
**Telecom New Zealand's response
to the Commerce Commission's
*"Guide to Regulatory Decision
Making by the Commerce
Commission for the
Telecommunications Sector"***

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EXECUTIVE SUMMARY

- 1 Telecom New Zealand Limited (**Telecom**) welcomes the opportunity to comment on the “Guide to Regulatory Decision Making by the Commerce Commission for the Telecommunications Sector” (**Guidelines**). It is clear that a lot of effort has gone into their preparation and that they demonstrate the Commerce Commission’s (**Commission**) willingness to get industry participants’ input into how the Commission should approach its regulatory functions for the telecommunications sector.

Why guidelines are important

- 2 Historically, New Zealand’s physical isolation from the rest of the world has limited the country’s ability to participate in international markets.
- 3 Recent developments in telecommunications have closed this gap to some extent, and going forward, the deployment of new technologies driven by customer demands, such as the development of mobile networks with greatly enhanced data carrying capabilities, enhancements to broadband delivery and new applications will help to advance New Zealand’s overall growth prospects. These innovations require substantial investment, and therefore investor confidence in the regulatory setting.
- 4 Clear guidelines about how a regulator will approach its decision-making functions – the principles it will apply and the objectives it will seek to achieve – help to provide investors, both local and international, with the necessary confidence to invest.
- 5 Clear guidelines will thereby ensure that the emergence of new technologies is facilitated and even accelerated, in accordance with consumer preferences and demand.

What guidelines should deliver

- 6 Regulatory guidelines should deliver predictability (both procedural and substantive) for the benefit of all industry stakeholders by providing clarity around regulatory principles and their application with consequential regulatory certainty.
- 7 This can be further strengthened through an explicit commitment to pre-declared decision-making principles. To promote certainty industry needs to know how the regulator sees its role and how it will approach the implementation of regulation. This is the function of clear regulatory decision-making guidelines.
- 8 International regulatory best practice principles¹ provide sound, proven templates and include, for example:
 - 8.1 Clearly communicating executable regulatory objectives to guide the regulator, promote certainty around decision-making, and provide a yardstick for measuring the performance of regulation;

¹ **Annex 1** provides an illustration of how New Zealand’s framework compares to overseas frameworks in terms of international best practice principles. Annex 1 also sets out Ofcom’s voluntary commitment to regulatory principles.

- 8.2 Ongoing and regular engagement with market participants to ensure that regulatory decisions are well-informed, proportionate, and made against an assessment of the wider context (including investor perceptions) – this is crucial where aspects of the wider context are constantly changing;
- 8.3 Adopting a presumption against regulation;
- 8.4 Seeking to minimise regulatory burdens, so that regulation is targeted, proportionate and least intrusive;
- 8.5 Seeking and facilitating engagement with industry and other key stakeholders to facilitate appropriate and pro-competitive solutions through industry self- and co-regulation, recognising that industry has the skill set and the motivation to work through the hard issues;
- 8.6 Regularly reviewing the effectiveness of existing regulation with the objective to deregulate where appropriate; and
- 8.7 Being accountable through review of performance by the regulator against regulatory targets and market reviews as well as being accountable for decisions through judicial and merits review.

The importance of engagement

- 9 Engagement is crucial. For regulation to be proportionate and forward looking the regulator must be well-informed. A well informed regulator will understand the industry, its structure, its economics and business models, the services it offers and end-user demands. To do so, it will have engaged with industry and assimilated information gathered through that process to build a comprehensive understanding of the industry it regulates.
- 10 We would welcome further discussion to set up an appropriate model for engagement that maximizes the practical value for the industry and Commission alike, acknowledging that both sides have constraints on their resources.

A deep understanding of the economic principles

- 11 The Commission rightly makes its regulatory decisions by applying economic principles. We acknowledge that the Commission is a good regulator by world standards in terms of the level of analysis that it undertakes before making a decision and in terms of its genuine endeavour to grapple with economic principles in an open minded way.
- 12 However, the regulatory problems are becoming more complex, the economic models that must be applied are becoming more sophisticated and questions are being raised that businesses, Governments and regulators around the world are struggling to answer, such as:
 - 12.1 If dynamic efficiency is critically important, how do you measure it or take it into proper account?
 - 12.2 What is the best model for carrying out cost benefit analysis?

- 12.3 How does the presence of a two sided market change the analysis of competition issues?
- 12.4 To what extent is transferring benefits from one group of consumers to another a relevant consideration in regulatory decisions?
- 12.5 How does assessment of WACC need to change when we are thinking about regulating markets for which investment is yet to be committed to?
- 12.6 What is workable competition?
- 13 The Commission has to tackle these kinds of question head-on as the answers are critical to whether the regulatory decisions being made are sound.
- 14 We would therefore encourage the Commission to drill down into these kinds of economic topics further and we would very much like to participate and contribute to the Commission's early thinking in this regard.

Appreciating the wider context

- 15 Building a comprehensive understanding of the industry and the way in which the economic principles play out in practice, also requires regulators to step back and appreciate the wider context of the markets they regulate and consider – to the extent they can - future market developments, including the impact of new technologies. Consideration of the wider context is as important as considering specific markets issues. If, having assessed both the specific market issue in question and the wider context, intervention is to be considered, the final decision of such a well-informed regulator is likely to result in better and intended outcomes than that of a regulator who is not. There is persuasive empirical evidence² that regulation which is implemented in a piecemeal way, or purely on an issue by issue basis:

- 15.1 May be compromised by ill-informed public commentary;
- 15.2 Risks divorce from wider context considerations;
- 15.3 Introduces unnecessary burdens and complexity;
- 15.4 Increases the risk of market distortions; and
- 15.5 Reduces overall welfare for stakeholders whilst potentially lessening the efficacy of the regulation itself.

Deregulation as a measure of regulatory success

- 16 The opportunity for deregulation must not be forgotten. An effective regulatory regime should position deregulation as an active and dynamic part of the regulator's core function and the ultimate achievement in effective and successful regulation. Guidance on when regulation will be removed provides important commercial incentives for industry. The Commission's recent announcement to review the potential for resale deregulation is a positive example of this.

² See for example Ofcom's assessment of Oftel's performance as a regulator in the Strategic Review of Telecommunications of 2004/2005.

- 17 However, New Zealand telecommunications regulation is highly prescriptive. This has created uncertainty in terms of the operational challenges to the business in complying while continuing business as usual, and in terms of maintaining the consistency of the regulatory framework given the speed at which change has occurred and continues to occur, which is not matched anywhere else in the world.³
- 18 By way of simple illustration, **Annex 2** compares the level of prescription under the Local Loop Unbundling (**UCLL**) determination in New Zealand and the equivalent determination in the UK, which demonstrates that:
- 18.1 Telecom's obligations are around 3.5 times more prescriptive than the reasoning accompanying those obligations and around 5.5 times more prescriptive than comparable obligations imposed on two substantial market power (**SMP**) operators in the UK for LLU; and
- 18.2 BT's comparable obligations are accompanied by around twice as much reasoning from the regulator and are at least 5.5 times less prescriptive than those imposed on Telecom⁴.
- 19 Such comparisons, together with the complexities that have arisen under the New Zealand regulatory framework (attributable at least in part to the highly prescriptive nature of service/market-centric regulation, which we touch on later in our response), should cause pause for thought. We think it is time for a re-assessment to ensure that regulation of the New Zealand telecommunications sector is consistent with international regulatory best practice principles and is fit for purpose.
- 20 The key point is that a large quantity of regulation does not equal a good regulatory outcome, or even an effective constraint on the forms of behaviour that a good regulator should seek to eliminate. Instead, regulations should be targeted on addressing the problems and otherwise kept to a minimum.
- 21 This concept has been well articulated previously by Ofcom in relation to its assessment of its predecessor Oftel:
- 21.1 *"... the continuance of a complex regulatory mesh, devised over twenty years of regulation and in many areas dependent upon intrusive micro-management to achieve its purposes, yet which, in aggregate, has failed effectively to address the core issue of BT's control of the UK-wide access network."*⁵ and
- 21.2 *"...This outcome is not optimal for citizens and consumers, for BT's competitors nor for BT itself. It is restrictive and costly to all parties, and at this stage of network and technology development it is potentially damaging to our long-term competitiveness as a nation. This will become an even more critical issue with the deployment of next generation technologies, where*

³ **Annex 3** contains a timeline of the regulatory design in New Zealand with a comparison to the UK and Australia.

⁴ This quantification of the relative levels of prescription can be criticised as it is based on the numbers of words in each of the documents rather than the content. However, the overall point that the NZ equivalents of the UK documents is broadly correct and the difference in the size of the documents is generally reflective of this.

⁵ See Foreword to the Ofcom Strategic Review of Telecommunications 2004/2005

*current rules of interconnection and many of the related wholesale products will no longer apply*⁶.

Putting the regulatory principles into practice

- 22 The Commission's Guidelines are a positive step in the direction of best regulatory practice and we are encouraged by a number of regulatory objectives that the Commission identifies as central to its regulatory decision making. However, the Guidelines stop at a fairly descriptive treatment of the Telecommunications Act framework, and are silent on *how* the Commission will go about establishing the common objectives of certainty, and regulation that is sensitive to market context. They also do not drill down to any of the emerging difficult questions in relation to the application of economic principles that regulators around the world are grappling with (referred to above). We encourage the Commission to develop the Guidelines further and in a way that addresses these kinds of implementation issues.
- 23 We have proposed some ways in which the Commission can engage the industry on these issues, drawing materially from international regulatory best practice principles. We welcome further engagement with the Commission on how to move forward in an open and constructive way.
- 24 Ultimately, we hope that above all else, the Commission's subsequent development of the Guidelines would highlight the importance of embracing principles of regulatory best practice, developing further thinking around the economic questions we have raised above and the need for fulsome, regular, dialogue with industry to arrive at shared understandings and mutually acceptable regulatory solutions to both the economic questions and the forward looking challenges that industry faces.
- 25 Ongoing dialogue will help ensure that regulation moves in an enabling and proportionate way as the market and industry meets additional challenges in the current economic climate. These challenges give rise to some difficult but nevertheless important topics. The answers are not yet clear anywhere in the world, but the issues are being thoroughly discussed in many fora and jurisdictions at the moment, and this needs to occur here too.
- 26 To facilitate this dialogue we think the Commission should adopt processes used elsewhere in the world by formulating a series of questions around the challenges facing the sector that need to be debated and from which decisions made as to appropriate regulatory outcomes⁷. We would encourage the Commission to carry out such an exercise with industry as soon as practicable.
- 27 In doing so, the Commission may wish to consider asking key questions as Ofcom did, as a way of enhancing dialogue between key stakeholders and its own level of understanding. A helpful reference point for this exercise is Ofcom's "Final consultation document for its Strategic Review of Telecommunications", published in 2005. That review was "designed to set out a strategic direction for Ofcom's activities in relation to telecoms, and to create a new settlement" between the

⁶ See paragraph 1.22 of Telecommunications Strategic Review Discussion Document – Ofcom 2004/2005

⁷ **Annexes 5 and 7** provide a flavour of the level of thinking and industry engagement occurring on telecommunication regulatory issues overseas compared with New Zealand.

regulator, the companies it regulates, and citizens and consumers. By using the word “settlement”, we take this to mean that the intention was to set up a model of engagement that was permanent, sustainable and which all parties could place confidence in.

- 28 To achieve those objectives Ofcom posed a number of fundamental questions for review. These were:
- 28.1 In relation to the interests of citizen-consumers, what are the key attributes of a well-functioning telecoms market?
 - 28.2 Where can effective and sustainable competition be achieved in the domestic telecoms market?
 - 28.3 Is there scope for a significant reduction in regulation, or is the market power of incumbents too entrenched? and
 - 28.4 How can [the regulator] incentivise timely and efficient investment in NGNs?⁸
- 29 For at least some of the difficult but key economic issues, the Commission should consider whether it may be appropriate to develop, through industry engagement, a toolbox, or subset, of issue-specific guidelines. We would find this particularly helpful in respect of:
- 29.1 How the Commission will seek industry engagement on the regulatory settings prior to investment;
 - 29.2 How the Commission will engage with industry and carry out its market monitoring function;
 - 29.3 How the Commission will approach market definitions and competition assessments in this sector;
 - 29.4 How the Commission will approach cost benefit analysis;
 - 29.5 How the Commission will assess the dynamic efficiency implications of a regulatory decision;
 - 29.6 Applying the weighted cost of capital (**WACC**) in this sector⁹; and
 - 29.7 Applying pricing principles and particularly, TSLRIC¹⁰.
- 30 We think the Commission should increase the certainty of the regulatory framework through ongoing engagement with industry on these issues, and others, outside the

⁸ We set out some additional questions that Ofcom asked industry and consumers in **Annex 7**. The Commission could ask similar questions.

⁹ We acknowledge that the Commission is currently working on guidelines for estimating the cost of capital. Once this generic uber document is completed some further guidance on approaches specific to the telecommunications sector would be helpful.

¹⁰ We acknowledge that there is a paper on this. However, it too general to provide helpful guidance and requires updating

constraints of a particular regulatory process. One example of moving forward with stakeholder feedback was the process used by the Commission in relation to mergers that culminated in merger process guidelines last year. A similar process could be considered for regulatory engagement.

- 31 Major decisions need to be made with far-reaching implications for the regulatory and commercial landscape. There is no time better than the present for the Government, regulator and industry to understand each other's roles and accountabilities in the telecommunications environment. Establishing, acknowledging, and then fully utilising, all parts of the regulatory process - as noted by the Commission in Figure 1 of the Guidelines – is a critical part of this exercise.
- 32 In summary, in this submission Telecom:
- 32.1 Provides support for many of the statements in the Commission's Guidelines;
 - 32.2 Comments on the importance of constructive engagement in the New Zealand context;
 - 32.3 Comments on coherent regulation;
 - 32.4 Supports and discusses the value of committing to regulatory principles;
 - 32.5 Raises some of the difficult economic questions that require further exploration and suggests topics for the Commission to include in a regulatory "tool box";
 - 32.6 Supports the value of facilitating industry self- and co-regulation; and
 - 32.7 Offers comments on institutional arrangements in support of these goals.

THE GUIDELINES

- 33 The Commission's Guidelines identify a number of objectives, and acknowledge a number of key contextual characteristics, which we agree are central to sound regulatory decision-making in the telecommunications sector based on appropriate policies determined from time to time by Government as part of any engagement process. In particular:
- 33.1 We agree that the purpose of the Commission's Guidelines should be "to provide greater clarity to stakeholders on how the Commerce Commission discharges its powers and functions under the Telecommunications Act 2001";¹¹
- 33.2 The Guidelines note that they are an initiative produced in support of "the Commission's strategy of proactive engagement with stakeholders to enhance mutual understanding and promote regulatory certainty in telecommunications markets";¹² and
- 33.3 The Guidelines acknowledge that:
- (a) The telecommunications industry "is a key enabler of productivity and innovation in other sectors and the wider economy" and that the industry plays a key role in providing leading-edge technologies and services that enable New Zealand to produce innovative goods and services of higher value, and that emerging telecommunications technologies will enable New Zealand firms to establish or improve linkages to international markets and access know-how from the rest of the world more quickly and at lower costs;¹³
 - (b) The underlying economic implications of a decision is critical (by virtue of the extent of discussion of general economic principles in Chapters 4 and 5) of the Guidelines;
 - (c) The need to ultimately give greater weight to dynamic efficiency than other forms of efficiency¹⁴;
 - (d) The markets are dynamic and are characterised by technological progress and uptake of new technologies. Industry participants are looking for regulatory certainty and incentives to invest and innovate as they go forward;
 - (e) "[T]he migration from legacy to future technologies will have an impact on competition in telecommunications markets.... In light of

¹¹ Guidelines, Executive Summary.

¹² Guidelines, Executive Summary.

¹³ Guidelines, paras 1 and 2.

¹⁴ Guidelines para 182

technological developments, existing regulatory settings may have to be reviewed”;¹⁵

- (f) Regulatory decision making is “an evolving process in which regulatory settings are reviewed to ensure that they remain appropriate and proportionate. ...and could involve actions that could lead to...the alteration or removal of existing regulation (deregulation) in particular market segments”;¹⁶
- (g) “[A]n important part of [the regulatory] process is an effective monitoring strategy to ensure that relevant information is collected, for example, on the development of competition and the effectiveness of existing regulatory interventions”;¹⁷
- (h) The Commission will continue to review the appropriateness of legacy models of regulation, particularly as the telecommunications markets continue to change, and whether there are opportunities to consider deregulation;¹⁸
- (i) “[T]he Commission will maintain its focus on responsive and flexible regulation. The Commission will adopt forward-looking perspectives that encourage investment and innovation in the sector, giving consideration to dynamic efficiency aspects where competition is to be promoted, and taking into account investment incentives for all operators”;¹⁹
- (j) “The Commission will target communication with key stakeholders, engage with industry early and proactively, and consult with relevant stakeholders in an open and fair manner”;²⁰ and
- (k) “The Commission has a preference for commercial solutions”.²¹

34 Put another way, the Guidelines articulate the following high-level themes:

34.1 Achieving regulatory certainty and transparency, both substantively and procedurally, for stakeholders;

34.2 The importance of correctly understanding the underlying economics of any decision and making a decision based upon a clear understanding of all relevant economic principles;

34.3 Engaging proactively with stakeholders;

¹⁵ Guidelines, para 41.

¹⁶ Guidelines, para 138.

¹⁷ Guidelines, para 140.

¹⁸ Guidelines, paras 224, 232.

¹⁹ Guidelines, para 234.

²⁰ Guidelines, para 235.

²¹ Guidelines, para 152.

- 34.4 Getting the regulatory settings right to promote the successful growth of the telecommunications sector;
- 34.5 Acknowledging that the industry is dynamic and that regulation (including the review of existing regulation) must also be dynamic to encourage ongoing investment and innovation; and
- 34.6 Ensuring that wherever possible, sector issues are resolved commercially.
- 35 Telecom supports these themes.
- 36 Whilst the Guidelines provide a helpful start, as noted above they stop short of exploring *how* the Commission will implement these key themes when it approaches its regulatory decision-making functions in practice.
- 37 We do not purport to have all of the answers, but in this submission we set out some suggestions, including some concrete examples from international regulatory models, that we hope will inform the Commission's thinking going forward and which can assist in finding appropriate answers. Specifically, these focus on:
- 37.1 Fostering a partnership approach between the industry and the Commission to arrive at mutually acceptable regulatory solutions to issues;
- 37.2 Raising some of the difficult economic questions that require further exploration;
- 37.3 The importance of regular, ongoing, fulsome engagement between industry participants and the Commission to:
- (a) Tackle the difficult topics collaboratively;
 - (b) Help promote sound, well-informed decision-making and coherent regulation;
 - (c) Help minimise the cost and duration of regulation, and the risk of regulatory error; and
 - (d) Enable the regulatory framework to respond effectively to an increasingly dynamic sector;
- 37.4 Why a commitment to clear decision-making objectives and principles is essential; and
- 37.5 Achieving greater industry self- and co-regulation and encouraging, where appropriate, a greater degree of regulatory forbearance.

ENGAGEMENT ON THE MARKET CONTEXT

Update on the market

- 38 The Commission's Guidelines acknowledge that telecommunications markets are dynamic and important to the New Zealand economy.
- 39 The market is in a state of transformation:
- 39.1 Significant changes to the key technological platforms, requiring significant new investment, are taking place with:
- (a) The development of significant enhancements to broadband capability;
 - (b) Increasing substitutability between, and convergence of, fixed line and mobile technologies;
 - (c) The development of mobile platforms with the capability to transmit increasing amounts of data; and
 - (d) The roll out of new mobile and fibre networks and migration to an IP based platform;
- 39.2 There are increasing numbers of participants involved in the supply chain for increasingly sophisticated products to end users (with related logistical challenges); and
- 39.3 Yet, despite all this, traditional revenues are static or declining.
- 40 These changes are happening now and the pace of change occurring in the market is accelerating. These changes will necessitate the development of new economic models and a cautious approach to investment to avoid the risk of inefficient duplication.
- 41 New investments to meet consumer demands will involve sinking substantial capital and moving from relatively static to more dynamic models. Indeed, although traditional business models are in decline, future models are only beginning to emerge particularly in light of IP based telephony, with consequential impact on, for example, traditional interconnection and mobile termination practices, which will require many long-held business models to be re-evaluated.
- 42 The Commission explored some of the implications of technology changes in its NGN Study. It recognised that a key consequence of technology changes is that the value chain is evolving as voice and entertainment services are delivered to end users without using intermediate parties. This disintermediation of the current value chain means that, as with the advent of IP based telephony, business models must change.
- 43 As the value chain in the provision of new services lengthens, new markets and new competitors are emerging that challenge the traditional telecommunications market bottlenecks. For example, there are now as many questions to be considered in relation to the control of content as there are in relation to the control of access

infrastructure. There are also questions to be considered in relation to global search engines, which are fundamentally important for accessing information.

Convergence is driving market change

- 44 The Commission has considered the implications of technology, ownership and market convergence in the context of its submission to the Broadcasting Review of Regulation (Broadcasting Review) and the NGN Study. As the Commission notes, the previously distinct worlds of telecommunications, broadcasting, information technology and media are merging, and will soon be indistinguishable.
- 45 There are a number of important regulatory implications, including a potential lowering of barriers to entry, the increasing importance of spectrum allocation and the need to think differently about the value chain and where market power may lie. The Commission has identified that a key risk is that premium content can become the source of market power which can be leveraged into other markets. Restrictions on content providers are not uncommon in developed broadcasting markets. Equally, search engine businesses are emerging as players with substantial market power in global markets and the implications of this need to be considered carefully.
- 46 The OECD has also recommended that a key ongoing focus for officials should be to identify and remedy barriers to the development of digital content and online business, particularly impediments to competition, and to review possible bottlenecks in digital content markets and barriers to e-commerce. It is the promotion of competition that is likely to be the most effective means for growth of the digital content market.
- 47 From a wider perspective, IPTV and video-on-demand are key services for driving broadband take up and investment. Accordingly, the business case for further development of the broadband market is unlikely to stack up without access to premium content. Current vertically-integrated broadcasters, with existing broadcasting/distribution platforms, control access to premium content in the New Zealand market and have limited incentives to push content onto new broadband platforms. It is unlikely that service providers will be able to deliver comprehensive IPTV and video-on-demand services without a change to the market structure that currently determines access to content.

Role of the Commission

- 48 Whilst the Government has decided not to progress the Broadcasting Review at this time, the implications of convergence for telecommunications markets remain and need to be considered and factored into the overall policy and regulatory framework for the sector.
- 49 Accordingly, the Commission should develop a set of principles relating to how it will consider issues around access to content, how it will approach market definitions in this area, and how vertically-integrated content providers may be permitted to participate in telecommunications markets.
- 50 We look forward to engaging with the Commission on these important issues in due course.

Reality facing investors

- 51 It is unclear what the overall market context will look like as these changes take place. But it *is* clear that the approach to decision-making under the prevailing regulatory framework will need to be guided by sufficiently clear principles to encourage the investment needed for these changes to happen, and to happen quickly, notwithstanding the current economic climate and the competing calls and priorities on capital available.
- 52 This highly dynamic landscape relies on significant investment by local and predominately international investors. New Zealand needs to attract capital to invest in key infrastructure. Its ability to do this will in part rely on the degree to which investors have confidence in the regulatory framework in an economic environment that has become more risk averse.
- 53 Regulatory decision-making impacts considerably on the attractiveness of investment opportunities, the willingness of investors to make large sunk investments, and ultimately the cost to access capital for infrastructure developments. In particular:
- 53.1 The predictability of the regulatory environment over the long term relative to other jurisdictions (since investors must take a long term view where the investment is infrastructure-based); and
- 53.2 The returns that might be available when investing in New Zealand relative to other jurisdictions in both regulated and unregulated scenarios;
- are key considerations for investors when assessing New Zealand as an investment destination.
- 54 Regulatory decisions must therefore be well informed, predictable and least intrusive if they are to stimulate ongoing investment.
- 55 Policy decisions also play their part in achieving or detracting from certainty for investors. International investors are particularly sensitive to policy/political decisions that impose significant costs on private businesses, particularly when the costs are perceived to fall in an inequitable way. The reason for this is that overseas observers may have limited understanding of how political/policy decisions in New Zealand come to be made, and have limited visibility of the processes that lead to them. This can be contrasted with regulatory decisions for which the economic principles that are at play are transparent and understood even if the decision itself is of a controversial nature.
- 56 The relationship between regulatory certainty and investor willingness has been identified in similarly transforming contexts in Australia. In April this year, the Minister for Broadband, Communications and the Digital Economy noted that, in tandem with the Australian Government's commitment to invest with the private sector to build the new National Broadband Network, the Government would "consider a range of regulatory reforms to improve competition and service during the rollout period." Materially, the Minister explained that: "It is important that

industry have the certainty they need to plan for their future and the development of new services.”²²

- 57 It is essential then that we get the regulatory settings, and the approach to decision-making under them, right. The regulatory model must be applied in a principled way and an internally consistent manner. To achieve this, proactive and constructive engagement with the industry is required in order to develop both market-led solutions and shared understandings that can be revisited and improved over time.
- 58 There is good precedent to support such a collaborative approach: in the context of UCLL Co-location, for example, the Commission consulted on and obtained agreement from market participants for a proposed alternative approach to its (initially) literal interpretation of the Initial Pricing Principle when it was demonstrated that such an approach would result in an illogical outcome. The point is that constructive engagement led to a practical solution to a regulatory problem. We would like to think that this kind of engagement will not be limited to “one-off” cases.
- 59 Whilst engagement is essential, it will only get us so far. Ultimately it is the Commission’s responsibility to be aware of the signals its regulatory decisions and practices send to investors and its demonstrated ability to apply the economic principles in an appropriate way. If we are to improve the prevailing investor attitudes, can be enhanced, particularly where investment is desperately needed by industry but investment decisions are yet to be made.

What our investors are telling us

- 60 We constantly receive feedback from our investors on the regulatory framework. Their feedback indicates a perception that:
- 60.1 The New Zealand current regulatory environment is unpredictable and uncertain;
- 60.2 The regulatory framework is inconsistent with international trends;
- 60.3 Insufficient regard is had to the impact regulatory uncertainty has on investor behaviour; and
- 60.4 The recent focus on the Government securing investment commitments up front with prices set by the Commission *ex post* is undermining confidence in the regime.

²² <http://www.minister.dbcde.gov.au/media/speeches/2009/14>. Similarly, in the context of the re-issue of spectrum licences, the Department of Broadband, Communications and the Digital Economy has signalled an appreciation of the need for certainty: “industry needs certainty to plan for and develop services.” (Public Interest Criteria for re-issue of Spectrum Licences, Discussion Paper for Public Consultation, April 2009; http://www.dbcde.gov.au/consultation_and_submissions/public_interest_criteria_for_re-issue_of_spectrum_licences/discussion_paper) The Discussion Paper recognises that any uncertainty over licence renewal discourages capital investments and will hamper longer term investment and innovation beyond the licence period. The importance of providing certainty for investors was also discussed by the Market Dynamics Limited and Moore Wright Associates Pty Limited final report on “Competition Safeguards in relation to initial allocation of and secondary markets for the radio frequency spectrum in New Zealand” prepared for MED in 2003.

61 Commentators have portrayed similar concerns, including:

61.1 "the unpredictable nature of both the Commerce Commission and Government's decisions has created an environment of regulatory uncertainty";²³

61.2 "we consider that this inconsistency and non-conformance with key regulatory principles ... will lead to a gradual diminishing of capital investment, adverse long-term outcomes for New Zealand consumers and for economic growth as a whole";²⁴ and

61.3 "sources of capital are finite. An investor chooses where to invest based on an assessment of returns available weighed against the risks involved. In the current regulatory environment in New Zealand, BBI considers that New Zealand ranks at the lower end of jurisdictions conducive to infrastructure investment."²⁵

62 There is also market data, which shows that telecommunications businesses trade on less favourable terms than other forms of infrastructure business in New Zealand. For example, AIAL and CEN currently trade on far more favourable cashflow multiples than Telecom, reflecting the more predictable nature of those sectors and the less uncertain regulatory environment of those businesses.

63 This is worrying for us, as it is for any operator, service provider or investor. To the extent that investors are deterred by regulatory conditions, deployment of new technologies will be compromised and the transition to new models will be slowed down or simply won't happen. We appreciate that this cannot be the Commission's intention, or entirely within the Commission's control. But it is a real issue and we are keen to work with the Commission (and the Government) to restore investor confidence.

The way forward: Market context and investment

64 The quality of the Commission's regulatory decision-making in the telecommunications sector relies substantially on the Commission being kept abreast of the market context and on the broader evolution of economic models and principles. Regular, ongoing, engagement with key market participants about the industry generally, its structure, business and economic models, the services offered, and the demands of end-users, is therefore critical as is ongoing discussion of the changing understanding of the economic principles at play.

65 New Zealand would significantly benefit from the regulator, in partnership with the industry and key stakeholders:

65.1 Proactively engaging in regular consultations and discussions to increase its knowledge and understanding of the industry;

²³ "Threats the Commerce Commission stance poses to the industry"; presentation by James Miller, Head of Equities, ABN AMRO (now Craigs Investment Partners), page 10.

²⁴ Steve Boulton, CEO, Babcock & Brown Infrastructure, quoted *ibid* at page 18.

²⁵ *Ibid*.

- 65.2 Providing for open, frank, structured and unbiased discussions;
 - 65.3 Sharing the resolution of challenges facing the sector;
 - 65.4 Articulating what it has learned about the industry, what problems it thinks the market faces, and guidance on how it will approach solving these; and
 - 65.5 Exchanging views on the difficult economic principles that go into regulatory decision making.
- 66 The NGN Conference on Broadband at the Crossroads in February this year is a good example of the kind of engagement industry needs to move confidently into the mobile and new broadband world and for the Commission to make well-informed regulatory decisions in what is an increasingly technologically complex landscape. However, the setting for engagement need not be so formal, or involved. We are happy to organise briefing sessions open to all relevant comers on topical issues of interest to the Commission and we would appreciate the Commission doing the same.
- 67 In addition to regular industry engagement, market monitoring will enable the Commission's decision-making to move quickly with the market where regulation is not delivering the outcomes expected or is no longer needed.
- 68 To ensure that the Commission's market monitoring functions are (measurably) effective, it may be necessary for the Commission to ensure that the function of market monitoring is:
- 68.1 Appropriately resourced;
 - 68.2 Focused against a clear articulation of:
 - (a) The expected outcomes from regulated services; and
 - (b) The strategic priorities and communicated plans of the Commission; and
 - 68.3 Not designed to enable retrospective enforcement – it must be forward-looking and regulatory-, not enforcement-, focused.
- 69 The clear division of regulatory and enforcement roles and tools is vital. Market monitoring is an important regulatory tool. Monitoring as regulator must be undertaken independently of the Commission's competition enforcement role if it is to foster open, unbiased dialogue, grow its understanding of the industry, and develop a genuine partnership approach to regulatory decision-making.
- 70 We are disappointed and concerned that the Commission's Guidelines see the Commission's section 9A power discussed under the enforcement heading of "Commerce Act". The Commission suggests that the Commission will use its section 9A monitoring powers to complement the Commerce Act regime. We do not think that approach is correct, nor are the signals it sends.

- 71 The Commission's view on this will be instructive of its approach to engagement with the industry and regulatory decision making. If industry engagement is to be effective, it is imperative that the Commission's role as sector-specific economic regulator and its role as the competition authority are not blurred.
- 72 Although we accept that the Telecommunications and Commerce Acts overlap and that competition issues that arise in the telecommunications sector can be considered under the Commerce Act, we emphasise the importance of regulatory and competition issues being dealt with by the correct internal Commission team using the correct regulatory or legislative tools. The development of a regulator-industry partnership (i.e. with the Commission's Telecommunications Branch) and genuine two-way dialogue is likely to be undermined if the regulator's monitoring tool is used for enforcement purposes in tandem.
- 73 Maintaining a strict separation of responsibilities and tools will enable the Telecommunications Branch to focus on developing a genuinely collaborative, long-term relationship with industry participants. We are hopeful that such a facilitative and constructive relationship with the Commission will lead to the resolution of industry issues in their wider context, an approach which is notably different and requires different skills, leadership and attitudes to an *ex post* issue by issue approach.
- 74 Another way to ensure that the Commission's approach to regulatory decision-making keeps apace with industry developments is through continuing education. We would welcome the opportunity to participate in conferences, training workshops, seminars, and field trips and share our industry knowledge and understandings with the Commission.

COHERENT REGULATION

The current framework is too complex

- 75 As a matter of policy, we would urge the Government to reassess how “fit for purpose” the current regulatory framework is for the future with a particular focus on simplification. A high quality regulatory environment is promoted by having *both* a well designed and prescribed legislative framework, grounded in a thorough and sophisticated understanding of the economics, as well as principled, transparent and certain implementation of that regime by the regulator.
- 76 The Government and the regulator both have roles here. The Government sets the policy agenda and regulatory framework. The regulator implements the regulatory framework within its remit from Government. The regulator will have an element of discretion around how it interprets and implements the applicable framework and also how it approaches and engages with industry and other stakeholders.
- 77 While the legislative framework has moved fast, we believe that we have reached a point where a reassessment of how the Commission has interpreted and implemented the regulatory framework is also needed. A series of incremental decisions (see **Annex 3**) across various functional levels has resulted in a regulatory framework that now includes:
- 77.1 Resale of retail services;
 - 77.2 Interconnection;
 - 77.3 UBA (which does not take into account the implications of cabinetisation (compared with LLU, which did));
 - 77.4 LLU;
 - 77.5 SLU;
 - 77.6 Comprehensive operational separation (based on the UK model but twice as prescriptive²⁶);
 - 77.7 The addition of services to the operational separation model with no link to the regulatory model;
 - 77.8 Non-discrimination commitments;
 - 77.9 EOI commitments;
 - 77.10 Milestone commitments to roll out broadband and migrate all New Zealanders off copper according to a set timetable;
 - 77.11 Regulatory intervention in mobile markets; and

²⁶ BT's Undertakings are 22,000 words and it has worked with the regulator and been granted 31 exemptions and 19 variations. New Zealand's model is 50,000 words. One variation has been granted by Government and another is pending.

77.12 TSO commitments.

- 78 Keeping all of these regulatory settings lined up and internally consistent as the market transitions to new technologies and investment is required closer to the home is proving a herculean and confusing task. In some cases, the focus on regulating one service without regard to the full regulatory picture has led to perverse or unintended effects.
- 79 We are not unsympathetic with the position of the regulator because in some cases, the vast range of regulatory matters means that the market is moving too fast for regulation to keep up. Likewise though we would hope that the regulator also has some sympathy for industry in circumstances where business decisions have to be made at a time of regulatory uncertainty. For example:
- 79.1 A lengthy and costly process to establish the de-averaged LLU product was run at the same time as the Government was securing commitments from Telecom to cabinetise large parts of the network. As the Commission knows, this created real commercial challenges and risks for both access seekers and Telecom;
- 79.2 The averaged basic unbundled bitstream access products – basic and enhanced – were also subject to an involved standard determination process at the same time as LLU was being established and Telecom’s operational separation regime was being bedded down. Yet, that determination does not take into account the impacts of cabinetisation; and
- 79.3 A lengthy and costly process to establish the SLU product was run at a time when it was very predictable that the SLU business case would not stack up for access seekers compared to UBA (and this has proved to be the case) thus Telecom now bears the cost of providing a service that is unwanted.
- 80 This “spill-over” effect of fragmented regulation needs to be addressed both now, as a one-off exercise, and more generally going forward. We would encourage the Commission to engage industry and then the Government on these issues outside the constraint of any particular regulatory process. We are confident that engagement with industry on these issues would help ensure that regulation is appropriately targeted in response to specific issues whilst taking full account of how it will impact on the wider context.
- 81 The Commission should not be afraid to undertake the reassessment that is needed. Ofcom undertook a similar strategic review to determine whether regulation was and was not working and where deregulation was appropriate.²⁷

Challenge of regulation being fit for upcoming mobile and broadband developments

- 82 When reassessing the complexity of the current regulatory framework, it will be particularly important to anticipate regulation that is fit for purpose to take into account enhancements to mobile and broadband services.

²⁷ Strategic Review of Telecommunications 2004

- 83 The Commission is aware of this challenge, and states in the Guidelines that “[t]he increasing penetration of fibre in the access network is likely to have implications for the take-up of regulated access products.”²⁸ The Commission’s decision-making will need to be “future proofed” by reference to the potential impact fibre penetration, and enhancements to broadband and mobile platforms generally, will have on market dynamics. To the extent that this cannot be forecast with any certainty, the Commission’s approach should be cautious and should err on the side of non-intervention.
- 84 We note that the Commission has previously indicated that it was “very cautious” about regulating in areas of emerging technology. Ex-Chair of the Commission acknowledged: “it can be dangerous to get ahead of the market so you want to see what the evolution is before you regulate, because you do risk chilling investment and innovation.”²⁹ It was also signalled that if the Commission could identify ways for the development of the next-generation network to be competitive, then regulation might be avoided: “we do want to get the demand side right to drive the development of the infrastructure.”³⁰
- 85 That is a sound approach. However, there is a fine line between the regulator wanting to hold back before it makes a decision and the uncertainty that is generated where there is a need for investment and an absence of any signalling as to what interventions might be considered or when. Thus while holding back and moving slowly is important, it is equally important for the regulator to signal its thinking as far ahead as practicable and to only impose regulation in a well signalled and incremental way.
- 86 We also think that the Guidelines – in signalling a new leaning towards promoting more facilities-based competition – are consistent with this forward-looking approach and the likelihood of increasing facilities-based competition under the Broadband Investment Initiative. This is a significant signal that should be engaged upon. This will mean that a focus on minimising and scaling back existing regulation against a backdrop of developing competition will be appropriate.
- 87 To the extent that there is uncertainty around what facilities-based competition would look like in the future, we hope the Commission will seek industry engagement on this topic.

Tracking overseas developments

- 88 A degree of guidance is likely to emerge from other jurisdictions where models are more advanced and will provide the Commission with some suggestions for how a New Zealand-specific fibre-fit model could be tailored.

The United Kingdom (UK)

- 89 Over the past year Ofcom has been considering its approach to Next Generation Access (**NGA**) through multiple overlapping proceedings as part of its ongoing

²⁸ Guidelines, para 50.

²⁹ “Commission may cut Telecom regulation”, The Independent, March 5 2009.

³⁰ *ibid.*

review of the products and pricing of BT's functionally separate access arm, BT Openreach.³¹

90 Ofcom's objectives are:

90.1 To promote timely and efficient next-generation investments; and

90.2 To promote timely and efficient competition.

91 Ofcom's proposals for future regulation are based on the following principles:

91.1 Pricing flexibility and freedoms for next-generation wholesale access products;

91.2 Pricing flexibility for active products;

91.3 Returns that reflect risk for passive products;

91.4 The development of passive access products dictated by demand;

91.5 Industry-led development of active access products; and

91.6 Establishing framework for transition.

92 Ofcom has issued investment guidelines for new build super fast broadband networks – indicating that it expects builders of new fibre networks to provide non-discriminatory wholesale access to competitors and provision spare duct capacity as network.

93 Ofcom is also considering multiple next generation wholesale options, which include unbundling of FTTH, P2P and PON wavelengths and has been very focussed on active line access in the form of Ethernet bitstream access and developing a generic Ethernet access product based on both FTTH and FTTC.³²

The European Community (EC)

94 The EC has commenced a consultation process on pricing for NGAN. Already, the EC Draft Recommendations³³ provide some indication of what might be happening in Europe. Submissions in response to the Draft Recommendations closed on the 25 August 2009,³⁴ and New Zealand will be able to track the development of the EC fibre model.

95 From its draft recommendations on NGN access regulatory principles, the EC broadly:

³¹ <http://www.openreach.co.uk/orpg/home/home.do>.

³² Yankee Report Part II, pages 5 and 6.

³³ Draft Commission Recommendations on Regulated Access to Next Generation Access Networks (NGA) – Brussels 2008

³⁴ The second consultation paper can be access at:
http://ec.europa.eu/information_society/policy/ecommm/doc/library/public_consult/nga_2/090611_nga_recommendation_spc.pdf.

- 95.1 Supports sharing the legacy infrastructure such as ducts and where such sharing is not viable, passive sharing based on dark fibre access is favoured;
- 95.2 Supports shared access to in-building wiring – in respect of which it notes that NRA's should be in a position to apply sharing obligations symmetrically on all infrastructure owners – not just those with SMP;
- 95.3 For FTTH deployment, the EC recognises the case for mandating physical access to fibre sub-loops, or access to dark fibre and the ODF and is of the view that existing bitstream access obligations remain relevant for FTTC and FTTN (in market 5, defined below);
- 95.4 Diversification of investment risk in fibre deployments and cooperative arrangements between industry players, including co-investment, multiple FTTH fibre lines and factoring in investment risk-premium is important;
- 95.5 Where SMP operators are deploying FTTH, the EC considers mandated access to fibre loops should be based on cost-oriented pricing and a risk premium. However, cost-oriented pricing should not apply where:
- (a) there are multiple fibre lines and equitable access to the infrastructure is offered to competitors; or
 - (b) deployment is undertaken jointly by 2 or more operators of which one is an SMP operator; and

if WBA is mandated if fibre deployment is based on the scenarios above.

- 96 A Report by Yankee Group entitled *Next-Generation Access Regulation Takes Shape in Europe – Part I and Part II*³⁵ (**Yankee Report**) reviews European National Regulatory Authorities (**NRAs**) that have already made decisions on the regulation of NGA. The Yankee Report tracks the current thinking of, and processes engaged in by, NRAs that are in the process of market reviews and the development of thinking on NGN regulation.
- 97 European NRAs operate in the context of EC directives, guidelines and recommendations that aim to steer a harmonised course for NGN policy development and regulatory processes. The Yankee Report focuses on the way in which NRAs analyse two key product markets and the proposed regulatory measures to be imposed.
- 98 The Yankee Report summarises EC NGN access regulation as follows:
- 98.1 NGN access must be considered within the context of two markets of key importance:
- (a) EU Market 4 – defined as a wholesale (physical) network infrastructure access, including shared or fully unbundled access (LLU) at a defined location (**market 4**); and

³⁵ August 2009

(b) EU Market 5 – wholesale broadband access; virtual network access including bitstream access at a fixed location (**market 5**).

98.2 NRAs use a diverse range of approaches but their findings and evaluations are based on the market factors specific to their countries and common principles, subject to substantive assessment by the EC (a form of pre-implementation review); and

98.3 The development of NGA policy across each of these nations is based on a wealth of information derived from regular market reviews, consultation documents, responses to consultations, regulatory decisions separate from market reviews and national legislation.

NRA processes generally

99 The Yankee Report notes that there are three critical steps in an NRA's market review process:

99.1 The NRA must first define what is included in the relevant market (notably here, whether fibre is part of market 4 and/or 5);

99.2 It must determine whether there are SMP operators in the relevant markets; and

99.3 It must decide on the obligations it must impose on these SMP operators in the relevant markets (while retaining the capacity to apply symmetrical obligations on all operators irrespective of market power).

Recommendations for NRAs

100 The Yankee Report makes the following recommendations for NRAs in respect of NGN regulation:

100.1 Information on NGN plans is a critical input to both NGA policy setting and alternative network operators as they assess viable business models going forward. Regulators cannot make informed decisions without access to such commercial and economic plans;

100.2 NRAs must urgently complete market 4 and market 5 market reviews in tandem to update two or three year old market data – and base decisions on updated market definitions;

100.3 Irrespective of the technologies being deployed regulators must maintain a technologically neutral stance in conducting market reviews and not base judgments on the current state of play;

100.4 NRAs should closely review EC comments on their peers' market review notifications (especially during the "checking and approval" process);

100.5 The technical, physical and economic feasibility of shared ducts varies from country to country and within countries and NRAs should keep access options open. The provision or availability of alternatives such as dark fibre should be open to competitors rather than placing restrictions on access only when duct access is unavailable;

100.6 NRAs must set comprehensive policies that include clear migration conditions, cost allocation time frames and NGA pricing methods (such as the Netherlands model). A lack of clarity and a migration plan can be debilitating;

100.7 NRAs must clarify the position on in-building cabling;

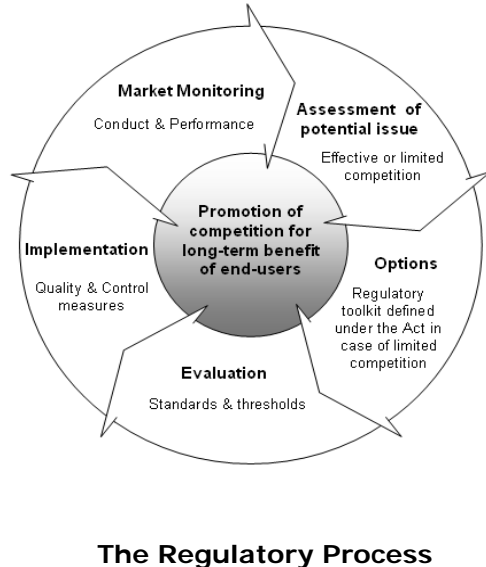
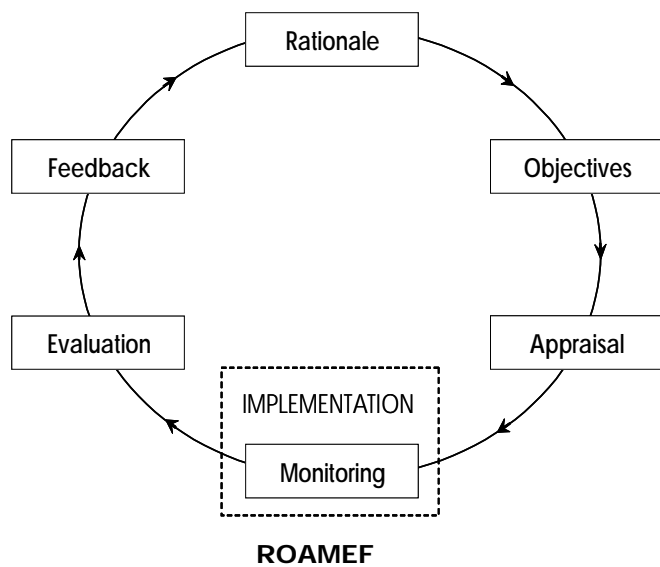
100.8 Investment risk must be factored into regulation on fibre access. If access pricing is mandated, a risk premium should be added to regulated costs; and

100.9 NRAs should continue to work in a clear policy framework, take into consideration several levels of competitor and stakeholder inputs and make informed, reasoned decisions based on the information and policies before them.

101 The Commission may find some of these recommendations helpful when approaching its decision-making in respect of NGN regulation in the New Zealand context. However, the exact market structure will also be a product of the arrangements that the Crown Fibre Investment Company enters into.

The regulatory cycle

102 The Commission discusses its approach to decision-making by reference to the cycle of activities depicted in Figure 1 of the Guidelines.³⁶ The Regulatory Process diagram is based on similar decision-making phases to those in the revised *HM Treasury Green Book (Green Book)*. The Green Book³⁷ describes itself as a “best practice guide for all central departments and agencies” in the United Kingdom and it “aims to make the appraisal process throughout government more consistent and transparent.” It contains the ROAMEF appraisal and evaluation cycle, which is widely accepted as a robust and well-tested approach to regulatory decision-making and an approach we support.



³⁶ Guidelines, page 29.

³⁷ *The Green Book – Appraisal and Evaluation in Central Government* – HM Treasury, para 1.4.

103 Setting such clear processes in place will help ensure that:

103.1 The Commission promotes the legislative aim set out in section 18 of the Telecommunications Act by requiring the Commission to undertake a consistent, comprehensive, transparent and proportionate assessment of regulation using an objective framework to minimise the risk of errors and omissions;

103.2 Stakeholders can have confidence in the regulatory settings, particularly their predictability; and

103.3 The wider economic and social costs and benefits of regulation are appropriately balanced.

104 Ultimately though, the effectiveness of the regulatory cycle (and therefore the achievement of the objectives set out above) relies on a deliberate, concerted and transparent approach by the Commission to undertake *each* discrete phase in the cycle whenever it considers and implements a regulatory decision.

105 There is a real opportunity for the Commission to engage the industry on the best way to approach each stage of the regulatory cycle, and in doing so provide additional guidance and certainty on decision-making under the Telecommunications Act. For some key issues, this might involve the Commission developing a specific subset of guidelines to achieve greater certainty for stakeholders.

106 As outlined earlier the importance of the beginning of the cycle – market monitoring – must not be under-estimated, or blurred with other roles. Market monitoring encompasses robust engagement in, and understanding of, the wider context to ensure that any decision to assess a market with a view to regulation is properly informed. Market monitoring should also not be blurred with the “end” of the cycle where regulation should be regularly, and objectively, reviewed for its effectiveness and for opportunities to minimise regulation or deregulate.

107 In Annex 5 we have illustrated the beginning of the cycle as “know the industry” and the end of the cycle as “review for effectiveness and opportunities for simplification”.

The regulatory tool box: development of issue-specific guidelines

108 In addition to engagement on the wider context, Telecom would welcome the development of issue-specific guidelines. These might include the following topics:

108.1 Seeking industry agreement on the regulatory settings prior to committing to large investments;

108.2 Market context and monitoring;

108.3 Defining markets and assessing workable competition;

108.4 Undertaking cost benefit analysis;

108.5 How the Commission will seek to achieve dynamic efficiency;

108.6 Applying the weighted cost of capital (WACC);

108.7 Applying TSLRIC; and

108.8 How the Commission seeks to implement the section 18 purpose statement in making regulatory decisions.

109 These are difficult topics and regulatory decisions in respect of each have a significant impact on the industry and also the fundamental economics of service offerings. Specific guidelines on each of them would provide certainty for market participants.

Seeking industry agreement on the regulatory settings prior to investment

110 As noted above, our investors are telling us that the recent dynamic of the Government securing investment commitments and then the Commission setting prices *ex post* is corrosive of confidence in the regulatory regime. We are keen to discuss with the Commission (and the Government) ways that we could establish a commitment on the regulatory settings before substantial further investment is made by market participants.

111 These issues remain “live” during the long life of an infrastructure asset. Investment decisions drive off the prevailing regulatory conditions. If these might change, the Commission ought to signal this possibility so that investors are fully informed. The Commission should then seek to engage market participants in shaping the regulatory settings together with the Commission to ensure that the settings are proportionate, relevant, sustainable, and low cost, and to avoid unnecessary infrastructure duplication or the stranding of assets.

Market context and monitoring

112 The importance of market context and monitoring to achieving quality regulation is discussed above. The Commission’s market monitoring process is an important tool.

113 The Commission has a significant responsibility in exercising its regulatory functions. The Commission’s decisions shape and direct commercial decision-making by all telecommunications market participants. The Commission should therefore utilise its market monitoring function extensively to build a broad understanding of telecommunications markets in New Zealand.

114 By having regard to international developments and best practice, the Commission can also consider market trends in other countries. As the Commission acknowledges elsewhere in the Guidelines, telecommunications markets are changing, and new technologies emerging rapidly. Market developments, and changing consumer demand patterns and behaviours are occurring just as swiftly, which ultimately will determine the technologies that succeed in the market and those that fail. Ongoing market monitoring and review will enable the Commission to keep up with these.

115 In addition to the reports which the Commission produces for its stakeholders, Telecom encourages the Commission to consider building a broader model of telecommunications markets which would better inform its decision-making process and enable it to more accurately assess information and submissions provided to it by industry participants. This in turn would inform the Commission’s market definition assessment.

- 116 A particular concern that we have is that the Commission currently appears to divert minimal resource to market monitoring and it appears that what is done is confused with the Commission's enforcement role. As we have said above, monitoring is a core part of the Commission's functions as a regulator in terms of understanding the markets and hence the ability to make informed regulatory decisions, the efficacy of interventions and whether they are still required.
- 117 As a parallel to the points that we have made we note that one of the recommendations arising from the Digital Britain Report is that Ofcom should place a much greater emphasis on market monitoring as part of its role.
- 118 In accordance with this recommendation the UK Department for Business Innovation & skills has BIS has been consulting on whether an express duty should be imposed on Ofcom to provide a full assessment of UK communications infrastructure every two years. The rationale for this is as follows:

*"[T]he report [Digital Britain Report] emphasised the increasing importance of monitoring the national communications infrastructure, and the need for both Government and Ofcom to take a broad view of the nation's needs and any ways in which those needs may not be being met. The new duty on Ofcom to report to the Secretaries of State for Business, Innovation and Skills and for Culture, Media and Sport every two years giving an assessment of the UK's communications infrastructure will address this. Further, Ofcom will be required to alert those Secretaries of State to any matters of high concern regarding developments affecting the communications infrastructure."*³⁸

Market definition

- 119 The Guidelines refer to the market definition approach set out in the Commission's Mergers and Acquisitions Guidelines as the basis for the approach to defining telecommunications markets.
- 120 There is widespread agreement that telecommunications markets display characteristics of two-sided markets (also known as two-sided platforms), and we recommend that the Commission consider formulating an industry specific market definition guideline which takes appropriate account of the difficult issues associated with two-sided market analysis. In particular, the application of the hypothetical monopolist (**ssnip**) test³⁹ requires full consideration of two-sided market conditions in the telecommunications context if the Commission is to get an accurate picture of the relevant market.
- 121 The Commission's approach to defining markets for the purpose of regulatory decision-making will also need to take account of evolving technologies and market practices and how these variables change the market landscape. For example, the Commission may need to consider how peering (through barter arrangements

³⁸ See foreword to Digital Britain Report - Consultation on the proposed new duties for Ofcom; to promote efficient investment in infrastructure, to provide a full assessment of UK communications infrastructure every two years (August 2009) BIS

³⁹ Guidelines, para 159.

between ISPs) inform interconnection and termination practices on mobile NGN, and whether the issue of network termination monopolies no longer applies.

- 122 We note, for example, that there already have been cases in the United States and the European Community that acknowledge that ISP connectivity markets are effectively competitive (insofar as they replace calling party pays externalities with reciprocity) and no termination monopoly exists.⁴⁰
- 123 The New Zealand framework has been unique over the last few years in that proper assessments of competition in markets were removed from the legislative framework for the key services of UCLL and UBA. This may mean that an appreciation of the full market context (and therefore appropriate market definitions) has not developed in the same way as other international frameworks grounded in such analyses. There may be scope for further engagement with, and guidance from, the Commission on developing appropriate market definitions.

Cost benefit analysis

- 124 The Commission is aware of the importance of cost benefit analysis (**CBA**). CBA is often perceived to be an arcane topic, and for that reason is not regularly revisited to check that it is being applied to decision-making in a way that properly assesses the relevant decision against the current market circumstances.
- 125 A good CBA framework is not all about equations. For example, the Green Book not only sets out the steps which would typically inform a standard cost-benefit appraisal based on net present value, but also establishes explicit processes which are designed to address the “demonstrated, systematic tendency for ... appraisers to be overly optimistic ... [and to] ...tend to overestimate benefits and underestimate timings and costs, both capital and operational” in the face of uncertainty.⁴¹ The New Zealand Treasury Cost Benefit Analysis Primer⁴² endorses the Green Book approach to optimism and the management of uncertainty.
- 126 We think there is a real opportunity to engage on whether the current CBA framework is fit for the imminent changes to the telecommunications landscape. In the uncertain environment that telecommunications investors now face, it will be important that risks are considered over the term of the CBA so that the analysis takes into account:

126.1 The full effect of the sunk and irreversible nature of telecommunications investment;

126.2 The existence of any network externalities or effects which need to be internalised in the regulated access price;

126.3 The full impact of technological change over the CBA duration (including disruptive technologies);

⁴⁰ See *FCC Approves SBC/AT&T and Verizon/MCI Mergers, Transactions Offer Significant Public Interest Benefits*, Press Release 31 October 2005 - http://scrawford.net/courses/fcc_mergers.doc; and Case M 3752, *Verizon/MCI*, OJ 2005 C309/10 – Press Release <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/05/1234>.

⁴¹ HM Treasury – The Green Book – Appraisal and Evaluation in Central Government, see para 5.61

⁴² See multiple references to parts recorded as being adaptations from the UK Green book

- 126.4 The possibility that the service may not succeed during the term of the CBA;
- 126.5 The possibility that all capital investment may not be used up over the period examined by the CBA;
- 126.6 The possibility that prices for the goods/services may decrease over the duration of the CBA due to shifts in the demand curve over time, the emergence of substitutes, obsolescence due to the impact of disruptive technologies, reductions in costs due to the incremental technological improvement which reduces the costs of production, and so forth;
- 126.7 The possibility that the investment may not be used at full capacity during the period covered by the CBA (e.g. UBA);
- 126.8 The full range of risks when determining the cost of capital; and
- 126.9 The termination of options around investment due to the irreversibility of the high sunk costs.

Dynamic Efficiency

- 127 The Commission states at paragraph 135 of the Guidelines that:

“The Commission has previously indicated that where a tension exists between short-term allocative efficiency and long-term dynamic efficiency, the Commission will give greater weight to the promotion of the latter. The Commission considers that this approach remains appropriate. Ongoing innovation and efficient investment over time can deliver significant long-term benefits to end-users, and the adverse consequences of deterring or delaying such investment may be substantial.”

- 128 We agree with the Commission’s assessment that dynamic efficiency is ultimately the most important form of efficiency to promote. However, we think that there is merit in further discussions around how to assess the implications of a regulatory decision on dynamic efficiency since this is a difficult thing to achieve in practice.
- 129 A particular problem that arises is that changes to short-term allocative efficiency are the easiest to quantify, assess and factor into a CBA. In contrast, the dynamic efficiency implications of a decision may well be abstract and intangible, and often may not be fully apparent at the time that a regulatory decision is made.
- 130 When the Commission is then asked to weigh a known and quantifiable benefit in allocative efficiency against a form of efficiency that may be less certain, we recognise the Commission’s potential difficulty with giving due weight to dynamic efficiency in practice.
- 131 As the Commission clearly cannot fail to take into account the most important form of efficiency, simply because it is hard to quantify we would welcome further discussion around how the parameters of dynamic efficiency could be determined.
- 132 In the meantime, an approach that could help to identify the dynamic efficiency implications of a decision may be for the Commission to stand back from the minutiae of the particular decision at hand and to ask itself questions along these lines:

- 132.1 Is regulation of the kind contemplated predictable and in-keeping with global trends?
- 132.2 Will this decision make the New Zealand regulatory environment more or less predictable?
- 132.3 What signals will this decision send about the New Zealand regulatory environment (particularly to international investors)?
- 132.4 What is the cumulative weight of current regulatory burdens if the regulation being considered is imposed?
- 132.5 How does this decision fit with other regulatory decisions in terms of consistency and complementarity?
- 132.6 Does the process and basis for the decision apply sound principles and best regulatory practice?
- 133 While these questions are not exhaustive and do not cover all aspects of dynamic efficiency, they will provide the Commission with a practical interim yardstick for thinking about how a decision might actually impact on innovation and investment until there is greater understanding of how to treat this form of efficiency.
- 134 It is also worth noting that there is a natural alignment between the Commission engaging more, and placing greater emphasis on, its monitoring function and it having a more practical understanding as to how dynamic efficiency may manifest itself.
- 135 There is also an alignment between the Commission adopting the best practice regulatory principles that we propose and promoting dynamic efficiency by creating a more certain regulatory environment.

Proposed new duties for Ofcom

- 136 A relevant parallel to the points made above about the practical difficulty of properly considering dynamic efficiency in the face of easily quantifiable short term gains, we note that The Department for Business, Innovation and Skills (BIS) in the UK has consulted on proposed new duties for Ofcom to:
- 136.1 promote efficient investment in communications infrastructure; and
- 136.2 provide a full assessment of UK communications infrastructure to the government every two years.
- 137 The rationale for the change is as follows:
- "The Government considers that over recent years Ofcom's duty when carrying out its functions to further the interests of consumers of communications services where appropriate by promoting competition, has tended to put the emphasis on short term cost reduction rather than longer term investment in future infrastructure. The Government therefore concluded that it should give Ofcom an additional duty to promote efficient investment in communications infrastructure (where appropriate),*

*alongside the promotion of competition, when furthering the interests of consumers. Such a duty will sit alongside the existing duty to further the interests of citizens in relation to communication matters.*⁴³

Applying WACC

- 138 Telecom appreciates that the Commission is fully aware of the complexities and debates associated with setting the WACC in a regulatory process.
- 139 From the perspective of an investor, these complexities and debates translate to real risk. From Telecom's perspective, this risk has been increased by recent decisions of the Commission which took quite surprising approaches to determining the WACC.
- 140 As the WACC is an important consideration in any decision to invest, any initiative to reduce the uncertainties associated with identifying the WACC is an investment well made. For this reason we encourage the Commission to engage specifically on developing a WACC guideline for the telecommunications sector. This could leverage off the work being done under Part 4 of the Commerce Act and the associated high level generic guidelines for estimating the cost of capital, but does not have to involve the same degree of formality.
- 141 A key issue with respect to WACC that we would like to discuss further is the level of risk premium which the Commission will be prepared to endorse for new investments in new technologies. (This is a fundamental point of difference between the issues facing our sector and the work that the Commission is undertaking to establish WACC for other sectors for which there is not such an element of technological innovation.)

Pricing principles and TSLRIC – how it applies

- 142 When considering the regulation of a new service, the Commission is required to specify the appropriate Initial Pricing Principle (**IPP**) and Final Pricing Principle (**FPP**). It would be useful to augment the discussion in paragraphs 195 to 199 of the Guidelines by identifying the factors which would suggest that setting a forward looking cost based price is best met by selecting TSLRIC as an FPP, and those which determine when approximations to it, such as retail minus or other methods, are viewed as preferable. In addition, the Guidelines should set out the approaches to the IPP which generally represent the best proxies for the relevant FPP.
- 143 It would also be useful for market participants to have some guidance from the Commission as to how it might go about carrying out the FPP using the TSLRIC methodology, preferably a worked example. Telecom submits this might well sit best as a separate guideline and be included in an update to the Commission's 2002 Discussion Paper on the Application of a TSLRIC Pricing Methodology.
- 144 This is becoming a pressing issue. In the past, the limited technological and economic risks surrounding the supply of telecommunications services over the PSTN has meant that the limitations of TSLRIC have been less apparent and have been largely overlooked by the Commission. Only a few FPP applications have been

⁴³ See foreword to Digital Britain Report - Consultation on the proposed new duties for Ofcom; to promote efficient investment in infrastructure, to provide a full assessment of UK communications infrastructure every two years (August 2009) BIS

made. All have been settled so that decisions were not made. Guidance has therefore not evolved.

- 145 In recent years, improvements in xDSL technologies, cabinetisation, and the increasing proximity of fibre to the end user connection point have changed the technological and economic risks facing telecommunications companies. The effect of this highlights the limitations of TSLRIC.
- 146 Nowhere is this more evident than in relation to the pricing of access to FTTx. There is uncertainty over the limits of fibre technology, and the existence of a range of substitute delivery technologies for connectivity, together with the potential for enhancements and changes to elements of transport technologies. In addition, there is material economic uncertainty over the demand for access and bandwidth from both content providers and consumers.
- 147 For the FPP to have any role, investors need to be confident that the TSLRIC methodology (like CBA) will take account of:
- 147.1 The full effect of the sunk and irreversible nature of telecommunications investment;
 - 147.2 The existence of any network externalities or effects which need to be internalised in the regulated access price;
 - 147.3 The full impact of technological change, (including disruptive technologies);
 - 147.4 The possibility that the service may not succeed;
 - 147.5 The possibility that all capital investment may not be used up over the entire economic life of the investment;
 - 147.6 The possibility that prices for the goods/services may decrease over time, due to changes in demand/shifts in the demand curve over time, emergence of substitutes, obsolescence due to the impact of disruptive technologies, reductions in costs due to the incremental technological improvement which reduces the costs of production, and so on;
 - 147.7 The possibility that the investment may not be used at full capacity; and
 - 147.8 The full range of risks when determining the cost of capital.
- 148 A number of issues will result if no adjustment is made to reflect the uncertainties arising from these factors when estimating a TSLRIC cost. Perhaps the most significant is that market participants will be unable to enjoy the benefits of returns on successful investments, but will be completely exposed to the full downside risk on unsuccessful investments. This asymmetry in market outcomes has the obvious impact that the incentives for a market participant to invest and innovate will reduce significantly. In practice, this will mean that a telecommunications provider will delay investment in new services until it is clear that the risk of failure has been sufficiently decreased.

149 New telecommunications services create significant value for both suppliers and consumers. Regulation which either delays introduction and uptake of new services by delaying the setting of access pricing, or indirectly delays investment by market participants and thus delays introduction and uptake of these new services creates a loss for both consumers and market participants. Just as there is a clear cost from regulatory delay, there are also clear corollary costs from delayed investment by market participants.

Section 18 of the Telecommunications Act 2001

150 The section 18 purpose statement governs and dictates the exercise of all regulatory decision-making under the Part 2 access regime. Further, as the section 18 purpose statement was inserted by Parliament into the main body of the statute, it will have primacy over the schedules of the Act, the content of which have generally been inserted by Orders in Council. The implication of this is that the wording in the purpose statement will drive the way in which the wording of schedules will need to be interpreted, rather than the other way around.

151 It is important that there is a common understanding between the Commission and industry of the underlying principles of the section and how they will be implemented by the Commission in making regulatory decisions.

152 We set out in **Annex 6** to this response a brief account of the way in which we think section 18 applies and we would welcome further discussion with the Commission on these views.

Taking the tool box forward

153 These are all important issues, and we appreciate that it is easier to identify the hard questions than to resolve them when implementing regulation in practice. It is for this reason that Telecom invites the Commission to engage the industry on these issues outside the constraints of a particular regulatory process, and build up a tool box of specific guidelines as discussed above.

THE VALUE IN A COMMITMENT TO REGULATORY PRINCIPLES

154 There is no direct requirement under the Telecommunications Act 2001 for the Commission to abide by or apply specific principles when making regulatory decisions. However, we think that there is real value in the Commission making a voluntary commitment to adhere to clear objectives that would guide its decision-making, as a model of best practice and to demonstrate how and why it will exercise its discretionary decision-making powers in particular ways. We believe that would be a useful outcome from the introduction of new Guidelines.

155 There are a number of reasons why a voluntary commitment to clear decision-making objectives and principles would be valuable, including that:

155.1 Clear objectives provide good guidance for the regulator and a yardstick against which to measure the performance of regulation; and

155.2 Clear objectives promote certainty and transparency for all industry participants, particularly when considering future investment (whereas the assertion of discretion, with no concrete guidance on how that discretion will be exercised, gives rise to uncertainty).

156 Some key decision-making principles would include:

156.1 A commitment to proactive, early, regular, ongoing, and fulsome engagement with market participants (the value of this has been discussed at paragraphs 28 to 63 above);

156.2 Adopting a presumption against regulation;

156.3 Seeking to minimise regulatory burdens;

156.4 Regularly reviewing the effectiveness of intervention and the potential to deregulate;

156.5 Facilitating industry-led solutions (discussed further below); and

156.6 Accepting accountability through the exercise of merits review rights (discussed further below).

Presumption against regulation

157 The Commission should seek to intervene only where there is a clear market problem and where the benefits of doing so clearly outweigh the costs so as to avoid the risk of error in early intervention. This is consistent with the principle articulated in *Powerco v Commerce Commission* [2008] NZCA 289:

“The New Zealand approach is to start with a presumption of non-regulation. This can be displaced if the appropriate criteria in the Act are met. The burden to displace the presumption against non-regulation falls to the Commission and the Minister.”⁴⁴

⁴⁴ Para 48.

Way forward

- 158 To comply with this principle, the Commission needs to undertake a thorough analysis of the available options and their respective potential impacts each time it considers regulatory intervention.
- 159 To determine whether intervention may be necessary, the Commission should consider developing some quantitative metrics against which to test whether a market exhibits a competition problem, together with some statements as to what changes would need to be made to result in competitive outcomes. This process would both enable the Commission to quantitatively test whether:
- 159.1 A particular regulatory solution would result in metrics consistent with competitive outcomes; and
- 159.2 On review, the regulatory solution is indeed producing competitive outcomes and therefore whether deregulation would be appropriate.

Minimising regulatory burdens

- 160 Regulatory intervention should be targeted, proportionate and least intrusive so as to minimise the regulatory burden on those subject to it. Excessive regulatory burdens stifle innovation and the deployment and take-up of new products and services. This results in both a direct cost to the industry and losses to end users. These risks can be minimised through the discipline of, and a commitment to, effective review, efficiency goals and the removal of unnecessary burdens.
- 161 The risk of regulatory error through the use of *ex ante* regulation in this industry is high given that there are unavoidable limitations on the regulator's ability to foresee or predict how the market will develop in the short term, let alone the long term. To minimise the risk of *ex ante* error and the market distortions that might flow from this, a light-handed or non-interventionist approach to regulation is appropriate.
- 162 Where any *ex ante* intervention is implemented, the Commission should commit to the regular review of regulatory burdens. To illustrate how this commitment could be implemented, we note that a duty to regularly review the ongoing effectiveness and minimisation of regulatory burdens is a statutory requirement for Ofcom. Section 6 of the Communications Act 2003 (United Kingdom) therefore provides:

6 Duties to review regulatory burdens

- (1) OFCOM must keep the carrying out of their functions under review with a view to securing that regulation by OFCOM does not involve—
 - (a) the imposition of burdens which are unnecessary; or
 - (b) the maintenance of burdens which have become unnecessary.
- (2) In reviewing their functions under this section it shall be the duty of OFCOM—
 - (a) to have regard to the extent to which the matters which they are required under section 3 to further or to secure are already furthered or secured, or are likely to be furthered or secured, by effective self-regulation; and
 - (b) in the light of that, to consider to what extent it would be appropriate to remove or reduce regulatory burdens imposed by OFCOM.
- (3) In determining for the purposes of this section whether procedures for self-regulation are effective OFCOM must consider, in particular—
 - (a) whether those procedures are administered by a person who is sufficiently independent of the persons who may be subjected to the procedures; and

- (b) whether adequate arrangements are in force for funding the activities of that person in relation to those procedures.
- (4) OFCOM must, from time to time, publish a statement setting out how they propose, during the period for which the statement is made, to secure that regulation by OFCOM does not involve the imposition or maintenance of unnecessary burdens.
- (5) The first statement to be published under this section—
 - (a) must be published as soon as practicable after the commencement of this section; and
 - (b) shall be a statement for the period of twelve months beginning with the day of its publication.
- (6) A subsequent statement—
 - (a) must be published during the period to which the previous statement related; and
 - (b) must be a statement for the period of twelve months beginning with the end of the previous period.
- (7) It shall be the duty of OFCOM, in carrying out their functions at times during a period for which a statement is in force under this section, to have regard to that statement.
- (8) OFCOM may, if they think fit, revise a statement under this section at any time before or during the period for which it is made.
- (9) Where OFCOM revise a statement, they must publish the revision as soon as practicable.
- (10) The publication under this section of a statement, or of a revision of a statement, must be in such manner as OFCOM consider appropriate for bringing it to the attention of the persons who, in their opinion, are likely to be affected by the matters to which it relates.

163 Ofcom has implemented these obligations in a meaningful way through developing detailed Simplification Plans, which it publishes annually alongside its Annual Plans. Simplification Plans consist of detailed tables setting out the following matters in respect of existing regulation:

163.1 The issue and planned simplification work;

163.2 The policy objective & stakeholders who will benefit;

163.3 Reasons for examining the issue;

163.4 Updates on progress and key milestones;

163.5 The estimated impact on regulatory burdens and/or benefits to be realised;

163.6 Contacts; and

163.7 Current status.⁴⁵

164 Ofcom recognises that deregulation has as much of a role as regulation in supporting competition between firms and enabling customers to benefit from new services and products.

⁴⁵ See for example Ofcom's 2007 Simplification plan at <http://www.ofcom.org.uk/about/accoun/simp/> and its 2008 Simplification Plan at <http://www.ofcom.org.uk/about/accoun/simpl08/>

165 With similar effect, the purpose of the Telecommunications Act 1996 (United States) is:

*“...to promote competition and **reduce regulation** in order to secure lower prices and higher-quality services for American telecommunications consumers and encourage the rapid deployment of new telecommunications technologies.*

166 That Act also requires that the regulator (the Federal Communications Commission (**FCC**)) must not impose regulation unless it is necessary to ensure that tariffs are just and reasonable, to ensure protection of consumers, and to ensure that pricing is consistent with the public interest.⁴⁶ To comply with this obligation, the FCC must undertake biennial reviews of all regulations to determine whether they are consistent with these purposes. This biennial review function has enabled the FCC to decide that deregulation or no regulation is appropriate, including in relation to:

166.1 Long distance calls (considered to be subject to sufficient competition and therefore retail regulation was unnecessary);

166.2 Local retail regulation in some states (deregulated);

166.3 Wholesale line rental (not regulated);

166.4 Fibre to the home (exempt from regulation);

166.5 Bitstream access (supplied on a commercial basis); and

166.6 Local loop unbundling (relaxation of regulation where it is considered competitive).

167 The European Commission has also embarked on a substantial project to deregulate:

“Effective regulation has brought competition to telecoms markets and managed to stimulate investment and innovation. Consumers benefit from lower prices and greater choice. Where there is a clear tendency towards competition the Commission proposes to substantially deregulate. Regulation will be refocused on those areas where it is still necessary and where competition bottlenecks persist which will not disappear without dedicated regulation.”⁴⁷

168 The specific goal that the European Commission has set is to reduce regulation by 50%, with particular focus on deregulating at retail and some wholesale levels.⁴⁸

Way forward

169 We encourage the Commission to consider committing to a similar review obligation and targets for de regulating like the European Commission. This would ensure that

⁴⁷ Less But Better Regulation (2007) EU Telecoms Reform #8

⁴⁸ Commission acts to reduce telecoms regulation by 50% to focus on broadband competition (Brussels 13 November 2007).

the prevailing regulatory burden is appropriate to the needs of the market. For example, we note that Telecom is currently required to offer various resale, mobile co-location, sub-loop, and EUBA services for which there is limited demand. Such requirements come at a cost to Telecom without delivering any tangible benefits to end-users or indeed meeting a genuine end-user demand for these services.

- 170 In this regard, the Commission's decision to investigate the deregulation of resale services (25 September 2009) is an encouraging step. Telecom agrees with the Commission that "regulatory intervention should be scaled back in areas where there is effective competition" and that regulation should not "impose or maintain burdens that are unnecessary". We look forward to participating in that investigation.
- 171 The broader point to be made here is that the Commission should improve the regulatory environment by more explicitly and formally committing to this regulatory principle. Further, in aspiring to scale back regulatory intervention, we would encourage the Commission to view the minimisation of regulatory burdens and deregulation as a measure of its success.
- 172 This would also be in-keeping with the new Government Policy Statement on Regulation, which includes a commitment to review existing regulation to identify and remove requirements that are unnecessary, ineffective and excessively costly.
- 173 Another way in which the regular review of regulatory burdens could be implemented could involve imposing fixed term regulation. This approach has been adopted in Australia, whereby declared (regulated) services have fixed expiry dates. Before the declaration expires, the Australian Competition and Consumer Commission (**ACCC**) must consider whether the declaration is still needed to promote the long-term interests of end-users. While the ACCC has shown a tendency to re-declare a service, it drives an important discipline of reconsidering the upfront objectives of the regulation (and an evaluation of its success to date) before any re-declaration is implemented.
- 174 Despite its tendency to re-declare, the ACCC has acknowledged Australia's changing competitive landscape and that, given these changes, there is merit in targeted regulatory forbearance. For example, the ACCC has acknowledged that the extensive DSLAM rollout in metropolitan areas by new entrants represents a competitive constraint on Telstra and has wound back the scope of access regulation relating to the provision of key PSTN services local call resale, wholesale line rental and originating access.⁴⁹
- 175 It should be noted that undertaking regular reviews of regulation for the purposes of de-regulation, would complement the Commission's approach to market monitoring and keeping abreast of what the strengths and weaknesses of the market are.

Regular review of regulatory intervention practices

- 176 Review of existing regulatory burdens should be combined with regular review of the Commission's intervention practices. This is important to ensure that the

⁴⁹ This decision was appealed to the Australian Competition Tribunal, and while not fully upholding the ACCC's decision, the Tribunal's determination nonetheless allowed for substantial regulatory roll-back.

Commission's approach to regulatory intervention (and therefore the Commission's performance) is:

176.1 Appropriate (i.e. necessary);

176.2 Proportionate (i.e. takes into account the principles of presumptions against non-intervention and minimising regulatory burdens);

176.3 Effective; and

176.4 Measurable.

Way forward

177 An example of how a commitment to the regular review of regulatory intervention practices and effectiveness might be implemented could be for the Commission to adopt Ofcom's quarterly performance evaluation and reporting practice. Ofcom measures its performance against:

177.1 Its [statutory] objectives;

177.2 Its application of [its own] pre-declared (binding) regulatory principles;

177.3 Its internal efficiency and effectiveness;

177.4 Market developments; and

177.5 Stakeholder perceptions.⁵⁰

178 Similarly, we think that the Commission could measure its success by:

178.1 Submitting to a stakeholder questionnaire process;

178.2 Being subject to a merits review process;

178.3 Reference to a commitment to achieve particular and measurable market outcomes;

178.4 Reference to its record of engagement with industry; and

178.5 Reference to evidence of its initiatives to regularly review and minimise regulatory burdens, including through deregulation.

179 An appropriately skilled, independent institution (perhaps the Treasury, in accordance with its new regulatory oversight responsibilities, or an external body, somewhat akin to the Australian Productivity Commission) could be empowered to review the Commission's quarterly reports and conduct its own assessment of the Commission's performance against the measures set out above. This second tier of review would ensure robust accountability for regulatory decisions.

⁵⁰ See <http://www.ofcom.org.uk/consumeradvice/guide/#aboutus> (in particular go to accountability)

THE VALUE IN GREATER INDUSTRY SELF-/CO-REGULATION

- 180 In line with the promotion of increased industry engagement and a collaborative partnership between the Commission and market participants, we think there is considerable scope for the Commission to facilitate greater industry self- or co-regulation.
- 181 For example, the Commission should ensure that the regulatory regime provides market participants the opportunity to negotiate commercial solutions before regulatory intervention is considered. Alternatively, the approach recently announced in Australia could equally achieve a better balance between regulatory and commercial solutions. There, the ACCC can, for example, establish default price and non-price terms for access seekers to fall back on whilst still allowing parties to negotiate different terms.
- 182 Seeking greater industry self- or co-regulation is also consistent with the principles of minimising regulatory burdens and enabling deregulation. Ofcom guidelines in this area show what can be done with a balance of hard-line regulation and forbearance if the parties are willing to enter into genuine (self-interested) self-regulation and change behaviours.⁵¹
- 183 The Commission recognises the role of the Telecommunications Carriers Forum (**TCF**) in achieving a number of successful industry initiatives in New Zealand, such as Number Portability, the Customer Transfer Code, and settling the operational aspects of Standard Terms Determinations (**STDs**). The Commission has also sought to implement the unanimous recommendations of the TCF in relation to certain STDs.
- 184 Like Ofcom, the Commission's record of engagement with the TCF recognises that "self- and co-regulation can, in the right circumstances, provide an effective means to address citizens' and consumers' interests in line with [the regulator's] statutory obligations."⁵²
- 185 We submit that there is a real opportunity to utilise and further develop the existing relationship between the Commission and industry participants, either through the TCF or some other means, to increase the scope for industry self- and/or co-regulation.
- 186 We also encourage the Commission to remain open to the proposal of undertakings as an alternative to regulation. Indeed, we encourage the Commission to view the facilitation of self- and co-regulatory situations – through such means as undertakings – as a measure of its success as regulator.
- 187 The advantages of undertakings (and self- and co-regulatory solutions generally) include that they:

187.1 are low cost;

⁵¹ "Identifying appropriate regulatory solutions: principles for analysing self- and co-regulation", (10 December 2008) Ofcom

⁵² Ibid Executive Summary, para 3.

187.2 lead to quicker outcomes;

187.3 can be more flexible to changing market conditions; and

187.4 can be approached by the parties on a commercial basis.

188 Schedule 3A of the Telecommunications Act 2001 was intended to facilitate co-regulation by these means. It is unfortunate that the Schedule 3A process has instead been the source of considerable confusion in practice. The Commission has made a number of general comments around the scope and substance of undertakings required under Schedule 3A during the course of the MTAS investigation.

189 The Guidelines provide a good opportunity for the Commission to develop these general comments into more concrete guidance. We would like to work with the Commission to improve the Schedule 3A process, including a requirement for the Commission to provide comprehensive feedback on undertakings proposed pursuant to Schedule 3A, together with its cost benefit analysis.

190 We would also find it useful if the Commission provided guidance on its interpretation of clause 8 of Schedule 3A. For example, if the Commission accepts an undertaking from a party it seems reasonable for that party not to expect to be regulated over top of that. Otherwise, there is potential for the voluntary undertakings regime to be undermined.

Way forward

191 A helpful reference point for developing industry self- and co-regulation is the Ofcom's Statement on "Identifying appropriate regulatory solutions: principles for analysing self- and co-regulation". That statement notes that:

"...industry approaches work best where the incentives of industry are aligned with those of the public ...we have found that self-regulation is most likely to work where the following issues are present: industry collectively has an interest in solving the issue; industry is able to establish clear objectives for a potential scheme; and the likely industry solution matches the legitimate needs of citizens and consumers...Where we determine that self-regulation is unlikely to succeed, co-regulation may be used to ensure that incentives are effectively aligned..."⁵³

192 The first step may be for the Commission to invite the TCF and the industry generally to suggest areas where these conditions apply.

⁵³ Ibid, para 7.

INSTITUTIONAL ARRANGEMENTS

- 193 The regulatory framework for the telecommunications sector can be broadly divided into four stakeholder groups:
- 193.1 Ministers and Government departments;
 - 193.2 The Commission as regulator and enforcement agency;
 - 193.3 The industry and industry bodies; and
 - 193.4 End users and consumer groups.
- 194 Each has its own duties, responsibilities, objectives, drivers, and functions. Each also brings to bear expertise that can usefully contribute to the overall design of the regulatory regime. For example:
- 194.1 Government articulates policy objectives and acts pursuant to a broad political mandate;
 - 194.2 The Commission acts as an independent regulator of the industry for the long-term benefit of consumers and implements the policy set by Government;
 - 194.3 Industry participants provide operational expertise; and
 - 194.4 End users communicate price and quality preferences.
- 195 It is important that the various objectives, drivers, functions and expertise of each tier are communicated freely to the others to ensure that decisions for the sector are made against a backdrop of comprehensive information and shared understandings.
- 196 The separation of enforcement and economic regulatory roles in New Zealand will be important to facilitate constructive engagement and international best practice aspirations to reduce regulation over time. The Commission is both an economic regulator and a competition authority.
- 197 These two roles may require similar skill sets in terms of market definition and market analyses. However, the culture and the focus in *ex post* as compared to *ex ante* regulation is quite different. If there is a blurring of roles and focus – which we have raised a concern about in relation to the Commission’s view on its monitoring powers – there is a risk of undermining genuine, constructive engagement and the achievement of outcomes consistent with regulatory best practice principles.
- 198 As the telecommunications regulator, the Commission must adopt a long-term, forward-looking approach, informed by a close understanding of the regulated industries, the regulated industries’ customers and the end-consumers. This requires regular and ongoing engagement with the industry.
- 199 In contrast, as the competition authority, the Commission enforces competition law, pursues offenders and punishes bad behaviour. As the competition authority, the Commission only needs to understand the relevant market to the extent required for

investigation of particular conduct. Any engagement with participants is on an issue by issue basis, and is relatively short term. Developing meaningful relationships in that context is less important. Having said that, even in the enforcement context there is scope for the Commission to promote a culture of encouraging compliance and understanding, rather than adopting solely a prosecution–focussed approach. To this end, we would encourage the Commission to implement the Office of Fair Trading (the UK Competition authority) approach to enforcement. In its 2009 annual simplification plan it recognises that enforcement should be seen as an instrument of last resort:

"A.17 Preventing harm in the first place is better for consumers than taking enforcement action afterwards. It is also less burdensome for business, provided it is achieved by cooperation rather than compulsion...."

19 We also work to achieve compliance through equipping businesses and consumers with knowledge about their legal obligations and rights..."

200 We think that approach is both constructive and desirable.

201 Another aspect of the institutional arrangements which requires further careful thought is how to make involvement by the Commission and Government more seamless. As noted above, the disconnection between when Government drives investment and when the Commission then prices that investment is a significant problem for investors.

Way forward

202 Some ways in which institutional role clarity and greater communication between institutions could be improved include:

202.1 Fostering a culture of partnership between the Commission as regulator and the industry;

202.2 Seeking to resolve operational issues through the TCF (with the Commission taking responsibility to ensure that parties adhere to what they agree at TCF meetings);

202.3 Guarding against throwing major policy issues to the Commission to resolve; and

202.4 Ensuring that the regulator remains apolitical, subject to decision-making accountability (both procedural and substantive).

203 In addition the accountability of the Commission as regulator should be improved. This would best be achieved through the introduction of merits-review appeal rights. Introducing merits review rights is desirable for a number of reasons:

203.1 They provide a helpful overlay of accountability, credibility, and quality assurance and incentivise high quality decision-making – the contribution of merits review in driving this discipline is most important;

- 203.2 They also provide a formal check on the exercise of the regulator's discretionary powers to ensure that regulatory issues are not played out in a public and political way, which we accept is not constructive for the industry;
- 203.3 They give rise to useful precedent that guides future decision-making, which increases certainty and predictability for both the regulator and industry participants; and
- 203.4 They provide flexibility for regulatory errors to be corrected – this is particularly important where the telecommunications market is changing so quickly, making it difficult to anticipate developments.⁵⁴
- 204 These benefits outweigh the costs associated with merits review, including:
- 204.1 Litigation costs;
- 204.2 The cost to the regulator in seeking to ensure all decisions are sufficiently robust to withstand merits review;
- 204.3 The cost of delay and potential gaming of regulatory decisions; and
- 204.4 The potential for different rather than better decisions by another decision maker.⁵⁵
- 205 As well as permitting consideration of the substantive impact of regulatory decisions (rather than just consideration of procedural propriety), merits review recognises that regulatory decision makers will not always get it right. Where they don't, the exercise of appeal rights is both justified and necessary. That should not be viewed as a criticism. The absence of merits review, combined with the current output agreements between Government and the regulator, risk driving a focus on decision-making procedure to avoid judicial review, leaving the substantive quality of the decision as a secondary concern. We do not think that balance is appropriate.

⁵⁴ There is also a danger "that in the absence of merits review, parties will seek judicial review of issues that are really products of the decision-making process, and are not concerned with the process itself. This will either waste valuable time, or will lead to Judges venturing into areas that are not really within their realm of expertise. The availability of merits review, which seeks to determine whether the regulator's decision was "correct" (or, at least, not inconsistent with the statute's objectives) given the facts and the guiding statutory principles, solves this problem." The merits of merits review...

...merits review is a fundamental right that should be available to firms that are subject to regulation where the relevant statute is worded in such a way so as to allow regulatory discretion. **Any society that believes that merits review is unnecessary is neither on the frontier of best regulatory practice, nor is it likely to be one that is seen by firms as one where long-term investment initiatives are desirable.** The merits review process:

- Promotes transparency, accountability, and consistency in regulators' decisions;
- Diminishes the likelihood of regulatory error and its consequential private and social costs;
- Clarifies the operation of statutes and indicates where amendments may be necessary;
- Promotes an environment in which long-term investment decisions can be made with confidence;
- Ensures that regulatory outcomes are consistent with policy intentions."

The Merits of Merits Review - NZLJ (July 2006), Paras 237, 238 and 240, Professor David Round,

⁵⁵ See New Zealand Legislative Advisory Committee Guidelines on Process & Content

- 206 The exclusion of merits review should not be driven by a fear that appeals will, or are likely, to be brought in respect of all regulatory decisions. It will be the responsibility of the industry, in line with what should also be the Commission's view, that litigation is used as a last resort. That approach is consistent with a culture of regular constructive engagement and partnership.
- 207 Merits review rights are available in the regulation of other infrastructure sectors in New Zealand. The policy in New Zealand shifted towards best practice accountability through merits review in the Part 4 Commerce Act Amendments last year. There is no policy, or other unique, reason for excluding regulatory decision-making under the Telecommunications Act.
- 208 In Australia, merits review has been consistently retained under the National Electricity and Gas laws. Appeal rights in telecommunications in Australia have changed from time to time. The current proposal by Government is to remove the merits review rights currently available. That, however, is a response to the particular exercise of telecommunication regulatory merits review rights in Australia. The proposal to remove these was not undertaken lightly⁵⁶ has more been a result of appeal process since, while the subject of appeal, the relevant regulatory decision is suspended. This has encouraged regulated suppliers to game the process and delay the implementation of regulated outcomes.
- 209 The ability of market participants (both access providers and access seekers) to manipulate the regulatory process in Australia by abusing appeal rights is a result of a design flaw in the merits review process and is a concern that could be easily avoided if implemented in the New Zealand context by simply providing a general rule that the regulatory decision stands unless, and until, it is overturned.
- 210 We acknowledge that this particular implementation suggestion is beyond the scope of what the Commission can do and that it would require legislative change. But it is a best practice issue and is relevant to developing a culture of engagement and continual improvement of the regulatory framework that we hope that Commission will keep front of mind going forward.

⁵⁶ Explanatory Memorandum, Telecommunications Legislation Amendment (Competition And Consumer Safeguards) Bill 2009 – see for example p 5 and also p 18 and pp 48f which shows that the provisions have been in effect for over 12 years and that attempts were made to resolve these problems http://www.dbcde.gov.au/communications/telecommunications_regulatory_reform.

ANNEX 1 – HOW THE NEW ZEALAND REGULATORY FRAMEWORK COMPARES TO INTERNATIONAL REGULATORY BEST PRACTICE PRINCIPLES

NZ needs to step up to move towards international best practice



Key components of best practice regulation	NZ	UK	Aust	Sing
A legislated purpose statement that includes investment incentives		4	14	19
A legislated duty to minimise regulatory burdens		5		20
Regulator has clear communicated policy objectives		6		
Regulation has a bias against intervention		7	15	
Regulators facilitate self and co-regulation solutions	1	8	16	21
Least intrusive form of regulation (minimum necessary)		9	15	
Cost benefit analysis – clear benefit before intervention	2	10	17	?
Reviews intervention and market developments and state of competition in markets	3	11		
Accountability through appeal right and merits review to promote high quality outcomes		12	18	22
A plan to minimise burdens and de-regulate		13		

1. At best, TCF offers some co-regulation, when accepted by Commission.
2. On occasion, but poorly implemented and rare.
3. In some circumstances, but in key cases not permitted.
4. Communications Act 2003 (UK) and Art. 8 relevant EU Directive
5. Communications Act 2003 (UK)
6. Ofcom: *Annual Plan*
7. Ofcom: *Regulatory principle*
8. Ofcom supports industry groups and has a commercial relationship. Draft document on *Initial Assessments on when to adopt self- or co-regulation*
9. Ofcom: *Regulatory principles*
10. Ofcom: *Better Regulation Making – Ofcom's approach to impact assessments*

11. Ofcom performance and evaluation (quarterly updates in annual plan)
12. Communications Act 2003 (UK)
13. Ofcom: *Simplification plan*
14. Trade Practices Act 1974, section 152AB
15. Some public statements to this effect but no clear policy statements
16. ACMA is responsible for facilitating industry codes with bodies like ACIF and CIC. Includes number portability, emergency calling etc. Some evidence in individual decisions
17. Not all decisions can be appealed on merits but key ones can
18. Information-Communications Development Authority of Singapore Act (IDA Act), s6.
19. Code of Practice for competition in the Provision of Telecommunications Services 2005, section 1.
20. IDA Act, s6.
22. Parties have the right to require reconsideration by the IDA, and then to appeal a reconsideration to the Minister.

Telecom Corporation of New Zealand Limited

NB: There are processes in train that will remove merits review in Australia. This will change the assessment of merits review from a green light to a red light.

OFCOM'S VOLUNTARY COMMITMENT TO REGULATORY PRINCIPLES

FIGURE 1: OFCOM'S REGULATORY PRINCIPLES

WHEN WE REGULATE

- Ofcom will operate with a bias against intervention, but with a willingness to intervene promptly and effectively where required.
- Ofcom will intervene where there is a specific statutory duty to work towards a public policy goal that markets alone cannot achieve.

HOW WE REGULATE

- Ofcom will always seek the least intrusive regulatory methods of achieving our policy objectives.
- Ofcom will strive to ensure that our interventions are evidence-based, proportionate, consistent, accountable and transparent in both deliberation and outcome.
- Ofcom will regulate with a clearly articulated and publicly reviewed annual plan, with stated policy objectives.

HOW WE SUPPORT REGULATION

- Ofcom will research markets constantly and will aim to remain at the forefront of technological understanding.
- Ofcom will consult widely with all relevant stakeholders and assess the impact of regulatory action before imposing regulation on a market.

ANNEX 2 – PRESCRIPTION VERSUS REASONING – A COMPARISON BETWEEN NEW ZEALAND AND THE UK

The level of prescription in regulatory determinations is high and the level of guidance is low by a simple comparison

NEW ZEALAND UCLL STD	UNITED KINGDOM LLU⁵⁷
<p>128,500+ words prescribing obligations on Telecom</p> <ul style="list-style-type: none"> - General Terms 20,000 words - Service description 1,500 words - Price list 3,000 words - SLA 5,000 words - Ops Manual 20,000 words - Implementation Plan 6,000 words - Interference Plan – 73,000+ words <p>37,000 words – reasoning</p> <p>TOTAL:</p> <p>165,500+ words</p>	<p>24,000* words prescribing obligations on two operators through the notification and conditions imposed on BT and Kingston</p> <p>50,000 words – reasoning</p> <p>TOTAL:</p> <p>Less than 74,000 words</p> <p>* Close approximations</p>

⁵⁷ Wholesale local access market review – December 2004

ANNEX 3 - THE DYNAMIC NEW ZEALAND REGULATORY ENVIRONMENT

NEW ZEALAND	Australia	UNITED KINGDOM
<p>2001: Introduction of ex ante regulation</p> <ul style="list-style-type: none"> • Resale regulation • Commercial solutions promoted first <p>2006: Significant amendments to the Act leading to:</p> <ul style="list-style-type: none"> • 2008 LLU STD • 2008 UBA STD • 2009 SLU STD <p>2008: Operational Separation</p> <ul style="list-style-type: none"> • Cabinetisation • Unregulated services caught in the model • Resale retained <p>2009: Accounting separation introduced</p> <p>2009: Government Broadband investment initiative announced</p>	<p>1989: Independent industry regulator, AUSTEL, established.</p> <p>1991: Introduction of seven telecommunications-related Acts, including the <i>Telecommunications Act 1991</i>, which established a market duopoly for the provision of fixed network telecommunications services and an oligopoly for the provision of mobile services.</p> <p>1997: Removal of general carrier duopoly and mobile carrier oligopoly, established a mandatory access regime for services and facilities (negotiate-arbitrate model), and regulated anti-competitive conduct (sections XIB and XIC of the Trade Practices Act 1974).</p> <p>2002: ACCC required to publish indicative core service prices (ULL, LCS, PSTN, OTA)</p> <p>2003: 'Accounting separation' of Telstra's wholesale and retail accounts introduced.</p> <p>2005: 'Operational separation' for Telstra introduced, Telstra's operational separation plan approved June 2006.</p> <p>2009: April Government National Broadband Network announced.</p> <p>2009: September proposed regulatory changes to separate Telstra (voluntary structural separation or strong mandated functional separation), reforms to the access regime to give the ACCC more powers and introduce an ex ante access regime, and consumer safeguard reforms.</p>	<p>1984: Introduction of sector specific ex ante [and economic regulation] regulation</p> <p>Accounting separation</p> <p>2000 LLU introduced (OfTel condition 83 of BT licence)</p> <p>Post 1999 Review concurrent competition law powers with OFT</p> <p>2003: EU framework grounding regulation further in market analyses</p> <p>2004: Launch of 18 month Telecommunications Strategic Review (TSR) engagement</p> <p>2005: Completion of TSR</p> <p>2005: BT operational separation (and progressive physical separation)</p> <ul style="list-style-type: none"> • Linked to SMP services • 31 exemptions, 19 variations

ANNEX 4 – ONGOING REGULATION

Ongoing regulatory intervention required	Type	Date requested, due or commenced	Date completed
UBA			
Adjustment type	In respect of	Date submitted	Commission response
Quarterly	Dec quarter	31 January 2008	Approved by email of 4 April
Quarterly	March quarter	22 April 2008	Approved 3 July 2008
Quarterly	June quarter	31 July 2008	Approved 26 August 2008
Quarterly	Sept quarter	31 October 2008	Approved 3 Dec 2008
Service	Retail launch of Total Home (in October 08)	28 November 2008	Approved 20 July 2009
Annual	Required by Price List (clause 3)	12 Dec 08, extra info 5 February 09	Approved 10 March 2009
Quarterly	Dec quarter	30 January 2009	Approved 20 July 2009
Quarterly	March quarter	28 April 2009	Approved 20 July 2009
Service	Retail launch of "Double your data" on 1 May 2009	30 June 2009	Pending
Quarterly	June quarter	31 July 2009	Pending
Service	Retail launch of new plan	31 August 2009	Pending

	(in July 09)		
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Number	Reason	Decision number/Status	Date
1	Various changes	636	11 April 2008
2	Various changes to price list	644	5 June 2008
3	Early Termination Charge	Pending	Submitted 9 Sept 2008
4	Make amendment to price list to incorporate changes to Telecom's Retail broadband offerings – impact on UBA core charges	671	22 April 2009
5	Rejection Codes and Modem Installation	679	Dated 23 July but Telecom notified 21 August 2009
6	VDSL	withdrawn	

Clarification and reviews of UCLL

STD	Date	Process	Topic	Status
UCLL and UCLL Co-lo	24 Jan 08	Clarification	"Acting as a bank"; No fault found price list; Service Level Terms; requirement to publish on "Telecom's website"; Interference Management plan	Decision 643 dated 21 May 2008
UCLL	20 Feb 08	Clarification	Number portability	Decision 643 dated 21 May 2008
UCLL Backhaul	11 Sept 08	Clarification	Aggregation; pricing; capital carrying cost formula; soft launch; jitter	Decision 665 dated 5 March 2009

UCLL and UCLL Co-lo	7 Nov 08	Price review	LCIQ and power	21 April 2009
UCLL and UCLL Co-lo	24 Feb 09	Clarification	Transfer costs	Still with the Commission
UCLL; UCLL Co-lo; UCLL Backhaul	12 Mar 09	Change mechanism	Service level terms and ops manuals	Still with the Commission
UCLL and UCLL Co-lo	12 May 2009	Clarification	Waiver process for cabinetisation notice	Still with the Commission
UCLL Backhaul	12 May 2009 ⁵⁸	Clarification	Service Description	Decision 681 dated 9 September 2009
Sub-loop Services STD	26 Aug 2009	Clarification	Notification of Distribution Cabinet information; backhaul charging methodology; market share assessment; timing of first assessment date; service level terms notifications	Still with the Commission
All	14 Sept 09	Price review	Price changes triggered by service company contract renegotiations	Still with the Commission

⁵⁸ We acknowledge that there was some confusion with this clarification; Chorus sought to withdraw the clarification application when we discovered there was an error with it, the TCF Working Party agreed, but the Commission helpfully went ahead with the clarification, ensuring that the error was fixed.

ANNEX 5 - IMPLEMENTATION OF REGULATORY LIFE CYCLE PROCESSES: A COMPARISON OF THE UK, EC, AUSTRALIA AND NEW ZEALAND

Red = major strategic documents

	UK / Ofcom Reports	EC	Australia / ACCC	NZ / Commerce Commission
KNOW THE INDUSTRY (Monitoring and data collection to understand the wider context)	<u>Annual Communications Market Reports</u> - report on trends and developments in UK communications market, with aim of providing a context for decision-making by Ofcom	<u>Internet of Things — An action plan for Europe</u> - broad policy paper analysing the future development of internet in the EU	<u>Annual Telecommunications reports</u> - reports focusing on competitive safeguards in the telecommunications market and changes in prices paid for telecommunications services	<u>Telecommunications Market Annual Monitoring Reports</u> - report monitoring competition in New Zealand telecommunications markets and the performance and development of those markets
	<u>Nations and Regions Communications Market Reports</u> - annual market reports with a geographical focus	<u>Green Paper on the Review of the Consumer Acquis</u> - this Green Paper launched a major new drive to adapt core EU consumer rules to the challenges of the fast-changing digital world	<u>Snapshot of Broadband Deployment</u> - quarterly report detailing broadband deployment and uptake	<u>Telecommunications Key Statistics Quarterly Monitoring Reports</u> - regular reports detailing key developments/statistics in the telecommunications market
	<u>International Communications Market Reports</u> - annual reports on developments in international communications markets	<u>Communication 'Bridging the broadband gap'</u> - this Communication assesses the instruments available at EU level to address the lack of adequate broadband services in the less developed areas of the Union	<u>Communications Infrastructure and Service Availability in Australia</u> - regular reports detailing the stock of telecommunications infrastructure owned and operated by Australian telecommunications carriers	<u>Broadband quality quarterly reports</u> - regular reports on broadband performance in NZ
	<u>Communications Market – Special Reports</u> - adhoc market reports on selected narrow topics		<u>Market indicator reports</u> - regular reports disclosing revenue and usage information provided by Telstra, Optus, AAPT, Primus and Vodafone as part of their regulatory reporting requirements under the Regulatory Accounting Framework	<u>Broadband at crossroads</u> - series of papers presented at a conference addressing key broadband issues
	<u>Communications Market – Digital Progress Report</u> - quarterly reports on the progress of digital technologies such as broadband		<u>Emerging market structures in the communications sector</u> - one-off report which advises on the extent to which emerging market structures are likely to affect competition across the communications sector, including through the provision of bundled pay TV, telephony and broadband services	<u>NGN: Strategic issues and key themes</u> - an overview of the key themes relating to NGN and the views of stakeholders on those themes
	<u>Ofcom Fixed Telecoms Market Information Update</u> - a summary of revenue, volume and market share trends from the residential and business fixed telecoms markets		<u>Evolution of infrastructure regulation in Australia—working paper no. 1</u> - an overview of historical developments as well as an outline of the current form of economic regulation for telecommunication, posts, airports, energy, rail, ports, shipping, water and petrol	
	<u>Converged Communications in</u>		<u>"Network" Publication</u>	

	UK / Ofcom Reports	EC	Australia / ACCC	NZ / Commerce Commission
	<u>Tomorrow's World (2009)</u> - collaboration with industry on future of communications market		- a publication of the Utility Regulators Forum which addresses developments in utilities regulation	
	<u>Delivering super-fast broadband in the UK (2008)</u> - outline of Ofcom's plans to aid delivery of super-fast broadband, with particular emphasis on private investment		<u>Telecommunication infrastructures in Australia 2001: a BIS Shrapnel report prepared for the ACCC</u> - one-off publication comprehensively detailing telecommunications infrastructure in Australia	
	<u>Estimating the commercial trading value of spectrum (2009)</u> - a project to facilitate spectrum trading by providing increased information to the market			
	<u>Large Business Use of Telecoms Services: Research Report 2006</u> - a report to show how large businesses in the UK use fixed line telecoms, mobile telecoms and advanced data services			
	<u>Communications: The next decade (2006)</u> - understanding the future of the communications market in the regulatory context			
	<u>Assessment of the theoretical limits of copper in the last mile (2008)</u> - a project to establish a theoretical, rather than practical, limit of copper in the last mile			
	<u>Research Report: Voice over Internet Protocol (VoIP) (2007)</u> - report on developments in VoIP services to inform Ofcom's regulatory approach			
ANALYSING AND ENGAGING ON THE ASSESSMENT OF THE STATE OF COMPETITION	<u>Strategic Review of Telecommunications</u> - major review designed to set out a strategic direction for Ofcom's activities in relation to telecoms, and to agree on Undertakings with BT	<u>'The Challenges of Convergence' working paper of the i2010 High Level Group</u> - this paper highlights various technological, market and policy challenges posed by digital convergence and addresses the effectiveness of the overall legal and regulatory framework	<u>Competition in data markets (1998)</u> - final report on whether to declare certain ISDN services, and whether to amend declarations for the digital data access service and transmission capacity under Part XIC of the TPA	<u>Investigations</u> - Mobile Terminations Access - Resale Services - Mobile Roaming and Co-location - Mobile Termination - Review of Regulated Services
	<u>Business connectivity market review</u> - SMP assessment and proposals for regulation of leased lines market	<u>Communication on market reviews under the EU Regulatory Framework</u> - the report reviews the state of the electronic communications markets in 2005	<u>Competition in the corporation customer segment of telecommunications markets</u> - six-monthly reports on competition in the telecommunications industry in the corporate segment of the business customer group	
	<u>How will Ofcom consult?</u> - guidelines and principles for consultation with Ofcom	<u>Communication on Strengthening the Internal Market for Mobile</u> - paper outlining a strategy favouring the take-up of mobile TV across the 27 EU Member States	<u>Inquiry into domestic intercarrier roaming declaration</u> - public inquiry into whether services enabling domestic intercarrier roaming should be declared under the TPA	
	<u>Assessment of whether H3G holds a position of SMP in the market for</u>	<u>Communication 'Better access for rural areas to modern ICT'</u>	<u>Local telecommunications services (1999)</u> - a report on the declaration of an	

	UK / Ofcom Reports	EC	Australia / ACCC	NZ / Commerce Commission
	wholesale mobile voice call termination on its network	- outlines Commission's plan to boost internet networks and services in rural areas	unconditioned local loop service, local PSTN originating and terminating services, and a local carriage service under the TPA	
	Assessing the impact of NGNs on interconnection tariffs' distance gradients - independent report to understand the impact on interconnection charges of BT's planned NGN, and also the impact on platform-based competition	Communication on market reviews under the EU Regulatory Framework - regular reports reviewing operation of telecommunications	Telecommunication charges in Australia 1995–99 - report surveying price changes from 1995 to 1999 for all services included in the Telstra carrier charges—price control arrangements, notification and disallowance determination 1997—but not leased line services	
	Competition to supply business telecoms - analysis of the behaviour and attitudes of telecoms purchasers across a range of businesses, and business sizes, in order to help to assess whether regulation should be amended in any of the remaining regulated fixed markets	Communication on a market-based approach to spectrum management in the European Union - outline of Commission's intentions to introduce spectrum markets	Strategic review of the regulation of fixed network services - major review and decision to continue to declare certain fixed line services	
	Cost of the BT UK local loop network - Report for Ofcom by Analysys	Towards a reinforced culture of consultation and dialogue - General principles and minimum standards for consultation of interested parties by the Commission - document which lays down a number of general principles that govern Commission relations with interested parties, and a set of minimum standards for the Commission's consultation processes	Analysys Cost Model Discussion Paper - December 2008 - consultation paper on an approach of estimating the long-run efficient cost of providing services on the Australian fixed network over 2007-2012	
	End-to-end connectivity - review of end-to-end connectivity			
	Fixed Narrowband Retail Services Markets - Identification of markets and determination of market power - review of the state of competition in the retail narrowband telephony markets			
	Mobile call termination – market review - review of the market(s) for supply of wholesale mobile voice call termination, including conclusions on market definition and SMP			
	Review of the fixed narrowband services wholesale markets - assessment of the state of competition in the wholesale fixed narrowband services markets and possible regulatory responses			
	Review of the wholesale broadband access markets - assessment of the state of competition in the wholesale broadband access market and possible regulatory			

	UK / Ofcom Reports	EC	Australia / ACCC	NZ / Commerce Commission
	responses			
ASSESS WHETHER INTERVENTION SHOULD OCCUR AND IF SO, HOW (THROUGH PROPORTIONAL OPTION ANALYSIS AND CBA)	Better Policy Making: Ofcom's approach to Impact Assessment	Commission Impact Assessment Guidelines - general guidance for assessing potential impacts of different policy and regulatory options	Best practice utility regulation - Utility Regulators Forum paper to promote discussion on the issue of best practice in utility regulation	Investigations - Mobile Terminations Access - Resale Services - Mobile Roaming and Co-location - Mobile Termination - Review of Regulated Services
	An assessment of alternative solutions for UK number portability	Communication from the Commission on Impact Assessment - strategy document outlining how impact assessment for regulation will be implemented in the EU	Access pricing principles: telecommunications a guide - document outlining the ACCC's approach when considering access pricing issues under Part XIC of the TPA	Input methodologies discussion paper and consultation
	Identifying appropriate regulatory solutions: principles for analysing self- and co-regulation - statement of the high-level principles that Ofcom will use to determine appropriate regulatory solutions	Evaluation of the Commission's Impact Assessment System - reviews the experience with regard to the set-up, implementation and results of the Commission's approach to Impact Assessments	Infrastructure regulation and market reform: principles and practice	TSLRIC methodology reports
	Mobile call termination – market review Delivering super-fast broadband in the UK - sets out Ofcom's regulatory plan to incentivise investment in broadband infrastructure	EU common methodology for assessing administrative costs imposed by legislation - methodology for assessing administrative costs set by EU legislation	Inquiry into domestic intercarrier roaming declaration - inquiry into whether services enabling domestic roaming should be declared	
	Future broadband - Policy approach to next generation access - outline of next generation access networks regulatory strategy	Communication 'Preparing Europe's digital future: i2010 Mid-Term Review' - assessment of whether the Commission's i2010 programme to promote ICT in the EU is effective	Local telecommunications services - document outlines the ACCC's approach when considering access pricing issues under Part XIC of the TPA	
	Mostly Mobile - ongoing review of mobile services to form Ofcom's mobile regulatory strategy	Proposal for a Regulation on roaming on public mobile networks within the Community - proposal to regulate through price ceilings, so that mobile roaming charges are not unjustifiably higher than those for domestic mobile phone use	Telecommunications services—declaration provisions: a guide to the declaration provisions of Part XIC of the Trade Practices Act - a guide setting out the regime under which providers of carriage services, and of services supplied by means of carriage services, can access specific services to conduct their businesses	
	Next Generation New Build: Delivering super-fast broadband in new build housing developments - outline of the regulatory environment for fibre network deployments in new build developments	Proposals for a reform of the EU regulatory framework for electronic communications - proposal to reform electronic communications regulation including access and interconnection		
	Next Generation Networks: Developing the regulatory framework - Ofcom's strategic approach to NGN regulation	User and consumer perspective in the context of convergence: working paper of the i2010 High Level Group - this issue paper identifies the gaps in the protection of users in the digital environment and reviews options for policy response		

	UK / Ofcom Reports	EC	Australia / ACCC	NZ / Commerce Commission
	<p><u>Review of the fixed narrowband services wholesale markets</u> - major review of fixed narrowband services wholesale markets, including assessment of SMP and possible solutions</p> <p><u>Review of the wholesale broadband access markets</u> - major review of wholesale broadband access markets, including assessment of SMP and possible solutions</p> <p><u>Proposed guidance as to how Ofcom may interpret the meaning of “fair, reasonable and non-discriminatory” and other regulatory conditions when assessing charges and terms offered by regulated providers of Technical Platform Services</u></p>	<p><u>‘Content and Convergence’ working paper of the i2010 Level Group</u> - this issue paper outlines the main economic and cultural challenges arising from digital convergence</p>		
EVALUATE AND IMPLEMENT		<p><u>Communication ‘European Electronic Communications Regulation and Markets’</u> - regular reports on the Member States’ implementation of the EU framework for electronic communications</p>		<p><u>Determination on the multi-party application for determination of ‘local telephone number portability service’ and ‘cellular telephone number portability service’ designated multinetwork</u></p>
		<p><u>Communication on the legal framework for mobile TV networks and services: best practice for authorisation – the EU model</u> - guidelines identifying the main principles which regulators and governments in the EU should follow when authorising operators to provide Mobile TV services</p>		<p><u>Report on whether to amend the roaming service or accept the Vodafone undertaking as an alternative to amending the regulations</u></p>
		<p><u>Commission Recommendation on the Regulatory Treatment of Fixed and Mobile Termination Rates in the EU</u> - document which sets out guidance for EU telecoms regulators on the cost-based method to be used when calculating termination rates</p>		<p><u>Report on whether to amend the co-location service on cellular mobile telephone transmission sites or accept the Vodafone co-location undertaking as an alternative to amending the regulation</u></p>
		<p><u>Implementing the Community Lisbon programme: A strategy for the simplification of the regulatory environment</u> - strategy document outlining the European Union’s plan to simplify regulation</p>		<p><u>Reconsideration Final Report on whether mobile termination should become a designated or specified service</u></p>
		<p><u>Action plan: Simplifying and Improving the Regulatory Environment</u> - Document setting out methods and approaches to evaluate regulation</p>		
REVIEW FOR	<p><u>Evaluating the impact of the Telecoms Review</u></p>	<p><u>Strategic Reviews of Better Regulation in the European Union</u></p>	<p><u>Annual report</u> - broad review of ACCC’s regulatory activities</p>	<p><u>Review of regulated services</u> - report under the Telecommunications</p>

	UK / Ofcom Reports	EC	Australia / ACCC	NZ / Commerce Commission
EFFECTIVENESS AND OPPORTUNITIES FOR SIMPLIFICATION	- evaluating the impact of the Strategic Telecoms Review on the fixed telecoms market, including BT's undertakings	- reviews progress on initiatives to simplify regulation and highlights areas where further efforts are necessary	and policies	Act 2001 on whether to extend the period of regulation of certain telecommunications services
	<u>Annual report</u> - broad review of Ofcom's regulatory activities and policies	<u>Better Regulation for Growth and Jobs in the European Union</u> - broad strategy document highlighting the need for more effective regulation and setting out approaches to achieve better regulation	<u>ACCCount</u> - details the ACCC's activities in the enforcement of the TPA, merger reviews, compliance actions, adjudication issues, economic regulation and international involvement	
	<u>Broadband regulation</u> - overview of regulatory action to date and future policy/action	<u>Updating and Simplifying the Community Acquis</u> - strategy document setting out particular objectives for improving and simplifying European Union regulation	<u>Telstra's compliance with price control arrangements Jan98 to June99</u>	
	<u>Competition and Regulation in Telecoms and Broadcasting</u> - an overview of Ofcom's competition and regulatory policy and outline of policy priorities	<u>Action Programme for Reducing Administrative Burdens in the European Union</u> - document setting out the Commission's proposed actions to reduce administrative burdens	<u>2004 review of Telstra price control arrangements</u> - review of Telstra price control arrangements and recommendations on arrangements going forward	
	<u>Review of the Universal Service Obligation - Statement</u> - review of the effectiveness of the USO	<u>Annual reports</u> - monitoring the application of EU law	<u>Incentive regulation, benchmarking and utility performance</u> - Utility Regulators Forum paper reviewing approaches to measure utility performance and regulation, with particular reference on the CPI-X regulatory approach	
	<u>Telecommunications Statement</u> - broad statement on Ofcom's activities and objectives in the telecoms sector	<u>Better Law-making – Annual reports on subsidiarity and proportionality</u> - annual review of the implementation of the subsidiarity and proportionality principles		
	<u>The replicability of BT's regulated retail business services and the regulation of business retail markets</u> - review of regulation of business retail markets to determine effectiveness of regulation	<u>Progress reports on the strategy for simplifying the regulatory environment</u> - annual reporting on the simplification strategy		
	<u>Report on the Implementation of BT's Undertakings</u> - regular reports on the effectiveness of the undertakings and BT's progress towards delivering on the undertakings			
	<u>Topcomm Review</u> - review of effectiveness of consumer satisfaction programme			

ANNEX 6 – TELECOM'S UNDERSTANDING OF SECTION 18

Overview

1. Section 18 of the Telecommunications Act 2001 states:

Purpose

(1) The purpose of this Part and Schedules 1 to 3 is to promote competition in telecommunications markets for the long-term benefit of end-users of telecommunications services within New Zealand by regulating, and providing for the regulation of, the supply of certain telecommunications services between service providers.

(2) In determining whether or not, or the extent to which, any act or omission will result, or will be likely to result, in competition in telecommunications markets for the long-term benefit of end-users of telecommunications services within New Zealand, the efficiencies that will result, or will be likely to result, from that act or omission must be considered.

(3)

2. We are of the view that the core elements of this purpose statement are that:
 - a. Any action taken by the Commission (or Minister) must promote competition for the long term benefit of consumers; and
 - b. When determining this question, the Commission must consider the efficiencies that would result from any regulation. This implies that Parliament intended that regulation would only be imposed when there was likely to be a net efficiency gain.
3. We consider section 18 therefore provides the following parameters around the introduction of regulation:
 - a. There should not be regulation of markets where there is "*workable and effective*" competition; However,
 - b. If the Commission decides that a service is not subject to competitive constraint, regulation still does not automatically follow. The Commission must be satisfied that regulation will or is likely to promote competition for the long term benefit of end users. Specifically:
 - i. The Commission should be able to show that regulating to constrain market power at the wholesale level is likely to increase competition at some functional level of the telecommunications markets which then results in benefits that will flow into retail markets, where benefits to end-users will be achieved;
 - ii. The Commission must also show that greater efficiency will likely result. The Commission tends to presume that greater competition will lead to greater efficiency, but this is not always the case. The courts have noted (in the merger authorisation context) that if competition already exists, then excluding

further competition may not be serious and can be outweighed by public benefits in economies of scale and other efficiencies; and

- iii. There are costs and potentially chilling effects from imposing regulation that can potentially outweigh the benefits arising from regulation that results in long term harm to end users.

Workable and effective competition:

4. The Commission's Guidelines acknowledge that the word "competition" for the purposes of the Act means "workable and effective competition", as is the case for the Commerce Act .
5. If it is accepted that "workable and effective competition" is the relevant standard by which to judge whether or not to impose regulation and the relevant standard to regulate to it is then necessary to understand what this phrase means
6. Without traversing all the case law from both New Zealand and Australia, our understanding of what workable competition means is as follows:
 - a. "Workable competition" is not the same as "perfect competition", it includes a degree of tolerance from perfect competition outcomes;
 - b. Assessing competition in markets has more dimensions than price alone;
 - c. The only elements that "workable competition" specifically includes are:
 - i. The presence of rivalry between competitors;
 - ii. Some level of constraint on product and service provision and/or the threat of new entry, which constrains participants to act efficiently (although "perfect" efficiency is not required); and
 - iii. Prices in the long run being determined by market forces rather than market power (however the exercise of market power, even for a prolonged period, does not mean competition is unworkable or ineffective and prices may never achieve theoretically ideal efficiency).
7. We would be happy to engage further on these points.

"For the long-term benefit":

8. Even if there is an absence of workable or effective competition in the relevant wholesale market, regulation does not automatically follow. Promoting competition is not an end in itself. The Commission still needs to be satisfied that regulation would promote competition for the long term benefit of end users.
9. The Commission must consider efficiencies when exercising its discretion to determine whether regulation will promote competition for the long term benefit of end users. It appears established that the words used in section 18 imply that dynamic efficiency should be favoured in the event of a conflict with productive and allocative efficiency (static efficiencies).

10. The Commission has indicated that it will favour dynamic efficiency at Paragraph 182 of the Guidelines which states:

"...where a tension arises between the different forms of efficiency, and given the importance of investment in the telecommunications industry, the Commission is likely to give more weight to dynamic efficiency, which is more likely to benefit end-users in the longer term, over static efficiency".

11. This approach is consistent with Parliament's intent. It was noted in the Commerce Committee's report on the Telecommunications Bill that:

"...the use of the words 'long-term' recognises that there may be a need to make short term sacrifices to achieve a long run benefit. Over the long-term, the interests of consumers would be maximised, and therefore the benefits of efficiency are realised."

12. The consequence is that Parliament accepted that higher short term prices can nevertheless be efficient and it is arguable that Parliament expressly recognised that dynamic efficiency was especially important under the Act.

"Of end-users"

13. End users' is a broad class under the Act and should be considered in line with 'consumers' under section 1A of the Commerce Act. The use of "end users" should not be interpreted as requiring the Commission to favour the interests of a distinct class of users as opposed to following a "total consumer welfare" approach.
14. This supports a general contention that to the extent that a regulated outcome simply shifts benefits from one group of customers to another there are no overall benefits to regulation.
15. One exception to this would be where the service is supplied in a two sided market and it can be shown that different end users will respond differently depending on where the benefits fall. In particular if it is likely that some end users will be more likely to exit a market (or not enter a market they would otherwise enter) as a result in a transfer and that all customers could be effected by the reduction in network benefits from the loss of those consumers then a redistribution of wealth would also tip a change in the general efficiency of the market.

"the supply of certain telecommunications services between service providers"

16. This wording confirms that the Part 2 regime is targeted at access bottlenecks, rather than providing a mechanism for regulating every layer of the market.
17. The Commerce Committee stated in its report on the Telecommunications Bill that (at page 8):

*The Commerce Act achieves its intent by promoting competition in general markets, except in cases where competition may not result in net benefit to New Zealand. The intent of the Bill is to maximise long-term benefits to end-users of telecommunications services within New Zealand. **The bill will achieve its intent by regulating bottleneck services so that other telecommunications service providers can***

efficiently access those services. *With the Commerce Act, efficiency criteria are applied in cases where competition may not result in net benefit to New Zealand, consistent with the purpose of the Commerce Act. Under the bill, efficiency criteria will be applied to determine if an action would achieve net benefit to New Zealand.*

18. The implication of this is that the Commission cannot regulate at retail.
19. Another point that discussion of this aspect of section 18 demonstrates is that the Telecommunications Act provides tools for regulating access to bottlenecks coupled with an emphasis on efficiency.
20. We have noted the shift in the Guidelines toward promoting facilities based competition over access-based competition.
21. If there were a shift to greater promotion of facilities based competition, then this would support a scale back of access regulation in order to create incentives for parties to deploy their own infrastructure. We would be happy to discuss this point further.

Requirement to consider efficiencies

22. The requirement to consider the efficiency outcome for any “act” or “omissions” implies that the Commission must always weigh up the relative efficiency benefits of whether to regulate or not regulate when it is presented with these options.
23. When this obligation to consider benefits is combined with the Judgment in the AMPS-A case which found that the Commission must quantify benefits where it can, the provision seems to imply that the Commission must carry out some form of quantitative cost benefit analysis that is particularly focused on efficiency.

Minimising inefficiencies arising from regulation

24. Another point to consider is whether there is any merit in regulating a service, even if it is supplied in a market that is not workably competitive, if the regulated outcome is unlikely to result in any significant uptake by service providers and which is therefore inefficient.
25. To date, Telecom has been required to divert significant resource producing regulated products for which there has been little if any uptake. With the benefit of hindsight, the benefits of regulating these services has not outweighed the costs.
26. One solution going forward may be to only require the regulated party to commence the build of a regulated service, on receipt of orders.

Wealth transfers

27. In its investigation into unbundling the local loop, the Commission stated for the first time that while s 18(2) expressly requires it to consider efficiencies, it does not exclude other relevant considerations which are linked to section 18.⁵⁹
28. In particular, the Commission's view is that it is permitted to take distributive issues into account when making recommendations.⁶⁰ It considers this appropriate where markets suffer limited competition, which is distinct from regulation in the mergers and authorisations context, where competition can normally be relied on to drive the excess profits out.⁶¹ The Commission has essentially followed this approach under the Act since then, which has yet to be tested before the courts.
29. In placing significant weight on wealth transfers, from a legal perspective the Commission must ensure that:
 - a. The consideration is relevant to the purpose under section 18; and
 - b. Giving weight to the consideration does not result in the Commission acting for an improper purpose.
30. As we have noted above, the Act is concerned with regulating arrangements between suppliers to promote competition and then consider that in the context of efficiency considerations. It is therefore questionable whether considerations of transferring wealth to consumers are relevant to section 18. This is illustrated by the difficulties the Commission encounters when trying to determine whether in fact efficiency gains will be passed through to end users. The Part 2 regime was not designed to deal with such issues.
31. The Commission accepts that the focus of the Commerce Act on efficiency means that dead weight loss is an important consideration, whereas wealth transfers between producers and suppliers is less relevant as such a transfer would not add to total welfare. Indeed, it expressly recognises that producer surplus can lead to innovation and new entry which is desirable - an apparent recognition of the value of dynamic efficiency.⁶²
32. The fact that section 18 is analogous to section 1A of the Commerce Act, and therefore wealth transfers are similarly irrelevant, has been argued numerous times before the Commission, by Telecom and others. This follows *Air New Zealand v Commerce Commission*,⁶³ where the High Court agreed that the introduction of section 1A was not intended to disturb the Commission's established practice of treating as neutral any wealth transfers between New Zealand consumers and producers in decisions outside of Part 4.
33. In Telecom's view, following the Court of Appeal's decision in *Powerco*, this remains the strongest argument against wealth transfers under the Act. In the absence of express language to the contrary, such as under Part 4 of the Commerce Act,

⁵⁹ Section 64 Review, at p. 10.

⁶⁰ *ibid.*, at [56].

⁶¹ *ibid.*, at [58].

⁶² *Ibid.*, at [34, 35].

⁶³ (No 6) (2004) 11 TCLR 347.

Parliament's intent was the same for both Acts. The Court of Appeal in *Powerco* said that:

We also accept Mr Weston's submission that, after much litigation over the scope and application of Part 2 (restrictive trade practices), Part 3 (business acquisitions) and the implementation provisions in Part 5, **there is an accepted approach to regulation under the [Commerce] Act which in the main excludes valuation of wealth transfers.**⁶⁴[Emphasis added]

34. The Court of Appeal confirmed the High Court's decision that the position was different under the then Part 4. Wealth transfers were a relevant consideration in implementing the purpose section of Part 4 of the Commerce Act. That was because "s 52 expressly ^{provides} for acquirers."⁶⁵ That is, section 52 was an express statutory direction which meant the section 1A purpose statement did not apply to Part 4. Further:

There is no statutory prohibition upon declaring control where to do so would result in a net economic cost. *The purview of s 52 of the Act does not extend to the economy as a whole. It focuses on one discrete part of the economy, namely acquirers. The Minister is able to declare control if he determines simply that to do so is necessary or desirable in the interests of acquirers.*⁶⁶ [Emphasis added]

35. In contrast, there is a clear direction under section 18 that regulatory action should be efficient. There is nothing in the Act to suggest that Parliament intended to allow the Commission and/or Minister to regulate if it resulted in a net economic cost. Rather, Parliament believed that efficiency criteria would be applied to determine if an action would achieve a net benefit for New Zealand (see the Commerce Committee report on the Telecommunications Bill as cited above);

In amending Part 4 of the Commerce Act, Parliament recognised that it was necessary to expressly direct the Commission on wealth transfers if they were to be appropriately taken into account. In deciding whether to recommend regulation under Part 4 the Commission must, among other things, "quantify material distributional and welfare consequences on suppliers and consumers" (section 52(3)(b) of the Commerce Act). Again, this is an express statutory direction which, in this case, is now consistent with the new Part 4 purpose statement (section 52A), which requires the Commission to prevent excess profits and ensure that efficiency gains are shared with consumers.

36. Requiring an express statutory direction is consistent with the Commission's own guidance (in relation to the Commerce Act):⁶⁷

⁶⁴ *Powerco Ltd v Commerce Commission* [2008] NZCA 289, at [27].

⁶⁵ *ibid.*, at [29].

⁶⁶ *ibid.*, at [36].

⁶⁷ Commerce Commission, *Guidelines to the Analysis of Public Benefits and Detriments*, October 1994 (revised December 1997), at p. 14.

The Act contains no explicit distributional objectives. In these circumstances, the Commission and the Courts should be slow to read them into the Act, especially since the Government has access to, and utilises, social welfare and taxation policy instruments to address distributional issues. Current recommendations by officials are, via amendment to the Act and a s 26 statement, that distributional objectives should be excluded from consideration by the Commission.

37. The distinction between Part 4 and the Act is logical and appropriate when the differing nature of regulation is considered. Under Part 4, price control, which gives the Commission power to directly transfer wealth from suppliers to consumers, is possible. This is one aspect of its role to mimic competition. That should therefore be considered as a benefit when deciding whether to impose regulation. The Commission has no power to directly transfer wealth from service providers to end users under the Telecommunications Act. The only pricing power is to establish efficient prices at the wholesale level. The competitive market then determines what wealth is transferred to end users. Wealth transfers as a potential benefit are therefore irrelevant when deciding whether to impose regulation.
38. The broader legal point is that valuing wealth transfers risks inefficient regulatory decisions. Taking them into account is therefore arguably contrary to Parliament's clear direction under section 18 to promote efficiency.

ANNEX 7 – GETTING THE REGULATORY SETTINGS RIGHT: QUESTIONS THE COMMISSION SHOULD ASK STAKEHOLDERS AND CONSUMERS

- 1 How successful is the New Zealand telecoms sector currently in delivering benefits to citizens and consumers?
- 2 How rapidly and extensively will fixed and mobile networks become substitutes for one another?
- 3 What impact will Voice over IP have on the telecoms market?
- 4 How rapidly and extensively will broadband be taken up in New Zealand, and what are the regulatory implications of such growth?
- 5 What scope is there for new, competing broadband platforms to be rolled out, and which technologies are most likely to be used?
- 6 When are operators likely to move towards 'all IP' architectures, if at all?
- 7 What are the implications of 'all IP' networks for the way networks interconnect with one another, and for the scope of competition?
- 8 Is there likely to be widespread demand for services that require 'broaderband' networks to be rolled out and, if so, how will such infrastructure be supplied?
- 9 How rapidly are broadband content businesses likely to emerge, and what factors will affect their viability?
- 10 How will future network evolution, such as growth of intelligence at the edge of networks, and the increased importance of control over technical standards and interfaces, affect the requirements of telecoms regulation?
- 11 Will it become uneconomic for operators to maintain the existing circuit-switched architecture at some point and, if so, when? What regulatory issues will this transition to IP networks raise?
- 12 Are consolidation, alliances, market entry or other forms of market evolution likely? What will their implications be for telecoms regulation?
- 13 What impact do different regulatory approaches have on investment decisions in telecoms, and what regulatory approaches does this imply that the Commission should adopt?
- 14 What is the right role for consumer policy? What impact do different approaches have on telecoms companies' perceptions of risk and return?
- 15 What role should the Commission take in signposting, providing, or ensuring that the market provides clear information to consumers, enabling them to make effective choices?
- 16 How may universal service arrangements need to evolve in response to changes in the telecoms market?