchanges.

(c) Digital cross connect switches (DCS), which separate individual data streams from the aggregated flows coming in from a multiplexer and route them through the core or backbone part of the network to connect with another DCS near the destination for the data. The data

[20] The description of the technical background in this section and the description of Telecom's pricing structure and pricing of data tails in the following sections are largely taken from the Liability Judgment, above n 6. More detail is provided in that judgment at [13]–[32].

is then delivered through another multiplexer to its destination, the NTU at the customer's premises.

[15] The entire connection between the two premises of a customer is known as an end-to-end connection. In the first platform or system used by Telecom to transmit data in digital format, the Digital Services Transport Network (DSTN), each end-to-end connection was a dedicated circuit. It was a permanent connection between the two points with a fixed transmission capacity and was never shared with any other user. Such circuits are said to provide a constant bit rate (CBR) service. The bit rate is the speed at which data is transmitted. Industry usage refers to speeds between 64 kilobits per second (kbps) and two megabits per second (Mbps) as high speed, speeds lower than that as low speed and speeds higher as very high speed.[21] A CBR service ensures that the speed and quality of transmission is constant and assured. There are, however, associated inefficiencies. When a user is not using its full allocated capacity, additional capacity in the circuits cannot be used to meet the needs of other users.

[16] A CBR service is to be distinguished from a variable bit rate (VBR) service, which is provided when circuits are shared by a number of users. The speed of transmission then will depend on the volume of traffic; at peak times service will be slower. A VBR service offers a Committed Information Rate (CIR) and a Peak Information Rate (PIR). A TSP guarantees the minimum speed of the CIR while offering the potential for the higher PIR at off-peak times.

[17] A VBR service was introduced by Telecom with its Frame Relay (FR) network installed in 1994. It enabled data to be transmitted at higher speeds and a circuit to be connected to any customer on a switch: any-to-any rather than point-to-point transmission. This was achieved by the transmission of data in packets, known as frames.

[18] From 1997 Telecom progressively rolled out a new network, the Asynchronous Transfer Mode (ATM), which enabled packets (now called cells) to be

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[21] The typical Digital Services Transport Network (DSTN) connection was low speed (64 kbps) and, in fact, there was evidence that a DSTN network terminating unit (NTU) could not operate over copper at more than 128 kbps.

tagged with different service qualities and carried with different service guarantees. This permitted the ATM network to carry different types of traffic according to the service quality required. FR services were progressively migrated onto the ATM network, which was then able to provide VBR FR services and CBR services such as Digital Data Service (DDS).[22]

[19] In the mid-1990s Telecom began introducing a connectionless technology known as the Internet Protocol (IP) technology. Since 2000 it has supported an increasing range of data communication services.

[20] During the 1990s other TSPs rolled out limited networks and network components. Both Clear Communications Ltd (Clear) and Telstra Saturn Ltd (Telstra)[23] installed a fibre backbone network connecting some of the main centres. Both companies, and a number of other TSPs, constructed fibre networks in the CBDs of major cities. However, in non-major CBD areas Telecom had the only local access network or the only access network capable of transmitting business data. TSPs who wished to compete in the retail market for end-to-end HSDT services were dependent on access to Telecom's access network in non-major CBD areas.

Telecom's pricing structure

Retail pricing

[21] Before 1999, Telecom's retail prices for end-to-end data services were contained in Telecom's List of Charges (TLoC). In addition to a one-off installation charge, there was a monthly charge that normally included:

(a) A charge for access to the customer's premises at each end of the service.

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22 These changes were gradual with different network elements being rolled out in different geographic areas at different times. The same applied to the application of the technology to different customers.

23 Clear and Telstra later merged and became TelstraClear.

(b) A charge for transmission between the two data exchanges to which the premises were connected. The charge varied according to the distance the data was carried.

(c) Incidental charges for service delivery and the like.

[22] Access and transmission charges varied according to the speed of the circuit: the higher the speed the higher the charge.

[23] It was common ground between the commercial witnesses at trial that, by late 1999, Telecom's charges under TLoC had become uncompetitive, and, particularly in relation to the relativity of CBR and VBR HSDT services (the less valuable VBR services were more expensive than CBR services with the same PIR), irrational.

[24] We note at this point that Telecom's retail pricing prior to the introduction of Streamline pricing (described below), and in particular the irrational price relativity of CBR and VBR products, created an arbitrage opportunity for competing TSPs in respect of data tails. TSPs could purchase CBR circuits cheaply from Telecom, overlay their own FR switches and other core network equipment, and sell VBR services in competition with Telecom's expensive VBR services.

[25] In 1998 Telecom commenced an initiative to address the issues with TLoC pricing of HSDT services. The initiative was progressed by a project team under the name "Project Nike". The pricing proposed by Project Nike was later rebranded, for introduction as "Streamline" pricing, which was signed off by the Chief Executive Officer of Telecom, Dr Roderick Deane, on 24 December 1998.

[26] Streamline pricing involved major price reductions from TLoC and a rebalancing of VBR and CBR prices, so that the less valuable VBR services were less expensive than CBR services with the same PIR. The number of transmission steps was also reduced to two: local and national. The choice of access speed was also reduced to a choice of 128 kbps or more.

[27] Streamline pricing was rolled out progressively to Telecom's top 100 corporate customers from around February 1999. Subsequently, the business rules were changed to permit other customers to be offered Streamline pricing.

[28] Streamline became and, remained, Telecom's price book for data services. It is accepted by the Commission that Telecom was entitled to correct the anomalies in its retail pricing structure. The issue in the High Court was Telecom's alleged failure to adjust its wholesale prices accordingly.

Wholesale pricing

[29] Between 1996 and 1997, under the 1996 Interconnection Agreement,[24] TSPs could purchase data connections at TLoC prices less six per cent pursuant to the terms of their interconnection agreements with Telecom. Under pressure from TSPs, a wholesale pricing regime was introduced known as Wholesale Integrated Network (WIN) pricing. Telecom offered TSPs discounts of between 15 and 30 per cent off TLoC prices. Discounts were higher in major CBD areas.

[30] Following the introduction of Streamline retail prices, new wholesale prices were not offered to TSPs immediately. TSPs continued purchasing data tails at TLoC less 15–30 per cent under WIN pricing. The Commission alleges that this was the beginning of the price squeeze. It was only after some months that Telecom introduced new wholesale prices. The new offer became known as Carrier Data Pricing (CDP). Typically it provided TSPs with a discount of between six and 15 per cent off Streamline pricing.

[31] The Commission's case was that under CDP, wholesale prices did not fall commensurately with the large reductions brought about by the introduction of Streamline retail prices. It asserted that the prices of two data tails in most instances were above the retail end-to-end price charged by Telecom to its customers. As

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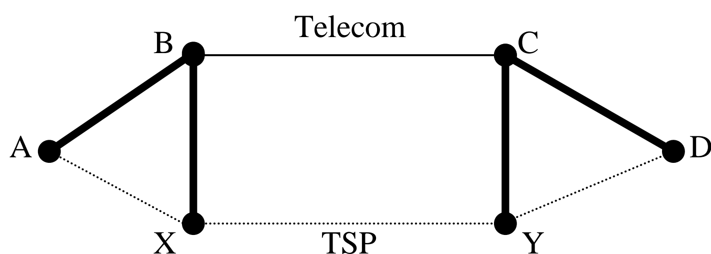
[24] After substantial difficulties in negotiations between Telecom and Clear regarding the terms on which Clear might have access to Telecom's network, which resulted in the Privy Council's decision in *Telecom v Clear*, above n 4, the parties eventually signed an interconnection agreement in 1996.

noted above,[25] the Commission said that Telecom's anti-competitive pricing of data tails did not come to an end until June 2004, when Telecom introduced an Unbundled Partial Circuit (UPC) service to TSPs at cost-based pricing, which was developed into an agreement with TelstraClear and others.

[32] We note at this point that, in 2003, pursuant to an application by TelstraClear for wholesale determinations under the Telecommunications Act 2001, the Commission made a determination (Decision 497)[26] that required Telecom to supply wholesale end-to-end HSDT services in non-metropolitan areas at specified prices. The effect of Decision 497 is discussed in Chambers J's judgment at [330]–[336] below.

Pricing of data tails

[33] As noted above, a data tail is the connection between an end customer's premises and the point where a TSP can take delivery of data signals from Telecom. The High Court used the following diagram to illustrate the concept:



[34] In this diagram, an end-to-end circuit connects a customer's premises at point A to another of their premises at point D. The links AB and CD represent connections from the physical premises to an exchange building and the links BX and CY represent connections from an exchange to a point at which a rival TSP can pick up the transmission. This is known as a point of presence (POP).[27] The links

[25] At fn 3 above.
[26] *Re TelstraClear Ltd and Clear Communications Ltd* CC Decision No 497, 12 May 2003.
[27] The point of presence (POP) is the building where a TSP has installed its network equipment. The POP may also be the physical point where two network operators arrange to interconnect their respective networks (known as a point of interconnection (POI)).

BC and XY represent the core or backbone network transmissions of Telecom and the rival TSP respectively. The heavy lines ABX and YCD are data tails: the links from the customer's location to the point at which the TSP can take up the signal.

[35] If the customer were served by Telecom, the circuit would be represented by ABCD. If the customer were served by a TSP and both data tails were provided by Telecom the circuit would be ABXYCD. If the TSP provided one tail itself (because it had its own access network at one end of the circuit or obtained it from a provider other than Telecom) the circuit would be AXYCD or ABXYD, depending on which tail was leased. It was also open to a TSP simply to lease the entire circuit ABCD from Telecom and resell it to the customer.

[36] The Commission asserted that Telecom wrongly treated data tails as just another end-to-end data transmission service for resale, and TSPs as just another corporate customer. This meant that it priced each data tail in the same manner as its resale end-to-end circuits (ABCD) rather than as an essential wholesale input. The Commission's position is that, while in a technical sense data tails resembled end-to-end circuits,[28] their function and purpose was that of an input. We accept that this is the case.[29]

[37] If a TSP leased the entire retail circuit ABCD from Telecom to resell it to the customer, Telecom would charge two access charges and one transport charge. As a result of Telecom's treatment of data tails as an end-to-end circuit, in relation to each data tail (ABX or YCD) there were two access charges and one transport charge. This meant that when a TSP purchased two Telecom tails to provide its own retail service ABXYCD, it had to pay to Telecom a total of four access charges and two transport charges. On top of that the TSP still had its own backbone transmission (XY) costs and its retail costs.

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[28] Telecom provisioned the data tails technically in the same manner as an end-to-end circuit, with an NTU at each end, instead of providing the interconnect model that was technically feasible and which both parties' technical experts agreed would be more efficient.

[29] We discuss this further at [141]–[143] below.

[38] The Commission's case was that, in continuing to price data tails in exactly the same way as an end-to-end service, Telecom was furthering a deliberate pricing policy driven by two main goals:

(a) to turn rivals into mere resellers of Telecom's product and, by that means, to grow the market; and

(b) to encourage competitors to view Telecom as the network of choice. That would not only keep them as resellers but discourage them from developing their own networks.

The High Court judgment

Market definition

[39] The Commission alleged that the relevant markets were:

(a) The national retail market for end-to-end HSDT services.

(b) The wholesale market outside major CBD areas for data tails where major CBD areas are defined as those:

(i) served by multiple telecommunications networks (owned by both Telecom and other network operators) capable of being used to provide retail HSDT services; and

(ii) with relatively low barriers of entry by reason of sufficient aggregation of demand relative to minimum viable scale.

(c) The national wholesale market for backbone services.

[40] Telecom admitted there was a national retail market for end-to-end HSDT services. Although the wholesale market definitions were not admitted by Telecom in its pleadings, they were not challenged in argument in the High Court. However,

Telecom did submit that the definition relied on by the Commission meant that it was not possible to say with respect to any tail, whether it was within a CBD area or not. The High Court acknowledged that the precise geographical locations of the market boundaries were unclear, but considered the definition adequate to permit a determination of the appropriate market for the vast majority of data tails in issue.

Dominance/market power

[41] It was accepted in the High Court that Telecom had both dominance and a substantial degree of market power in the wholesale market outside major CBD areas for data tails as well as the national wholesale market for backbone services.[30] It was thus not necessary for the High Court to consider whether there was any difference between the two concepts.

Use of dominant position

[42] The High Court noted that, in order to show "use" of a dominant position, a causal relationship is required between an incumbent's alleged conduct and its dominance or market power.[31] The causal link is shown by the application of a counterfactual test: Telecom's actions are compared to the way in which a hypothetical firm, not in a dominant position, but otherwise similarly placed, would have acted. If Telecom acted in a way in which it would not have acted if it had not been dominant, it will have used its dominant position.[32]

[43] It was agreed that the characteristics of the counterfactual scenario in this case were:

(a) two vertically integrated firms (T1 and T2), each with a "ubiquitous" access network (that is, a network with the capacity to provide

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30 Liability Judgment, above n 6, at [9] and [41]–[42]. This had been challenged in Telecom's statement of claim but not in evidence before the High Court.

31 Liability Judgment at [11], citing *Carter Holt Harvey Building Products Group Ltd v Commerce Commission* [2004] UKPC 37, [2006] 1 NZLR 145 at [51].

32 Liability Judgment at [11], citing *Telecom v Clear* (PC), above n 4, at 403 and *Carter Holt* at [29] and [52].

connectivity to all areas and customers) and a 50 per cent share of the retail HSDT market; and

(b) an entrant or access seeker (T3) who has a core network but no ubiquitous access network and no ability to construct access on economic terms, and who therefore needs to lease data tails.

[44] The High Court went on to say that in cases where the conduct in issue concerns the pricing of a dominant vertically integrated provider of network infrastructure and services, the ECPR economic model is employed.[33] There are two methods by which ECPR can be applied but both have the same end effect. In this case the "Kahn-Taylor" approach was used.[34]

[45] The Court considered the evidence presented as to the calculation of ECPR prices.[35] It noted that the parties were at odds on two pivotal issues: the implications of a TSP self-provisioning tails in a circuit and the correct approach when data transmission is part of a bundle of services.

[46] In terms of self-provisioning, Telecom argued that it was entitled to recover the profit foregone on the entire network (that is, the profit foregone on the self-provided tails as well as the Telecom-provided tails). Professor Gabel, an expert economist who gave evidence for the Commission, was of the view that Telecom should only be able to recover for each tail it leases the proportion of profit share that the leased tail bears to the total number of tails in the network. This would mean that, if Telecom provided one of five tails, it should be able to apportion 20 per cent of the profit foregone on the entire network to that tail. The Commission argued that the position contended for by Telecom ignored the effect of the sunk or fixed costs[36] in self-provisioning a tail and effectively required a TSP to pay twice for the tails.

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33 ECPR is discussed in further detail at [64] below.

34 Liability Judgment at [48] and [51], referring to the method set out by Professor Alfred E Kahn and Dr William E Taylor in "The Pricing of Inputs Sold to Competitors: A Comment" (1994) 11 Yale Journal on Regulation 225.

35 The Court made a number of findings regarding the proper calculation of ECPR prices, which are summarised in the Liability Judgment at [123].

36 These are the initial startup costs that are independent of the volume of output. They are in two categories: fixed costs which can be recouped if the firm subsequently exits the industry, and sunk costs which cannot be recouped.

[47] Regarding partial self-provisioning, the High Court concluded that the correct application of ECPR was largely as contended by Telecom.[37] It held that, in the one-tail scenario where a TSP self-provisions a tail or tails in a circuit and Telecom provisions the remainder, under ECPR pricing, Telecom is entitled to recover the profit foregone on the entire network. It considered that the pricing of data tails on this basis would not preclude entry by a more efficient rival.[38] The Court said that ECPR pricing does not prevent a more efficient entrant from building its own access network, as the incentive to do so is driven by any efficiency advantages an entrant may have.[39]

[48] The High Court sought to demonstrate that pricing of data tails on this basis would not preclude entry by a more efficient rival by the use of examples that assumed a five-tail customer network (of which two tails were in the CBD and three were in a rural area).[40] The High Court's examples assumed a retail price of the network of $14, with a direct incremental network cost to Telecom of each tail of $1, a direct incremental network backbone cost of $2 and a direct incremental retail cost of serving the customer of $3. This would lead to a $4 profit for Telecom for the customer's business. As one of its examples, the High Court noted that, if a TSP wished to self-provision one tail and lease four from Telecom, Telecom could, under ECPR, charge the TSP $8: that is, $2 per tail (being the cost of $1 per tail and the $4 opportunity cost spread over four tails). Assuming the same $14 retail cost and $5 for the TSP's backbone and retail costs, this would leave a surplus of $1. The High Court said that it would be profitable for a TSP to self-provision only if it could provide the tail more cheaply than Telecom could (that is, for less than $1).[41]

[49] The High Court did not accept that new entrants' incentive to build access would be removed if, in addition to compensating the incumbent for profits foregone on the entire network, an entrant also incurred sunk or fixed costs in self-provisioning a tail. It accepted that the task of efficient competition is to ensure that

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37 We note that, in evidence for Telecom, Professor Hausman had also argued that ECPR pricing should include an option fee, which compensates Telecom for the opportunity it confers on an entrant to defer a decision to build out its own access network, but this argument was not accepted by the High Court: at [74]–[75].

38 At [60].

39 At [59].

40 At [55]–[59].

41 At [57]. Other examples were provided at [56] and [58] of the Liability Judgment.

the aspiring competitor prevails only to the extent that the total incremental costs (including fixed and sunk costs) to society involved in its supplying the service are equal to or lower than those of the incumbent. It did not consider that this outcome would be "irremediably inconsistent" with *Telecom v Clear*.[42] This meant that the High Court found no breach of ECPR in the one-tail scenario. It held that there was, however, breach in the two-tail scenario.

[50] Regarding bundled services, Telecom argued that when data services are supplied to a customer as part of a "bundle" (including voice and/or internet services) the profits lost on all services, not just the data service component, should be taken into account in calculating the ECPR price. The Court said that the Commission was not given proper notice that this issue would be raised and so the issue could be disregarded for the purpose of calculating the ECPR price. The Court also said that, in any event, if the incumbent is to be compensated in an ECPR price for losing a data service customer, it is only to the extent of the additional profit derived from supplying the services as a bundle.[43] It concluded that there was no risk that ECPR prices calculated by the Commission were materially understated on this account.[44]

[51] Having accepted evidence that Telecom had offered data tails to rivals at above ECPR prices when Telecom supplied both tails in a two-tail circuit,[45] the High Court said that it was satisfied that, in the agreed counterfactual comprising two vertically integrated firms, each with a 50 per cent share of the HSDT market, a non-dominant Telecom would not set prices for data tails at above ECPR. This was for the simple reason that, if it did so, the backbone provider would purchase input from another company and Telecom would lose the sale entirely.[46]

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42 At [61]–[63].

43 The Court said that this was because what is foregone by the incumbent when it loses a data service customer is the ability to offer a bundle of services, not the ability to offer other components of the service such as voice or internet: at [71].

44 At [72].

45 The expert for the Commission, Professor Gabel, had concluded that, except in one scenario, there were ECPR violations throughout the period when Telecom supplied both tails in a two-tail circuit. This conclusion was largely accepted by the expert for Telecom. See the Liability Judgment at [124].

46 At [129].

[52] The High Court rejected a submission made by counsel for Telecom that the absence of information about the magnitude and distribution of ECPR violations was fatal to the Commission's case.[47] The Court accepted that, as long as non-compliance was more than *de minimis*, it may found a breach of s 36.[48]

Use of dominance for proscribed purpose

[53] In relation to whether Telecom had used its dominance for a proscribed purpose, the Court said that this may be inferred from evidence that the conduct had an anti-competitive effect[49] or may be shown by direct evidence of what the conduct was intended to achieve.[50] The Court concluded that an anti-competitive purpose was established by both means.

[54] The Court concluded that the readily foreseeable effects of pricing two-tail circuits to TSPs above ECPR and, in many cases, above retail prices, was sufficient to support an inference that Telecom used its dominance for the pleaded purposes.[51]

[55] In regard to the direct evidence of what Telecom's conduct was intended to achieve, the Court concluded that two factors demonstrated a strategy on the part of Telecom to deny rival TSPs access to data tails at prices that would permit them to utilise and develop their own networks for the purpose of data transmission.[52] The first was the way in which Streamline and CDP were introduced (that is, by rolling out Streamline retail pricing quickly and "covertly"[53] on 1 February 1999 but not completing the revision of wholesale prices under CDP until August 1999). The second was the statements of those responsible for their introduction (that is, acknowledgements by Telecom that its philosophy was that there should be no price competition between Telecom and rival TSPs).[54]

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47 At [130]–[131].
48 At [131]. The Court said that the number and extent of breaches goes to the gravity of the breach, not to its existence.
49 At [137], citing *Telecom v Clear* (PC), above n 4, at 402.
50 At [138]. This includes evidence that an anti-competitive outcome was a substantial purpose of Telecom's conduct: s 2(5)(b) of the Commerce Act 1986.
51 At [151].
52 Ibid.
53 At [140].
54 At [145]–[146].

Telecom v Clear litigation

[56] At issue in the *Telecom v Clear* proceedings was the appropriate charge that Telecom could make to Clear, a new entrant in the market for the provision of local telecommunications services in New Zealand, for connection to the PSTN. Clear required access to the PSTN, owned by Telecom, because the size and nature of this infrastructure made replication uneconomic for competitors. Telecom admitted that it was dominant over the PSTN and had a duty to provide interconnection to a new entrant.

[57] Telecom relied on ECPR (or the "Baumol-Willig rule", as it was referred to in those proceedings) to assert that the appropriate price of interconnection included both the direct incremental costs of providing the interconnection and Telecom's opportunity cost foregone due to Clear's use of the facility. Clear alleged that the price offered by Telecom was so high as to amount to a use of its dominant position, in contravention of s 36 of the Commerce Act.

[58] Under ECPR, a firm seeking access must pay the incumbent a sum sufficient to compensate the incumbent for the opportunity cost of customers lost by the incumbent to the entrant, including the incumbent's foregone profits, if any. Hence, the ECPR access price may include the monopoly profits (that is, profits received from setting prices above the level that would be charged in a competitive market)[55] that the incumbent loses by selling access. This implication of the rule was the central issue before the Privy Council.

[59] In the High Court,[56] it was determined that Telecom was entitled to make a charge to Clear for interconnection, equal to its opportunity cost. The Court also held that the existence of monopoly rents had not been proved.[57] The Court considered whether the risk of monopoly rents at a level sufficient to exclude Clear

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55 Monopoly profits are a kind of "monopoly rent". The other type of monopoly rent is inefficiency in a monopolist firm's provision of a service, giving rise to higher costs.

56 *Clear Communications Ltd v Telecom Corporation of New Zealand Ltd* (1992) 5 TCLR 166 (HC) [*Telecom v Clear* (HC)].

57 At 217.

should lead it to reject ECPR as a model, but concluded that this risk was outweighed by the fact that failure to use a pricing rule that charges for access to Telecom's network (to cover the incremental cost imposed on Telecom) would foster the development of uneconomic bypass and the proliferation of uneconomic operators.[58]

[60] This Court overturned the High Court's decision on the ground that it allowed Telecom to charge a monopoly price.[59] Gault J[60] considered that, in a perfectly contestable market, monopoly profits would not be obtainable, and that this cast doubt on the validity of ECPR as an appropriate pricing rule.[61] He said that the inclusion of monopoly profits in the access price must affect the price at which Clear can enter the market and so affect the vigour of its competitive conduct.[62]

[61] In Gault J's view, an appropriate access price would allow Telecom to recover a contribution for its "true costs": that is, the incremental cost of providing interconnection plus a reasonable return on capital employed.[63] Such an approach would eliminate any element of monopoly profits, as it would only allow Telecom to recover the level of charge that could be recovered in a competitive market.[64]

[62] The Privy Council overturned this Court's decision. The Privy Council held that Telecom's reliance on ECPR to set its access price did not breach s 36 since it did not involve the use by Telecom of its dominant position.[65] Their Lordships said that Telecom would be acting uncompetitively if it refused to permit Clear to interconnect with Telecom's network. But it was not acting uncompetitively in charging its opportunity cost since that is what it would have charged in a fully competitive market.[66]

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58 Ibid.

59 *Clear Communications Ltd v Telecom Corporation of New Zealand Ltd* (1993) 5 TCLR 413 (CA) [*Telecom v Clear* (CA)].

60 With whom Cooke P and Richardson J agreed.

61 At 433.

62 At 434.

63 At 442.

64 Ibid.

65 *Telecom v Clear* (PC), above n 4, at 408.

66 At 406.

[63] The Privy Council was not concerned by the fact that Telecom's opportunity cost could include monopoly profits. Their Lordships said that monopoly rents would initially be preserved but that these would eventually be competed out by Clear's competition in the contested area.[67] Further, Clear had not produced any figures to establish that Telecom's charges would be so high that Clear would be unable to enter the CBD market at all and thus it followed that the risk of monopoly rents had no bearing upon the question whether the application of ECPR prevented competition in the contested area.[68] Their Lordships also said that monopoly profits could be removed by regulatory action and said that s 36 did not have any wider purpose, beyond producing fair competition, of eliminating monopoly profits currently obtained by the person in the dominant market position.[69]

Explanation of ECPR

[64] ECPR was devised as a regulatory tool to be used in addressing the problem of how to price network access in markets dominated by a single vertically integrated provider of network infrastructure and services.[70] In the telecommunications sector, the application of ECPR was intended to ensure that the wholesale pricing of network access to competitors did not restrict or distort competition in the relevant downstream markets for telecommunications services. More succinctly, the proper application of ECPR was seen as the means by which regulatory agencies could establish an appropriate relationship between the profits an owner of a bottleneck facility (such as Telecom) earns from providing access to itself, and those profits it earns from selling access to its competitors in the wholesale market.[71]

[65] As argued by Professors Baumol and Sidak, the price of access must be selected in a manner that provides compensation to the incumbent for all of its properly incurred costs, including its foregone profits, while at the same time the price of access must be sufficiently low that it does not act as a barrier to entry:[72]

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67 At 407.
68 Ibid.
69 Ibid.
70 The seminal article on ECPR is by Professors Baumol and Sidak, above n 5.
71 Ibid, at 173.
72 Ibid.

> If X charges its rival more for the input than it implicitly charges itself, it will have handicapped that rival's ability to compete with X, perhaps seriously. The reverse will be true if regulation forces X to charge the rival less for the input than X charges itself …

[66] The rationale for allowing an incumbent to recover its opportunity costs in cases of natural monopoly is that there is a typical pattern of high fixed costs and economies of scale. Pricing at incremental costs would result in revenues failing to recoup capital costs. This would be inimical to dynamic efficiency, as there would be little incentive to maintain existing or create new facilities.[73]

[67] As mentioned above, there are two methods by which ECPR can be applied but both arrive at the same results. The first methodology[74] was illustrated in the following manner by Professor Gabel.

[68] Assume that the prevailing retail price for data circuit AD is $11, the direct incremental network cost of using data tails ABX and YCD is $2, the direct incremental network cost of using backbone BC is $2, and finally, that the direct incremental retail cost of serving the customer is $3. Given this set of assumptions, when providing data circuit AD as a retail service the integrated firm will earn a profit of $4 ($11 – $2 tail cost – $2 backbone cost – $3 incremental retail cost = $4).

[69] ECPR states that the wholesale price for using data tails ABX and YCD is equal to the direct incremental cost of the tails ($2) plus the foregone profit ($4), so the ECPR price for the data tails is $6 ($2 + $4 = $6).

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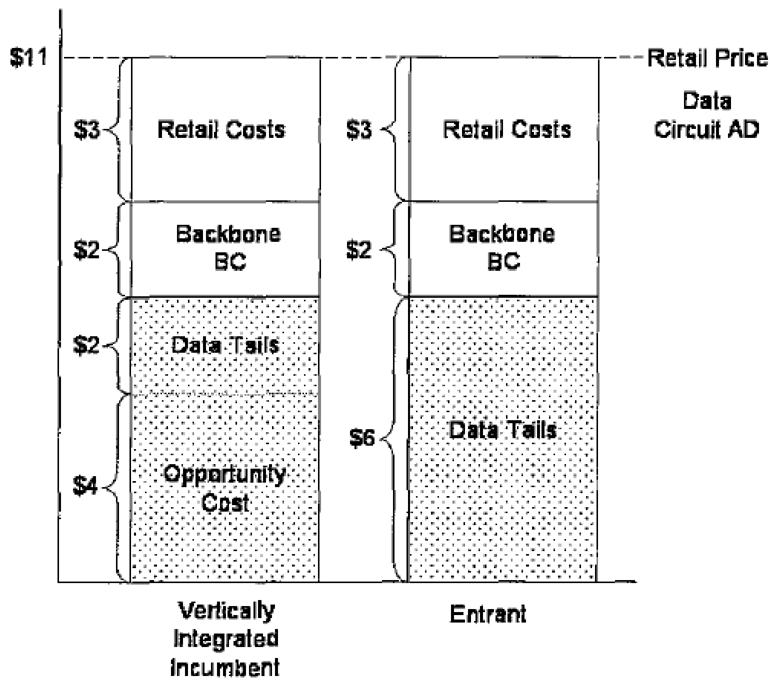
73 Brenda Marshall "Pricing Third Party Access to Essential Infrastructure: Principles and Practice" (2005) 24 ARELJ 172 at 177 and fns 54 and 55 (and the references cited therein).

74 The approach put forward by Professors Baumol and Sidak, above n 5.



[70] In this diagram, the shaded grey areas represent the costs (including opportunity costs, being profit) of those parts of the retail service in which the incumbent firm is dominant – that is, the service that the entrant is required to purchase from the incumbent. The white areas represent the costs of those parts of the retail service where the firms are in competition with each other. It can be seen from the diagram that:

(a) $6 is the proper ECPR price for the data tails in this example because the profit earned by the integrated firm as a wholesale supplier to the entrant ($4) is equal to the profit it would have earned providing circuit AD as a retail service;

(b) if the entrant is more efficient in the area of competition – that is, in the provision of backbone and retail support – than the incumbent, it will be able to compete effectively in the retail market by lowering its retail price; and

(c) if the incumbent was to charge more than $6 then the entrant would not be able to compete by lowering its retail price (either at all or to the same extent) even if it was more efficient in the area of

competition, so that competition will have been impeded or restricted in the retail market.

[71] An alternative approach was put forward by Professor Kahn and Dr Taylor.[75] This approach can be demonstrated by using the same assumptions as in the example above.

[72] The Kahn-Taylor price for data tails is the retail price, less the costs avoided by the vertically integrated firm because another TSP is providing the retail service and backbone facilities. Those costs are $2 for the backbone and $3 for retail costs which, when deducted from the retail price ($11), produce $6, as in the earlier example.

[73] The Kahn-Taylor approach was used in this case, as it requires an analyst to identify only three items as against the four items required under the traditional ECPR formula.

Issues on appeal

[74] On appeal, Telecom mounts a full-scale attack on the Liability Judgment. It first argues that the High Court erred in its assumption that any pricing above ECPR entailed use of a dominant position. In its submission, the Privy Council in *Telecom v Clear* merely held that ECPR provides a safe harbour (or a floor) where a dominant firm can be assured of not falling foul of s 36.

[75] Telecom argues in addition that, as it was impossible for Telecom to calculate, in advance, ECPR prices as a matter of practical reality, this breaches the requirement for commercial certainty and is contrary to the rule of law. Telecom also argues that the High Court should have followed the United States approach to price squeeze claims and concluded that such claims do not fall within the scope of s 36.

[76] The more particular issues for determination identified by the parties were:

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[75] Kahn and Taylor, above n 34.

(a) Did the High Court err in concluding that Telecom had used and/or taken advantage of its dominant position/market power? Specifically:

(i) in concluding that Telecom had an obligation to supply data tails to competitors?

(ii) in concluding that a non-dominant Telecom would not have supplied data tails to competitors at a price that exceeded ECPR?

(iii) alternatively, in concluding that the Commission had proved that the Telecom pricing in the two-tail scenario in fact relevantly breached ECPR?

(iv) in addition, or alternatively, in concluding that the Commission had not proved that the Telecom pricing in the one-tail scenario breached ECPR?

(b) Did the High Court err in finding that the Commission had proved that the Telecom pricing involved a purpose proscribed by s 36 of the Commerce Act?

[77] In addition, the implications of a settlement reached in 2000 between Telecom and Clear will be dealt with in this judgment.[76] We will also deal with a submission made by the Commission regarding the appropriate measure of Telecom's avoided marketing costs.[77]

[78] There are also issues as to whether the High Court erred in holding that there was no jurisdiction to grant a declaration in relation to Telecom's conduct prior to 18 March 2001 and whether the High Court erred in concluding that the commencement of the Telecommunications Act 2001 and the Commission's Decision 497 did not reduce or pre-empt the application of s 36 of the Commerce

76 At [218] below.
77 At [222] below.

Act to the Telecom pricing in issue. Those issues are dealt with in Chambers J's judgment.[78] We agree with his judgment on those issues.

Is ECPR merely a safe harbour rather than a price ceiling?

Telecom's argument

[79] Telecom argues that the Privy Council in *Telecom v Clear* did not hold that charging prices above ECPR constitutes a use of a dominant position. It merely held that, if ECPR prices are charged, then this provides a safe harbour whereby a dominant incumbent player can be assured of not breaching the Commerce Act. The ECPR price is therefore submitted to be a floor rather than a ceiling. This argument is partly predicated on the assumption that ECPR provides an efficient price (and thus any lower price is inefficient).

Our assessment

[80] We do not accept this submission.

(a) ECPR is not, by itself, sufficient to ensure efficiency

[81] To the extent that Telecom's argument relies on ECPR producing efficiency, ECPR is not, by itself, sufficient to ensure efficiency. If a firm obtains monopoly profits, its opportunity cost will include monopoly profits. Similarly, monopoly rents in the form of inefficiencies in a monopolist firm's provision of a service, giving rise to higher costs, will be preserved. ECPR can therefore preserve the allocative or consumption inefficiency that results from the monopolist's excessively high final product prices.[79]

[82] The proponents of the model have stressed that ECPR plays its full beneficial role only when a number of underlying assumptions are valid.[80] An important

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78 From [281] below.

79 Nicholas Economides and Lawrence White "Access and interconnection pricing: how efficient is the 'efficient component pricing rule'?" (1995) 40(3) Antitrust Bulletin 557 at 564.

80 Baumol and Sidak, above n 5, at 195–196.

underlying assumption, which Professors Baumol and Sidak have described as a "second economic efficiency requirement", is that, in addition to ECPR, final product prices must be constrained by market forces or regulation so as to preclude monopoly profits.[81]

[83] ECPR has sometimes been described as setting both a floor and a ceiling:[82]

(a) ECPR sets a floor because a rival seeking access should never be charged less than the average incremental cost of its usage of the incumbent's facility (this is to avoid cross-subsidy). Thus ECPR precludes inefficient entry by ensuring that a rival enters and produces in the market only if its costs are no greater than those of the incumbent.[83]

(b) ECPR sets a ceiling because the rival should never be charged in excess of the "stand-alone cost" of producing the final product (that is, the price that would rule in a competitive market, which would not include monopoly profits). ECPR then encourages efficient entry.

[84] In principle, therefore, ECPR does arrive at a price floor, but the full validity of the ECPR model is conditional upon downstream pricing being constrained by regulation or market forces so that no supernormal returns accrue to the incumbent. In the present case, the High Court said that:[84]

> [T]he objective of ECPR [is] to price access in a manner that compensates the incumbent for properly incurred costs, including profits foregone, *while at the same time ensuring that the price of access is sufficiently low so as not*

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81 William J Baumol and J Gregory Sidak "The Pricing of Inputs Sold to Competitors: Rejoinder and Epilogue" (1995) 12 Yale Journal on Regulation 177 at 178. See also J Vickers "Regulation, competition, and the structure of prices" (1997) 13 Oxford Review of Economic Policy 15.

82 For example, in *Telecommunications Pricing: Theory and Practice* (Cambridge University Press, Cambridge, 1991) at 146, Bridger Mitchell and Ingo Vogelsang describe ECPR as allowing a firm "freedom to set its price structure within the range provided by incremental cost of a service as a lower bound and stand-alone cost (SAC) of a service as an upper bound … SAC is characteri[s]ed by Willig… as the price that would rule for the service if the market were contestable, and by Baumol … as the price that would induce entry by an efficient entrant in the absence of entry barriers." See also Vickers, ibid, and William J Baumol and Robert D Willig "Competitive Rail Regulation Rules: Should Price Ceilings Constrain Final Products or Inputs?" (1999) 33 Journal of Transport Economics and Policy 43 at 43–44.

83 See the explanation given by Economides and White, above n 79, at 563.

84 Liability Judgment, above n 6, at [45] (emphasis added).

> *to deter entry*. A price set in accordance with ECPR will permit efficient entry by ensuring that an entrant's costs will not exceed those of the incumbent. A price which exceeds it will be harmful because it impedes efficient entry.

The italicised part of this passage is an accurate summary of ECPR only when the underlying assumption that final product prices do not include monopoly profits is valid. The fact that ECPR without regulation or competition does not produce efficient pricing reinforces the conclusion that ECPR as applied by the Privy Council cannot be seen as a safe harbour with firms free to charge more.

[85] Indeed, the difficulty inherent in the Privy Council's decision in *Telecom v Clear* is that Telecom was not constrained in its downstream pricing decisions by competition law or by a regulator, which meant that, in those circumstances, ECPR could not calculate a price that a non-dominant firm in a hypothetical competitive market would charge.[85] Yet their Lordships endorsed the counterfactual test (that is, comparing the dominant firm's actions to the way in which a hypothetical firm, not in a dominant position but similarly placed, would have acted) but at the same time endorsed ECPR, thus allowing monopoly profits in a hypothetical competitive market. If one did assume a commercially functioning market with workable competition then clearly monopoly profits (which could be included in ECPR) would not occur.[86]

(b) The Privy Council's application of ECPR

[86] The Privy Council concluded that a non-dominant Telecom in a competitive market would not have charged below ECPR, so Telecom had not used its dominant position in charging its opportunity cost since that is what it would have charged in a fully competitive market. Telecom submits that their Lordships' treatment of ECPR

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[85] As Economides and White argue, above n 79, at 568, if ECPR is placed in this context, the "luster of its rationale tarnishes rapidly". Brenda Marshall notes that ECPR was developed for regulated markets in the United States, where price or other controls restrict monopoly profits. In markets that are subject to light-handed regulation where there are no such controls, such as in New Zealand, "the rule's effect is blunted": Marshall, above n 73, at 193 and fn 210.

[86] Brenda Marshall and Rachael Mulheron "Access to Essential Facilities under Section 36 of the Commerce Act 1986: Lessons From Australian Competition Law" (2003) 9 Cant L Rev 248 at 254. See also George Hay "Reflections on Clear" (1996) 3 CCLJ 231 at 243–244, Warren Pengilley "The Privy Council Speaks on Essential Facilities Access in New Zealand: What are the Australasian Lessons?" (1995) 3 CCLJ 26 at 45, 59 and fn 43 and Michael O'Bryan "Access Pricing: Law Before Economics?" (1996) 4 CCLJ 85 at 96.

illustrates that ECPR was seen as a safe harbour, relying in particular on their Lordships' statement that a dominant firm "[would] not be acting uncompetitively if [it] refuses to deal at a figure less than that which [it] is currently receiving".[87]

[87] We do not accept that their Lordships' statement that a hypothetical firm would not have charged prices below ECPR can be interpreted as suggesting that, had Telecom's prices been higher than ECPR, it would not have been using its dominant position. The essential question was whether the terms Telecom was seeking to extract were "no higher than those which a hypothetical firm would seek in a perfectly contestable market".[88] If a hypothetical firm would charge ECPR prices (and not less than ECPR), it follows that charging prices above ECPR would amount to a use of a dominant position.

[88] Further, the Privy Council recognised that ECPR pricing could allow the continuation of monopoly profits (although Clear had not proved their existence). Their Lordships considered that monopoly profits would be competed out (that is, prices would be lowered over time). It is inconceivable that the Privy Council considered that an incumbent could with impunity charge more than ECPR, effectively increasing rather than decreasing any monopoly profits.

(c) No alternative model proposed

[89] Finally, as we note below,[89] there was no evidence that Telecom ever had regard to ECPR when setting its wholesale prices. Mr Shavin QC describes Telecom as instead adopting a "generous" approach to its wholesale pricing.

[90] It must be remembered that it was Telecom that put ECPR before the Court in *Telecom v Clear* as the proper pricing model. In the present proceedings, Telecom did not propose that its allegedly "generous" methodology (or indeed any other methodology) was a suitable alternative for assessing whether pricing structures could potentially lead to a breach of s 36.

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87 *Telecom v Clear* (PC), above n 4, at 405.
88 At 403.
89 At [93] below.

[91] While it is strictly the case, as Mr Shavin points out, that there is no obligation on Telecom to place an alternative before the Court, given that ECPR is the pricing method endorsed by the Privy Council in *Telecom v Clear*, it is difficult for this Court to put a gloss on the pricing methodology approved in that case[90] without some alternative methodology to assess whether pricing amounts to use of a dominant position.

Does requiring ECPR breach the need for commercial certainty?

Telecom's argument

[92] Telecom submits that reliance on the ECPR model in the present case breached the requirement for commercial certainty.[91] Telecom says that ECPR was inapplicable because Telecom was unable to calculate, in advance, ECPR prices as a matter of practical or commercial reality. Telecom says that, in order to calculate ECPR prices, Telecom would have needed a level of knowledge of a TSP's activities that was unachievable.

Our assessment

[93] There is no evidence that Telecom ever had regard to ECPR when setting its wholesale prices. It is hard to assess how difficult it was for Telecom to calculate ECPR prices in advance, when there is no evidence that Telecom ever attempted to do so. As the Commission points out, Telecom in fact had no interest in how TSPs used their tails, because it charged for them as if they were end-to-end circuits rather than inputs.

[94] We do not accept Telecom's submission that ECPR would have been too difficult to calculate even if all information was available. As the Commission

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90 Remembering of course that decisions of the Privy Council which are given on appeals from New Zealand remain binding unless and until they are reversed by the Supreme Court: *Couch v Attorney-General (No 2)* [2010] NZSC 27, [2010] 3 NZLR 149 at [32] and [51]; *Shannon v Shannon* [2005] 3 NZLR 757 (CA) at [40]; and *R v Chilton* [2006] 2 NZLR 341 (CA) at [111].

91 In *Telecom v Clear* (PC), above n 4, their Lordships said that s 36 needed to be construed in such a way as to enable a monopolist, before entering upon a line of conduct, to know with some certainty whether or not it was lawful: at 403. See also *Commerce Commission v Telecom Corporation of New Zealand Ltd* [2010] NZSC 111, [2011] 1 NZLR 577 at [30] [*0867 Case*].

points out, the *Telecom v Clear* decision envisaged that the calculation of ECPR prices would necessitate a high degree of input by Telecom, including "regular reviews of Telecom's opportunity costs being charged to Clear",[92] a process that Telecom was happy to embrace at that time. Further, the calculations are not as complicated as Telecom tries to make out. Telecom is a sophisticated company with full capability to set up computer models to calculate ECPR prices for the wholesale data tails it sold.

[95] However, it is accepted by the parties that, to calculate individual ECPR prices for each tail, Telecom would require information about the characteristics of the tail that a TSP required for use in the TSP's network, that is, the configuration of the retail customer network (in the sense of the circuit speed, whether local or national step, and whether the input required was VBR or CBR).

[96] Telecom only appears to identify two specific difficulties in calculating ECPR that arise from not knowing enough information about the use to which each data tail was put in the TSP's network:

(a) in both the two-tail and one-tail scenarios, if Telecom supplied a CBR tail to a TSP, Telecom did not know whether the TSP would use that tail to provide a CBR or VBR retail service, so Telecom did not know whether it was losing the opportunity to provide a CBR retail service or a cheaper VBR retail service; and

(b) in the one-tail scenario, Telecom did not know how many tails in a network were to be self-provided by the TSP (or their characteristics), so Telecom did not know what it was losing the opportunity to provide (for example, whether it was losing the opportunity to provide only one retail HSDT service, or an unknown number of HSDT services in a network).

[97] The Commission responds to Telecom's first concern by arguing that Telecom was well aware that TSPs were using CBR tails as inputs to provide VBR

[92] *Telecom v Clear* (PC) at 397.

retail services.[93] Further, Telecom could readily have included in its supply contracts a provision regarding the use of CBR tails (to ensure the tails were used for a VBR service), in order to prevent arbitrage. Contrary to Telecom's submission, Telecom would not also need a technical ability to monitor how a particular circuit was being used by a TSP. We largely accept the Commission's submissions on this point.

[98] In relation to Telecom's second concern, there was acknowledgement by the Commission that slightly more information would be required in order to calculate ECPR prices in the one-tail scenario, as Professor Gabel considered that the profit share that Telecom could recover for each tail it leased to a TSP was the proportion that the leased tail bore to the total number of tails in the network.[94] However, the Commission says that Telecom could readily have included in its supply contracts a requirement for TSPs to supply the further information it claimed it needed to calculate ECPR.

[99] Telecom submits that a contractual approach would have required the transfer of enormous volumes of information of competitive value between competitors in order to monitor the contractual arrangements. We have some sympathy for the view that Telecom and other TSPs were competing in a climate of mutual suspicion and mistrust in litigation and that therefore this transfer of information in the contractual arrangements would have been an issue. We doubt that Telecom's competitors would have been as ready to supply the information as the Commission maintains. However, we accept the Commission's submission that much of the information, including as to customers, was necessarily acquired by Telecom on a regular basis through supplying tails.

[100] In our view, in any event, Telecom could have made a number of assumptions based on its own market knowledge. We acknowledge that Telecom had organisational structures in place to protect confidential information and to prevent information flow between its wholesale and retail divisions. However, as we have mentioned, Telecom's interconnection group would have acquired a great deal of

93 We discuss this is in further detail at [211] below.
94 See at [46] above.

market knowledge by virtue of supplying the data tails. As a sophisticated company Telecom also had the capability to set up a research division.

[101] We acknowledge that the Privy Council expressed reservations concerning Gault J's comments in this Court[95] that it may be helpful, in determining whether "use" has been made of a dominant position, to consider whether the incumbent firm has acted reasonably.[96] Their Lordships considered that such an inquiry would be contrary to the requirement of certainty, and were concerned about the serious consequences that a monopolist firm could face under the Commerce Act if a Court subsequently disagreed with the firm's genuine assessment that it was acting reasonably.[97] Against the background of these comments, we suggest that, if Telecom had made a genuine attempt to apply ECPR prices, then the Court would not have second guessed its pricing on the basis that the Court would have made different assumptions to underpin the analysis or that the assumptions made by Telecom turned out to be factually wrong.[98]

[102] In any event, Telecom could have applied other accepted pricing methods that did not result in the stifling of competition. Although this Court's methodology was rejected by the Privy Council in *Telecom v Clear*, it would, if used, clearly not lead to use of a dominant position (being lower than ECPR). Indeed, the Privy Council observed without any apparent disapproval the pricing negotiations between Telecom and Clear which did not appear to be based on ECPR and which appeared to be similar to the Court of Appeal methodology.[99] The Privy Council said that Clear had accepted that it must pay something (in excess of traffic charges) for access to Telecom's network, such payment being based on Telecom's true costs, including a reasonable return on capital. Telecom, on the other hand, had accepted that it should not seek to recover any element of monopoly rents from Clear.[100]

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95 *Telecom v Clear* (CA), above n 59, at 430.
96 *Telecom v Clear* (PC), above n 4, at 403.
97 Ibid.
98 Except perhaps on the grounds of lack of reasonableness akin to that in *Associated Provincial Picture Houses Ltd v Wednesbury Corporation* [1948] 1 KB 223 (CA).
99 We acknowledge that those negotiations took place before the Privy Council decision. The Privy Council itself acknowledged that its decision did not deal with whether Clear's past stance in negotiations was reasonable, let alone fix the terms for interconnection: *Telecom v Clear* (PC) at 390.
100 On the basis that, if necessary, these could be stripped out by the activation of Part 4 of the Commerce Act 1986. See *Telecom v Clear* (PC) at 409.

[103] Finally, we note that the difficulty with courts being involved in setting prices where there is no history of prior dealing is well recognised.[101] The result of the *Telecom v Clear* litigation has been called a "philosophical abstraction" that is almost impossible to convert to a practical market price with any degree of certainty.[102] In Professor Pengilley's opinion, a regulatory authority is needed for setting prices where there has been no prior access.[103] However, in our view, whilst there are acknowledged difficulties for the courts in the area of pricing, they do not mean that the courts should abdicate responsibility to enforce s 36.

Did the High Court err by not following the United States approach to price squeeze claims?

Telecom's argument

[104] Telecom argues that the High Court should have followed the United States approach to price squeeze claims and concluded that such claims do not fall within the scope of s 36. Telecom relies in particular on two decisions of the United States Supreme Court: *Verizon Communications Inc v Law Offices of Curtis V Trinko* (*Trinko*)[104] and *Pacific Bell Telephone Company v Linkline Communications Inc* (*Linkline*).[105] Telecom submits that the United States jurisprudence is to be preferred over the divergent approach taken towards price squeeze claims in European Union cases. Telecom also submits that, in line with the United States jurisprudence, price squeezes should be treated as a form of predatory pricing, and thus the requirements of a predatory pricing claim should be fulfilled in order for a breach of s 36 to be established.[106]

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101 Pengilley, above n 86, at 29.
102 Ibid, at 50.
103 Ibid, at 60.
104 *Verizon Communications Inc v Law Offices of Curtis V Trinko* 540 US 398 (2004) [*Trinko*].
105 *Pacific Bell Telephone Company v Linkline Communications Inc* 129 SCt 1109 (2009) [*Linkline*].
106 Predatory pricing occurs when a dominant firm sets its downstream prices below the firm's variable costs and there is a likelihood of recoupment of the lost profit: *Carter Holt*, above n 31, at [67].

Our assessment

(a) United States cases

[105] In *Trinko*, the United States Supreme Court considered whether a vertically integrated telecommunications company's failure to share elements of its network with competitors (as required under the Telecommunications Act 1996) was exclusionary conduct contrary to s 2 of the Sherman Act,[107] which prohibits monopolisation and attempts to create a monopoly. The principal opinion was written by Scalia J,[108] who began his discussion of refusal to deal claims by stating that a dominant firm has the right to exercise its discretion freely as to the parties with whom it will deal.[109] He acknowledged that this right is not unqualified, but stressed that the Court had been very cautious in recognising exceptions.[110]

[106] Scalia J concluded that the present case did not fall within the existing exceptions, and also cast doubt on the validity of an "essential facilities" doctrine,[111] which had developed in the Federal Circuit Courts but had never been expressly endorsed by the Supreme Court, by declining either to recognise or repudiate the doctrine.[112]

[107] Scalia J also considered that traditional antitrust principles did not justify adding the present case to the existing exceptions to the proposition that there is no duty to aid competitors.[113] He said that the 1996 Act created an extensive regulatory framework, which was "an effective steward of the antitrust function".[114] He also noted that competition law obligations to help rivals and share resources risk chilling incentives to innovate, and that the Court needed to be wary of "false positives", namely wrongfully condemning conduct that is efficient and beneficial as

[107] Sherman Act 15 USC § 2.

[108] On behalf of himself, Rehnquist CJ, O'Connor, Kennedy, Ginsburg and Breyer JJ. A separate opinion was written by Stevens J, on behalf of himself, Souter and Thomas JJ.

[109] At 408.

[110] Ibid.

[111] Whereby a firm which controls a facility that is considered essential to a competitor's ability to compete would be required to provide access to an upstream or downstream competitor.

[112] At 411.

[113] Ibid.

[114] At 413.

monopolistic.[115] Finally, he also approved Professor Areeda's observation that no court should impose a duty to deal that it cannot explain or adequately and reasonably supervise.[116]

[108] After *Trinko*, the effect of the decision on refusal to deal claims was unclear. The Circuit Courts issued conflicting decisions as to whether refusal to deal claims were still viable, outside of a very narrow set of exceptions.[117] The interaction between competition law and regulatory regimes and the continued viability of price squeeze claims was particularly unclear.[118]

[109] In 2009, in *Linkline*, the Supreme Court[119] reversed a decision from the Ninth Circuit Court of Appeals[120] that recognised that a price squeeze claim may be brought under s 2. In that case, a vertically integrated telecommunications company was alleged to have charged its competitors wholesale prices that were unfairly high in relation to its retail prices. Under the 1996 Act, the incumbent was required to supply wholesale Digital Subscriber Line services to competitors at a reasonable and non-discriminatory price. The central issue before the courts was therefore whether a price squeeze claim could be brought under s 2 when the incumbent is under no antitrust duty to deal with its competitors.

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115 At 414.

116 At 415, referring to Phillip Areeda "Essential Facilities: An Epithet in Need of Limiting Principles" (1990) 58 Antitrust Law Journal 841 at 853.

117 See for example *American Central Eastern Texas Gas Company v Union Pacific Resources Group Inc* 93 Fed Appx 1 (5th Cir 2004), *Tucker v Apple Computer Inc* 493 F Supp 2d (ND Cal 2006), *AIB Express Inc v FEDEX Corp* 358 F Supp 2d 239 (SD NY 2004) and *Z-Tel Communications Inc v SBC Communications Inc* 331 F Supp 2d 513 (ED Tex 2004).

118 For example, in *Covad Communications Company v Bellsouth Corporation* 374 F 3d 1044 (11th Cir 2004) at 1050, the Court said that price squeeze claims were not specifically excluded by *Trinko*, but in *Covad Communications Company v Bell Atlantic Corporation* 398 F 3d 666 (DC Cir 2005) at 673–674, the Court said that, because there was no antitrust duty to deal, it made no sense to prohibit a predatory price squeeze in those circumstances.

119 Roberts CJ delivered the principal opinion of the Court, on behalf of himself, Scalia, Kennedy, Thomas and Alito JJ. Breyer J wrote a separate concurring opinion, on behalf of himself, Stevens, Souter and Ginsburg JJ.

120 *Linkline Communications Inc v SBC California Inc* 503 F 3d 876 (9th Cir 2007).

[110] The Supreme Court held that, if there is no antitrust duty to deal with a competitor at the wholesale level, a price squeeze cannot violate s 2 unless the dominant firm's retail prices are predatory.[121]

[111] The Supreme Court also expressed some reservations about the recognition of a price squeeze claim even where there is an antitrust duty to deal. The Court considered that institutional concerns counselled against recognition of price squeeze claims.[122] The Court was concerned that recognising price squeeze claims would require courts to police both the wholesale and retail prices and courts would be aiming at a moving target, since it is the interaction between these two prices that may result in a squeeze.[123]

[112] The effect of *Trinko* and *Linkline* is still a debated topic amongst academic commentators, with some commentators arguing that these two Supreme Court decisions do not expressly overrule any of the prior refusal to deal or price squeeze decisions, but are instead limited to the regulatory context in which they were decided.[124]

(b) European Union cases

[113] Unlike s 36 of the Commerce Act, the European courts have interpreted their equivalent provision[125] as not requiring the use of a dominant position.[126] This is because, under European law, a dominant firm has a "special responsibility not to allow its conduct to impair genuine undistorted competition".[127] The special

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[121] This would mean that the requirements of a predatory pricing claim, as defined by the Supreme Court in *Brooke Group Ltd v Brown & Williamson Tobacco Corporation* 509 US 209 (1993), would need to be met.

[122] *Linkline*, above n 105, at 1114.

[123] Ibid.

[124] Daniel Shulman "Refusals to Deal: Is Anything Left; Should There Be?" (2010) 11 Sedona Conf J 95 at 108–109. Compare Erik Hovenkamp and Herbert Hovenkamp "The Viability of Antitrust Price Squeeze Claims" (2009) 51 Arizona L Rev 273 at 274.

[125] Article 102 of the Treaty on the Functioning of the European Union (formerly art 82 of the Treaty establishing the European Community).

[126] See the description of the European approach in *Carter Holt*, above n 31, at [63]–[64].

[127] Case 322/81 *NV Nederlandsche Banden-Industrie Michelin v Commission of the European Communities* [1983] ECR 3461 at [57]; Case C-62/86 *AKZO Chemie BV v Commission of the European Communities* [1993] 5 CMLR 215; Case C-333/94P *Tetra Pak International SA v Commission of the European Communities* [1997] 4 CMLR 662; Cases C-395/96P and C-396/96P *Compagnie Maritime Belge Transports SA v EC Commission* [2000] 4 CMLR 1076 at

responsibility arises because of the inherent prejudice that a dominant firm's conduct may cause to competition. Thus activities that might be acceptable in a normal competitive situation might amount to abuse if carried out by a dominant firm.[128]

[114] The European price squeeze cases suggest that a price squeeze will amount to an abuse of a dominant position where a dominant firm sets its pricing in a manner that prevents an efficient competitor from competing.

[115] In *Deutsche Telekom*,[129] a vertically integrated telecommunications company was held to have abused its dominant position by engaging in a price squeeze in circumstances where it charged its rivals more for unbundled broadband access at the wholesale level than at the retail level. It was not necessary to demonstrate that the wholesale prices were excessive or that the retail prices were predatory in order to find that there was an abusive price squeeze. Instead, the spread between the retail and wholesale prices needed to be either negative or at least insufficient to cover the incumbent's own downstream costs.[130]

[116] The price squeeze was attributed to the incumbent firm despite the fact that its pricing practice at the wholesale level was regulated by the national telecommunications authority. It was said that "competition rules may apply where the sector-specific legislation does not preclude the undertakings it governs from engaging in autonomous conduct that prevents, restricts or distorts competition".[131] The incumbent firm was still able to adjust its retail prices in such a way as to prevent a squeeze from occurring, and therefore was capable of engaging in autonomous conduct that was subject to competition rules.[132]

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[114] and T-201/04 *Microsoft Corp v Commission of the European Communities* [2007] 5 CMLR 11 at [775].

128 Case 85/76 *Hoffmann-La Roche and Co AG v Commission of the European Communities* [1979] ECR 461 at [6]. See also Case T-219/99 *British Airways plc v Commission of the European Communities* [2004] 4 CMLR 19; Case T-210/99 *General Electric Company v Commission of the European Communities* [2006] 4 CMLR 15.

129 Case COMP/C-1/37.451 *Deutsche Telekom AG* OJ L 263/9 [*Deutsche* (EC Commission)], upheld by the Court of First Instance in Case T-271/03 *Deutsche Telekom AG v Commission of the European Communities* [2008] ECR II-477, upheld by the European Court of Justice (ECJ) in Case C-280/08P *Deutsche Telekom AG v European Commission* [2010] 5 CMLR 27 [*Deutsche* (ECJ)].

130 *Deutsche* (EC Commission) at [107] and [140]; *Deutsche* (ECJ) at [159] and [167]–[169].

131 *Deutsche* (EC Commission) at [54].

132 *Deutsche* (ECJ) at [92].

[117] In *Wanadoo*,[133] a vertically integrated telecommunications operator was held to have abused its dominant position by engaging in a price squeeze.[134] The incumbent firm's conduct had had an exclusionary effect because the price squeeze affected its competitors' ability to enter the relevant market and exert a competitive constraint on the incumbent.[135]

[118] The anti-competitive effect of a price squeeze was explained by reference to an "investment ladder".[136] Due to the risks involved in investments that entail high sunk costs, alternative operators are likely to climb a ladder of investment, by following a step-by-step approach to continuously expanding their infrastructure investments. When climbing that ladder, alternative operators seek to obtain a minimum critical mass in order to be able to make further investments. The Commission of the European Communities (EC Commission) considered it necessary that there should not be any price squeeze in relation to any "step" of the ladder (that is, in relation to any wholesale product). If there was such a price squeeze, it considered that new entrants that were climbing the ladder of investment would be foreclosed.[137]

[119] *Teliasonera*[138] establishes the test for a price squeeze in the European Union as one solely concerned with the spread between wholesale and retail prices.[139] It was emphasised that, in the absence of any objective justification, if a dominant firm's wholesale prices are higher than its retail prices, an effect that is at least potentially exclusionary is probable.[140] This is because the competitors of the dominant firm would be compelled to sell at a loss, even if they were equally or more efficient.

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133 Case COMP/38.784 *Wanadoo España v Telefónica* (4 July 2007). The General Court upheld this decision on appeal in Case T-336/07 *Telefónica and Telefónica España v Commission* OJ C 269.

134 Again, the incumbent firm had a duty to supply wholesale services imposed by regulation: at [303].

135 At [586].

136 At [92], fn 82, and [177]–[178], the Commission of the European Communities describes the concept of the "investment ladder" as referring to "the gradual nature of investments by alternative operators in telecommunications".

137 At [392].

138 Case C-52/09 *Konkurrensverketk v Teliasonera Sverige AB* [2011] 4 CMLR 18.

139 The ECJ confirmed that an abusive price squeeze would be established where the spread between the prices was insufficient to allow a competitor which was equally as efficient as the dominant firm to compete: at [32] and [42]. There would be no need for the prices to be abusive in themselves on account of their excessive or predatory nature: at [34].

140 At [73].

(c) Summary

[120] We do not accept Telecom's submission that the High Court should have followed the United States approach to price squeezes and concluded that such claims do not fall within the scope of s 36. The United States and European cases on refusals to deal (and in particular, on price squeeze claims) that we were referred to by the parties, address the question of whether there is any room for the application of competition law, where there is regulation. The position in the United States appears to be that, once a sector-specific regulatory scheme "designed to deter and remedy anticompetitive harm"[141] is in existence, there is no scope for the courts to further intervene through the application of competition law. In contrast, regulation and competition law applies concurrently in the European Union, so that competition law may still apply where sector-specific legislation does not prevent a dominant firm from engaging in autonomous conduct that prevents, restricts or distorts competition.[142]

[121] However, the difficult issues about the appropriate interaction between competition law and regulatory regimes do not arise in the present case, given that Telecom was not subject to regulation at the wholesale or retail level at the time of the alleged price squeeze.[143] In our view the United States jurisprudence therefore does not provide compelling authority for the proposition that a constructive refusal to supply essential inputs arising from a price squeeze is outside the scope of s 36. The United States Supreme Court's dismissive view of the essential facilities doctrine and price squeeze claims was undoubtedly influenced by the fact that it viewed the pro-competitive objects of competition law as adequately protected by a regulatory framework.

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141 *Trinko*, above n 104, at 881.

142 See Damien Geradin and Robert O'Donoghue "The Concurrent Application of Competition Law and Regulation: The Case of Margin Squeeze Abuses in the Telecommunications Sector" (2005) 1 Journal of Competition Law and Economics 355 at 380 and 417–420 and George Hay and Kathryn McMahon "The Diverging Approach to Price Squeezes in the United States and Europe" (Cornell Law Faculty Working Papers, Paper 91, 2012) at 19 for a discussion of whether the United States or European approach is preferable.

143 Indeed, as Chambers J notes in his judgment, at [334] below, Telecom had actively lobbied for the exclusion of data tails from the Telecommunications Act 2001.

[122] The United States jurisprudence does illustrate a more general concern about entertaining a price squeeze claim because it may "chill" incumbents' incentives to make investments, and it may require the courts to impose a duty to deal that it cannot explain or reasonably supervise.[144] However, these concerns are not specific to price squeeze claims. Rather, these are the concerns raised when engaging in the more general debate about whether an obligation to supply should be imposed on a dominant firm at all.[145] Given that an obligation to supply essential inputs was accepted as falling within the scope of s 36 in *Telecom v Clear*, these concerns do not, of themselves, provide compelling reasons for concluding that a price squeeze claim should fall outside the scope of s 36.

[123] Similarly, we do not accept that this Court should follow the United States approach of establishing a price squeeze claim through the lens of a predatory pricing claim, for the reasons we have stated above. We also note that, whilst predatory prices may create price squeezes, not every price squeeze will involve predatory pricing. Indeed, as the Commission points out, it had no complaint with Telecom's retail pricing as such; rather, the complaint concerned the relativity between Telecom's wholesale and retail prices. We therefore do not accept that there was any need for the Commission to establish the requirements of a predatory pricing claim in the present case.

[124] Finally, we acknowledge that caution in drawing assistance from the European cases is required. Unlike in Europe, a firm with a lawful monopoly in New Zealand is not under a general duty to assist its competitors.[146] The monopolist firm is entitled to compete with its competitors and does not have to "[hold] an umbrella over inefficient competitors".[147] However, we do not consider that this

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[144] See the concerns set out in *Trinko*, above n 104, which are summarised at [107] above.

[145] See Valentine Korah "Access to Essential Facilities Under the Commerce Act in the Light of Experience in Australia, the European Union and the United States" (2000) 31 VUWLR 231, Valentine Korah "Charges for Inter-Connection to a Telecommunications Network" (1995) 2 CCLJ 213 at 215, 232 and 239; Warren Pengilley "Misuse of Market Power: The Unbearable Uncertainties Facing Australian Management" (2000) 8 Trade Practices Law Journal 56 at 60; Hovenkamp and Hovenkamp, above n 124, at 277; Hay, above n 86, at 235. Compare Shulman, above n 124, at 107.

[146] *Union Shipping NZ Ltd v Port Nelson Ltd* [1992] 2 NZLR 662 (HC) at 706. See also *NZ Magic Millions Ltd v Wrightson Bloodstock Ltd* [1990] 1 NZLR 731 (HC) at 761.

[147] *Olympia Equipment Leasing Co v Western Union Telegraph Co* 797 F 2d 370 (7th 1986) at 375, quoted with approval in *Telecom v Clear* (HC), above n 56, and *Telecom v Clear* (PC), above n 4, at 402–403.

means that the European cases cannot provide some assistance in highlighting the anti-competitive effect of a price squeeze. We note that the Commission relied on the European cases to demonstrate that price squeezes have an anti-competitive effect by preventing equally efficient competitors from "climbing the ladder of investment". We emphasise the requirement for competitors to be "equally efficient". The Commission did not attempt to rely on the European cases inappropriately by arguing that Telecom had a special responsibility akin to dominant firms in Europe.

Did the High Court err in concluding that Telecom had an obligation to supply data tails to competitors?

Telecom's argument

[125] Telecom argues that the High Court erred in reaching the conclusion that Telecom had an obligation to supply data tails to competitors. First, Telecom submits that the High Court erred in accepting that a constructive refusal to supply essential inputs arising from a price squeeze could contravene s 36. We dismissed that argument for the reasons stated at [105]–[124] above.

[126] Secondly, Telecom says that the High Court erred in making a finding that Telecom had an obligation to supply data tails to competitors that was independent of its conclusion on the counterfactual.

[127] Thirdly, Telecom seeks to distinguish both *Telecom v Clear* and *Queensland Wire*[148] (where the Privy Council and High Court of Australia accepted that there was a duty on a dominant vertically integrated incumbent to supply an essential input to competitors) from the present case.

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148 *Queensland Wire Industries Pty Ltd v Broken Hill Pty Co Ltd* (1989) 167 CLR 177 (HCA).

Our assessment

(a) Did the High Court reach its conclusion independently of the counterfactual?

[128] The High Court accepted the Commission's invitation to look at the issue of whether a non-dominant firm (otherwise in the same position as Telecom) would have offered data tails to rivals at prices above ECPR in two steps. The first step was to enquire whether there was an obligation to supply data tails at all. The second step was to consider whether supply in the counterfactual by a non-dominant incumbent would be at prices in excess of ECPR.[149]

[129] The Court noted that no essential facilities doctrine[150] or statutory obligation existed that required Telecom to supply data tails to TSPs.[151] The Court accepted the Commission's submission that there was a duty on a vertically integrated incumbent to supply an essential wholesale input to a competitor in a downstream market based on *Queensland Wire* and also the obligation apparently assumed to exist in *Telecom v Clear*. The Court also held that Telecom's obligation to supply data tails to TSPs carried with it a concomitant duty to supply data tails at a price not exceeding ECPR.[152]

[130] We accept Telecom's submission that the first step of the High Court's analysis could be taken as assuming a general duty to supply. There was no express reference to why a counterfactual would result in supply. However, in context, it is clear that the High Court was relying on a counterfactual analysis. It referred to *Queensland Wire* and *Telecom v Clear*, which were counterfactual cases. It also started its analysis by stating that it was examining whether there was an obligation to supply data tails as the first of a two-stage approach to assessing the counterfactual.

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149 Liability Judgment, above n 6, at [126].

150 Save to provide valuable insights into the operation of s 36: *Union Shipping*, above n 146, at 705–706.

151 At [127].

152 At [129].

[131] In any event, implicit in the discussion of whether a non-dominant firm would supply at prices in excess of ECPR is an analysis of whether, under the counterfactual, a non-dominant incumbent would supply at all.

[132] We thus accept the Commission's submission that the High Court did not hold that Telecom had an obligation to supply independent of s 36 and the counterfactual. The High Court expressly eschewed reliance on the United States essential facilities doctrine and it did not rely on a nascent New Zealand equivalent.[153] Nor did the Commission seek to rely on a separate legal obligation to supply, independent from the counterfactual analysis under s 36, as it was not necessary to do so. The High Court properly concluded that Telecom had an "obligation" to supply data tails to competitors, in the sense that in the agreed counterfactual a non-dominant Telecom would not rationally have refused supply, and therefore would be in breach of s 36 if it did refuse supply.

(b) Can this case be distinguished from *Telecom v Clear* and *Queensland Wire*?

[133] We do not accept the submission that *Telecom v Clear* and *Queensland Wire* are distinguishable from the present case.

[134] Telecom argues that, while an obligation to supply was accepted in *Telecom v Clear*, this was because Telecom had to offer ubiquitous services to its customers and it had to have the ability to connect a customer to any person with a telephone, even if on a rival network. There was therefore a mutual need for interconnection. This meant that a non-dominant communications provider would have provided access.

[135] The High Court considered whether *Telecom v Clear* was distinguishable because access in that case was essential to enable rivals to provide a competing service, whereas a data transmission service could be provided by a TSP acquiring an end-to-end circuit from Telecom or building its own circuit. The Court did not see this as a point of distinction. It said that TSPs required access to data tails

[153] We thus do not need to make any comment on whether there is a nascent essential facilities doctrine in New Zealand, particularly following *Commerce Commission v Bay of Plenty Electricity Ltd* HC Wellington CIV-2001-485-917, 13 December 2007.

because they could not effectively provide a competing HSDT service unless they were able to connect to any location from which a business customer wished to transmit and receive data.[154] Outside major CBDs, TSPs did not have access networks and it was uneconomic for them to build networks.[155]

[136] This is true and we accept that this does not provide a point of distinction from *Telecom v Clear* for the reasons given in the High Court. However, as we understand Telecom's submission (at least in this Court), it is that, in *Telecom v Clear*, Telecom itself required ubiquitous access: it required access to Clear's network in the same way Clear required access to Telecom's network. This is not the case, we accept, in relation to data tails. This is because data tails are connections between particular customers' premises.

[137] Nevertheless, we do not consider that this difference between the two cases means that, absent a need for mutual ubiquitous access, a non-dominant firm otherwise in the position of Telecom would not supply in the counterfactual. The analysis of the counterfactual[156] by Professor Ordover (one of the expert economists called by the Commission), which was accepted by the High Court,[157] does not depend on there being mutual ubiquitous access issues. It merely depends on T1 not wishing to lose both the access and the related retail sale to T2 and T3, and therefore, under the counterfactual, accepting the obligation to supply. In other words, T1 would have no business incentive to refuse to sell data tails because T3 could lease data tails from its rival T2, so that T1 would lose not only the retail sale that T3 was intending to make, but the wholesale sale of access as well.

[138] The Commission referred us to a decision of the High Court of Australia, *NT Power*,[158] in which a majority of the Court held that the Power and Water Authority would not have refused NT Power access to its electricity infrastructure if it had been operating in a competitive market. The Commission submits that the

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154 Liability Judgment, above n 6, at [47].
155 Ibid.
156 The agreed characteristics of the counterfactual are set out at [43] above.
157 At [129].
158 *NT Power Generation Pty Ltd v Power and Water Authority* [2004] HCA 48, (2004) 219 CLR 90 [*NT Power* (HCA)].

judgment of Finkelstein J in the Full Federal Court[159] contains a particularly useful description of why a rational, profit-maximising firm would supply in the counterfactual.

[139] Finkelstein J said that, in a competitive market, the incumbent would grant access to its infrastructure to a third party. This was because a profit-maximising firm in a competitive market would not stand by and allow a competitor to supply the third party with transmission and distribution services.[160] He considered whether a rational firm would deny access to its infrastructure as a means of protecting its downstream business and concluded that it would not. This was because the incumbent would face that retail competition whether or not it granted access (because of the third party's ability to access a competitor's hypothetical infrastructure).[161]

[140] Telecom argues that *NT Power* is unhelpful because it involved an outright refusal to supply rather than a constructive refusal to supply by offering to provide access on unreasonable terms. Telecom also says that there is nothing remarkable about the analysis of the counterfactual in *NT Power*, which it describes as an example of the uncontroversial proposition that, in constructing the counterfactual, a number of unrealistic assumptions may need to be made. We do not accept those submissions. In our view Finkelstein J's articulation of how the counterfactual may operate in natural monopoly circumstances explains the logic of supply in the counterfactual in the present case: T1 will supply because it will not wish to lose both the access and the related retail sale to T2 and T3.

[141] Finally, Telecom seeks to distinguish the present case from *Queensland Wire* on the basis that, contrary to the circumstances in *Queensland Wire*, there was no separately identifiable input product that emerged from a stage of a vertically integrated production process from which all other products were sold. In

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159 *NT Power Generation v Power and Water Authority* [2002] FCAFC 302, (2002) 122 FCR 399. The majority of the Full Federal Court held that s 46 of the Trade Practices Act 1974 (the equivalent provision to s 36) was inapplicable because the incumbent's conduct had immunity from s 46. Finkelstein J delivered a dissenting judgment in the Full Federal Court, concluding that the conduct did not attract immunity and that the incumbent's conduct had contravened s 46. A majority of the High Court of Australia followed the approach taken by Finkelstein J.

160 At [179].

161 Ibid.

Queensland Wire, the input was Y-bar, which was used to make star picket posts. The incumbent manufactured steel products at its rolling mill, and offered all those products for general sale except for Y-bar. In contrast, in the present case Telecom submits that TSPs were essentially seeking unbundling of Telecom's network and the creation of new wholesale products. Telecom denies that it sold "data tails". It maintains that it saw itself as selling data circuits rather than an essential component or input and was therefore entitled to price on the basis that a TSP was effectively obtaining two end-to-end services.

[142] However, in our view Telecom's argument is inconsistent with the High Court's identification of the relevant markets. The High Court accepted the Commission's allegation that a relevant market for the purposes of the decision was the wholesale market for "data tails" outside major CBD areas.[162] The High Court noted that, although this market definition was not admitted by Telecom in its pleading, it was not challenged by Telecom in the High Court hearing.[163] Telecom has not challenged the market definition on appeal. Without challenging the market definition, it is hard to see how Telecom can successfully argue that it was not selling "data tails".

[143] Further, as the Commission points out, Telecom was not providing a service to TSPs that could be sold at retail as connections between two end users' premises. Rather, Telecom was providing a connection between an end user customer's premises and a TSP's POP, utilising the TSP's own core backbone network infrastructure.

Did the High Court err in concluding that a non-dominant Telecom would not have supplied data tails to competitors at a price that exceeded ECPR?

Telecom's argument

[144] Telecom argues that the High Court erred in concluding that a non-dominant Telecom would not have supplied data tails to competitors at a price that exceeded ECPR. First, Telecom submits that the High Court misapplied *Telecom v Clear* by

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162 Liability Judgment, above n 6, at [35].
163 At [40].

using ECPR as a ceiling rather than as a mere safe harbour. We dismissed that argument for the reasons stated at [81]–[91] above. Secondly, Telecom submits that ECPR was inapplicable because ECPR prices could not be calculated, in advance, as a matter of practical or commercial reality. We dismissed that argument for the reasons stated at [93]–[103] above.

[145] Thirdly, Telecom submits that, to determine what a non-dominant firm in a hypothetical competitive market would do, recourse to an economic model was not necessary. Instead, Telecom submits that direct evidence of the actions of Telecom in markets where it was not dominant and the actions of Clear (and later TelstraClear)[164] confirmed that a non-dominant firm otherwise in Telecom's position would not have supplied data tails on different terms and that a non-dominant TSP could have refused to supply.

[146] Next, Telecom submits that the High Court erred in accepting evidence given by Professor Ordover that, in a competitive market, Telecom would eventually have been forced to supply at prices below ECPR and approaching marginal cost.

[147] Finally, Telecom submits that Professor Ordover's explanation of how a non-dominant Telecom would behave in the counterfactual was flawed because he relied on a "Bertrand model" of competition in product-differentiated markets. Telecom submits that this model is dependent on a number of assumptions that cannot be assumed in this case and consequently cannot be relied upon to ascertain what a non-dominant firm would do in a competitive market as a matter of rational commercial judgment.

Our assessment

(a) Direct observation

[148] Telecom submits that, to determine what a non-dominant firm in a hypothetical competitive market for data tails outside major CBD areas would do, recourse to ECPR was not necessary. Telecom submits that direct observation of

[164] For simplicity, we will refer to the actions of Clear and TelstraClear as the actions of TelstraClear in this section of the judgment.

Telecom's behaviour within major CBD areas and TelstraClear's behaviour over the relevant period provides the answer as to how a non-dominant firm would have behaved.

[149] Telecom relies on the High Court of Australia's decision in *Melway*,[165] where Gleeson CJ, Gummow, Hayne and Callinan JJ said that "[i]n some cases, a process of inference, based upon economic analysis, may be unnecessary. Direct observation may lead to the correct conclusion".[166] In that case, there was direct evidence that the incumbent firm would have acted in the same way as that impugned, even before it had acquired dominance in the market.

[150] In the Supreme Court's decision in *Commerce Commission v Telecom Corporation of New Zealand Ltd* (the *0867 Case*), Blanchard and Tipping JJ (who gave the reasons of the Court) said that the reference to direct observation in *Melway* did not suggest abandonment of the comparative exercise by the Court in that case.[167] This was made clear when the High Court of Australia said that the real question was whether, without its market power, the incumbent firm could have maintained its distributorship system. The reference to direct observation was a reflection of the point that in some cases the comparison may be made without the need for economic analysis.[168]

[151] Telecom submits that it was subject to effective competition (both real and anticipated) from competing access networks built by TelstraClear in the major CBD areas (Auckland, Wellington and Christchurch) from 2000. These areas expanded to Hastings, New Plymouth, Hamilton and Palmerston North over 2000–2004 as TelstraClear expanded its access network. Telecom says that, because Telecom was not alleged by the Commission to have had dominance or substantial market power in these major CBD areas, the direct evidence of Telecom and TelstraClear's behaviour in these areas provides the answer as to how two non-dominant firms

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165 *Melway Publishing Pty Ltd v Robert Hicks Pty Ltd* [2001] HCA 13, (2001) 205 CLR 1.

166 At [53].

167 *0867 Case*, above n 91, at [24].

168 Ibid. The Supreme Court went on to say that economic analysis may be helpful in constructing the hypothetically competitive market and to point to those factors that would influence the firm in that market. But it pointed out that the "use" question is a practical one, concerned with what the firm in question would (rather than could) have done in the hypothetically competitive market: at [35].

would behave in a competitive market for data tails outside major CBD areas. Telecom says that the direct evidence of the conduct of both firms indicated that:

(a) Telecom did not change its behaviour between major and non-major CBD areas. Telecom's pricing approach in major CBD areas was to price wholesale HSDT services as end-to-end circuits rather than as "data tails".

(b) TelstraClear did not provide data tails to other TSPs in the major CBD areas. Telecom says that this demonstrates that a non-dominant firm (T2) in a competitive market would be able to refuse to supply data tails.

[152] The Commission says that Telecom's contention is contrary to the counterfactual agreed upon by the parties in the High Court because the evidence indicates that Telecom, through its pricing, still exercised market power in the major CBD market. Whilst the Commission had not alleged that Telecom was dominant in the major CBD areas, it does not follow that the market was workably competitive. In addition, the Commission submits that TelstraClear's behaviour is not indicative of what T2 would have done. Unlike T2, TelstraClear did not have a ubiquitous network throughout the major CBD areas[169] and did not have a 50 per cent share of the retail HSDT market. Further, the evidence does not establish that TelstraClear "refused" to supply data tails to other TSPs. Rather, the inference is that TelstraClear (unlike T2), was unable to supply profitably because of the limited extent of its network.

[153] In our view, the fact that TelstraClear did not have a ubiquitous network throughout the major CBD areas during the relevant period means that it cannot be said that Telecom was denied all aspects of its dominance in the major CBD areas, or that the behaviour of TelstraClear is indicative of what T2 would have done. In the *0867 Case*, the Supreme Court emphasised the importance of removing all aspects of a firm's dominance when considering the counterfactual: "the hypothetically

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[169] Evidence was given in the High Court hearing that TelstraClear had only a very limited access network in the major CBD areas.

competitive market must *genuinely deny that firm all aspects of its dominance*".[170] Direct observation of the behaviour of Telecom and TelstraClear in the major CBD areas therefore does not assist in answering the question of what T1 and T2 would do. We thus accept the Commission's submissions.

(b) The issue of marginal cost

[154] The High Court was satisfied that, in the agreed counterfactual,[171] a non-dominant Telecom would not set prices for data tails at prices above ECPR.[172] The Court accepted Professor Ordover's evidence that, if it did so, the backbone provider would purchase input from another company and Telecom would lose the sale entirely. The High Court accepted Professor Ordover's evidence that in a competitive market Telecom would eventually have been forced to supply at prices below ECPR and approaching marginal cost. The Court agreed with the Commission's submission that this was consistent with what was envisaged by the Privy Council in *Telecom v Clear*, which referred to the process by which Telecom's prices to Clear would be forced down until any element of monopoly profit was "competed out".[173]

[155] Telecom submits that the High Court erred in accepting Professor Ordover's evidence that, in a competitive market, Telecom would eventually have been forced to supply at prices below ECPR and approaching marginal cost. Telecom submits that the Privy Council in *Telecom v Clear* envisaged a reduction in the ECPR price as the retail price was lowered in response to the activity of the efficient entrant. Their Lordships did not envisage supply at a price below ECPR. Further, in an industry that enjoys economies of scale and scope such as the telecommunications market, it is incorrect to use marginal costs as a yardstick. Telecom relies on evidence given by Professor Hausman (an expert economist) that, if a company were to charge marginal cost, it would not cover its fixed costs and would go out of business.

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170 *0867 Case*, above n 91, at [36] (emphasis added).
171 The agreed characteristics of the counterfactual are set out at [43] above.
172 Liability Judgment, above n 6, at [129].
173 Ibid, referring to *Telecom v Clear* (PC), above n 4, at 397.

[156] We accept Telecom's submission that the process of undercutting envisaged by the Privy Council in *Telecom v Clear* would drive ECPR prices down, rather than driving wholesale prices below ECPR.

[157] We also have some sympathy for the view that, in telecommunications, if a firm were to charge marginal cost it would go out of business. In a practical commonsense business model in the counterfactual, T1 and T2 would not force prices down to marginal costs. However, we do not consider that this means that T1 and T2 would necessarily continue to charge ECPR prices either. Certainly neither would be able to charge ECPR prices that included any element of monopoly profit because any such profits would have been competed out.

[158] In any event, we accept the Commission's submission that the High Court's comment about prices eventually approaching marginal cost was not essential to the Court's conclusion that a non-dominant firm in a hypothetical competitive market would not price above ECPR. Further, Professor Ordover's evidence that was accepted by the High Court was that prices would approach marginal cost, not that they would actually reach marginal cost. Professor Hausman did not say that a firm would never charge at a price approaching marginal cost.

[159] We also accept the Commission's submission that the High Court's acceptance of Professor Ordover's evidence that Telecom would eventually have been forced to supply at below ECPR prices does not affect its conclusion that a non-dominant firm would not set prices for data tails above ECPR. The evidence given by Professor Ordover that was essential in supporting the Court's conclusion was his evidence that T1 would have no incentive to charge T3 for data tails at prices above ECPR because, if T1 charged above ECPR, T3 would purchase the data tail from T2, resulting in T1 losing the sale entirely.

(c) The Bertrand model of competition

[160] Telecom submits that Professor Ordover had relied on a "Bertrand model" of competition in product-differentiated markets in order to reach the conclusion that T1 would not price data tails above ECPR because it would not want to lose the sale

to T2. Telecom submits that the Bertrand model is an unsuitable economic model to rely on because it is dependent on a number of assumptions that cannot be assumed in this case.[174] Telecom says that this means that the model cannot be relied upon to ascertain what a non-dominant firm would do in a competitive market as a matter of rational commercial judgment.[175]

[161] We consider that it is a matter of commonsense that T1 would not price data tails above ECPR because it would not want to lose the sale to T2. We therefore do not consider it necessary to engage in a discussion of whether the assumptions underpinning the Bertrand model were present in this case. In any event, in the *0867 Case* the Supreme Court emphasised that the need for economic analysis of sufficient cogency showing how firms would behave in the hypothetical market does not prevent unrealistic assumptions from being made. The necessary assumptions are made for the purpose of identifying the features of the hypothetically competitive market and, ex hypothesi, will depart substantially from the realities of the actual market in which the firm in question is dominant.[176]

Did the High Court err in concluding that the Commission had proved that the Telecom pricing in the two-tail scenario in fact relevantly breached ECPR?

[162] The High Court accepted evidence that, in the wholesale market outside major CBD areas for data tails, Telecom had offered data tails to TSPs at prices above ECPR "in virtually every scenario" when Telecom supplied both tails in a two-tail circuit.[177] The prices often exceeded Telecom's price to retail customers for the equivalent end-to-end circuits.[178] This was because Telecom's pricing involved treating a TSP as if it were in effect obtaining two end-to-end services with charges for access and transmission essentially doubled.[179]

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[174] Telecom refers to three assumptions that it says were identified by the experts: differentiated products at the retail level; stimulation (that is, that the access seeker would cannibalise the sales of the access provider); and that the access seeker cannot be profitable at ECPR prices, because of its additional cost of functioning or being in business.

[175] Referring to the *0867 Case*, above n 91, at [23] and [35].

[176] *0867 Case* at [29], referring to *NT Power* (HCA), above n 158, at [147], where the High Court of Australia discussed *Melway*, above n 165. In *Melway* the Court had said that there was a need for economic analysis of sufficient cogency showing how firms would behave in the hypothetical market: at [52].

[177] Liability Judgment, above n 6, at [132].

[178] Ibid.

[179] Ibid.

[163] As we mentioned above, the two-tail scenario referred to the situation where Telecom provided all the tails in a TSP's customer network, whether two or more, and the TSP did not self-provide any tails. In contrast, in the one-tail scenario, where a TSP self-provided one or more tails and Telecom supplied the remainder, the Court did not find that there had been ECPR breaches.

[164] In the High Court, Telecom submitted that violations in the two-tail scenario were insufficient to establish use of a dominant position, because the violations could not be viewed in isolation from Telecom's pricing over the variety of data transmission service offerings in the market.[180] The High Court rejected this argument, holding that its finding that there were violations of ECPR in virtually every scenario in the two-tail case was sufficient to establish a relevant breach of ECPR.[181] The Court said that pricing at above ECPR would have the effect of discouraging efficient competition for backbone services and in the retail data services market. Rivals would have higher costs than Telecom, and potential entrants would be discouraged or would enter on a smaller scale.[182] The Court said that these exclusionary outcomes could still be expected, albeit on a reduced scale, when violations were confined to the two-tail scenario.

Telecom's argument

[165] Telecom argues that the High Court erred in concluding that the Commission had proved that Telecom pricing in the two-tail scenario relevantly breached ECPR. It makes a number of submissions in support of this argument.

[166] First, Telecom submits that an incumbent's breach of ECPR must be determined from the aggregate of ECPR calculations over the full wholesale market (the "whole of the market"). Such an approach would require consideration of all data tails leased by TSPs from Telecom in the data tail wholesale market outside major CBD areas, rather than confining the analysis to the two-tail scenario. Telecom submits that this approach would reveal that there was no relevant breach of ECPR in the data tail wholesale market, because unlawful gains arising from two-tail

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[180] At [130].
[181] At [131]–[133].
[182] At [133].

violations of ECPR were outweighed by compliance with ECPR in the one-tail scenario.

[167] Secondly, Telecom submits that the Commission had to prove the alleged price squeeze by reference to the number, configuration and distribution of data tails purchased by TSPs from Telecom. Telecom says that the Commission's failure to provide this evidence meant that the magnitude and distribution of ECPR violations could not be known. Telecom also submits that the High Court erred in holding that, as long as non-compliance with ECPR pricing is "more than *de minimis*", it may found a breach of s 36.

[168] Telecom's next submission is that ECPR cannot be legitimately applied to the two-tail scenario because it is inherently inefficient (as it is duplicative of infrastructure engaged in the end-to-end retail circuit, without any countervailing saving from self-provision), and an equally efficient T3 could not compete with T1 (or T2) in the two-tail scenario.

[169] Telecom also submits that, when data services are supplied to a customer as part of a bundle (including voice and/or internet services), the profits lost on all services, not just the data service component, should be reflected in Telecom's opportunity costs of supply and thus the calculation of the ECPR price.

[170] Finally, Telecom submits that the High Court overstated the extent of ECPR violations in the two-tail scenario because the retail price of a VBR service should not have been used to determine the ECPR price for CBR tails.

Our assessment

(a) Breach in the aggregate

[171] Telecom's argument that the Commission had to prove a breach of ECPR in the aggregate, off-setting the two-tail and one-tail scenarios, was rightly rejected by the High Court.[183] There is no established principle requiring aggregation.

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[183] At [130]–[132].

[172] It is convenient to consider the European and United States cases and their relevance, as Telecom argues that these cases support the adoption of a "whole of the market" approach. Telecom submits that the approach in Europe and the United States reflects an underlying policy that competition law should not interfere with conduct that occasions no harm to the competitive process. Absent proof of a price squeeze in the aggregate, no harm to the competitive process, by the exclusion of equally efficient competitors, can be demonstrated.

[173] *Deutsche Telekom* involved the supply of a single wholesale service: local loop access to the incumbent firm's retail competitors. This wholesale service was used to provide a number of derivative retail services: access to analogue, integrated services digital network and asymmetrical digital subscriber line connections. In order to examine whether the incumbent had engaged in an abusive price squeeze, a "weighted" or "aggregated" approach was adopted whereby the regulated single charge for the upstream wholesale input was compared with the average price of the incumbent's range of retail services.[184]

[174] The EC Commission explained that the aggregated approach was based on the principle that the incumbent's pricing structure must enable competitors to compete with it effectively, and at least to replicate its customer pattern.[185] By considering whether there was a sufficient margin between the relevant wholesale price and the average price of all the retail products, the EC Commission could analyse whether an equally efficient competitor was able to replicate the incumbent's product pattern profitably, even if the competitor derived a loss for one of the products. A competitor was unlikely to be prevented from competing due to the manner in which the incumbent had priced one of its products if there was a range of related products in the same market where the competitor could earn adequate returns overall.

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[184] *Deutsche* (EC Commission), above n 129, at [111].
[185] At [127].

[175] In *Wanadoo*, a price squeeze was alleged in relation to the incumbent firm's retail prices[186] and its prices for two wholesale products: national wholesale offers and regional wholesale offers. Alternative operators generally entered the retail market on the basis of national wholesale offers, and, as their customer base increased, some of them gradually climbed up the "investment ladder" by rolling out networks and equipment in order to contract the incumbent firm's regional wholesale offer.[187]

[176] The incumbent firm argued that its two wholesale products belonged to the same relevant market because they were substitutable, in the sense that a small but significant increase in one of the wholesale products' price would result in an increase of the demand of the other wholesale product. The EC Commission rejected this argument. It said that alternative operators that rely on national wholesale offers (and consequently do not have their own network) to penetrate the broadband retail market would not decide to make considerable investments in rolling out a network just because there was a small but significant increase in the price of the national wholesale offer.[188] Conversely, in view of the sunk costs associated with rolling out a network in order to contract the regional wholesale offer, alternative operators would capitalise on their investment rather than concentrating traffic at a unique national access point.[189]

[177] The EC Commission conducted its price squeeze analysis on the basis of an aggregated approach to the incumbent's retail products. Thus, in order to determine whether the incumbent's retail prices were replicable by an equally efficient competitor on the basis of the national wholesale product on the one hand, and the regional wholesale product on the other hand, the EC Commission compared the price for the two wholesale products with the aggregate of several retail broadband products offered in the retail market.[190] The EC Commission concluded that the

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[186] The relevant retail market comprised all the non-differentiated broadband products marketed in the "mass market" for both residential and non-residential users: *Wanadoo*, above n 133, at [153].

[187] At [96].

[188] At [185].

[189] At [187].

[190] At [388].

incumbent's retail prices were not replicable by an equally efficient competitor on the basis of either upstream product.

[178] The EC Commission rejected an argument raised by the incumbent that the Commission should adopt an aggregated approach to the wholesale products. The incumbent had argued that, in order to operate on the retail market, competitors do not rely on a single specific wholesale product but on a mix of wholesale inputs.[191] The EC Commission said that it was appropriate to examine whether the incumbent's retail prices could be replicated on the basis of each of its non-substitutable relevant wholesale products taken one by one, as opposed to any specific mix of its upstream products.[192] This was because it was necessary that there should not be any price squeeze in relation to any "step" of the "investment ladder" (that is, in relation to any wholesale product).[193] If there was such a price squeeze, new entrants that were climbing the ladder of investment would be foreclosed.[194]

[179] In the United States, as we mentioned above, price squeezes are considered under a predatory pricing framework.[195] The claimant must show that the "overall prices" charged by the incumbent in the relevant market are predatory. The inquiry is "whether, given the aggregate losses caused by the below-cost pricing, the intended target would likely succumb".[196] The United States courts have been wary of claimants' attempts to prove predatory pricing through evidence of a low price charged for a single product out of many, or to a single customer.[197] This is because the pricing of one product at a predatory level would not necessarily drive out rivals

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[191] At [390].
[192] At [396].
[193] At [392].
[194] Ibid.
[195] See our discussion of *Linkline*, above n 105, at [109]–[112] above. To establish a predatory pricing claim, the claimant must prove that: the prices complained of are below an appropriate measure of the dominant firm's costs (that is, the average incremental cost of the dominant firm's downstream operations); and the dominant firm had a reasonable prospect of recouping its investment in below-cost prices: *Brooke Group*, above n 121, at 2587–2588.
[196] *Brooke Group* at 2581.
[197] *Morgan v Ponder* 892 F 2d 1355 (8th Cir 1989) at 1362. See also *Taylor Publishing Company v Jostens Inc* 216 F 3d 465 (5th Cir 2000) at 479 and *International Travel Arrangers v NWA Inc* 991 F 2d 1389 (8th Cir 1993).

who were selling a full line, unless this placed the overall price at a predatory level.[198]

[180] In summary, *Deutsche Telekom, Wanadoo* and the United States predatory pricing cases indicate that price squeeze analyses should be conducted on the basis of an aggregated approach to the incumbent's retail prices. In the present case, there were two wholesale scenarios (the two-tail and one-tail scenarios) that could be used to provide multiple retail services (for different types of transmission pathways and speeds). The High Court accepted evidence that Telecom had offered data tails to rivals at above ECPR prices in virtually every scenario when Telecom supplied both tails in a two-tail circuit. This was essentially a finding that there was a breach of ECPR in the two-tail scenario across the aggregate of retail services.

[181] In our view, this finding was sufficient to reach the conclusion that Telecom's pricing in the wholesale market outside major CBD areas for data tails was above that which a non-dominant firm in a hypothetical competitive market would charge (so as to establish Telecom's use of a dominant position).

[182] It would not be appropriate to adopt an aggregated approach to the wholesale products so as to "off-set" violations in the two-tail scenario with compliance in the one-tail scenario. Each wholesale product should be assessed individually. The two-tail and one-tail scenarios are not substitutable in the sense that an increase in one of the wholesale products' price would result in an increase of the demand of the other wholesale product.

[183] Another way of expressing this point is to note that the two-tail scenario is below the one-tail scenario on the ladder of investment. A TSP that relies on Telecom to provide all data tails in a circuit to penetrate the retail market would not decide to (or perhaps more importantly, would not be able to) make considerable investments to self-provide part of the network in order to receive one-tail pricing because of two-tail pricing violations. Similarly, in view of the sunk costs associated with self-providing part of the network, it would not make economic sense for a TSP

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198 *Janich Bros Inc v The American Distilling Co* 570 F 2d 848 (9th Cir 1977) at 856, quoted with approval in *Bayou Bottling Inc v Dr Pepper Company* 725 F 2d 300 (5th Cir 1984) at 305.

that has already invested in the roll-out of a network to bear the opportunity cost of not using its network and instead seek two-tail pricing because of one-tail pricing violations.

[184] A breach of ECPR in the two-tail scenario, across the aggregate of retail services, would prevent or deter an equally efficient competitor from providing the derivative retail services. Pursuing the analogy, it is no answer to this to say that that competitor could still compete if there is another wholesale service higher up the investment ladder that would allow the competitor to offer retail services where it could earn an adequate rate of return. In markets where large, sunk costs are involved, competitors who are climbing the investment ladder would be foreclosed due to a price squeeze in relation to any of the steps in the ladder.

[185] As Professor Ordover explained, a significant breach of ECPR cannot be excused by other instances of compliance or by resort to a "whole of the market" approach. Professor Ordover said:

> if the product is actually priced at a level exceeding ECPR then some equally efficient competitors will be driven out no matter how much room there is to cross-subsidise. Cross-subsidis[ing] is not necessarily an efficient arrangement and … pricing above ECPR puts a competitive floor on what the efficient rival can do.

[186] Finally, we also accept the Commission's submission that the evidence in the present case did not demonstrate that Telecom's pricing in the one-tail scenario created a profit margin for TSPs that could be used to recover the two-tail losses. We accept the Commission's submission that there was unchallenged evidence that TelstraClear, the only TSP that had some access network of its own, was significantly affected by the two-tail breaches, as it was unable to bid for business where all the tails in a customer network had to be acquired from Telecom. We also accept there was unchallenged evidence of one-tail violations of ECPR for a substantial number of higher speed tails, particularly 2 Mbps circuits.[199]

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[199] We understand that the two megabits per second circuits were important to TSPs and that the wholesale revenue derived from these circuits made up a significant proportion of TSPs' total revenue.

(b) Level of proof and the *de minimis* approach

[187] As to level of proof, we consider that Telecom is wrong to suggest that the Commission had to prove the price squeeze by reference to the number, configuration and distribution of data tails purchased by TSPs from Telecom.

[188] First, that would have been a difficult, error-prone and unreliable exercise. The Commission was right to rely on Professor Gabel's modelling analysis, which had integrity, as it was based on Telecom's retail and wholesale offerings and prices, and Telecom's costs. Similarly, proof of the price squeezes in *Deutsche Telekom*, *Wanadoo* and *Teliasonera* was based on the incumbent's prices and costs.

[189] Secondly, the number and distribution of two-tail data tails purchased by TSPs over the relevant period was necessarily reduced and distorted by the exclusionary effect of the price squeeze. As the Commission points out, the two-tail breach was exclusionary conduct. Thus the key issue was not how many two-tail data tails Telecom in fact sold, but rather the number that were not sold because of the price squeeze. We agree with the Commission's submission that Professor Gabel's evidence of what was offered by Telecom during the relevant period, rather than what was purchased, is the best measure.

[190] We also do not accept Telecom's submission that the High Court erred in holding that, as long as non-compliance with ECPR pricing is "more than *de minimis* it may found a breach of s 36".[200]

[191] The *de minimis* approach operates as an exception. As we noted above,[201] Professor Ordover considered that, by overpricing relative to ECPR, there was a real and credible danger of excluding equally or more efficient competitors from the market. However, he accepted that there was a *de minimis* exception, whereby a breach of ECPR in the relevant market might not amount to a use of dominance if the breach was too slight and insignificant (the example he gave was if one tail out of 100,000 tails was overpriced relative to ECPR).

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200 Liability Judgment, above n 6, at [131].
201 At [185] above.

[192] Telecom submits that the *de minimis* approach is "inconsistent with international competition law jurisprudence", namely the "whole of the market" approach. However, as we have explained above, contrary to Telecom's contention, the approach followed in the European cases and United States predatory pricing cases requires an aggregated approach to retail products or services, rather than an aggregated approach to wholesale products. The *de minimis* approach is not inconsistent with such an approach. The rationale behind the aggregated approach and the *de minimis* approach is the same: a conclusion that there has been a use of dominance cannot be justified if the breach is too slight or insignificant.

[193] Telecom also says that, in any event, the assessment of the *de minimis* threshold requires the Court to know the number, configuration and distribution of data tails purchased by TSPs from Telecom, and that without this data, there is no basis upon which: (a) the significance of an abstract ECPR price breach can be assessed; or (b) the conclusion that the breach is material can be reached.

[194] We consider that this level of detail is unnecessary for determining the significance of the ECPR breach in the two-tail scenario. Professor Gabel had concluded that all usable[202] data tails in the two-tail scenario offered by Telecom to TSPs had breached ECPR. His modelling analysis demonstrated that there was a price squeeze for all speed combinations and scenarios (except one) during the relevant period. As we mentioned above,[203] the two-tail breach was exclusionary conduct, so it was Professor Gabel's evidence of what was offered by Telecom during the relevant period, rather than what was purchased, that was important.

[195] We also note that the *de minimis* exception does not require a breach to be of greater substance than is needed in order to take the breach out of the *de minimis* category. This was explained by the High Court in *New Zealand Co-operative Dairy Co Ltd v Commerce Commission*,[204] albeit in the context of determining whether a

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[202] Professor Gabel found ECPR violations in the first three scenarios he developed when analysing the two-tail circuits, but not in the fourth scenario he developed. However, this fourth scenario applied only to variable bit rate tails using Asynchronous Transfer Mode access, which was not a viable option for TSPs over the relevant period. The fourth scenario was apparently included in Professor Gabel's analysis for completeness only.

[203] At [189] above.

[204] *New Zealand Co-operative Dairy Co Ltd v Commerce Commission* [1992] 1 NZLR 601 (HC).

merger proposal between two co-operative dairy companies would result in a party "strengthening a dominant position in the market". The Commission had refused to authorise the proposal, as it had concluded that the proposed merger would result in the exclusion of alternative suppliers and the significance of this constraint was markedly more than *de minimis*.[205] The High Court said that the term "*de minimis*" referred to a change so slight and insignificant as not to justify the intervention of the law. It did not consider it appropriate to introduce the concept of something of greater substance than was necessary merely to take the change out of the *de minimis* category.[206]

[196] In any event, we accept the Commission's submission that the two-tail breach of ECPR demonstrated by Professor Gabel was far more than *de minimis*. It was a significant breach. It was a "universal" breach of ECPR in that it applied to all usable data tails offered by Telecom over the relevant period, for all speed and transmission pathway combinations. This was not contested by Mr Fraser (an economist employed by Telecom), as the High Court noted.[207] Professor Gabel also gave unchallenged evidence that the breach of ECPR applied no matter how many tails were added to the customer network.

[197] The price squeeze was so severe that the CDP pricing also "consistently"[208] exceeded Telecom's retail prices. Professor Gabel gave uncontested evidence that the CDP pricing of 64 kbps tails exceeded the retail price of the faster 128 kbps service. If the wholesale price exceeds the retail price in the two-tail scenario, that is necessarily also a breach of ECPR. This is because under the (agreed) ECPR formula the wholesale price should be less than the retail price unless the avoided backbone and retail costs (combined) are less than the incremental cost of providing access, which was not the position in this case.

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205 *New Zealand Co-operative Dairy* at 608.
206 At 619–620.
207 Liability Judgment, above n 6, at [88].
208 Liability Judgment at [124].

(c) Were two-tail providers inherently inefficient?

[198] Telecom submits that ECPR cannot be legitimately applied to the two-tail scenario, because it is inherently inefficient, and an equally efficient T3 could not compete with T1 (or T2) in the two-tail scenario. This issue was not debated amongst the experts in the High Court hearing.

[199] Telecom submits that the two-tail scenario is inherently inefficient because it is duplicative of infrastructure engaged in the end-to-end retail circuit, without any countervailing saving from self-provision of the core transmission network. Telecom says that, because any HSDT service supplied by a TSP requiring two tails would inevitably involve more network elements than Telecom itself required, TSPs would have no prospect of competing out any supra-competitive profits earned by Telecom.

[200] In the two-tail scenario, a TSP purchases two tails from Telecom to connect customer sites to either its own backbone network, or to another TSP's backbone network, and thus provide a single HSDT retail service (AD). The "area of competition" at the retail level is thus the backbone network (BC compared with XY).[209] Telecom points to evidence given by Mr Emanuel, the Commission's technical expert, which characterised this area of competition as limited. Telecom says that because the backbone network had very low variable costs, an entrant without an access network had no prospect of ever competing away Telecom's monopoly rents. It also says that the ECPR price for two-tail circuits would inevitably be higher than the ECPR price for the ABCD circuit for resale because the avoided incremental costs of the backbone were outweighed by the additional costs to Telecom in connecting the TSP's POP to the Telecom network.

[201] Telecom submits that one TSP, Attica Communications Ltd, provides an example of a rival that had no realistic prospect of competing on the basis of network efficiency because it lacked any access or backbone network.

[202] In our view, Telecom's arguments are without merit. First, the objective of constructing the counterfactual scenario is to ascertain the price that a non-dominant

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209 Refer to the diagram set out at [33] above.

T1 would charge for data tails to an equally efficient T3. The objective is not to construct a scenario where T3 can compete out T1's monopoly profits. When constructing the hypothetical competitive market, all elements of a firm's dominance must be removed[210] and so monopoly profits would not be present. Accordingly, the ability (or inability) of a TSP to compete out Telecom's monopoly profits has no bearing on whether the two-tail scenario can provide an appropriate counterfactual analysis.

[203] Secondly, as the Commission points out, an efficient new entrant could find it profitable to compete if its backbone and retail costs along with incremental costs of connection are less than the incumbent's marginal backbone and retail costs. Telecom's focus on the limited area of competition in the backbone network ignores a TSP's ability to compete with it in two main areas: the backbone and the provision of retail support. It is accepted by the Commission that potential savings in relation to the production costs in the backbone are not high. However, competition in respect of the backbone service can be effective through the TSP differentiating its service on the backbone. Efficiencies may also be obtained from retail support, in the area of marketing and customer care (such as improved customer service). The new entrant who is more efficient in one or both of these areas of competition and can produce the final retail product at a lower economic cost will compete effectively in the retail market.

[204] We also note that, whilst Telecom seeks to portray Attica as an inefficient rival, Professor Gabel strongly disagreed with this suggestion. Whilst Attica had no access or backbone network, we accept the Commission's submission that Attica may have been able to operate more efficiently than Telecom by, for example, differentiating its service and having a smaller number of skilled staff providing customer service across the entire product range.

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[210] *0867 Case*, above n 91, at [36]. See also *Turners & Growers Ltd v Zespri Group Ltd* HC Auckland CIV-2009-404-4392, 12 August 2011 at [342].

(d) Bundled services

[205] As we noted above,[211] the High Court said that the Commission was not given proper notice that the issue of bundled services would be raised, so the issue could be disregarded for the purpose of calculating the ECPR price.[212] The Court said that there was no pleading of a market for bundled services; rather, the product market was admitted to be HSDT services. It considered that references in the briefs of evidence were insufficient to amount to notice that the issue would become a major plank in Telecom's defence. The Court said that the Commission was undoubtedly prejudiced as a result, as the scope of discovery and evidence of fact would have been affected and the opportunity to brief experts before the hot tub was lost.[213]

[206] The High Court considered that, in any event, the ability to make data sales was not essential to the sale of voice or internet services.[214] The incumbent lost the ability to offer a bundle of services when it lost a data service customer, not the ability to offer other components of the service such as voice or internet. The Court said that, if the incumbent is to be compensated for losing a data service customer, "it is only to the extent of the additional profit derived from supplying the services as a bundle".[215] However, neither party had attempted to quantify the additional value placed by customers on having downstream services bundled, and the Court concluded that there was no risk that ECPR prices calculated by the Commission were materially understated on this account.[216]

[207] Telecom says that it did not need to plead affirmatively a retail market for bundled services and that it was sufficient that there was evidence before the High Court that suggested that the supply of voice and internet services was frequently important to the supply of HSDT services. It submits that the High Court erred in finding that, where the customer relationship in relation to bundled services was lost as the result of supply of a data tail, this did not have to be reflected in Telecom's

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[211] At [50] above.
[212] Liability Judgment, above n 6, at [67] and [123].
[213] At [67].
[214] At [70].
[215] At [71].
[216] At [72].

opportunity costs and thus the calculation of the ECPR price. Telecom says that this error meant that the Court overstated the extent of ECPR violations in the two-tail scenario.

[208] We accept that Telecom is correct in its contention that it did not need to plead affirmatively that there was a retail market for bundled services. A retail market for HSDT services had been pleaded by the Commission (and admitted by Telecom) in order to identify an "effects" (or "impact") market. That is, the Commission had alleged that Telecom had used its dominant position in the wholesale market for data tails outside major CBD areas for the purpose of deterring potential or existing competitors in the retail market for HSDT services (and the wholesale market for backbone transmission services). ECPR prices are calculated by reference to opportunity costs, and thus the relevant retail products into which the wholesale HSDT service is an input. We accept Telecom's submission that the relevant retail products do not necessarily have to be those products within the "effects" market.

[209] However, whilst we do not consider that Telecom needed to plead that there was a market for bundled services, in our view the High Court correctly held that Telecom's references to evidence that the supply of voice and internet services was frequently important to the supply of HSDT services were insufficient to amount to notice that the issue of lost profits in relation to bundled services would become an important part of Telecom's arguments. As the Commission points out, the evidence referred to by Telecom was at a high level of generality, and Telecom did not provide any empirical data on the profits foregone on these other services.

[210] Because we agree with the High Court's conclusion that the issue of bundled services could be disregarded because the Commission was not given proper notice that the issue would be raised, we do not need to consider whether Telecom's opportunity costs should include foregone revenues on services that are bundled with data services, such as voice and internet. However, we would in any event have accepted the Commission's submission that Telecom had provided no evidence on the extent of bundling and that the High Court correctly concluded that any additional value placed by customers on bundling would not be significant.

(e) CBR vs VBR

[211] We do not accept Telecom's submission that the High Court overstated the extent of ECPR violations in the two-tail scenario because the retail price of a VBR service should not have been used to determine the ECPR price for CBR tails.

[212] Professor Gabel had priced many of his ECPR simulations on the basis that a CBR tail was provided for use in a VBR end-to-end service. This meant that the retail price used for the calculation of the ECPR price of a CBR tail was derived from the retail price of a VBR service.

[213] In the High Court, Telecom argued that, because the CBR input could be used by TSPs to provide a higher priced CBR service, the appropriate retail price for the calculation of ECPR should be derived from the retail price of a CBR service. Telecom argued that the lower ECPR price of a CBR input that resulted from using the VBR retail price would provide TSPs with an artificial price advantage – an arbitrage opportunity – in providing CBR services.

[214] The Court dealt with this issue at length.[217] The Court said that any loss of ability to price different downstream products differently was irrelevant to the central issue of whether there had been a breach of s 36. The issue was whether a non-dominant firm would supply tails to a rival in the counterfactual and the downstream pricing consequences of that were immaterial.[218]

[215] The Court said that, although TSPs used CBR tails, they generally offered a VBR service to customers.[219] The Court concluded that the appropriate basis on which to determine ECPR prices was the retail price of a VBR service actually provided, notwithstanding that it utilised CBR inputs.[220] The Court assumed that, prior to leasing a data tail to a TSP for use in a VBR retail service, Telecom would have also used that data tail to provide a VBR retail service, because a customer would be unlikely to change the nature of its end-to-end service upon switching from

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217 At [78]–[85] and [105]–[110].
218 At [84].
219 At [79].
220 At [85].

Telecom to a TSP. Telecom's true opportunity cost of supplying a data tail to a TSP should therefore only reflect the loss of ability to provide a VBR retail service.[221]

[216] Telecom argues that there was no evidence that TSPs exclusively provided VBR retail services. Telecom alleges that Clear provided CBR retail services. However, the evidence given by Ms Hindle (Clear's Data Services Manager over the relevant period) was that:

> The data connections Clear leased from Telecom were all CBR connections. None of those CBR circuits were used by Clear to provide end-to-end CBR services to customers… Clear Line services (the equivalent of Telecom's CBR end-to-end service) were generally all Clear build as they were high speed of 2Mbps. These were located in the major CBDs …

[217] In light of this, we do not consider that this Court should depart from the High Court's finding that the calculation of the ECPR price of a CBR tail should be derived from the retail price of a VBR service. We accept the Commission's submission that there was no evidence of arbitrage having actually occurred. We also accept the Commission's submission that, even if there was a real risk of arbitrage, and thus a loss of ability to price discriminate downstream products, this does not alter the conclusion as to whether a non-dominant firm would supply tails to a rival in the counterfactual. As Professor Ordover explained, the question for T1 is simply "whether it will get some revenue from the sale … or lose the sale entirely".

Additional issues

Settlement agreement

[218] In September 2000, Telecom and Clear reached a settlement that specifically included CDP pricing as part of settling a wide range of issues. In the High Court, Telecom argued that any claim that Telecom unlawfully exercised its market power in relation to Clear must end on 1 October 2000, when the settlement agreement came into effect. Telecom also argued that the agreement was relevant in

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[221] At [106].

considering Telecom's exercise of market power in relation to other TSPs after that date.

[219] The High Court held that, while the settlement agreement between Telecom and Clear involved compromises for both parties, and Clear agreed to CDP pricing for the purpose of settling a range of issues, that was irrelevant to the question of whether Telecom's data tail prices were ECPR-compliant in the first place, and the implications for the competitive process if they were not.[222]

[220] Telecom submits that the High Court erred in holding that the settlement agreement between Telecom and Clear was irrelevant. We do not accept that submission. The settlement agreement between Telecom and Clear did not make any change to existing CDP pricing offers, so it did not remove the fundamental complaint that the price of two data tails was higher than the retail price of the equivalent end-to-end service.

[221] We accept that the Commission's claim under s 36 is concerned with the anti-competitive pricing of data tails in the wholesale market, the impact of that in the retail market and the effect of competition in those markets. A settlement agreement that Telecom entered into with a TSP had no effect on Telecom's unlawful pricing or its impact and effect.

Avoided costs

[222] The Commission submits that the 8.32 per cent discount accepted by the High Court for Telecom's avoided costs for the marketing of its retail service to customers[223] should be adjusted upwards.

[223] The experts had disagreed on the appropriate measure of Telecom's avoided marketing costs. They disagreed as to whether the 8.32 per cent figure used by Mr Fraser had already allowed for the additional marketing costs incurred at the wholesale level, and if not, whether an adjustment of two per cent was appropriate. The experts for the Commission said that a further adjustment to 8.32 per cent was

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222 At [165].
223 At [92]–[97].

required to make allowance for the additional marketing costs, preferring a figure in the vicinity of 16 per cent (which has been adopted in other jurisdictions, including the United States).

[224] The High Court held that, in the absence of evidence that wholesaling costs were omitted when sales and marketing costs were calculated, it would assume that they had been included and made no further allowance on that account.[224] The Court acknowledged that the 8.32 per cent figure was "conservative", but said that there was no empirical evidence that would permit the Court to adopt a higher figure.[225]

[225] The Commission has not pointed to any specific reason why the High Court's finding on this matter was in error. We can see no basis for altering the Court's finding.

Did the High Court err in concluding that the Commission had not proved that the Telecom pricing in the one-tail scenario breached ECPR?

The High Court judgment

[226] As we mentioned above,[226] the High Court did not make a finding that there were ECPR violations in the one-tail scenario. The High Court concluded that, in the one-tail scenario, Telecom was entitled to recover from a rival the profit foregone on the entire network. The Court said that pricing of data tails on this basis would not preclude entry by a more efficient rival.[227] The Court sought to demonstrate this by the use of examples that assumed a five-tail customer network.[228] In the Court's view, the examples showed that ECPR pricing does not prevent a more efficient entrant from building its own access network, as the incentive to do so is driven by any efficiency advantages an entrant may have.[229]

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224 At [94]. The Court made a similar finding in relation to Telecom's customer care costs: at [96].
225 At [97].
226 At [49] and [163] above.
227 At [60].
228 At [55]–[59].
229 At [59].

The parties' arguments

[227] Telecom supports the Liability Judgment on this issue. It says that the Commission seeks to impose additional conditions for the application of ECPR that destroy its central and informing "indifference" (opportunity cost) principle. It also argues that the Commission failed to adduce the evidence necessary to calculate ECPR in the one-tail scenario.

[228] The Commission submits that the High Court's examples of one-tail pricing were an incorrect application of ECPR principles because they ignore the significant sunk and fixed costs associated with operating a network. The Commission argues that the High Court concentrated on the "indifference" aspect to the exclusion of the other objectives endorsed by the Privy Council in *Telecom v Clear*, namely: encouraging efficient entry, ensuring a dominant firm does not charge its competitors more than it charges itself and ensuring the eventual competing out of monopoly profits.

[229] The Commission further submits that the High Court approach would effectively reward Telecom for imposing the two-tail price squeeze and forcing TSPs to build their own tails when it may otherwise have been more efficient for them to lease tails from Telecom. The Commission also says that allowing the inclusion of the profit foregone on the entire network cannot survive in the counterfactual because rivalry from T2 would prevent T1 from raising the wholesale price to recover its foregone profits on T3's self-provided tails.

Our assessment

(a) Were the High Court's examples of one-tail pricing inconsistent with ECPR principles?

[230] We do not accept the Commission's submission that the High Court's examples of one-tail pricing do not accord with ECPR because they ignore the fixed (including sunk) and common costs associated with operating a network.

[231] In our view, the High Court's examples of one-tail pricing were a correct application of ECPR principles. It is only the incumbent's costs that are relevant in calculating ECPR prices and not the rival's costs. A rival's sunk costs do not need to be taken into account when determining the ECPR price, for the reasons explained by Professor Kahn and Dr Taylor in "The Pricing of Inputs Sold to Competitors: A Comment".[230] They said that, if an incumbent could profitably retain competitive business at prices covering only its marginal costs but the entrant required some larger markup in order to recover for itself some of its fixed, common costs, then it is inefficient for society to make it possible for the latter to do so. It would involve the wasteful duplication and incurrence of new, additional common costs of facilities and activities already provided by the incumbent.

[232] Indeed, during the High Court hearing, Professor Gabel accepted that his approach to calculating the ECPR price in the one-tail scenario (whereby the incumbent would not be able to recover the opportunity cost for tails that are self-provided by a TSP) was a departure from the underlying ECPR principle that the incumbent must be indifferent:

> Professor Richardson:
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> > … I guess my confusion is that – the way you've characterised the appropriate pricing for providing one tail into a two-tail circuit where the other is self-provided, doesn't appear to leave the incumbent indifferent. The price it's charging for that single circuit is not covering the opportunity cost it's losing – sorry, for that single tail for the entire circuit so it would be worse off in price?
>
> Professor Gabel:
>
> > The way I believe it should be implemented, it should not be allowed to recover profit … associated with the leg where there is self-provision. So in that sense, yes, it's now not profit indifference, and as I stated yesterday, I've recognised that tension … therefore what I am doing, I recognise is stepping away from complete profit neutrality.

(b) Would the inclusion of profit foregone on Telecom's entire network in the ECPR price lead to the exclusion of competitors?

[233] We consider that the Commission's real complaint is not that the inclusion of profit foregone on Telecom's entire network in the ECPR price is inconsistent with

[230] Kahn and Taylor, above n 34, at 237–238, quoted in the Liability Judgment at [62].

ECPR principles. Rather, the Commission's main concern appears to be that, by allowing Telecom to recover the profit foregone on the entire network in the one-tail scenario, the application of ECPR to the present case allows Telecom to arrive at a price that would effectively preclude competition. Professor Gabel's view was that, under the pricing endorsed by the High Court, no TSP would enter the market unless it had a ubiquitous network. He therefore considered that such pricing would "effectively exclude rivals". The Commission submits that such an outcome is not only inconsistent with the Privy Council's judgment in *Telecom v Clear*, but that it is also inconsistent with the objective of s 36.

[234] The Commission submits that the High Court implicitly assumed that the entrant did not have any fixed and common costs. In the examples given by the High Court[231] Telecom would have a $4 margin to help cover its fixed and common costs. The entrant TSP would only have $1 (equal to Telecom's marginal cost) to cover its fixed and common costs. In the Commission's submission, an equally efficient TSP would be unable to enter unless its fixed and common costs were less than the incumbent's marginal costs, which would never occur in an industry such as telecommunications. The Commission notes that Professor Hausman repeatedly emphasised in his evidence that there was a high proportion of fixed costs in this industry.

[235] We accept the Commission's submission that it would be a misreading of *Telecom v Clear* to suggest that their Lordships were endorsing the use of ECPR to arrive at a price that would preclude competition. In *Telecom v Clear*, Clear was able to compete with Telecom even though the access price, calculated in accordance with ECPR, preserved monopoly rents. Their Lordships regarded it as important that Clear had not produced any figures to support the claim that Telecom's charges would be so high that Clear would be unable to enter the CBD market at all.

[236] In our view it is implicit in the Privy Council's decision that an incumbent cannot charge a price above which a rival is unable to compete. We note that Professor Ahdar argues that the Privy Council's concentration on total prevention of entry is misplaced. He says that s 36 is not concerned solely with conduct that

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[231] See at [48] above.

totally precludes competition but also embraces conduct that seriously restricts or deters competition. Thus to speak of a total restriction is to posit the wrong test and make the plaintiff's burden even more formidable than it already is.[232]

[237] We consider that the ECPR pricing accepted by the High Court would result in an inability to compete, even if total prevention of entry is the yardstick. This is for the reasons given by the Commission relating to the high fixed costs in the telecommunications industry.[233] We therefore conclude that it would be inconsistent with *Telecom v Clear* if Telecom was permitted to recover the profit foregone on Telecom's entire network in the one-tail scenario.

(c) Additional considerations

[238] We agree with the Commission that, if this Court endorsed Telecom's one-tail pricing and permitted Telecom to recover the profit foregone on the entire network, this would result in another inconsistency with the Privy Council judgment. Their Lordships envisaged a process of undercutting between Telecom and Clear that would eventually compete out any monopoly profits. We accept the Commission's submission that it is difficult to see how Telecom's one-tail pricing would allow monopoly profits or inefficiencies to be driven out of the market (short of the TSP building a ubiquitous network) as it permits Telecom to raise the wholesale price of its data tails as the TSP's network grows.

[239] We also accept the Commission's submission that Telecom's one-tail pricing seems to result in Telecom charging its competitors more than it does itself for the same services.[234] We note the Commission's submission that in *Deutsche Telekom*[235] the Court gave no consideration to self-provisioned facilities when analysing whether there was a price squeeze. The Court asked whether the incumbent's operations would have been profitable if it had charged itself for access what it charged its competitors. A one-tail scenario was not considered.

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[232] Rex Ahdar "Battles in New Zealand's Deregulated Telecommunications Industry" (1995) 23 Australian Business Law Review 77 at 104.

[233] See at [234] above.

[234] Contrary to what was envisaged by the Privy Council in *Telecom v Clear*, above n 4, at 407. See also at [65] above.

[235] See the references in fn 129 above.

[240] Similarly, Professor Gabel emphasised the need for the ECPR analysis to consider whether Telecom had been charging itself "the same access or interconnection charges as it imposes on its competitors, except to the extent that the (marginal) costs of providing that service to itself and to its competitors differ".[236] He considered that the two-tail scenario provided the "more relevant application of ECPR", as Telecom utilised two data tails in supplying data services to its own retail customers.

[241] Further, we agree with the Commission's submission that allowing Telecom to recover the profit foregone on its entire network in the one-tail scenario effectively rewards Telecom for imposing the two-tail price squeeze and forcing TSPs to build their own tails when it may otherwise have been more efficient for TSPs to lease tails from Telecom.

[242] Finally, it is difficult to endorse Telecom's one-tail pricing in light of the following comments made by an expert witness for Telecom. Dr Taylor said that "it seems like a horrible thing that a TSP does what we like it to do, go out and build its own tails, and yet when they do that the price they pay for the remaining tail goes up. That seems evil".

(d) Was the way in which the High Court applied ECPR in the one-tail scenario inconsistent with the counterfactual?

[243] As we noted above,[237] the use of ECPR to determine the price a firm would charge in a hypothetical competitive market was problematic in *Telecom v Clear* because Telecom was not constrained in its downstream pricing decisions by competition law or a regulator. By endorsing ECPR in those circumstances, their Lordships allowed the inclusion of monopoly profits in a hypothetical competitive market. As we noted, this has been described by a number of academic commentators as a misapplication of the counterfactual test.[238]

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236 Quoting Kahn and Taylor, above n 34, at 227–228.
237 At [85] above.
238 See the references in fn 86 above.

[244] In the *0867 Case*, the Supreme Court noted that there had been criticism of the way in which the Privy Council applied the counterfactual test in *Telecom v Clear*.[239] The Court was not called to comment on that matter, so did not discuss this further. However, the Court stressed that, in determining what a non-dominant firm would do in a hypothetically competitive market, all elements of a firm's dominance must be removed:[240]

> … for the comparative exercise to be effective in identifying when a dominant firm takes advantage of its dominance, the hypothetically competitive market must genuinely deny that firm all aspects of its dominance. The constraints acting upon the firm in the hypothetical market must neutralise the dominance in the actual market.

[245] The comments set out above suggest that the Supreme Court was sympathetic to the criticisms. Clearly, if all aspects of dominance were neutralised, then monopoly profits could not have been sustained. In any event, the Supreme Court clearly endorsed the counterfactual test.[241] It seems therefore that we could not uphold an approach that would clearly not survive the counterfactual analysis.

[246] In this case we accept the Commission's submission that the inclusion of the profit foregone on the entire network in Telecom's one-tail pricing would not survive in the counterfactual, because rivalry from T2 would prevent T1 from raising the wholesale price to recover its foregone profits on T3's self-provided tails. It cannot be assumed that, when T3 self-provides a tail, T1 and T2 will both raise their prices. The Commission gives an example where T3 initially leases three tails from T1. T3 then self-provisions one of the three tails. T3 continues to lease two tails from T1. It is submitted that T1 could not raise the price on the two tails leased to T3 because T2 would not raise its price. This is because T2 has no incentive to do so as it has no foregone profits, since it did not service T3.

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239 *0867 Case*, above n 91, at [14] and fn 15.

240 At [36]. This is similar to the view of the Privy Council minority in *Carter Holt*, above n 31, at [74] and [77] per Lord Scott and Baroness Hale.

241 We note that there has been some criticism of the Supreme Court's confirmation of the counterfactual test as the sole determinant for "use" or "taking advantage of substantial market power". See Paul Scott "Taking a Wrong Turn? The Supreme Court and Section 36 of the Commerce Act" (2011) 17 NZBLQ 260 at 282 and Matt Sumpter "Competition Law" [2012] NZ L Rev 113 at 123.

(e) What is the effect of the above analysis?

[247] Telecom, as noted above,[242] submits that the Commission failed to adduce the evidence necessary to calculate ECPR prices in the one-tail scenario. This appears to be a similar submission to that made with regard to the two-tail scenario which we rejected at [171]–[197] above.

[248] We are, however, left with the difficulty of determining whether Telecom's pricing in the one-tail scenario amounted to a use of its dominant position, given that the parties' evidence (and the Commission's case) focused on whether Telecom's pricing was ECPR-compliant. We have accepted that the recovery of profit foregone on the entire network is in accordance with ECPR.[243] However, we have held that it would not survive the counterfactual test[244] and is in other ways inconsistent with *Telecom v Clear* (in particular, that it would exclude competition).[245]

[249] In the circumstances we consider that we should apply a pragmatic approach and accept Professor Gabel's suggested pricing methodology whereby Telecom should only be able to recover a proportionate profit share on its leased tails.[246] In a memorandum filed after the hearing on wholesale/retail pricing, the parties compared a number of scenario examples against Professor Gabel's example of a 48/128 kbps VBR retail circuit with a local transport step. The wholesale data tails were assumed to be 128 kbps CBR data tails with a local transport step, terminating on a stacked wideband access located at a TSP's POP. The Streamline retail price (of $740) was based on a retail VBR service for A to D (see diagram set out at [33] above).

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[242] At [227].

[243] See at [230]–[232] above. We note, however, that the ECPR calculations likely overstated Telecom's opportunity cost, as the increased possibility of customer churn, through the sale of data services by a TSP to a new customer, would lower the opportunity cost to Telecom of giving up the tail. The High Court acknowledged that this was a "potentially significant factor", but did not consider that there was sufficient evidence to assess the impact of new customers on ECPR prices: Liability Judgment, above n 6, at [76]–[77]. This finding was not challenged in the course of this appeal.

[244] See at [243]–[246] above.

[245] See at [233]–[242] above.

[246] Set out at [46] above.

[250] In the parties' one-tail scenario example (where the TSP self-provides one tail and leases another tail from Telecom), the CDP wholesale price of a 128 kbps CBR data tail (ABX)[247] was $457.67. The ECPR price for this (calculated on Telecom's methodology as upheld by the High Court) was $642, meaning that the CDP price was $184.24 below the ECPR price.

[251] However, if Professor Gabel's pricing methodology is accepted, then Telecom cannot recover the profit foregone on the full retail service (which includes the self-provided tail) but can only recover half of the retail revenue. This means that the relevant comparator retail revenue for A to D becomes $370 (namely half the Streamline retail price that applied to the two-tail circuit). This is less than Telecom's charged CDP wholesale price for the one data tail (ABX) of $457.67.

[252] In terms of this analysis, this means that there was also a price squeeze (and the use of a dominant position) in the example given in the memorandum. We do not understand Telecom to challenge the proposition that, on Professor Gabel's methodology, overall there would be a price squeeze in the one-tail scenario for other transmission pathways and speeds and/or where more than one tail was self-provided.[248]

Did the High Court err in finding that the Commission had proved that the Telecom pricing involved a purpose proscribed by s 36 of the Commerce Act 1986?

[253] For a breach of s 36 to be established, a person with a substantial degree of power in a market must have taken advantage of that power for one or more of the proscribed purposes set out in s 36(2). The word "purpose" requires the conduct producing the consequences to be motivated or inspired by a wish for the occurrence of the consequences.[249] Proof of purpose may turn upon inferences drawn from the conduct of any relevant person or from any other relevant circumstances.[250] It will

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[247] See diagram at [33] above.
[248] Except on the grounds we dealt with at [247] above.
[249] *Union Shipping*, above n 146, at 707.
[250] Commerce Act 1986, s 36B. See also *Union Shipping* at 707. Evidence that an anti-competitive outcome was a substantial purpose of Telecom's conduct is sufficient to establish the requisite purpose: s 2(5)(b) of the Commerce Act 1986.

frequently be legitimate for a court to infer from a firm's use of its dominant position that its purpose was to produce the effect in fact produced.[251]

[254] As we noted above, it was the Commission's case that Telecom used its dominant position for the purpose of preventing or deterring existing or potential TSPs seeking access to Telecom's data tails (and using their own backbone infrastructure) from competing in the retail market for HSDT services and deterring existing or potential TSPs from competing in the national wholesale market for backbone transmission services.

[255] The High Court considered that the readily foreseeable effects of pricing two-tail circuits to TSPs above ECPR and, in many cases, above retail prices, was sufficient to support an inference that Telecom used its dominance for the pleaded purposes.[252] The Court also considered that an anti-competitive purpose was demonstrated by direct evidence of what Telecom's conduct was intended to achieve. The Court said that the way in which Streamline and CDP were introduced and the statements of those responsible for their introduction were consistent with a strategy on the part of Telecom to deny rival TSPs access to data tails at prices that would permit them to utilise and develop their own networks for the purpose of data transmission.[253]

Telecom's argument

[256] Telecom submits that an inference of anti-competitive purpose was not available to the High Court. Telecom says that such an inference was not available because Telecom did not know, in advance, whether its conduct amounted to a "use" of market power, because it did not know the use to which the TSP sought to put the data tails. It also says that the inference was not available because the Commission had not demonstrated that pricing data tails above ECPR caused harm to competition in the overall market. Telecom says that there was only anecdotal or theoretical evidence of exclusionary effects flowing from the alleged price squeeze.

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[251] *Telecom v Clear* (PC), above n 4, at 402.
[252] Liability Judgment, above n 6, at [151].
[253] Ibid.

[257] Telecom also submits that the High Court erred in concluding that there was direct evidence of an anti-competitive purpose. Telecom says that its actual purpose was at all times pro-competitive and commercially rational. It says that there was no relevant delay between the introduction of Streamline pricing and CDP pricing and says that the High Court misconstrued statements made by Telecom personnel responsible for the introduction of Telecom's new wholesale pricing in 1999 as indicating a purpose to avoid price competition.

[258] Finally, Telecom submits that the direct evidence relied on by the High Court related to a period outside the statutory limitation. It says that, pursuant to s 80(5) of the Commerce Act, the Court was unable to consider Telecom's conduct prior to 18 March 2001.

Our assessment

(a) Inference of anti-competitive purpose

[259] We do not consider that Telecom is correct in its contention that an inference of anti-competitive purpose was not available to the Court.

[260] Telecom's argument that it did not, and could not rationally, know in advance in respect of any particular wholesale supply of HSDT services, that its conduct amounted to a "use" of market power (because it did not know the use to which the TSP sought to put the data tails) is a repetition of its argument that it could not calculate ECPR prices in advance because it did not know the use to which the TSP sought to put the tails. We dismissed this argument for the reasons stated at [93]–[103] above.

[261] Telecom's argument that an inference of anti-competitive purpose was not available because the Commission had not demonstrated that pricing data tails above ECPR caused harm to competition in the overall market is a repetition of its "whole of the market" argument. We dismissed that argument for the reasons stated at [171]–[186] above.

[262] In our view, the finding of pricing above ECPR in the two-tail scenario was sufficient to support the inference that Telecom had an anti-competitive purpose. We agree with the Commission that a number of exclusionary effects from pricing data tails above ECPR were readily foreseeable, especially given that Telecom's data tails were an essential input into an HSDT service, and the price squeeze continued for five years. Further, as we have concluded that Telecom's pricing also amounted to a use of its dominant position in the one-tail scenario, our conclusion as to foreseeability is reinforced.

[263] Professor Ordover explained that pricing above ECPR would discourage otherwise efficient backbone providers from entering, and those that did enter would do so at a smaller scale than they otherwise would if the data tails were efficiently priced. We accept that it would be foreseeable that a TSP would be deterred from entering and competing in the retail market because the cost of data tails exceeded ECPR (and, in many cases, retail prices) and the TSP would still have its own retail and backbone costs to cover. We also accept that a TSP would be deterred from competing in the wholesale backbone market because it would be unable to combine the backbone with Telecom's above ECPR price data tails and compete effectively in the retail market.

[264] We also accept the Commission's submission that there were other foreseeable exclusionary effects from pricing data tails above ECPR, namely: driving new entrants out of the retail HSDT services market and wholesale backbone market; foreclosing competitors from bidding for new business where all data tails in the network need to be purchased from Telecom; and discouraging competitors from utilising and developing their own networks for the purposes of data transmission, and instead limiting their competitive activities to that of reselling Telecom's end-to-end data services.

[265] The Commission relies on anecdotal evidence to demonstrate the exclusionary effects of the two-tail breach. It says that Attica was forced out of the retail market in late 2002 by the Telecom price squeeze. The Commission also says that TelstraClear was foreclosed from bidding for new business where all the data tails in a network needed to be purchased from Telecom. While the Commission

acknowledges that the number of two-tail data tails leased by TelstraClear could not be quantified, it says that this does not mean that the breach did not affect it. The real issue was the number of two-tail data tails that TelstraClear did not lease because of the price squeeze. It says that the evidence shows that TelstraClear could not lease two-tail data tails because they were too expensive.

[266] The Commission also points to evidence that, after Streamline pricing was introduced, TSPs' rates of data growth declined markedly. It says that the fact that TSPs continued to experience some growth does not mean there was no anti-competitive effect. The Commission refers to a comment made by Professor Ordover that the evidence indicated that both retail and wholesale demand would be expected to be higher if Telecom had charged ECPR-compliant prices.

[267] The High Court made no finding as to whether the exclusionary outcomes indicated by the Commission's anecdotal evidence flowed directly from Telecom's pricing policies.[254] The Court acknowledged that a multitude of factors were likely to have contributed in each case. However, it said that they were consequences of the kind that economic theory would predict when prices exceed ECPR and, in some cases, Telecom's retail prices. Other consequences, for example, the discouragement of potential entrants, were by their very nature unobservable.[255] We agree with the High Court's assessment of the exclusionary effects of the two-tail breach.

(b) Direct evidence

[268] We also do not accept Telecom's submission that the High Court erred in concluding that there was direct evidence of an anti-competitive purpose.

[269] Telecom says that its purpose was at all times pro-competitive and points to the fact that it was not disputed that Telecom's lowering of retail prices under Project Nike/Streamline was pro-competitive. However, as the Commission points out, there was never any allegation that Telecom's introduction of Streamline pricing was anti-competitive. It was the reduction of the retail prices coupled with the

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254 At [135].
255 Ibid.

absence of a commensurate reduction in wholesale pricing that constituted the price squeeze.

[270] We also do not accept Telecom's submission that there was no relevant delay in the introduction of CDP pricing to the market because retail markets were not materially affected by Streamline pricing until June 1999 and TSPs had CDP available to them by April 1999. The precise length of the delay between the introduction of Streamline pricing and CDP is immaterial given that Mr Goodin (then Telecom's Strategy and Pricing Manager) accepted that the delay in introducing CDP would have disadvantaged rival TSPs, and Mr Goodman (then Telecom's Business Development Manager) agreed that the secrecy surrounding the introduction of Streamline enabled Telecom to sign up customers before competitors knew what was happening.

[271] We also do not accept that the High Court misconstrued a critical memorandum written by Mr Bruce Parkes (who headed Telecom's Industry Services Unit) and addressed to Ms Theresa Gattung (then the Group General Manager (Services)), dated 11 March 1999.[256] The Court considered that statements within the memorandum indicated a purpose to avoid price competition in the retail HSDT market and only enable competition on service quality. The relevant part of the memorandum says:

> Our negotiations to date with carriers have been to treat them exactly like other large corporate customers …
>
> In my view, carriers such as Telstra are obviously competitors in the retail market for many services but for data they are actually primarily resellers of our retail data services ... and as such are growing the market for our benefit and theirs.

[272] Telecom says that the statements made in the memorandum simply reflected the straightforward proposition that, in the case of resale, it was unlikely that TSPs' costs of retail would be lower than Telecom: thus, the ability to compete on price would be limited. We disagree. In our view, statements within the memorandum dated 11 March, as well as a further memorandum written by Mr Parkes, dated 18

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[256] In its written submissions, Telecom refers to the date of the memorandum as 24 March 1999. However, the memorandum referred to in the Liability Judgment at [145] appears to be an earlier memorandum, dated 11 March 1999.

March 1999, indicated that Telecom's philosophy was to avoid price competition. For example, in the memorandum dated 11 March, Mr Parkes proposes offering a six per cent discount off Nike prices to TSPs, which he describes as giving "very little room or no room for carriers to undercut retail prices given the costs carriers have to bear". In the memorandum dated 18 March, the following passage indicates that Telecom's philosophy involved treating other carriers merely as "a distribution channel for Telecom":

> Having talked to carriers and reflected on the current market conditions, I would like to propose the following as a pricing philosophy to underpin carrier data pricing:
>
> We will provide carriers discounts off the retail price for corporate sized customers at levels of discount that reflect the value carriers bring as a distribution channel for Telecom …

[273] We consider it significant that Mr Parkes was not called by Telecom to give evidence in the High Court. We also consider it significant that Mr Goodin accepted in evidence that Mr Parkes' philosophy was that there would not be price competition between Telecom and other TSPs, but only competition on service quality.

[274] Telecom says that the Court's finding in relation to the memorandum rested on an incorrect assumption that, had Telecom priced its data tails at ECPR-compliant prices, price competition would have increased due to TSPs' competition in the two-tail scenario. This is a repetition of its argument that the two-tail scenario was inherently inefficient. We dismissed this argument for the reasons stated at [198]–[204] above. As the Commission pointed out, Telecom's focus on the limited area of competition in the backbone network ignores a TSP's ability to compete by the provision of differentiated services on the backbone and retail support.

[275] Finally, we do not accept Telecom's submission that the Court may not have regard to Telecom's conduct prior to 18 March 2001 as evidence of a continuing purpose. The Commission commenced proceedings on 18 March 2004. It alleged that Telecom had engaged in a price squeeze over the period 1 December 1998 until late 2004. However, the Commission accepted that its claim for a pecuniary penalty was limited to the period from 18 March 2001, pursuant to s 80(5) of the Act, which

states that proceedings commenced by the Commission for the payment of pecuniary penalties by persons who have contravened Part 2 of the Act must be commenced within three years after the matter giving rise to the contravention was discovered or ought reasonably have been discovered.

[276] The Commission says that it is implicit in the High Court's findings that, although Telecom's anti-competitive purpose may have commenced in 1999, it continued through to the period for which pecuniary penalties may be claimed. The Commission says that there was no evidence that Telecom's approach changed after 2001. We accept the Commission's submissions on this point and consider that direct evidence of events occurring prior to the limitation period could be used to support a finding of continuing purpose.

[277] In any event, we have allowed the Commission's cross-appeal and held that declaratory relief is available for the earlier period. This means that evidence relating to the earlier period is clearly admissible.[257]

Conclusion

[278] We agree with the reasons given by Chambers J in his judgment and the conclusion he has reached at [337] below.

[279] We dismiss Telecom's appeal and also hold that Telecom's pricing in the one-tail scenario breached s 36. This means that Telecom used and/or took advantage of its dominant position/market power from 1 February 1999 until late 2004 for the purposes of deterring potential or existing competitors in the wholesale market for backbone transmission services and the retail market for end-to-end HSDT services in that regard also.

[280] The appellants must pay the respondent costs for a complex appeal on a band B basis and usual disbursements. We certify for three counsel.

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[257] See at [337] below.

CHAMBERS J

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Introduction

[281] I agree with the reasons given by Glazebrook and Ellen France JJ in their opinion. I also agree with the result they have propounded at [279] and [280] above.

[282] In this opinion I deal with four issues.

[283] The first is whether the High Court had jurisdiction to give declaratory relief with respect to Telecom's conduct prior to 18 March 2001, the so-called "limitation date".[258] The High Court held it had no such jurisdiction. The Commission challenges that view. For reasons I shall give, I agree with the Commission's stance.

[284] That leads onto the second issue. Even if the High Court did have jurisdiction to give declaratory relief with respect to pre-2001 conduct, was this an appropriate case in which to exercise that jurisdiction? The Commission submitted it was; Telecom disputed that.

[258] For convenience, I shall refer to this conduct as "pre-2001 conduct" and to conduct after 18 March 2001 as "post-2000 conduct".

[285] The third issue is whether the passage of the Telecommunications Act 2001 barred relief after its commencement. Telecom's argument was that the Court could grant relief only with respect to a nine month period beginning on 18 March 2001 and ending on 19 December 2001, the date on which the 2001 Act came into force.

[286] If that argument failed, Telecom's fallback position was that relief could be granted only with respect to the period from 18 March 2001 to 1 June 2002. That was the date on which the Commission's Decision 497[259] came into effect. The High Court rejected Telecom's submission that Decision 497 barred relief.

Did the High Court have jurisdiction to give declaratory relief with respect to pre-2001 conduct?

[287] The Commission commenced its proceeding against Telecom on 18 March 2004. In its pleading, the Commission sought declarations that Telecom had breached s 36 of the Commerce Act from about 1 December 1998[260] until 30 September 2004. The Commission also sought pecuniary penalties pursuant to s 80 of the Act. With respect to that relief, the Commission acknowledged that it could seek penalties only with respect to conduct within the last three years (that is, since 18 March 2001) because of the restriction imposed by s 80(5). No such limitation applied, however, the Commission said, with respect to the declaratory relief sought, as that relief was granted not under the Commerce Act but rather pursuant to the High Court's inherent jurisdiction, as supplemented by the Declaratory Judgments Act 1908. The Limitation Act 1950 did not provide a specific limitation period with respect to declaratory relief.

[288] The High Court did not accept this submission. I summarise what it held. I shall give each of the points the Court made a letter — (a), (b), (c) and so on — so as to provide a link back later when I am discussing these points. I acknowledge immediately that the points overlap. So to point (a). The Court said that the scheme

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259 *Re TelstraClear Ltd and Clear Communications Ltd* CC Decision No 497, 12 May 2003 at [742].

260 In its appeal, Telecom says the correct start date based on the High Court's findings was 1 February 1999.

of the Commerce Act did not permit "conduct to be examined for the purpose of declaratory relief for an indefinite period".[261] The Court went on:[262]

> … In our view, it would be anomalous and contrary to the intention of the Act if actions for a declaration alone could be undertaken without limit in relation to contraventions which could not be the subject of any other form of relief under the Act.

[289] In the same vein, the Court also held that declaratory relief was available only where there was "an enforceable right"[263] and here there was no enforceable right because no other form of relief was available for pre-2001 conduct.

[290] Now to point (b). The High Court said:

> [182] In our view, the relevant provisions of the Commerce Act show a clear legislative intent to confine any claim for relief to the three-year period following discovery of the matter giving rise to the contravention (or the time at which discovery might reasonably have occurred). …

[291] The High Court went on to cite s 75(1), which confers jurisdiction on the High Court with respect to proceedings for specified relief. Proceedings for declaratory relief are not mentioned in s 75 because the jurisdiction to grant that relief exists as part of the High Court's general or inherent jurisdiction, as affirmed by s 16 of the Judicature Act 1908. The High Court, after setting out s 75, went on to observe — and this is point (c):

> [183] The Court's jurisdiction to hear and determine proceedings for contraventions of Part 2 is dependent on the proceeding seeking one or more of the forms of relief available under s 75(1)(a). If there is no right to seek such relief, the Court has no jurisdiction to hear the proceeding. It follows that there is no jurisdiction to make a declaration in respect of a contravention which cannot be the subject of proceedings for a pecuniary penalty, injunction or damages.

[292] Finally, the High Court said — and this is point (d):

> [186] The Commission relied on *Sisters of Mercy (Roman Catholic Diocese of Auckland Trust Board) v The Attorney General* HC AK CP219/99 6 June 2001 Randerson J, where it was held that the Limitation Act 1950 did not apply to exclude jurisdiction to grant declaratory relief under the Judicature Amendment Act 1972. However, as Mr Shavin pointed out, the

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261 Liability Judgment, above n 6, at [184].
262 Ibid.
263 See for instance at [175], [181] and [186] of the Liability Judgment.

> question in this case is not whether the Limitation Act applies but whether, as a matter of statutory construction, there is jurisdiction to grant declaratory relief in the absence of an enforceable right.

[293] With respect to the High Court, I do not accept its reasoning. I shall explain why in the course of my answers to Telecom's counsel's submissions. Telecom's counsel essentially sought to uphold the High Court's reasoning, which no doubt reflected Telecom's submissions in that court. My reasoning largely reflects the submissions made to us by the Commission's counsel.

(a) Declarations only in respect of "enforceable rights"

[294] Telecom's counsel strongly supported the High Court's point (a).[264] They argued that "the Court's jurisdiction to grant declarations concerning private conduct is limited to declarations over '*enforceable rights'*, ie, legal rights in respect of which the Court has jurisdiction to grant a remedy other than a declaration". The principal case cited in support of that proposition was Lord Diplock's speech in *Gouriet v Union of Post Office Workers*.[265] Telecom's counsel acknowledged that there had been "cautious extensions" since Lord Diplock's judgment, but none of these "extensions" was applicable here. On the basis of this proposition, Telecom's counsel accepted there could be declaratory relief in respect of post-2000 conduct but not in respect of pre-2001 conduct as the Commission had no other remedy available to it in respect of such conduct.

[295] I do not accept that submission. The law has moved on since *Gouriet*, as Lord Woolf and his son Jeremy make clear in their classic text *The Declaratory Judgment*.[266] They describe declaratory jurisdiction in expansive terms:[267]

> ... within the limits of their general jurisdiction and subject to any express statutory provision to the contrary the courts have a discretion to grant declarations upon any matter whatsoever.

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264 At [288]–[289] above.

265 *Gouriet v Union of Post Office Workers* [1978] AC 435 (HL) at 501.

266 Lord Woolf and Jeremy Woolf *The Declaratory Judgment* (4th ed, Sweet & Maxwell, London, 2011), especially at [3-26]–[3-27].

267 At [3-19].

[296] To similar effect is the Supreme Court's recent decision in *Mandic v The Cornwall Park Trust Board (Inc)*, where the breadth of the jurisdiction was emphasised.[268]

[297] There can be no doubt that in this case the Commission was asserting that legal rights were affected: Telecom's competitors' right not to be subject to unlawful competition and the public's right not to have Telecom unlawfully taking advantage of its market power. It is irrelevant that these rights, at least in their current form, may not have existed at common law. It is also irrelevant, so far as declaratory relief is concerned, that the Commission might have no other remedy available to it with respect to pre-2001 conduct in breach of these rights. Telecom's submission that other relief must be available before a party can obtain a declaration is quite contrary to s 2 of the Declaratory Judgments Act, which specifically says that no proceeding in the High Court is to "be open to objection on the ground that a merely declaratory judgment or order is sought" and that the Court "may make binding declarations of right, whether any consequential relief is or could be claimed or not". In addition, s 11 of that Act provides that the jurisdiction conferred by the Act "to give or make any declaratory judgment or order shall not be excluded by the fact that the [High] Court has no power to give relief in the matter to which the judgment or order relates".

(b) The Commerce Act's three year limitation period must apply

[298] Telecom's counsel supported point (b),[269] submitting that the declaratory judgment jurisdiction was constrained by the clear intent of the Commerce Act. The Commerce Act implied, Telecom said, that "any possible jurisdiction to grant declaratory relief was excluded … [by the] statutory scheme whereby the Court's role in determining whether past conduct contravenes Part 2 of the [Commerce] Act is limited to three years".

[299] I do not accept this argument. The jurisdiction to grant declarations does not come from the Commerce Act and is not subject to any statutory limitation period.

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268 *Mandic v The Cornwall Park Trust Board (Inc)* [2011] NZSC 135, [2012] 2 NZLR 194 at [5]–[9] per Elias CJ and at [82] per Blanchard, Tipping, McGrath and William Young JJ.

269 At [290] above.

Everyone in this case accepts the High Court had jurisdiction to grant declaratory relief with respect to Telecom's conduct after 18 March 2001. If Telecom was conducting itself in the same way prior to the limitation date as it was after the limitation date, then the High Court has jurisdiction to declare the pre-2001 conduct to have been in breach of s 36 of the Commerce Act.

[300] The relevant provisions of the Commerce Act set out certain remedies which a claimant may wish to pursue. But the Act does not set forth every available remedy. Where a remedy is outside the Act, there is no reason why its availability should be governed by a specific limitation period in the Commerce Act, such as s 80(5), which relates specifically to a different remedy. That s 80(5) is not controlling is reinforced by the fact that the Commerce Act provides a number of different limitation periods relating to different remedies: the limitation period is not always three years, as the High Court itself acknowledged later in its judgment.[270] Since declaratory relief is not mentioned in the Commerce Act, why would one choose one of that Act's limitation periods in preference to another? In this case, the High Court appears to have chosen three years as, in effect, a deemed limitation period for declarations because three years happened to be the limitation period applicable to another remedy the Commission was seeking, namely a penalty order. What would have happened, however, if the other order sought had been an order to which a different limitation period applied? Would that different limitation period have applied to the application for declaratory relief by osmosis? And what if no other relief had been sought, even though other relief arguably could have been sought?

[301] Further, as the Woolfs state, the courts in general "lean firmly against construing a statute in a manner which ousts their own [declaratory] jurisdiction".[271] Telecom's argument is not even based on any express words in the Commerce Act, but merely on a contention that ouster is implicit. I do not accept that.

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270 Liability Judgment, above n 6, at [184].
271 Woolf and Woolf, above n 266, at [3-65].

(c) Court's jurisdiction limited to relief available under s 75(1)(a)

[302] Telecom's counsel also sought to uphold the High Court's point (c).[272] They argued that, because s 75 relief was not available for pre-2001 conduct, declaratory relief could not be available. They made the point that the time limitations in the Commerce Act sections differed in their functionality from limitations under the Limitation Act; under the Commerce Act, they submitted, the time limitations were "essential elements of the definition of the enforceable rights themselves".

[303] I do not accept the High Court's point (c) or Telecom's expansion on it. The starting point is that the High Court has jurisdiction to grant declaratory relief, as all counsel accept, even though that remedy is mentioned nowhere in the Commerce Act. The purpose of s 75 and s 76, which deals with the District Courts' jurisdiction, is to specify which Court has jurisdiction with respect to specific orders sought under the Commerce Act. These sections say nothing about which Court can grant declaratory relief. Nor do the sections purport to permit declaratory relief only if tied to an application for or an order of specific Commerce Act relief. Indeed, such a construction of the Commerce Act would be contrary to s 2 of the Declaratory Judgments Act, as I have said.

[304] Telecom's submission is also flawed in the distinction it attempts to draw between limitation provisions in the Limitation Act and limitation provisions in the Commerce Act. They all operate in the same way. They are "procedural" and may be waived. The Full Court of the Federal Court of Australia put it this way when considering the equivalent Commonwealth provision:[273]

> … [Section] 82(2) [the equivalent of our Commerce Act, s 82(2)] is a condition of the remedy rather than an element in the right and a prerequisite to jurisdiction which cannot be waived. It follows that it is for a defendant to assert non-compliance, rather than for a plaintiff to assert compliance with s 82(2) as an element of the cause of action.
>
> The need for compliance with s 82(2) may be waived by the defendant and an estoppel may prevent the defendant denying such a waiver. If the

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[272] At [291] above.

[273] *State of Western Australia v Wardley Australia Ltd* (1991) 30 FCR 245 (FCAFC) at 259. See also *Hook v Gulf Harbour Town Centre Ltd (in liq)* HC Auckland CIV-2002-404-1931, 2 March 2007.

> defendant fails to plead the limitation, this may be taken as a waiver of the need for compliance with s 82(2).

[305] I agree with the Full Court. Indeed, it is noteworthy that in the present case Telecom did plead a limitation defence "to the maximum extent of its application to each of the plaintiffs' causes of action" in just the same way as one would plead a limitation defence under the Limitation Act.

(d) Distinguishing Sisters of Mercy

[306] Contrary to the High Court's view, I consider Randerson J's judgment in *Sisters of Mercy* to be applicable to the present case. I do not accept the final sentence of the High Court's judgment at [186].[274]

[307] There is nothing to construe in the Commerce Act, as it does not provide jurisdiction for declaratory relief. Since the Limitation Act does not apply to the jurisdiction to grant declaratory relief, whether under general law, the Declaratory Judgments Act or the Judicature Amendment Act 1972, there is no statutory constraint on the Commission's application for a declaration with respect to pre-2001 conduct.

(e) Earlier cases

[308] Finally, Telecom's counsel referred to two earlier cases, which they said were consistent with its submission and "the analysis adopted by the High Court".

[309] The first of these cases is *Commerce Commission v Fletcher Challenge Ltd*.[275] That case does not help on the current issue, as no limitation problem arose.

[310] Similarly, I cannot see how the Federal Court's decision in *Tobacco Institute of Australia Ltd v Australian Federation of Consumer Organisations*[276] applies when, as Telecom's counsel acknowledge, "no issue of a limitation period arose in

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274 Set out above at [292].
275 *Commerce Commission v Fletcher Challenge Ltd* [1989] 2 NZLR 554 (HC).
276 *Tobacco Institute of Australia Ltd v Australian Federation of Consumer Organisations* (1993) 113 ALR 257 (FCAFC).

the case". In addition, the Federal Court has limited jurisdiction, unlike the High Court of New Zealand, which is a general court "in and for New Zealand" with unlimited jurisdiction in respect of "the administration of justice throughout New Zealand", except in so far as such jurisdiction may by statute be excluded.[277] The High Court has jurisdiction to make declarations with respect to any legal rights, whether common law or statutory, except in so far as such jurisdiction may be restricted by statute.

[311] The position I have adopted will not mean that defendants will be regularly facing stale claims. First, most claims in this area of Commerce Act litigation are brought by the Commerce Commission. While the Commission is not always right, it would be almost unthinkable that the Commission, as a State agency, would bring a vexatious or frivolous claim. Further, Commerce Act litigation is notoriously expensive. The Commission has a limited litigation budget. It would be very unlikely to waste that budget on pursuing stale claims. For instance, I have little doubt that, had Telecom desisted from its anti-competitive behaviour prior to 18 March 2001, there is no realistic likelihood that the Commission would in 2004 have brought proceedings for stale declaratory relief. Cost is also likely to deter other plaintiffs from pursuing stale claims. And defendants can always fall back on r 15.1 of the High Court Rules and apply to strike out all or part of a pleading which can be shown to be frivolous or vexatious or otherwise an abuse of the process of the Court.

[312] On this first issue, therefore, I accept the Commission's challenge to the High Court's conclusion. I would hold that the High Court did have jurisdiction to give declaratory relief with respect to Telecom's pre-2001 conduct.

Should we grant declaratory relief with respect to pre-2001 conduct?

[313] As the Woolfs say, "[a] most important feature of the declaratory judgment is that it is a flexible and discretionary remedy".[278] The authors go on to say that "[t]he discretion as to whether or not to grant relief is that of the trial judge", a discretion

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[277] Judicature Act 1908, s 3.
[278] Woolf and Woolf, above n 266, at [4-01].

which an appellate court will interfere with only "if it can clearly be shown to have been exercised wrongly".[279] The problem in this case is that the High Court did not consider whether it *should* grant declaratory relief with respect to pre-2001 conduct because of its view that it had no jurisdiction to grant it. I have determined there was jurisdiction. Accordingly it now falls to this Court to decide whether declaratory relief with respect to pre-2001 conduct should have been granted. Neither party sought to have that issue referred back to the High Court in the event we found there was jurisdiction.

[314] While the discretion is broad, it is not completely unfettered. A starting point, the Woolfs explain, is that "if a party has succeeded in his action he should not usually be sent away empty handed".[280] The learned authors conclude their general discussion of the development of principles as to the exercise of the discretion in these words:[281]

> In general, however, the present attitude of the judges to the exercise of the declaratory discretion has not changed from the way in which it was expressed by Bankes LJ who said[282]:
>
> > The relief claimed must be something which it would not be unlawful or unconstitutional or inequitable for the Court to grant, or contrary to the accepted principles upon which the Court exercises its jurisdiction. Subject to this limitation I see nothing to fetter the discretion of the Court in exercising a jurisdiction under the rule [now CPR Pt 40.20] to grant relief, and having regard to general business convenience and the importance of adapting the machinery of the Courts to the needs of suitors I think the rule should receive as liberal construction as possible.

[315] Telecom's counsel put forward four reasons why we should decline to grant declaratory relief with respect to pre-2001 conduct.

[316] They first point to the "policies [underlying] the statutory limitation periods in the [Commerce] Act". In the declaratory judgment context, the limitation periods in the Commerce Act with regard to Commerce Act claims have as much relevance

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279 At [4-04].

280 At [4-05], citing as authority *Chief Constable of the North Wales Police v Evans* [1982] 1 WLR 1155 (HL) at 1172 per Lord Brightman.

281 At [4-09].

282 *Guaranty Trust Co of New York v Hannay & Co* [1915] 2 KB 536 (CA) at 572. (Remainder of footnote omitted.)

as the limitation periods in the Limitation Act have with respect to claims, say, for contract or tort. That is to say, they are not definitive. They may indicate that a proceeding is an abuse of process; they may be a guide to the need to strike out a proceeding on the ground of staleness. But that is all.

[317] Telecom's second argument is that declaratory relief should be denied on the grounds of delay. I accept that delay could be a ground for refusing declaratory relief, especially in circumstances where the delay is unreasonable and prejudice has been caused to the defendant. That is the test generally applied in equity when determining whether discretionary equitable remedies should be refused.[283] (By mentioning the test in equity, I am not to be taken as saying this test would be applicable in every situation where declaratory relief was sought. But in a case of this sort, I think the equitable test has relevance. Were I satisfied *in this case* that the delay was unreasonable and prejudice had been caused to Telecom, I would be strongly inclined to exercise the discretion against granting declaratory relief.)

[318] Telecom's counsel submit the delay was unreasonable. I would have accorded that submission considerable weight had the allegedly unlawful conduct been confined to 1999 and 2000 and had the Commission not commenced a proceeding with respect to it until March 2004. There would then have been a strong argument that the claim was stale. But the argument is less convincing in circumstances where the 1999 and 2000 conduct is of the same kind as the 2001–2004 conduct and merely its precursor in time. Telecom was not being dragged to court solely to deal with a stale claim; it was inevitable *in this case* that its explanation of and justification of its post-2000 conduct would necessarily require detailed evidence as to what had been happening in the industry for at least the previous two years. I have emphasised "in this case" because I am not stating a general proposition that delay is excusable wherever "stale" conduct is tied to "recent" conduct. My comment is confined to the facts of this case.

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283 See for example Andrew Barker "Permanent Injunctions" in Peter Blanchard (ed) *Civil Remedies in New Zealand* (2nd ed, Thomson Reuters, Wellington, 2011) 227 at [5.2.2(3)] and Terence Prime and Gary Scanlan *The Law of Limitation* (2nd ed, Oxford University Press, Oxford, 2001) at ch 12.

[319] This leads on to the next point. I cannot see how Telecom has been prejudiced by the delay. Telecom has always known that it faced a claim that its pre-2001 conduct was said to be anti-competitive. It did not seek to strike out that part of the claim. Accordingly it went to trial and presented a defence which covered its pre-2001 conduct as well as its post-2000 conduct. So far as I can see, the inclusion of a claim for declaratory relief covering pre-2001 conduct as well as post-2000 conduct did not lead to any different evidence being called from what would have been called had no declaration with respect to pre-2001 conduct been sought.

[320] I therefore do not accept the submission that the Commission's delay in commencing the proceeding should prevent declaratory relief *in this case* with respect to pre-2001 conduct.

[321] Telecom's third argument was that a declaration with respect to pre-2001 conduct should be declined on the basis that it would be "purely hypothetical". It is true that the courts may decline declaratory relief in hypothetical cases, although the Woolfs note that "the courts have been expressing an increasing willingness to provide guidance in appropriate cases, even though the courts recognise that the case might be regarded as hypothetical".[284] But the present case is not "hypothetical" in the sense the courts have used that term in this context.[285] What I suspect Telecom really means is that a declaration as to pre-2001 conduct would have no "practical significance". That is a slightly different point. In any event, I do not accept the submission. After all, if it were right, why did Telecom not oppose a declaration with respect to post-2000 conduct on the basis that the declaration would have no practical significance? The declaration the High Court did make does not of itself hit Telecom in the pocket. It is possible that the declaration that was made will have no downstream consequences for Telecom: we simply do not know. But that is not a ground for denying the Commission, in the public interest, from obtaining a declaration that Telecom's conduct was anti-competitive. Once it is conceded that a declaration as to post-2000 conduct is available and may have practical significance,

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[284] Woolf and Woolf, above n 266, at [4-57].

[285] The Woolfs give the four classes of hypothetical cases for these purposes at [4-59]. This case does not come within any of the four classes.

it is hard to see why we should not extend the declaration to cover substantially similar conduct pre-2001.

[322] Telecom's final submission under this head was that Telecom had been "plainly placed in difficulty in relation to pre-March 2001 matters". I have already dealt with this when discussing prejudice under the heading of delay. I do not accept the submission. As I have said, Telecom did not attempt to strike out this part of the claim on the basis of prejudice in defending. Telecom amassed and led copious evidence with respect to its pre-2001 conduct.

[323] Telecom has not persuaded me that the discretion should be exercised against making a declaration with respect to pre-2001 conduct. Whether a declaration should be made, however, needs to await consideration of the two remaining issues.

Did the passage of the Telecommunications Act 2001 bar relief in respect of Telecom's conduct after the Act's commencement?

[324] The Telecommunications Act 2001 came into force on 19 December 2001. The High Court recorded Telecom's submission as follows:

> [153] Mr Shavin argued that on the Telecommunications Act coming into force, Telecom ceased to be able to take advantage of any market power over high speed data transmission services. He contended that the Act expressly and by necessary implication excluded review under the Commerce Act of Telecom's conduct subsequent to its passing. He relied on provisions in the Telecommunications Act which permit an access-seeker to apply to the Commission for a determination of the price of HSDT and which exclude from review under the Commerce Act such determination or any matter necessary to give effect to such a determination.

[325] The High Court rejected that submission.[286]

[326] On appeal before us, Telecom's counsel noted this argument at [7.3] of their submissions but then immediately went on to discuss Decision 497 (the next issue I shall be dealing with).

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[286] Liability Judgment, above n 6, at [161]–[162].

[327] In my respectful view, there is nothing in Telecom's argument that the 2001 Act in itself excluded review under the Commerce Act with respect to services covered by the Act. The argument that the exclusion of Commerce Act review was a "necessary implication" is clearly wrong. Such an argument is inconsistent with s 63 of the 2001 Act, which provides as follows:

> Part 2 of the Commerce Act 1986 does not apply in respect of the determination made under this Part or any matter necessary for giving effect to a determination made under this Part.

[328] This makes clear that Part 2 of the Commerce Act is excluded where a determination has been made under the 2001 Act. It is not excluded, however, until a relevant determination is made.

[329] I reject the submission that the passage of the 2001 Act in itself barred relief in respect of Telecom's conduct after the Act's commencement.

Did Decision 497 bar relief after 1 June 2002?

[330] Decision 497 was a determination made under Part 2 of the Telecommunications Act. Telecom's contention is that that decision fixed prices for the services at issue in this proceeding. The determination came into effect on 1 June 2002. From that date, therefore, by virtue of s 63, the determination applies and relief under the Commerce Act is barred.

[331] The High Court held that Decision 497 was concerned only with Telecom's pricing for specified data services in non-metropolitan areas.[287] Decision 497 was "not concerned with access to or the pricing of data tails".[288] The Court went on to say:

> [159] ... The Commission's claim focuses on CDP pricing of data tails; it is not concerned with the pricing of circuits for resale as an end-to-end retail service. The pricing of data tails as a component of the retail service is expressly excluded from Decision 497. Section 63 can have no application.

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[287] At [156].
[288] At [157].

[332] Telecom's counsel challenged the Court's decision. They argued that the distinction the Court drew between "the resale of an end-to-end HSDT service [and] a tail" was fallacious, as "the *actual* products were technically identical – that is, HSDT circuits were what TSPs used as 'data tails' *and* for resale".

[333] I do not accept that submission, for the reasons given by the High Court and by the Commission before us. A data tail is not an end-to-end retail service: it is, as Glazebrook and Ellen France JJ have made clear, an intermediate component, namely a connection between an end user's premises and a TSP's POP or POI. In my view, the following passage in the High Court's judgment is unanswerable:

> [162] While the Telecommunications Act plainly imposes constraints on Telecom in relation to designated access services, there is nothing to indicate that it provides (or provided) any material constraint in relation to the pricing of data tails. There was no change to CDP pricing after the Act came into force. It was recognised that the decision not to specify data tails as a designated access service may give rise to competition concerns. A ministerial paper submitted to the Ministerial Inquiry into Telecommunications in November 2000, acknowledged that data tail access issued could "prove to be a competition problem". It is clear there was no expectation that the legislation would remove the need for oversight in that sector. While the Commission's review under s 64 of the Telecommunications Act led to the introduction of UPC pricing, that was because of the threat of further regulation. The existing legislation had no discernible effect on Telecom's conduct.

[334] I think it is clear that the 2001 Act imposed constraints on Telecom in relation to designated access services, but it did not regulate data tails. We were shown the Cabinet Paper which led to the Act and which recommended that data tails were not to be designated access services.[289] In fact, as the Commission pointed out, the decision to exclude access to data tails from the statutory regime was to a significant extent a consequence of Telecom's submission to the Minister of Communications, dated 17 October 2000, requesting just that. That the Commission also thought the pricing of data tails was outside its remit was made very clear in Decision 497:

> [64] ... Telecom advised that it only sells end-to-end data services at the retail level, and a customer cannot purchase separately the components of data services such as the access components or "data tails". The Commission notes that the Relevant Wholesale Service is the end-to-end data service.

[289] Cabinet Paper "Telecommunications: Paper Three: Regulated Services" (29 November 2000) FIN (00)312 at [26].

> This Determination does not require Telecom to wholesale the individual components of an end-to-end data service, as they are not retail services.

[335] This makes it clear, as the Commission's counsel submitted, that the relevant wholesale service was the end-to-end data service and that its individual components – the data tails – were expressly excluded from the Decision's ambit.

[336] I reject Telecom's argument under this head. I agree with the High Court that s 63 of the Telecommunications Act and Decision 497 do not bar the Commission's proceeding.

Conclusion

[337] I have rejected Telecom's submissions on the four issues with which I have dealt. I have concluded that the Commission was entitled to a declaration covering the pre-2001 conduct as well as the post-2000 conduct. I would accordingly amend the declaration the High Court made to read as follows:

> The plaintiff is granted a declaration that Telecom used and/or took advantage of its dominant position/market power from 1 February 1999 until late 2004 (when Telecom introduced a UPC service) for the purposes of deterring potential or existing competitors in the wholesale market for backbone transmission services and the retail market for end-to-end high speed data transmission services.

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APPENDIX

GLOSSARY

ATM	Asynchronous Transfer Mode
CBD	central business district
CBR	constant bit rate
CDP	Carrier Data Pricing
CIR	Committed Information Rate
DCS	digital cross connect switches
DDS	digital data services
DSL	digital subscriber line
DSLAM	digital subscriber line access multiplexer
DSTN	Digital Services Transport Network
ECPR	Efficient Component Pricing Rule
FR	Frame Relay
HSDT	high-speed data transmission
IP	Internet Protocol
NTU	Network Terminating Unit
PIR	Peak Information Rate
POP	point of presence
PSTN	Public Switched Telephone Network
SWA	stacked wideband access
TLoC	Telecom List of Charges
TSP	Telecommunications Service Provider
UPC	Unbundled Partial Circuit
VBR	variable bit rate
WIN	Wholesale Integrated Network