

**MEMORANDUM**

**To:** Graham Walmsley, CallPlus Limited  
**From:** Andrew Matthews & Gus Stewart  
**Date:** 18 September 2014  
**Subject:** Consultation paper on issues relating to Chorus' proposed changes to the UBA service\*

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**Your instructions**

1. You asked us to comment briefly on the legal opinion provided to the Commerce Commission by David Laurenson QC and James Every-Palmer (**Opinion**).

**Our views**

2. We broadly agree with the substance of the opinion and its conclusions. In particular we agree that Chorus' proposed changes to the regulated UBA service would likely breach clause 2.2.1 of the STD, which requires the parties to "*carry out their obligations under the UBA Terms in good faith and in furtherance of those [section 18] purposes...*".
3. There may be more direct points to be made; namely that there is no ability under the STD to withdraw or vary the regulated service.<sup>1</sup> In other words, there may be no need to rely on the good faith obligations as the primary reason for there being a breach of the STD. Rather that there is simply no right to act as proposed under the STD.<sup>2</sup> Naturally the good faith obligations reinforce these arguments.
4. We consider that there appears to be a fundamental inconsistency between the setting of a TSLRIC price while seeking to provide what would appear a more limited service than that to which the price relates. We are not aware of any attempts to reconcile these points, which seems a significant omission. We agree that "[t]he *"capping"* of the regulated UBA service also seems to create a mismatch between what Chorus is being paid for (that is a service which improves over time due to ongoing investment in its network) and what it would be providing (a service with a capped average throughput)."<sup>3</sup>
5. Our review of case law and literature on "*good faith*" obligations suggests stronger obligations than the Opinion conveys.<sup>4</sup> Significantly, that good faith obligations *in a statutory context* like this go further than they do in a contractual context. They go beyond compliance with the black letter of the law, requiring adherence to the spirit of the law: "*A good faith provision offers a warning that game playing at the margins of a statutory prescription or obligation may attract a finding of liability.*"<sup>5</sup>

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\* This opinion is reissued on 23 September to change an incorrect reference to one of the cases in para 9 below - the 2nd sentence now notes *Bropho*.

<sup>1</sup> These points appear touched on in the Opinion, but perhaps not fully developed.

<sup>2</sup> There may (as you submitted) be grounds for arguing that Chorus is estopped from making the changes and / or that it may be worth considering obligations under the Fair Trading Act.

<sup>3</sup> Opinion, para 10e.

<sup>4</sup> We consider it significant that this is not an implied, or even a negotiated, good faith obligation. The obligation is specified by the regulator pursuant to its statutory powers. The Opinion refers to authority which appears sourced from a discussion of an *implied* obligations of good faith, which appears to be a lower standard.

<sup>5</sup> *Bropho v Human Rights & Equal Opportunity Commission* [2004] FCAFC 16.

6. In this memo we briefly touch on the points noted in para 3 above. (It is beyond the scope of this memo go into detail and we understand other parties have previously done so.) We then expand on good faith in greater detail. Our limitations follow that discussion.

### No apparent right to vary or withdraw the regulated service

7. We have not focused on these points but note:
- a. Your submission that Chorus is not permitted to unilaterally withdraw VDSL under the STD, Telecommunications Act, or otherwise<sup>6</sup> appears correct on the face of it. On our reading (as you have submitted) the STD terms only gives limited rights to terminate the regulated UBA service, none of which appear to apply here. The Commission has previously confirmed, “[Chorus] is not able to cease offering a part of the UBA service under the UBA Terms, until the Commission has amended the UBA Terms.”<sup>7</sup>
  - b. Similarly, your submission that Chorus cannot unilaterally degrade the regulated service also appears correct on its face.<sup>8</sup> We note your submission that standard access principle 2 requires that “the service must be supplied to a standard that is consistent with international best practice”;<sup>9</sup> and that clause 3.6 of schedule 1 to the STD which imports a “maximum” speed requirement, providing that “The Basic UBA Service available under this service description is a DSL enabled service which has a maximum downstream line speed for data traffic sent to the End User and a maximum upstream line speed for data traffic sent from the End User”.

### The meaning of “good faith” in a statutory context

8. Our review of the cases and literature highlighted these significant judgements:
- a. *Yam Seng Pte Limited v International Trade Corporation Limited*<sup>10</sup> (**Yam Seng**);
  - b. *CPC Group Limited v Qatari Diar Real Estate Investment Company*<sup>11</sup> (**CPC**);
  - c. *Berkeley Community Villages Limited & Anor v Pullen & Ors*<sup>12</sup> (**Berkeley**).
9. The *Berkeley* case cited the *Bropho* case<sup>13</sup> with approval at length, which was in turn cited with approval in *CPC*. *Yam Seng* also cited *Berkeley* and *CPC*.<sup>14</sup> The *Bropho* case is especially apt, dealing with legislative (rather than contractual) obligations of good faith. That seems a more relevant benchmark to the present *regulated* obligation of good faith. (Although, as noted, the judgement was cited at detail and with approval in a contractual context.)
10. In *Bropho* the court made a number of relevant observations (at para [90- 101]), extracts of which are noted below [emphasis added]:

[90] The ordinary English meaning of the word ‘faith’ as defined in the Shorter Oxford English Dictionary includes the following:

<sup>6</sup> CallPlus Submission, paras 51 & 59-61.

<sup>7</sup> Standard Terms Determination for the designated service Telecom’s unbundled bitstream access, Decision 611, 12 December 2007, para 346.

<sup>8</sup> CallPlus Submission, para 38.

<sup>9</sup> Section 5(a), subpart 2, part 1, schedule 1 of the Act.

<sup>10</sup> [2013] EWHC 111 (QB).

<sup>11</sup> [2010] EWHC 1535 (Ch).

<sup>12</sup> [2007] EWHC 1330 (Ch).

<sup>13</sup> *Supra* n3.

<sup>14</sup> Leggatt (at [140]) commented: “The two aspects of good faith which I have identified are consistent with the way in which express contractual duties of good faith have been interpreted in several recent cases: see *Berkeley Community Villages Ltd v Pullen* [2007] EWHC 1330 (Ch) at [95]-[97]; *CPC Group Ltd v Qatari Diar Real Estate Investment Co* [2010] EWHC 1535 (Ch) at [246].”

1. *The duty of fulfilling one's trust; fealty; the obligation of a promise or engagement.*
2. *The quality of fulfilling one's trust, fidelity, loyalty.'*

The term 'good faith' is noted against the second meaning as reflecting fidelity and loyalty and is contrasted with bad faith meaning faithlessness or having an intent to deceive. In Black's Law Dictionary, 7th Edition, West Group (1999) at 701, 'good faith' is defined thus:

*'A state of mind consisting in (1) honesty in belief or purpose, (2) faithfulness to one's duty or obligation, (3) observance of reasonable commercial standards of fair dealing in a given trade or business, or (4) absence of intent to defraud or to seek unconscionable advantage. – Also termed bona fides.'*

[91] Honesty is an element embedded in the ordinary meaning of good faith. It is the antithesis of bad faith. The idea of **fidelity or loyalty goes beyond honesty**. It is a relational concept. It involves adherence to **a commitment or an obligation or a principle**. Because it is relational it is ambulatory and because it is ambulatory so too is the concept of 'good faith' as a whole. In a less direct sense so too is honesty. In the context of an implied term of good faith in the performance of a contract, Sir Anthony Mason used the words *'mainly in the sense of loyalty to the promise itself and as excluding bad faith behaviour'* – AF Mason op cit at 69. **These elements are not contingent upon context**. They emerge from the ordinary meaning of the words although, like 'fairness' in administrative justice, they take their content from the particular circumstances in which it is sought to apply them.

[92] In the United States Second Restatement of Contracts par 205, it was said:

*'The phrase 'good faith' is used in a variety of contexts and its meaning varies somewhat with the context. **Good faith performance or enforcement of a contract emphasizes faithfulness to an agreed common purpose and consistency with the justified expectations of the other party;** it excludes a variety of types of conduct characterized as involving 'bad faith' because they violate community standards of decency, fairness or reasonableness.'*

[93] **In a statutory setting a requirement to act in good faith, absent any contrary intention express or implied, will require honest action and fidelity to whatever norm, or rule or obligation the statute prescribes as attracting the requirement of good faith observance. That fidelity may extend beyond compliance with the black letter of the law absent the good faith requirement. In ordinary parlance it may require adherence to the 'spirit' of the law.** This may attract the kind of penumbral judgments by courts of which Professor Stone wrote. That is not necessarily a matter for concern in the case of civil proscriptions. They are evaluative judgments which the courts are authorised and required by the legislature to make. **A good faith provision offers a warning that game playing at the margins of a statutory proscription or obligation may attract a finding of liability. There is nothing in principle to prevent the legislature protecting a rule by attaching an uncertain risk of liability to conduct in the shadow of the rule.**

...

[96] **It follows from the preceding discussion that good faith may be tested both subjectively and objectively.** Want of subjective good faith, ie seeking consciously to further an ulterior purpose of racial vilification may be sufficient to forfeit the protection of s 18D. But good faith requires more than subjective honesty and legitimate purposes. It requires, under the aegis of fidelity or loyalty to the relevant principles in the Act, a conscientious approach to the task of honouring the values asserted by the Act. This may be assessed objectively.

...

[101] **Generally speaking the absence of subjective good faith, eg dishonesty or the knowing pursuit of an improper purpose, should be sufficient to establish want of good faith for most purposes. But it may not be necessary where objective good faith, in the sense of a conscientious approach to the relevant obligation, is required.** In my opinion, having regard to the public mischief to which s 18C is directed, both subjective and objective good faith is required by s 18D in the doing of the free speech and expression activities protected by that section.

11. A number of principles can be drawn from the above discussion:

- a. Even in a purely contractual context, good faith arguably covers *"justified expectations"*- that is the codified US approach.

- b. The relevant standard must look at the "statutory norm" and it is not sufficient to simply rely on the "letter of the law" but rather the "spirit of the law".
  - c. A party "playing at the margins" does so at their own risk.
  - d. A party going "beyond the margins" must therefore be at even greater risk.
12. This "good faith" standard seems to go well beyond a simple "loyalty to a promise" standard. It also appears more appropriate. A number of other sources provide greater "flavour" to what the obligations of "good faith" entail.<sup>15</sup>

### Relevance of this expanded commentary on "good faith" to the Opinion's conclusions

13. The Opinion sets out good grounds for why the "good faith" requirement in the STD would not be met if the proposal went ahead. It appears that if the good faith standard (outlined above) were applied then the conclusions in the Opinion on this point may well have been stronger.
14. That would seem particularly the case when, as we understand:
- a. The STD provides no ability to withdraw or degrade the regulated service.
  - b. As such, the proposed actions would seem to go well beyond an area of ambiguity.
  - c. More specifically this approach would seem to go beyond the spirit of the STD, section 18 and the Telecommunications Act.
15. We agree that objectively, it appears that Chorus' proposed changes to the regulated service appear to have the "*ulterior motive of making Boost services more attractive by comparison and migrating RSPs away from the regulated (price controlled) service*"<sup>16</sup> and that such a motive is inconsistent with "good faith" obligations.
16. Another critical point is that it appears that both an objective and a subjective test would apply as to whether or not there was good faith, or an absence of good faith, in relation to the proposed conduct. The Commission may well have views on the relevant subjective purpose.
17. The fact that the Commission has obtained independent legal advice from eminent counsel suggesting likely breach could be relevant to any further conduct by Chorus. Unless it can demonstrate that the opinion is clearly incorrect as a matter of fact and/or law, then proceeding in itself may risk being seen as an act of "bad faith".

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<sup>15</sup> For example, in *Bobux Marketing Ltd v Raynor Marketing Ltd*, CA 245/00, 3 October 2001, Thomas J referred to the ethic requiring "consistency with the justified expectations of the other party" [41] and the need for "predictable performance" [44]. The article "Some Reflections On Good Faith In Contract Law" (Oxford University Obligations Group – February 2012) refers to Posner J and comments (p3) that "He said that...good faith was to **forbid opportunistic behaviour...**" [emphasis added] and discussed the need to avoid "sharp practice" which was "akin to theft...". An article by David Thomas QC, "Contractual Obligations of Good Faith" (Construction Law International, Volume 7, issue 3, October 2012) discussed the fact that the standard went beyond simply requiring honesty and required "contracting parties to have regard to legitimate or reasonable expectations of the other party." Similarly in *Yam Seng* (supra) the court noted (at 138): "In addition to honesty, there are other standards of commercial dealing which are so generally accepted that the contracting parties would reasonably be understood to take them has read without explicitly stating them in their contractual document. A key aspect of good faith, as I see it, is the observance of such standards. Put the other way round, not all bad faith conduct would necessarily be described as dishonest. **Other epithets which might be used to describe such conduct include "improper", "commercially unacceptable" or "unconscionable"**." [emphasis added]

<sup>16</sup> Opinion, para 10a.

## Other points

18. The Opinion mentioned the Commission's possible consideration of potential adverse effects on competition resulting from the proposals. If there were such effects then this would appear inconsistent with the section 18 purpose.
19. Given our understanding that the proposal could have different impacts on different players we suspect that this warrants greater scrutiny. (It may also be arguable that even if the proposal had a neutral effects on all competitors, if all competitors were able to offer less to customers then this in itself would be inconsistent with the section 18 purpose as potentially all RSPs would be "offering less".)
20. Related points are the Opinion's observations:
  - a. *"End-users throughput would be constrained even where network capacity was available."* [10.c.ii.]
  - b. *"The regulated UBA services would in effect be defined and constrained by Chorus' view..."* [10.c.iii.]
  - c. The proposed changes could see *"Boost's share of the market... increase... other than through 'competition on the merits'..."* [10.f.]

## Limitations

21. We have been instructed to prepare these comments on behalf of CallPlus. Our comments are provided for the sole purpose of assisting CallPlus with its feedback to the Commission. Our views are not for the benefit of any other party. We appreciate that our views may be put to the Commission as part of the formal consultation process.
22. In preparing this memo, we have relied on your instructions, and the factual conclusions and review set out in the Opinion, together with our review of what we understand are the key documents. We have not been fully involved in all aspects of this regulatory process.

Yours sincerely

MATTHEWS LAW



**Andrew Matthews / Gus Stewart**  
Principal / Associate

**phone** +64 9 972 3754 / +64 9 972 3755  
**email** andrew.matthews@matthewslaw.co.nz  
gus.stewart@matthewslaw.co.nz