Submission on Discussion Paper – Protecting businesses and consumers from unfair commercial practices dated 10 December 2018

22 February 2019

Overview

1 Thank you for the opportunity to comment on the Discussion Paper *Protecting businesses and consumers from unfair commercial practices* (**Discussion Paper**) released on 10 December 2018.

2 Due to our position as a wholesale telecommunications provider our comments are limited to the parts of the Discussion Paper regarding business to business interactions.

3 As the Discussion Paper notes, ensuring New Zealand has a regulatory environment in which businesses and consumers can transact effectively and efficiently is critical, and the fact New Zealand is considered one of the easiest countries in the world to do business illustrates to us that overall our settings are working well.[1]

4 In looking to address some of the behaviours on the margin we would note the importance of ensuring any proposed solutions are proportionate to the size of the problem. Any legislative 'safety net' against the poor behaviour of a minority should not disproportionately increase risk and uncertainty for the majority of businesses or conflict with bespoke regulatory regimes developed to regulate conduct and contracting between participants in specific industries, such as telecommunications.

5 We do not perceive a need for significant reform of the regulation of conduct by businesses in relation to other businesses.

Business to business practices: Option 1 – Introduce a high-level protection against unfair conduct

6 Our view is that the current regulatory environment relating to business conduct works well and that further general provisions to govern unfair conduct are not required. However, if some form of prohibition or restriction were nonetheless introduced, we would simply ask that a priority for its development should be limiting uncertainty for the vast majority of businesses such as ourselves, who consider

[1] "Doing Business in New Zealand 2019", The World Bank Group, May 2018 http://www.doingbusiness.org/en/data/exploreeconomies/new-zealand

themselves good corporate citizens and conduct our business dealings in a professional manner.

7 As the Discussion Paper notes, much of the unfair commercial conduct reported by businesses is already prohibited to a large extent, or is subject to existing remedies. This suggests that increasing compliance with existing standards should be the focus, rather than introducing further regulation across the business community.

Extending option 1 to address unfair contracts

8 While we understand the reasoning behind protecting vulnerable businesses from certain unfair contract terms, we do not support a general extension to the point where a contract as a whole could be declared 'unfair'. The main subject matter or price of a contract for example, are fundamental elements of the parties' bargain. The suggestion that these types of essential terms could subsequently become unenforceable due to a court's finding of 'unfairness' would significantly increase risk to contracting parties. The impact of the resulting reduction in certainty of contract would likely be felt most by precisely those more vulnerable parties that the option was designed to protect, namely smaller businesses without easy access to legal resources.

Business to business practices: Option 2 – Extend unfair contract terms protection to business

9 The Discussion Paper notes the current regulation of unfair contract terms in consumer contracts under the *Fair Trading Act* and questions whether similar protections should apply to contracts between businesses (Option 2 of the policy options proposed by the Discussion Paper). This regime includes a "grey list" of potentially unfair terms which may then be declared to be unfair by a court upon an application by the Commerce Commission.

Businesses do not generally face the same issues as consumers in contracting with other businesses

10 The particular issues encountered by consumers in contracting with businesses do not similarly apply to cases of contracting between businesses. In particular, consumers are more likely to face:

- "take it or leave it" offers in the nature of standard form contracts rather than negotiated contracts;
- difficulties in obtaining legal advice and other relevant support for negotiations due to shorter timeframes available for negotiating and entering into contracts; and
- an inequality of bargaining power due to the low marginal value to the business counterparty of entering into a contract with any particular consumer.

11 If consumer style protections were applied across the board to all businesses, it appears very likely that any benefit potentially afforded to more vulnerable businesses

would be significantly outweighed by the corresponding reduction in certainty and freedom of contract in commercial dealings between businesses.

12 As an alternative approach, the Discussion Paper raises the possibility of limiting the extension of consumer protections in relation to unfair contract terms to only a smaller subset of businesses based on:

- Employee count (eg. Businesses with fewer than 20 employees);
- Turnover (eg. Only businesses with a turnover of less than $2 million); or
- Whether there is a material imbalance in the negotiating power between the relevant businesses (this would be determined case-by-case, as opposed to an absolute metric).

13 It is possible that the first two of these proposed criteria would in some cases assist in identifying businesses more likely to be vulnerable to unfair contract terms (akin to the position of a consumer contracting with a business). However, employee count and turnover are not always representative of a company's bargaining power. For example, in some transactions although the actual contractual counterparty may be a smaller subsidiary or special purpose vehicle, the larger corporate group of which it is a part may have significant market share and hence bargaining power in negotiations. Similarly, the smaller company may be able to rely on the legal resources of the larger corporate group in contract negotiations.

14 As for the third proposed criterion, we submit that the concept of a "material imbalance of negotiating power" is inherently subjective. If it is to be determined "case-by-case" as the Discussion Paper suggests, then parties would be left in the uncertain situation of not knowing whether or not certain if their contracts were subject to unfair contract terms protections.

15 We do not believe that the rationale for consumer protections is as applicable for business to business contracting or that based on the information provided the threshold for additional government regulation in this area has been met.

Additional considerations arising in a regulatory environment

16 As well as general legal requirements, Chorus' activities are governed by:

- deeds of undertaking to the Crown in relation to both our copper and fibre businesses;
- regulatory requirements specifying terms of our copper-based services specified under the *Telecommunications Act 1991*; and
- contracts with the Crown in relation to the deployment of, and terms of access to, our fibre based services.

17 In addition to the above, the *Telecommunications (New Regulatory Framework) Act 2018* has established a new framework for the regulation of our fibre network. The

Commerce Commission, with the agreement of the Minister of Brodcasting, Communications and Digital Media, will take until 2022 to implement the first phase of this framework. In general, these regulatory instruments seek to address any potential issues arising from our market power in relevant wholesale markets.

18 The above examples illustrate how in heavily regulated industries potential imbalances in negotiating power have already been proactively identified and mitigated by lawmakers. As a result, specific regulation targeted at addressing the impact of unfair conduct or unfair contract terms would not have the same role to play in such industries and could conflict with some of the elements of telecommunications regulation.

19 Furthermore, we are subject to a regulatory obligation of non-discrimination in relation to many of our products and services. This means that we must offer those products and services to all of our customers on equally favourable terms. We cannot, for example, discriminate in the pricing of our services by offering bulk discounts to customers which purchase larger quantities of a particular product or service.

20 In regulated industries subject to non-discrimination obligations, the desired result of protecting smaller businesses from being forced to accept "unfair terms" is therefore already achieved by a different means. This is because all businesses enjoy the benefit of the most favourable contractual terms negotiated by larger businesses in any event.

21 In our case, most of the businesses to which we provide products and services to are large and sophisticated and enjoy the support of significant commercial and legal resources in negotiations. This means that any smaller businesses in the industry are equally able to benefit from the terms negotiated by their larger and better resourced competitors. In addition, the majority of Chorus' revenue is derived under contracts that have either been approved by a Crown agency such as Crown Infrastructure Partners or mandated by the Commerce Commission and, in both instances, subject to extensive industry negotiation. While a number of these contracts are in the form of standard form offers, this regulatory oversight of the negotiation of the contracts under which we offer products and services protects our customers against the inclusion of unfair terms.

22 In other words, the existing telecommunications regulation, as supplemented by the new regulatory model to be implemented post 2020, already performs the function proposed for new regulation against unfair commercial practices.

23 The overlay of a further generic regulatory regime targeted at unfair commercial practices runs the risk of resulting in an industry subject to multiple competing regulatory regimes. While these regimes may have some desired outcomes in common, there is a risk of unintended consequences arising from their interaction in application. The current telcommunications industry regime reflects a significant investment in building a bespoke regulatory environment in which businesses such as Chorus operate. It is difficult to see a generic regime which is designed to be applied across all industries providing a more efficient or effective regulatory result.

Enforcement, penalties, and remedies

24 The Discussion Paper proposes imposing penalties on businesses which include unfair contract terms in their standard form contracts, even without the need for a term to have previously been declared to be unfair (as is required under the equivalent consumer contracting regime).

25 In the event that a decision was taken to extend consumer protections against unfair contract terms to business to business contracts, we are of the view that a term should need to be the subject of a declaration by a court before any remedy should be available. This would ensure that the particular circumstances of the industry and transaction are taken into account, as opposed to a determination of unfairness being made in the abstract.

26 In terms of response to the inclusion of an unfair term, we would not support the application of penalties. Instead, we are of the view that the inability to enforce an unfair term should remove any incentive to include the term in a contract, and should also cancel out any detriment to the affected business. Such a response to the use of an unfair term is consistent with the objective of protecting vulnerable parties from unfair contract terms.

Retrospectivity

27 Also, given the inherent uncertainty of as to whether any given term is "unfair", it would be important to ensure that a declaration would void an unfair term only from the date of the declaration, not retrospectively. Voiding a term retrospectively could have severe and unpredictable consequences out of all proportion to any detriment caused by the unfair term.

28 For example, retrospectively invalidating a clause that gave one party the right to amend the contract terms could undermine a long series of ongoing dealings between the parties made in reliance on the terms that were assumed to apply at the time.

29 Similarly, retrospectively invalidating a liability limitation could leave a service provider exposed to unlimited liability for services going back several years, even where the service provider would not have accepted the work had it known that the term would be retrospectively invalidated.

30 At a minimum, retrospectivity should be avoided unless the party that included the term in the contract was reckless as to whether it was unfair. This would still have the effect of reducing the prevalence of unfair terms, without visiting disproportionate consequences on businesses that have made genuine efforts to comply.

31 We would be happy to discuss further any of the above if helpful.