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Copy sent to Paula

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Dear Paula

2009 COMMISSION WORK PROGRAMME

As I am sure you will agree, 2008 proved to be a watershed for telecommunications in New Zealand, and in particular for the regulatory environment. The level of regulatory change achieved in the calendar year was significant, with Operational Separation, local loop unbundling and the unbundled bitstream suite of products all introduced.

Looking ahead to the introduction of sub-loop unbundling, the Commission's MTR and STD Review processes, and the Government's ultra-fast broadband commitments, there is no doubt that 2009 will prove to be just as pivotal in determining the direction of telecommunications markets.

In the face of all of this change, it will become increasingly important that care is taken to ensure the regulatory regime as a whole remains consistent, transparent, and efficient. Regulation must not impose or maintain burdens that have become unnecessary, and new regulation must not be layered upon old without review of the continued appropriateness of old regulation.

Particularly in the current climate, it will be critical for the Commission to take a proactive lead in assessing opportunities for de-regulation and/or consolidation of regulation. The Commission must give confidence to the market and to investors that it will act quickly to wind-back regulation where it is no longer needed. Accordingly, I set out below several areas where Telecom considers immediate Commission action is required.

I am conscious that the Commission has a busy work programme planned for 2009, but continued review of regulatory settings, and de-regulation wherever appropriate, as soon as appropriate, are two critical foundations of any best practice regulatory regime, and accordingly, it is imperative that the Commission demonstrates the application of these principles in its management of the New Zealand regulatory regime.

Removal of Resale Regulation

Telecom is firmly of the view that the current co-existence of regulated input services (the UCLL and UBA families) with regulated resale services is inefficient and an unnecessary burden on Telecom, the industry and end-users.

We believe the conditions exist today to warrant the removal of some or all resale regulations, and request that the Commission commence an investigation, starting immediately, into whether the following Designated Access Services should be omitted from Part 2 of Schedule 1 of the Telecommunications Act 2001 (the **Act**):

- Retail services offered by means of Telecom's fixed telecommunications network;
- Residential local access and calling services offered by means of Telecom's fixed telecommunications network;
- Bundle of retail services offered by means of Telecom's fixed telecommunications network; and
- Retail services offered by means of Telecom's fixed telecommunications network as part of a bundle of retail services.

The Commission has previously signalled, but not taken any action on, such an investigation. This matter has not to date achieved sufficient priority in the Commission's work programme. It is now time to accord it that priority, and to acknowledge that the steps Telecom is taking to advance the competitive landscape in New Zealand, by providing a level playing field at the wholesale UCLL and bitstream levels, mean investigation of the roll-back of regulation in upstream retail markets is warranted. Strong, timely de-regulatory action by the Commission is just as fundamental to a well functioning regulatory regime as decisive regulation, and this needs to be evidenced in New Zealand.

Resale has been a regulated service since 2001, yet in all that time, only one category of resale service – access – has achieved reasonable uptake by wholesale customers. Telecom's resold broadband service, for example, accounts for less than 1% of Telecom's total retail and wholesale broadband connections.

In contrast, the costs to Telecom of maintaining regulated resale services are very real. The requirement to continue to support and build resale variants of existing and new/replacement retail services, for example, causes significant systems development costs for Telecom. Telecom's One Office resale services, for example, cost over \$850,000 to develop, and are currently used by less than 100 end customers. Just to undertake the quarterly audits of Telecom's resale Designated Service and Regulated Service Price Lists ("DSPL" and "RSPL" respectively) costs over \$150,000 per annum and these lists require two full time employees to maintain.

The continued regulation of these services is unwarranted and should accordingly be reviewed at the earliest opportunity.

Review of the Date of Application for the UBA and UBA Backhaul Competition Tests

As it is currently drafted, the Act does not permit the application of a competition test as a condition for the supply of the regulated UBA and UBA Backhaul services until 18 December 2009. This effectively requires Telecom to provide regulated bitstream access services at regulated prices, in parts of its network which are manifestly competitive, until the end of this year at the earliest. This is clearly an unnecessary burden and cost, and inconsistent with best practice regulation.

In a letter to interested parties to the UCLL and UBA Backhaul STDs, the Commission appeared to acknowledge this view, and advised that it was considering whether reasonable grounds existed to commence an investigation into whether the conditions applicable to the UBA Backhaul designated access service in the Act should be amended to include a competition assessment which would apply at a date earlier than 18 December 2009.

The Commission did not at that time go on to commence that investigation, but Telecom considers compelling grounds exist today for such an investigation, covering both the UBA Backhaul designated access service and the UBA designated access service. There is ample evidence to support the proposition that the absence of a competition test today is forcing regulation on Telecom, and the industry, in competitive markets:

UBA

- Telecom continues to consider that discrete wholesale markets for the supply of bitstream access services exist at a sub-national level and that this is the appropriate approach to defining the geographic dimension of the wholesale bitstream access market. When the Commission last undertook competition assessments in the wholesale market for bitstream access at a sub-national level (in 2003), it found that Telecom faced more than limited competition in the wholesale market for bitstream access in five CBD ESAs Auckland Central (AKCEN), Mt Wellington (MWN), Manukau City (MKY), Courtenay Place (CPC), and Wellington (WN)).¹ The Commission has also previously made the same determination in respect of the upstream retail broadband markets in networked metropolitan areas within Wellington and Christchurch.²
- Since these findings, competition in these markets has increased markedly. For example, both Vodafone and Orcon have launched, and announced aggressive plans for expansion of, their LLU-based services in the wider Auckland metropolitan area, and Telecom Wholesale has introduced loyalty discounts for wholesale services provided to end users within 48 urban Auckland exchanges. As at 31 December 2008, LLU uptake had grown to over 25,000 lines.

UBA Backhaul

- The Commission has also recently found that Telecom faces more than limited competition on 55 out of 75 UCLL Backhaul Primary Links and 13 out of 29 UCLL Secondary Backhaul Links. Given UBA Backhaul services are provided over these same routes, if a competition test were applied to that service today, the same competition finding would apply for UBA Backhaul links. Chorus further considers that since the date of the Commission's UCLL Backhaul competition assessment, a further 7 primary links have become competitive.

Continued regulation of Telecom in these markets or on these routes is inefficient and contrary to best practice regulation. Accordingly, Telecom requests that the Commission launch a Schedule 3 investigation into amendment of the conditions applicable to these Designated Access Services to enable the application of a competition test as soon as possible. Since the Commission does not need, for the purposes of such an investigation, to complete a full competition assessment, Telecom anticipates such an investigation could be completed in a relatively short period of time.

Preparation of Core Regulatory Operating Principles

Finally, Telecom also requests that the Commission consider commencing a formal consultation on a set of core regulatory operating principles.

¹ Section 64 Review and Schedule 3 Investigation into Unbundling the Local Loop Network and the Fixed Public Data Network, Final Report, Commerce Commission, December 2003, Table 5.3.

² Decision 497, Determination on the TelstraClear Application for Determination for "Wholesale" Designated Access Services, Commerce Commission, May 2003, para xi.

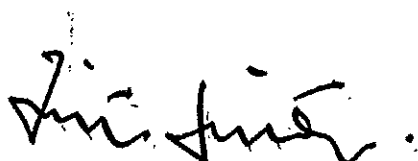
In the United Kingdom, Ofcom states that it considers it has a "general duty to be de-regulatory",³ and operates under a number of clearly stated regulatory principles, which include the following:

- A legislated requirement to minimise regulatory burdens;⁴
- A bias against intervention;⁵
- A requirement to "Always seek the least intrusive remedy";⁶ and
- A requirement to withdraw from upstream regulation as soon as conditions at other levels allow.⁷

Ofcom also publishes a Simplification Plan, which is intended to demonstrate Ofcom's commitment to minimising regulatory burdens on stakeholders, and which provides transparency and certainty to the industry looking forward about Ofcom's ongoing or planned simplification work.

Telecom considers that both Ofcom's general approach to regulatory principles, and the concept of an annual Simplification Plan, are useful precedents for New Zealand, and the Commission in particular, to consider. I note the Commission has published recently a set of draft principles to be taken into account during the transition to next generation services. While these provide a useful beginning for a wider consultation on regulatory principles, they do not diminish the need or urgency for that wider consultation.

Yours sincerely



Tristan Gilbertson
Group General Counsel

³ Final statements on the Strategic Review of Telecommunications, and undertakings in lieu of a reference under the Enterprise Act 2002, Ofcom, 22 September 2005, paragraph 5.2.

⁴ Communications Act 2003 (UK).

⁵ Ofcom: Regulatory Principles.

⁶ Ofcom: Regulatory Principles.

⁷ Final statements on the Strategic Review of Telecommunications, and undertakings in lieu of a reference under the Enterprise Act 2002, Ofcom, 22 September 2005, paragraph 5.4.