

**IN THE MATTER**

of a complaint under the Undertakings Given by Telecom to the Crown under Section 69K(2)(c) of the Telecommunications Act 2001

**BETWEEN**

**VODAFONE NEW ZEALAND LIMITED and KORDIA GROUP LIMITED**

**Complainants**

**AND**

**TELECOM WHOLESALE**

**Respondent**

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**REASONS FOR DECISION GIVEN**

**On 27 August 2009**

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## Introduction and Background

1. The complaints by Vodafone New Zealand Limited and Kordia Group Limited (the complainants) against Telecom Wholesale (TW) for allegedly breaching undertakings given to the Minister of Communications on 25 March 2008 under Part 2A of the Telecommunications Act 2001 (the Act) was upheld in a decision given on the 27<sup>th</sup> day of August 2009. The reasons for the decision are now given.
2. Part 2A of the Act required operational separation of Telecom and in accordance with s 69F of the Act, the Minister of Communications issued the Telecommunications (Operational Separation) Determination 2007 (the determination). The determination set out requirements, and Telecom under operational separation was required to enter into the undertakings and agree to comply with those requirements in the undertakings. The undertakings in many respects mirror the provisions of the determination.
3. The complainants allege that TW has breached clause 47 (equivalence of inputs) and clause 56 (discrimination) by making two loyalty offers to service providers.
4. The Auckland loyalty offer launched in December 2008 offered service providers discounts on some broadband combinations as well as PSTN access for specified Auckland exchanges if service providers:
  - (a) ensure that 100% of their existing Auckland residential customer base already served through Telecom Wholesale continue to be served through Telecom Wholesale for the next two years;
  - (b) ensure that 100% of their new Auckland customers are served through Telecom Wholesale for the next two years; and
  - (c) accepted the offer by 31 March 2009.
5. In March 2009, the New Zealand loyalty offer was launched. It offered service providers discounts on some broadband product combinations as well as PSTN access for Auckland customers, and discounts for broadband only for all of New Zealand if service providers:

- (a) ensure that 90% of their customer base already served through Telecom Wholesale continue to be served through Telecom Wholesale for the next two years;
  - (b) ensure that 90% of their new customers are served through Telecom Wholesale for the next two years; and
  - (c) accepted the offer by 24 April 2009.
6. The Independent Oversight Group Support Office (IOGSO) has sought relevant information from the complainants, TW and some other service providers. The IOG after receiving submissions from the parties issued a preliminary determination on 12 June 2009 and has since received the parties' submissions on that preliminary determination and on other matters raised in a subsequent memorandum of 9 July 2009. All parties have had an opportunity to comment on the relevant issues. The IOGSO also obtained independent legal advice.

### **Discrimination**

7. Clause 56 of the undertaking prohibits discrimination. The relevant parts read:
- 56.1 When doing or omitting to do anything in respect of the provision of a Relevant Wholesale Service, the Wholesale Unit (including its Employees, agents and contractors) will not discriminate between Service Providers and Retail Units or between Service Providers.
  - 56.2 For the avoidance of doubt:
    - (a) clause 56.1 does not prevent the Wholesale Unit from doing or omitting to do something in respect of the provision of a Relevant Wholesale Service that is different for different recipients of that service where those differences reflect the different requirements of the recipients;
    - (b) ...
    - (c) this clause does not limit clauses 47 to 49.
8. The parties differ on the meaning of the phrase "*will not discriminate*" in clause 56.1. The complainants adopt what may be termed a broad view of the definition while TW submitted that a narrow view is appropriate.

9. The narrow view is that for there to be discrimination there must be unjust or prejudicial treatment. It says that there is not discrimination because the offer was made to all service providers and open to all to accept. The offer is not converted into a discriminatory offer if a service provider cannot accept that offer because of its own different circumstances. Any other definition would, in TW's submission, force all service providers to act in the same way or for TW to second guess every service provider's business requirements. In its preliminary determination the IOG accepted that this may be the appropriate definition.
10. The complainants' position is that the loyalty discounts discriminated between service providers. This is particularly so because of the nature of their business and the investment that some providers have made in the unbundled copper local loop network service (UCLL) that Telecom was required to provide service providers with under an UCLL standard term determination.
11. Telecom's position may be summarised as follows:
  - (a) There cannot be discrimination as the same terms and conditions were offered to all service providers and there are no technical or operational reasons that would prevent a service provider from taking these offers.
  - (b) Business decisions of the service providers are not relevant to the test for non-discrimination. The fact that the complainants have made UCLL investments is irrelevant.
  - (c) That different treatment does not amount to discrimination is confirmed by clause 56.2(a) which enables TW to take into account the different requirements for service providers and business units.
12. The complainants submit that the TW position is not correct because:
  - (a) It is discrimination if the terms and conditions are offered in such a way that a service provider would be severely disadvantaged (whether technically, operationally or commercially) if it were to accept it.

- (b) It is discrimination under clause 56(1) to treat any service provider (or Telecom Retail) differently in any material way unless the exceptional circumstances of clause 56(2) apply.
- (c) "*Discriminate*" should be given its normal dictionary meaning. That meaning does not require the treatment to be unjust or prejudicial, it merely has to be different.
- (d) The purpose of operational separation is to remove the bottleneck control Telecom has had over the access network. It is to open up competition at the retail level between TW's downstream customers including Telecom Retail and others and to encourage investment. This prevents TW from competing in a selective manner at the wholesale level with offers which discriminate.
13. It is necessary to give the meaning to the words "*discriminate between*" as they appear in clause 56.1 of the undertakings. Is a broad or narrow meaning to be given? Case law authorities indicate that the purpose of the legislation may dictate which meaning applies. Human rights legislation for instance generally requires that there be a discrimination "*against*" a person, namely that the person be treated unfairly or unjustly. On the other hand, Courts have interpreted other legislation, where treatment between persons has been different but not necessarily prejudicial or unfair, as amounting to discrimination.
14. The issue of whether a broad or narrow approach should be adopted was considered by the High Court of Australia in *Bayside City Council v Telstra Corporation Limited* (2004) 206 ALR 1, where the Court said:
- [40] Discrimination is a concept that arises for consideration in a variety of constitutional and legislative contexts. It involves a comparison, and, where a certain kind of differential treatment is put forward as the basis of a claim of discrimination, it may require an **examination of the relevance, appropriateness, or permissibility of some distinction by reference to which such treatment occurs, or by reference to which it is sought to be explained or justified.** In the selection of comparable cases, and in forming a view as to the relevance, appropriateness, or permissibility of a distinction, a **judgment may be influenced strongly by the particular context in which the issue arises. Questions of degree may be involved.** (Emphasis added)
15. A similar approach to discrimination was recently taken by the Supreme Court in this country in *McAlister v Air New Zealand* [2009] NZFC 78, 20

July 2009 where it was said that in determining whether there is discrimination it is necessary to choose the:

... comparator which **best fits the statutory scheme** in relation to the **particular ground of discrimination which is in issue**, taking full account of all facets of the scheme, including particularly any defences made available to the person against whom discrimination is alleged. (Majority Judgment, Elias, Blanchard, Wilson JJ) para 34. (Emphasis added)

These authorities indicate that the meaning of "*discrimination between*" must be gleaned from the context in which it is used.

16. In considering the definition in context the purpose of the Act is an important base. Section 69A of the Act states:

The purposes of this Part are –

- (a) **to promote competition in telecommunications markets for the long-term benefit of end-users of telecommunications services in New Zealand;** and
- (b) to require transparency, **non-discrimination, and equivalence** of supply in relation to certain telecommunications services; and
- (c) **to facilitate efficient investment in telecommunications infrastructure and services.**  
(emphasis added)

17. TW's submissions supporting a narrow meaning of the term "*discrimination between*" may be summarised:

- (a) The undertakings allow for some differentiation and therefore differentiation in itself does not amount to discrimination. Something more such as prejudice and injustice is required. Clause 56.2(a) of the undertakings (paragraph 7 above) acknowledges that there may be differences in treatment. The use of the words "*avoidance of doubt*" in this clause rather than "*notwithstanding*" clearly indicates that differentiation of itself is not discrimination.
- (b) TW is not prevented from competing in the wholesale market. A narrow view of the meaning of the term is therefore required as to give it a broad meaning imposes too onerous a requirement on Telecom. It is contrary to commonsense and the concept of competition for the words "*discriminate between*" to be construed in a way that imposes on TW a requirement to second guess every

service provider's business requirements or prevent normal commercial business arrangements.

18. The following factors favour the complainants' submission that a broad meaning should be given to the words:

(a) When the purpose of the Act is considered, the words should be given a competition law meaning to ensure equivalence of inputs so that Telecom provides the "same" service to itself and service providers in order to achieve that equivalence. In this sense, non-discrimination and equivalence are aligned.

(b) A key objective of operational separation was the elimination of discrimination at the wholesale level. This is apparent from statements made at the time of the undertakings including the following:

- In a Ministry of Economic Development paper of April 2007, the Minister of Communications wrote a foreword which included:

... operational separation will ensure that all service providers, including Telecom, receive critical wholesale services on equivalent terms, and it will reduce the ability and incentives for the incumbent operator to discriminate against its wholesale customers.

- The Minister of Communications in a speech to TUANZ on 8 May 2008 said:

Equivalence of inputs is one of the cornerstones of operational separation as it removes the ability of Telecom to discriminate in favour of itself. Telecom must provide relevant regulated services at the same price, on the same technical and commercial terms, using the same operational support system and processes, **to all market participants including itself. Provision of relevant non-regulated services to other providers, if offered, must be non-discriminatory.** (emphasis added)

- In the third reading of the Telecommunications Amendment Bill the Minister said:

We will end up with an enforceable, binding, robust, three-way operational separation **that will require**

**non-discrimination in wholesale markets and fair access to bottleneck and wholesale services. It will also underpin the other pro-competitive disciplines in this Bill.** (emphasis added)

- (c) In many other legislative contexts the word "*discriminate*" is prefaced by words such as "*unjustifiably*" (Civil Aviation Act, s 88); "*unfairly*" (Companies Act, s 174); "*undue*" (Electricity Act 1992, s 172D(3)). There are no similar words before "*discriminate between*" in clause 56.1 which require an element of prejudice or injustice to be read into the meaning of the term.
- (d) The words "*discriminate against*" which are often used in human rights and employment contexts appear to carry notions of injustice and prejudices. The same inference is not necessarily drawn from the words "*discriminate between*" in legislation enacted for competitive purposes.
19. The IOG accepts that in the absence of a definition of the term "*discriminate between*" in the undertakings, it is necessary to balance the competing arguments and form a view. That view may not be shared by all participants in the telecommunications industry. It is obvious from the submissions received by the IOG that some of the smaller service providers support the TW view. On balance however, the IOG when considering the underlying purpose of operational separation, and the context in which the words appear in the undertakings, and the absence of pejorative words such as "*unjustifiably*", "*prejudicially*" or "*unfairly*" favours the broad view. This would appear to be the purpose of the Act and to give a narrow view would enable the provisions of clause 56 to be easily circumvented. In this case the distinction may be academic.
20. On the facts of this case, it is not necessary to determine the extent to which Telecom needs to take into account the different requirements for service providers and business units. However, it is appropriate to comment on clause 56.2 of the undertakings which does allow for some differentiation. That clause cannot in the view of the IOG be used to justify making different offers to different groups of service providers. Service providers will offer different products and have different means of delivery. The standard conditions of an offer may not apply to the

particular circumstances of a service provider. Clause 56.1 allows TW to adjust its offer to take into account the different requirements, which would presumably normally be technical, of the recipient service provider. It does not permit TW to frame its offers in a way which discriminates between service providers.

21. It is therefore the IOG's view that an offer which is made to all service providers on the same terms and conditions and where there are no technical or operational reasons that would prevent a service provider from accepting the offer, may nevertheless be discriminatory.
22. Its reasons for determining that the loyalty offers are discriminatory in this case are:

- (a) A fundamental element of the undertakings is to allow service providers the benefits of UCLL. The IOG is aware that one of the service providers has already expended a considerable sum of money on UCLL in Auckland. For the reasons given in paragraph 24 below, the IOG accepts that this complainant is not commercially in a position to accept the loyalty offers. Another complainant who proposes to utilise UCLL is in the same position.
- (b) The TW executive paper which formed the origin of the loyalty offers contains comments which in the IOG's view establish that the offers were constructed in a manner to prevent those utilising UCLL from accepting them (this paper went to a limited group of the Executive in accordance with the undertakings). The paper was concerned at competition which was emerging in the wholesale market.

There were comments in the paper which gave the rationale for the proposed offers which, in the IOG's view, carry the inference that the offers were designed in a way that although there may have been no technical reason for Vodafone not accepting them, the complainants because of their commitments to unbundling and UCLL would in effect not be able to accept them.

- (c) On 24 March 2009, a TW account manager emailed Vodafone to advise Vodafone of the New Zealand loyalty offer. The email contained:

This offer will not suit Vodafone but we are still considering those options that may be better suited to Vodafone.

TW's submissions downplay this email and said that "*the account manager chose to indicate effectively that the offer may not suit Vodafone and it may choose not to take the offer, however it was made available to Vodafone for its consideration along with all other customers*". The email was an indication however that the account manager was aware that Vodafone because of its UCLL application would not be accepting the offer.

(d) TW denies that it deliberately designed the offers so that certain service providers could not take them up. It said TW "*specifically designed these offers to meet the request of a group of customers, with a pressing need, in a manner that made reasonable commercial sense for Telecom Wholesale*". It noted that offers may be attractive to some customers and not to others. The IOG accepts that offers may not always be acceptable to some service providers because of their particular circumstances and may not amount to discrimination. However, the effect of the loyalty offers was to enter into contracts with a segment of customers who do not intend to unbundle and to provide Telecom with a competitive alternative to UCLL being provided by Vodafone and Orcon (a subsidiary of Kordia). The offers were in effect discriminating against those who had participated in unbundling.

23. When the effect of the loyalty offers on the complainants is analysed and the reason for their development taken into account, the knowledge that UCLL participants would not be in a position to accept them for commercial reasons, the considerable investment which one complainant has made in UCLL, the IOG is of the view that the loyalty offers do discriminate between service providers and effectively prevent those who have embraced UCLL, a fundamental plank of operational separation, from effectively competing with TW.
24. The IOG is of the view that a service provider which has expended a considerable sum on the unbundled exchanges is at a considerable competitive disadvantage because the loyalty offers apply to exchanges which are not unbundled and exchanges that will be cabinetised. It can

offer lower service prices from the Auckland exchanges it has unbundled but cannot do so for exchanges that it has not unbundled and the 50% of Auckland lines that are (or soon will be) served from street cabinets. Further, it cannot offer the service at those prices to those parts of New Zealand, which are most of the areas outside Auckland, which have not yet had their exchanges unbundled by the service providers. It would have to compensate its customers for the foregone loyalty discount for Auckland street cabinets and the rest of New Zealand to attract customers in this market. If it were to abandon its unbundled services it would lose a considerable investment.

25. It is therefore the IOG's view that in this case there was discrimination. In coming to this view, it notes that Telecom has embraced operational separation and even its competitors, some of them complainants in this case, accept that Telecom has, apart from this instance, complied with its undertakings in a transparent and open manner. In this case, TW believed it had the right to make the loyalty offers without breaching the undertaking, but for the reasons given the IOG does not share this view.

### **Equivalence of Inputs**

26. Clause 47.1 in the undertakings requires TW to provide service providers with relevant wholesale services on the EOI standard by specified dates set out in schedule 1 of the undertakings. Basic UBA referred to in the loyalty offers has to be offered on *December 2009 Requirements* (a migration step towards EOI) by 30 September 2009. This is an enforceable milestone under a variation to the undertakings agreed between Telecom and the Minister on 10 June 2009.
27. The *December 2009 Requirements* is defined for Relevant Service, which includes basic UBA, and a relevant portion of the definition reads:
- (i) Telecom Business Units and Service Providers are provided with the same service on the same terms (including price).
28. The undertakings provide that "*the same*" as used in the definition of *December 2009 Requirements*, "*means exactly the same*". There are some exceptions to "*exactly the same*" and the only one which would possibly apply in the circumstances of these complaints is the exception relating to "*differences that are requested by a Service Provider in writing*

*and agreed to by Telecom*". This exception is in paragraph 3.3 of the interpretation to the schedules of the undertakings.

29. The IOG does not consider that the exception referred to in the previous paragraph can apply to the loyalty offers. The intent appears to allow differences which are required to meet the particular technical requirements of a service provider.
30. The definition of EOI is specific. As from 30 September, in respect of Basic UBA to which the enforceable milestone applies on that date, Telecom must deliver the service to itself and the service providers on the same terms including price. It will not be doing this if it is providing the service to some service providers on loyalty terms and to others on terms with a different price because they have not complied with the loyalty conditions.
31. TW submitted that EOI did not apply to the loyalty issue for various reasons. The IOG does not accept its submission for the following reasons:
  - (a) The submission that the undertakings do not expressly provide for equivalence between service providers is not accepted. If there is not equivalence between service providers, except in those cases where exceptions apply, then the service providers are not receiving the services on the same terms and conditions.
  - (b) It is not accepted that it is sufficient that service providers are provided with the opportunity to "take" the same terms as Telecom Retail. TW's point is that the word "provide" in the definition does not require service providers to "take the same terms". This submission equates to the word "provide" with "offer". The undertakings do not use the term "offer" which they could have done if that was what was intended. It would be contrary to the objective of operational separation to give the term the meaning which TW contends for. The relevant consideration is the provision of services.
  - (c) TW suggests that the offers fall within the exemption of "*differences that are requested in writing by a service provider and agreed to by Telecom*". This right is referred to in para 3.3 of the interpretation

provision of the schedules to the undertakings. The IOG's interpretation of this provision has been referred to above. It would be inconsistent with the purpose of the undertakings to give this meaning to that provision. Further, this is not what happened in this case. The loyalty offers were made and the service providers were told that if they "*would like to participate in this offer or need more information please contact your Telecom Wholesale account manager*".

32. It is therefore the IOG's view that TW will be in breach of clause 47 in respect of Basic UBA on 30 September 2009 if on that date contracts arising from the loyalty offers remain in existence.

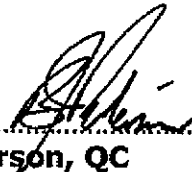
### **Comment**

33. TW's position is that the undertakings, if interpreted in the manner which the IOG interprets them is correct, effectively prevent it from competing in the wholesale market. It is not for the IOG at this stage to make any comment on that other than saying that in its view TW can compete in the wholesale market on price but any competition must not discriminate and EOI must be complied with.
34. There has been unfortunate media comment in respect of these complaints. The IOG's view is that TW moved to counter what it saw as a major competitive threat and did so in a way which it believed did not infringe the undertakings. While the IOG accepts that Telecom believed it was not infringing the undertaking and that the interpretation of clause 56 is not without its difficulties, it has for the reasons set out above, concluded that there is currently a breach of the undertakings and that there will be a further breach if contracts entered into pursuant to the loyalty offers are still in force when the EOI requirements become enforceable milestones.
35. It is not for the IOG in determining a complaint to make suggestions as to what methods may be employed by the industry in endeavouring to clarify what TW sees as an unjust result arising from how the IOG has interpreted the undertakings, or whether there is a compromise acceptable to all participants in the wholesale market.

**Result**

36. For the reasons given, the IOG determined that the loyalty offers are non-trivial breaches of clause 56 of the undertakings. If contracts pursuant to them for Basic UBA are still in existence on 30 September 2009, there will be non-trivial breaches of clause 47 of the undertakings.

Dated *27th day of* August 2009



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**B J Paterson, QC**  
**Chairman for and on behalf of IOG**