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BY EMAIL

Dear Anthony

Mobile termination proceedings – Response to TelstraClear letter regarding call origination service

We refer to the issues paper “*Telecommunications Act 2001: Schedule 3 Investigation into Regulation of Mobile Termination*” released in June 2004 (the **Issues Paper**) by the Commerce Commission (the **Commission**), where the Commission made reference to a request by TelstraClear Limited (**TelstraClear**) to expand the Commission’s current investigation into mobile termination to include certain mobile call origination services. The Commission suggested that parties comment on TelstraClear’s request. As Vodafone noted in its submission on the Issues Paper, Vodafone is responding separately to the TelstraClear request in this letter.

The requests from TelstraClear are contained in a letter from TelstraClear to the Commission dated 8 June 2004 (the **TelstraClear letter**). We discuss how the claims made in the TelstraClear letter are inaccurate, and how there is no justification for the Commission to expand its current investigation to cover certain mobile call origination services.

Vodafone notes that it is not making this response in the context of the Commission’s investigation into mobile termination. The information contained in this letter is provided in order to outline Vodafone’s views on the points raised by TelstraClear and to aid the Commission in its understanding of the issue.

Mobile calls to free-phone numbers on fixed networks

A call origination service at an interconnection level is currently provided by Vodafone to carriers with free-phone customers on their networks. The service involves originating a mobile call to a free-phone number and handing it over to another carrier (normally a fixed network operator). This is a standard service for Vodafone and we are happy to provide it to other interconnecting carriers.

The distinguishing feature of this type of service is that the terminating network (with the free-phone customer) pays the mobile network operator for originating that call,

with the mobile network operator currently agreeing to make that call available at no charge to its customer (the calling party).

Vodafone's position

Vodafone's position in relation to the assertions in the TelstraClear letter is as follows:

- Vodafone does not believe there is any justification for investigating the origination of calls to free-phone numbers, and we set out our reasons for this below; and
- There is no current retail offering for a "50XY" service and therefore it is premature to investigate the regulation of this service, as discussed below.

Accordingly, Vodafone believes the Commission should decline to investigate the matters in the TelstraClear letter.

Mutually beneficial relationship with terminating operators

It is very important, when considering the call origination service, to understand the commercial reality of the manner in which calls from mobiles to free-phone numbers are produced by both the mobile network operator and the other operator. In fact, Vodafone has strong incentives to maintain competitive provision of its call origination service.

The commercial reality is that the originating and terminating operators involved in a mobile call to a free-phone number are equally reliant on each other, and as such both have incentives to the same degree to ensure that they provide competitive offerings to one another.

Both operators provide a service that the other uses, along with other services, to produce a retail service. The provision of retail end-to-end mobile calls to free-phone numbers is mutually beneficial for Vodafone and the relevant other network operator.

Vodafone considers that a decrease in demand for its origination service could occur in either or both of two broad ways:

- any increase in origination costs is likely to be passed on by the other operator to its free-phone customer. Free-phone customers on other networks could request their network operator to bar all calls from the Vodafone network. This would in turn decrease the demand for Vodafone's origination service; or
- the other network operator itself could cease purchasing origination services from Vodafone outright, for example if there was a sufficient decrease in demand by free-phone customers for calls from the Vodafone network.

Clearly, any reduction in demand for our origination service would not be in Vodafone's interests. In addition to the obvious reduction in wholesale revenue, we believe our customers would become frustrated that they could not make calls to certain free-phone numbers. Consequently, Vodafone would be less able to compete in the mobile services market.

Discussion of mobile calls to free-phone numbers

TelstraClear asserts that similar concerns arise about the exercise of market power in the origination context, as do in the termination context. TelstraClear go on to say that where origination is used as an input to providing access to an end service, mobile operators have an incentive to overprice origination charges.

We do not believe these assertions are correct, for the reasons set out in this letter.

We believe that Vodafone has an incentive to provide a free-phone calling service as it is beneficial to Vodafone for our customers to be able to call free-phone numbers.

Not an essential input

TelstraClear say that mobile operators have control over access to an essential input in the provision of a telecommunications service, and this control gives them the ability to raise the price of the mobile origination service above competitive levels.

It is not accurate to characterise the origination service as an essential input into the provision of telecommunications services in the “downstream markets for special (origination access based) services”.

The origination service is not an essential input. For an input to be “essential”, there must be no way that the downstream service could possibly be supplied without that input being used.

Call origination is no more an essential input then the termination leg of the call, and there is a mutual dependency. If Telecom or TelstraClear refused to connect free-phone calls made by Vodafone customers this would have a detrimental impact on Vodafone and our customers.

Another network operator can still provide a free-phone service to its customers without using the origination service from Vodafone. The other operator’s free-phone customers can still receive calls from callers on the same network, and callers on the other fixed and mobile networks. As such, Vodafone’s origination service is not essential in any sense of the word.

This view is supported by the fact that a number of 0800 customers in New Zealand have specifically disallowed calls from mobile networks to their numbers. We believe the fact that these customers are willing to disallow calls from mobile networks, and still receive calls from fixed networks, is clear evidence that Vodafone’s origination service is not “essential” in order for other operators to provide a downstream free-phone service to their customers. Indeed, it appears many of these customers do not want the use of Vodafone’s origination service.

As such, it is not imperative for other operators to purchase call origination services from Vodafone. Indeed a failure to provide calls to free-phone numbers would have a detrimental impact on Vodafone’s ability to compete in the mobile services market.

Vodafone is constrained by customer expectations

Therefore, it is apparent that Vodafone is constrained in its ability to deny, or set unreasonable terms and conditions for, access to its origination service for calls to free-phone numbers by the expectation of our subscribers that they can make calls from their mobile phones to free-phone numbers in New Zealand.

Our subscribers have been able to use their mobiles to call free-phone numbers for a number of years now. This forms part of their expectation to be able to call any number in New Zealand from their mobile phone. Failing to fulfil this expectation would be a significant concern to our customers.

No evidence of limited competition or market failure

We also note that, despite the claims in the TelstraClear letter, there has been no evidence produced to suggest that there is limited competition, much less a market failure, in any market for call origination to free-phone numbers.

TelstraClear's reference to the suggestion made by the ACCC in its draft Mobile Services Review reports that origination rates were equal to or less than termination rates, is an inaccurate comparison. It does not compare "apples with apples", and can easily be explained.

In Australia, mobile network operators charge their own customers for making calls to 1800 numbers. As such, Australian mobile network operators earn part of their origination revenue from their customer, and the balance from the terminating fixed network operator. In this situation, it is not surprising that the origination rate is lower than the termination rate because the mobile operators are earning the balance of their revenue directly from their own subscribers.

For calls to 13/1300 numbers no origination charge is levied on the 13/1300 operators, in fact, a termination charge is paid.

In both cases the mobile operator sets the retail price for its customers to call 1800 and 13/1300 numbers.

The commercial arrangements are different in New Zealand. We do not currently charge our customers for making calls to free-phone numbers.

Given the entirely different commercial arrangements, it is not accurate to make a simple comparison between the rates in New Zealand and Australia as TelstraClear has done.

ACCC has recently decided not to continue regulation of mobile origination services

Just recently, the ACCC (in its final Mobile Services Review – Call Origination report of June 2004) concluded that it would not be in the long-term interests of end-users to continue declaration of a mobile originating access service (**MOAS**).

The ACCC had not received evidence to suggest that mobile network operators were taking advantage of their relationship with the mobile customer to set unreasonably

high prices for the MOAS, and the ACCC also noted the commercial incentives on mobile operators and fixed operators to interconnect with one another.

Contrary to TelstraClear's assertions, both of these considerations also hold true in New Zealand.

There are certain differences in the charging for free-phone type calls between New Zealand and Australia, as discussed above, however we emphasise that the ACCC's final decision was not dependent on the unique Australian features.

The ACCC decided not to continue regulation of mobile origination primarily because the commercial incentives to provide the services competitively were sufficient, and there was no evidence of market failure at the retail level. While Vodafone disagrees with much of the ACCC's reasoning in their Final Decision, we do agree that there is no evidence of problem to be addressed by continued regulation. The commercial incentives are the same in New Zealand, as discussed in this letter, and the lack of evidence also holds true in New Zealand.

Comments made by TelstraClear

TelstraClear notes that "the Australian mobile market has more players than the New Zealand market and the environment is therefore more competitive"¹. TelstraClear's assessment of competition in this regard is both simplistic and wrong. Vodafone has presented information to the Commission that demonstrates that competition in the New Zealand mobiles market is alive and well. The number of players in a market does not reflect the level of competition in that market.

TelstraClear also notes that "mobile origination access services for calls to toll-free and local rate services have been subject to regulation in Australia since 1997 and the competitive market may be further developed as a result"². Vodafone notes that call origination has only been notionally subject to regulation in Australia and pricing principles for the service were not set. Regulation has never been applied in Australia with respect to call origination.

Regulating termination and not origination would not cause problems

While we hold the position that there is no justification to regulate mobile termination services, we need to address a final point in the TelstraClear letter. TelstraClear say that they are concerned about the potential impacts on the market of a decision to regulate termination rates without also regulating origination rates. We can not see how there would be any potential impacts on the market if the Commission took this course.

Competition in downstream markets

TelstraClear assert that regulation of mobile origination rates would promote greater competition in downstream markets – presumably the market for free-phone number services.

¹ TelstraClear letter to the Commission, 8 Jun 2004, Mobile Termination: Origination Access Services
² Ibid

In our view there is not a distinct product market for free-phone services. These services are sold as part of a larger bundle, or cluster, of services. It is virtually impossible to conceive of what a hypothetical monopolist of free-phone service would look like. Presumably such a firm would need to control both of the main fixed-line networks, which would seem impossible for all practical purposes.

We have provided extensive analysis why the regulation of upstream mobile termination rates would not promote competition in any downstream retail markets in our submissions on the Issues Paper. Similar arguments are relevant in this context.

Further, when an operator provides free-phone number services to customers on its network, it is offering the ability to terminate calls from a wide range of networks, fixed and mobile. As mentioned above, Vodafone's mobile origination service is not an essential input into the free-phone number services of other interconnecting operators.

50XY calls

There is currently no retail offering of a mobile "50XY" service in New Zealand. Our understanding of "50XY" services is that they are services where the cost of a call may be divided between the caller and the called party.

Importantly, we believe that there is no evidence of market failure in the provision of mobile "50XY" services. The market has not yet even been created, nor had an opportunity to develop. It is premature to consider regulating any "50XY" service at this point in time.

TelstraClear's only reasoning for arguing "50XY" should be investigated is that it has encountered some difficulties in the past in negotiating a "50XY" fixed originating service. Vodafone respectfully rejects this reasoning and notes that Vodafone does not operate a fixed network.

Conclusion

In conclusion, we believe that the claims in the TelstraClear letter are unfounded and inaccurate. There are no reasonable grounds to investigate origination services offered by mobile operators in New Zealand.

We also reiterate that we do not even offer a "50XY" service as yet and as such it would be premature to investigate.

We again summarise our key points:

- Vodafone already provides a commercially negotiated origination service to other network operators;
- Vodafone's origination service is not an essential input in the provision of retail mobile calls to free-phone numbers, so Vodafone does not have the ability to set prices at anti-competitive levels;
- in commercial reality, Vodafone and the other network operator derive mutual benefit from the provision of retail mobile calls to free-phone numbers and Vodafone is incentivised to offer the origination service competitively;

- Vodafone is constrained in how it provides the origination service to other network operators by the expectation of our subscribers to be able to make calls to free-phone numbers;
- there has been no evidence produced to suggest that there is limited competition, or market failure, in any market for call origination to free-phone numbers;
- the ACCC has recently concluded that mobile call origination services to free-phone numbers should not be subject to regulation; and
- regulatory Intervention on call origination cannot be considered in isolation from changes to retail pricing structures that would become necessary.

Please contact the writer if you have any further queries or questions in relation to Vodafone's position on this issue.

Yours sincerely

Vodafone New Zealand Limited

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