

Submission on Domestic ICAs for Kordia, Woosh, and CallPlus – Public version (there is an AP version)

20August 2009

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1. Introduction

- 1.1 This submission deals only with the Vodafone/2Degrees ICA (the ICA), except in the final paragraph.
- 1.2 [] **VNZAPI/2DAPI** further demonstrates my clients' submission that there is a severe market failure calling for robust regulatory action. In addition to on/off net price considerations combined with high MTM rates, there is a further regulatory distortion: [] **VNZAPI/2DAPI** – with the consequences for wider telecommunications services and end users generally, noted already.
- 1.3 In view of this, and earlier submissions, a pragmatic way forward is suggested – at the end of this submission- to enable both
 - (a) an expedited process for the draft report. and
 - (b) sufficiently thorough review of pricing and other options.
- 1.4 In this submission, as before in submissions by Kordia, CallPlus and Woosh, references to TSLRIC are to the model under Schedule 1, and references to EU LRIC are to the model under the EU Recommendation (described as LRMC by Ofcom)

2. Key terms in the Vodafone/2degrees ICA

Disclosure by Vodafone in its submissions

- 2.1 To enable as much of this submission to be in a Public Version, I first refer to what is in Vodafone submissions. Then I deal with the ICA itself.
- 2.2 Implicit in Vodafone's submissions on the draft report is that the MTM and SMS rates are commercially agreed between Vodafone and 2degrees []¹
VNZAPI/2DAPI
- 2.3 Vodafone in its submissions on the Draft Report states:

2degrees has a secret deal that has terms far more favourable than those set out in our undertaking

248. The only expected new network operator in New Zealand in the foreseeable future is 2degrees. The prices it will face for MTM voice termination on Vodafone's network do not match those set out in the MTM voice undertaking provided by Vodafone during this investigation.

249. As the Commission would know, the prices contained in the interconnection agreement reached between Vodafone and 2degrees in September last year involve 2degrees paying a price for MTM voice termination on Vodafone's network of [] **VNZAPI**. This price is almost [] **VNZAPI** per cent [] **VNZAPI** the prices contained in Vodafone's MTM voice undertaking (and is even more favourable once [] **VNZAPI** are taken into account). Further, under the terms of the interconnection agreement, Vodafone will pay 2degrees [] **VNZAPI** rates to terminate traffic on its network in accordance with the [] **VNZAPI**. The [] **VNZAPI** terms contained in the undertaking represent a level of [] **VNZAPI** for 2degrees' entry into the market beyond that implied by the rates it will pay to terminate traffic on our network.

- 2.4 In addition, those Vodafone submissions note commercial agreement as to SMS termination between Vodafone and 2degrees.²

The Vodafone/2degrees ICA

- 2.5 MTM calls from the 2degrees network are [] **VNZAPI/2DAPI**
- 2.6 SMS [] **VNZAPI/2DAPI**
- 2.7 The agreement ends in [] **VNZAPI/2DAPI**

3. Immediate impact of changes

- 3.1 The improved MTM and SMS rates in favour of 2Degrees, whether or not this is efficient pricing (and on my client's submission it is not), do not solve the key problem associated with on/off net pricing. The examples and modelling by Concept, reworked with this data and taking into account the [] **VNZAPI/2DAPI** rates, would demonstrate this. So would other modelling and

¹ [] **VNZAPI/2DAPI**

² Para 384 Vodafone Submissions on draft Report dated 28 July 2009

examples. The fundamental problem is not taken away. In turn, this retains the wider consequences for the market, including the effects beyond mobile services, into fixed and NGN investment.

- 3.2 [] VNZAPI/2DAPI The difference also further fuels, in a substantial way, the market failure already identified which has substantial implications for the NGN and fixed line (and therefore end users). [] VNZAPI/2DAPI

4. Use of private agreements is unsatisfactory

- 4.1 The terms of the agreement and other developments reinforce my clients' submission that the use of confidential ICAs is unsatisfactory. The following is additional to those points.

Not knowing what questions to raise and deal with

- 4.2 There are the general objections to use of undisclosed information in ICAs in that the data cannot be tested by others. What particularly comes out here is that other parties don't know what questions to raise. [] VNZAPI/2DAPI What is emerging so strongly is that the issue is not just about rates per se. It is also about wider impacts including the severe market distortions caused by on/off net pricing and, now, the further distortions caused by [] VNZAPI/2DAPI
- 4.3 I can now see, with the benefit of having seen the ICA, that a little of this can be deduced from the Vodafone submissions. But I did not detect this earlier. I did not appreciate the fundamental point, for example, [] VNZAPI/2DAPI As noted above, and below, this has substantial implications for telecommunications services beyond mobile services.
- 4.4 Consideration of these issues does not emerge from the draft Commission report. We therefore welcome the Commission's decision to make the ICAs available.

The agreement ends in [] VNZAPI/2DAPI

- 4.5 As the Commission notes, regulated rates apply from 2011. The period under review is until 2016.
- 4.6 The agreement ends in [] VNZAPI/2DAPI It is difficult to see how an agreement with material application for only [] VNZAPI/2DAPI % of the period (at most) can be used as part of the counterfactual.

5. No other access seeker will agree the same terms

- 5.1 In its submissions, Vodafone has selectively released limited information about what it describes as the "secret deal". The implication is that this is a positive deal, available to others.
- 5.2 Releasing some information in this way, in Vodafone submissions, is a matter, in terms of confidentiality issues, for the Commission, Vodafone, and 2Degrees. From what I now know, and noting I cannot get my clients' instructions, the overall situation appears decidedly unusual and unsatisfactory, as I further develop

- 5.3 The impression given does not at all reflect, stating it as favourably as possible from Vodafone's perspective, the underlying reality. Public readers do not see for example [] VNZAPI/2DAPI
- 5.4 However, of particular concern is the statement that this is an agreement available to others on the same terms.
- 5.5 Vodafone knows for certain that no other operator will agree to these terms:
- (a) No fixed line operator will agree to it [] VNZAPI/2DAPI
 - (b) While other MNOs are possible before 2016, [] VNZAPI/2DAPI. So an MNO would not enter these terms.
- 5.6 Again, stating this as favourably as possible from Vodafone's perspective, an incomplete picture is made public.

6. Why isn't this "Secret Deal" in a draft undertaking?

- 6.1 Vodafone has chosen to make a thing of this "secret deal", with:
- (a) selective release of information;
 - (b) Highlighting that 2Degrees is keeping it secret, with the adverse public implications to be inferred from that.
- 6.2 This is clearly a tactical choice aimed at some sort of tactical outcome. That is apparent because Vodafone, instead, could have chosen to include the terms of the ICA in a draft Undertaking. Before trumpeting the 'secret deal', and with no reference to the secret deal, it could have produced an undertaking on similar terms. Confidentiality obligations to 2Degrees did not preclude that.
- 6.3 Instead the draft undertakings have [] VNZAPI/2DAPI onerous terms from the perspective of access seekers.
- 6.4 [] VNZAPI/2DAPI
- 6.5 [] VNZAPI/2DAPI, and the Vodafone trumpeting of the "secret deal", raises questions about their motive.
- 6.6 Vodafone appears to be attempting to play stakeholders, including the Commission. Vodafone appears to be endeavouring to drag the Commission into these tactics. Fortunately the Commission has, however, made the ICAs available so that parties can submit [] VNZAPI/2DAPI
- 6.7 Now we have the messy business about the leak.
- 6.8 Parties have a clear and public way to introduce a counterfactual: draft undertakings. (This is quite different to a clearance situation which involves only a few parties). In light of that, and in light of submissions in this submission, and earlier, the ICA, for the counterfactual analysis, should be disregarded.

7. What might the Commission do about this?

- 7.1 Stating it at its most favourable from Vodafone's perspective, the public and stakeholders are presented with a picture that does not tell the whole story but shines a glow on Vodafone. Those stakeholders potentially include the Minister, at the likely time when Ministerial undertakings are considered.
- 7.2 We suggest that the Commission look to make a statement about this to clarify the position so far as possible, consistent with confidentiality. This matter could be discussed, if it assists, with Nominated Counsel who have AP clearance.

8. The value of the ICA: highlighting substantial regulatory distortion

- 8.1 While the ICA cannot be used, my clients submit, in the counterfactual analysis, it can be used to show the problems with setting the rates too high, and the allied problems of bundling and on/off net pricing, etc.
- 8.2 As Telecom and our clients note, FTM and MTM rates need to be linked. The regulated rates should be the same.
- 8.3 However, that of course does not stop parties from agreeing rates commercially, provided, where the service is regulated, the price and non-price terms are no less favourable than the terms of the determination or registered undertaking.
- 8.4 That's subject to compliance with the Commerce Act. However, that legislation is close to irrelevant due to its limited application and the several years to achieve outcomes. It is useful to note in this regard that Ofcom came to a similar view even in relation to the more intrusive EU- based ex post regime in the UK. See its May Mobile Termination consultation paper at Paras 6.88 to 6.91.
- 8.5 What the ICA demonstrates is that such commercial agreements can create severe regulatory distortions if the regulated price for a related service is set too high. In this instance, if the regulated price for FTM is set too high (for this service over which MNOs have a monopoly), MNOs can gain substantial benefit
- 8.6 MNOs, individually or collectively, can benefit from []VNZAPI/2DAPI using off/on net strategies and the like against FNOs.
- 8.7 For example, the outcome will be increased substitution of mobile phones for fixed caused by the regulatory distortion. In this example, which can apply in other ways, the regulated price (FTM or FTM/MTM) is set too high, enabling MNOs to agree terms that undercut FNOs in the marketplace.
- 8.8 Having fixed to mobile substitution driven by genuine efficiencies is one thing. Having substitution driven by regulatory distortion is quite another.
- 8.9 All this highlights the importance of the Commission taking robust action in light of the severe market conditions and that a so-called "conservative" approach will not sort the market failure. The Commission now has clear evidence of what can happen in the mix of regulatory action and commercial agreements. The commercial agreements cannot be stopped (they may be "efficient" agreements but the Commerce Act will not stop them anyway): the key challenge is to get the right regulatory settings to reduce the potential problems.

9. A pragmatic solution

- 9.1 All this further highlights the importance of getting the right settings in place including as to the pricing model (e.g. TSLRIC, EU's LRIC,, etc) and the application of those models (on which the BT submission on Ofcom's May 2009 consultation provides useful insights).
- 9.2 The May 2009 MCT Ofcom paper³ is insightful on the benefits of the EU LRIC model in relation to problems between fixed and mobile, identified by this ICA. Such pricing (called LRMC by Ofcom):

“would reduce the absolute difference between fixed and mobile termination rates. This would be consistent with the anticipated general travel over the longer term and provide industry greater flexibility to adapt to ongoing market developments (e.g. fixed/mobile convergence....

....It would also remove potential concerns about competitive distortions between fixed and mobile operators that are related to common cost recovery...

.....It would most likely to lead to a reduction, if not elimination, of the on/off net differential in mobile cal charges, addressing any potential concerns about competitive distortions between mobile operators...”

A workable solution

- 9.3 While my client seeks a review of pricing methodology options in the investigation (as noted in earlier submissions), it is recognised that this will delay the investigation.
- 9.4 As a pragmatic solution, an option is suggested which achieves both:
- (a) Expedition; and
 - (b) Review of price methodology options.
- 9.5 The Commission's draft pricing principles allow consideration of the options of TSLRIC and BAK. We propose that the Commission add the option of consideration of the EU LRIC option as well. Ideally mandated reciprocity is included, recognising that CBC is unlikely in the near term. It is easy enough to frame short wording around these options.
- 9.6 This also has the benefit of alerting the parties, and the Minister, to the possibility of, for example, an EU LRIC outcome, during the likely negotiations for Ministerial undertakings.

10. [] VNZAPI/2DAPI

10.1 [] VNZAPI/2DAPI

11. International ICAs

11.1 [] TNZAPI/VNZAPI.

³ At Para 6.114

11.2 In any event they are, as already submitted, material to termination of internationally originated calls.