

22 December 2008

By email:

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Paula Rebstock – Chair
Osmond Borthwick – Director, Telecommunications Branch
Commerce Commission
PO Box 2351
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Mobile Termination Access Services (13.6/J10310): Voluntary undertaking

Dear Paula & Osmond

NZ Communications submits the attached voluntary undertaking in regard to Mobile to Mobile (MTM) call termination under Clause 15 of Schedule 3A of the Act.

In preparing this undertaking, we took 3 key factors into account:

1. Regulation is required – as noted in the 2008 BIM to the Minister¹:

“While the number of mobile phone subscribers in New Zealand is higher than the OECD average (6th out of 24 countries) mobile prices are very high by international standards (low and medium user plans are 25th or worse out of 30 OECD countries). Further investment - primarily through the entry of a third mobile network operator to the New Zealand market – would increase competition and put downward pressure on pricing.

The Commerce Commission announced on 6 November 2008 that it has launched a Schedule 3 investigation into whether to regulate mobile termination rates (including mobile-to-mobile voice termination, fixed-to-mobile termination and SMS termination). The outcome of this investigation may help determine the speed at which a third operator is likely to enter the market”.

2. Internationally, many regulated mobile termination rates (MTRs) have been recognised as being excessively high and there is strong downward momentum on MTRs to significantly lower rates and/or apply BAK; and
3. The significant costs of determining & monitoring regulated prices, including the potential for gaming, which will inevitably delay (possibly prevent) the realisation of long term benefit for consumers.

¹ Briefing for Incoming Minister (para 28 & 29)

The Commission will recall that our 5 September submission² discussed the merits of a BAK regime and the harm that other regimes would have on competition³. We submitted that BAK is the quickest, most efficient means of removing these distortions.⁴ We referred to international literature, including the work of *David Harbord* who concluded that BAK would:

“...likely result in a more efficient wholesale and retail price structure, help to eliminate barriers to entry caused by “tariff mediated” network effects, and increase welfare and competition in the mobile market”

With those factors in mind, we commissioned an independent report from Concept Economics on the most appropriate means of regulation for New Zealand (copy attached). Concept Economics concluded that:

“...BAK is the approach most likely to promote efficient competition for the long-term benefit of end-users in New Zealand”

BAK presents the lowest cost option that prevents competitive and market entry distortions and addresses the harm that high MTRs present (without the downside of setting non-optimal MTRs).

BAK matches current trends in the international MTR market and reflects the existing position in countries such as US, Singapore, Canada and Hong Kong where BAK or near zero MTRs have resulted in some of the highest utility levels, lowest prices and greatest competition for mobile services in the world.

There is no real downside in adopting BAK yet considerable upside.

Accordingly, the undertaking would amend the existing interconnection agreements we have with the incumbent mobile operators to provide for a BAK model as quickly as possible. There is significant New Zealand precedent for BAK and this undertaking is consistent with the terms Vodafone sought (and obtained) from the Commission in its *Homezone* interconnection application, the amended agreements would be on a BAK basis and provide for non-discrimination in retail pricing. This would address the harm that on-net / off-net retail pricing differentials present to ensuring efficient competition^{5 6}.

² NZ Communications detailed response on the Commerce Commission's Mobile Termination Issues Paper

³ Namely; (1) Increased incentives for incumbents to enable closed network pricing, creating/enhancing entry/expansion barriers. (2) Lead to significant financial transfers from small to large operators, (3) Lead to high retail prices, (4) Lead to low utilisation of mobile services reduce consumer choice, benefits of dynamic competition and delay the introduction of new services.

⁴ It is consistent with optimal termination rates as described in a number of recent academic studies. It moves away from the flawed assumption that only the call initiator benefits from the call and takes into account positive call externalities. It results in operators recovering costs from their own customers rather than competitors (thus encouraging efficiency).

⁵ As identified by Vodafone (accepted by the Commission) that: “ *If Telecom can require callers to Vodafone local numbers to pay higher rates than callers to other local numbers, there could be a significant disincentive to take up Vodafone's local service*”

⁶ NZ Communications addresses the anti-competitive outcomes of on-net discounting in this Voluntary Undertaking by making it a condition that under wholesale Bill & Keep, no NZ Communications retail customer will pay more to make calls or messages to either Telecom or Vodafone mobile customers and vice versa, so for example; Vodafone text 2000 customers would be able to text NZ Communication's customers as part of their package and Telecom's 'favourites' would not be restricted to having to nominate another Telecom customer as a 'favourite' and the offer (if continued) would be extended to include calls to an NZ Communication's customer.

NZ Communications firmly believe that moving swiftly to a BAK regime for Mobile to Mobile calling in New Zealand would provide maximum long term benefit to end users in the shortest possible timeframe. I will make myself available to discuss the merits of such a regime at the Commission's request.

Yours sincerely



Bill McCabe
Chief Commercial Officer