



COMMERCE COMMISSION

**Revised Draft Review of the Standard Terms Determination for the designated service
Telecom's unbundled bitstream access**

DECISION NO. XXX

Revised Draft Review Decision under section 30R of the Telecommunications Act 2001 of
Decision 611

The Commission:

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Date of Draft Review Decision:

8 June 2011

Confidential information cited in this Review Decision is subject to the confidentiality order made by the Commission under s 15(i) of the Act and s 100 of the Commerce Act 1986 ('the Order'). The Order in relation to the UBA section 30R review is dated 7 September 2010.

Chorus restricted information is denoted as [] **CRI**.

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Key documents are available on the Commission's website at:
<http://www.comcom.govt.nz/1st-competition-test-for-uba-std-june-2010/>

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EXECUTIVE SUMMARY

1. This is the first competition review of the designated access service of Telecom's unbundled bitstream access (**UBA Service**) conducted by the Commerce Commission (the **Commission**) under section 30R since the UBA Service standard terms determination (**STD**) was issued on 12 December 2007.
2. In this revised Draft Review Decision the Commission has reconsidered its preliminary views in the Draft Review, dated 28 October 2010, based on the submissions received. The Commission's current view is that:
 - the relevant markets for the UBA Service are the wholesale markets for broadband access in each of Telecom's exchange service areas (**ESA**). These markets include both cabinetised and non-cabinetised lines
 - Telecom does not face limited competition in an ESA when two or more competing providers are present and Telecom has a market share that is less than 80% in that ESA
 - 27 ESAs are now subject to competition ie Telecom does not face limited (or is not likely to face lessened) competition. Consequently the terms of the UBA STD will not apply to these 27 ESAs
 - the UBA price should only be calculated from UBA prices in regulated ESAs
 - six monthly reviews of the competition assessment for the UBA STD should be undertaken.

OVERVIEW

3. On 12 December 2007, the Commission issued the UBA Service STD under section 30M of the Telecommunications Act 2001 (the **Act**).¹
4. The UBA Service (as set out in Part 2 of Schedule 1 of the Act provides that three years from the date on which the Telecommunications Amendment Act (No 2) 2006 receives the Royal assent, i.e. 22 December 2009, the UBA Service is subject to the following competition conditions:

That either—

 - (i) Telecom faces limited, or is likely to face lessened, competition in the relevant market; or
 - (ii) Telecom does not face limited, or is not likely to face lessened, competition in the relevant market, and the Commission has decided to require Telecom's unbundled bitstream access to be wholesaled in that market.
5. On 23 June 2010² the Commission commenced a review (this **Review**) under section 30R of the Act to assess the state of competition in the markets in which UBA services are provided.
6. On 28 October 2010 the Commission issued a Draft Review of the UBA Service STD (the **Draft Review**).

¹ Commerce Commission, *Standard Terms Determination for the designated service Telecom's unbundled bitstream access*, 12 December 2007 (**UBA STD**).

² Commerce Commission, *Commencement of review of competition in the market in which unbundled bitstream access (UBA) services are provided under section 30R of the Telecommunications Act (No2) 2006 (the Act)*, 23 June 2010 (the **23 June 2010 letter**).

7. The Commission received submissions on the Draft Review on 25 November 2010 and cross-submissions on 21 December 2010.
8. The Commission sought further comment from interested parties on Telecom's submission that pricing data from deregulated ESAs should not be considered when calculating the UBA price for regulated ESAs. Submissions were received on 30 March 2011.
9. All submissions and cross submission are on the Commission's website and a summary is provided in Appendix 2.

DRAFT REVIEW

10. The Commission's preliminary conclusions in the Draft Review were that:
 - the relevant markets in which the UBA Service is supplied are:
 - the wholesale markets for broadband access in each of Telecom's exchange service areas
 - the wholesale market for broadband access in cabinetised areas
 - Telecom does not face limited competition in exchange service areas (excluding lines that are cabinetised) where either:
 - two or more Competing Providers are present
 - one UCLL-based Competing Provider is present and the exchange will serve at least 6,500 non-cabinetised lines (after the cabinetisation deployment is completed)
 - Telecom faces limited competition in all other areas, including all cabinetised lines
 - the Commission should undertake a review every six months to take into account competition developments.

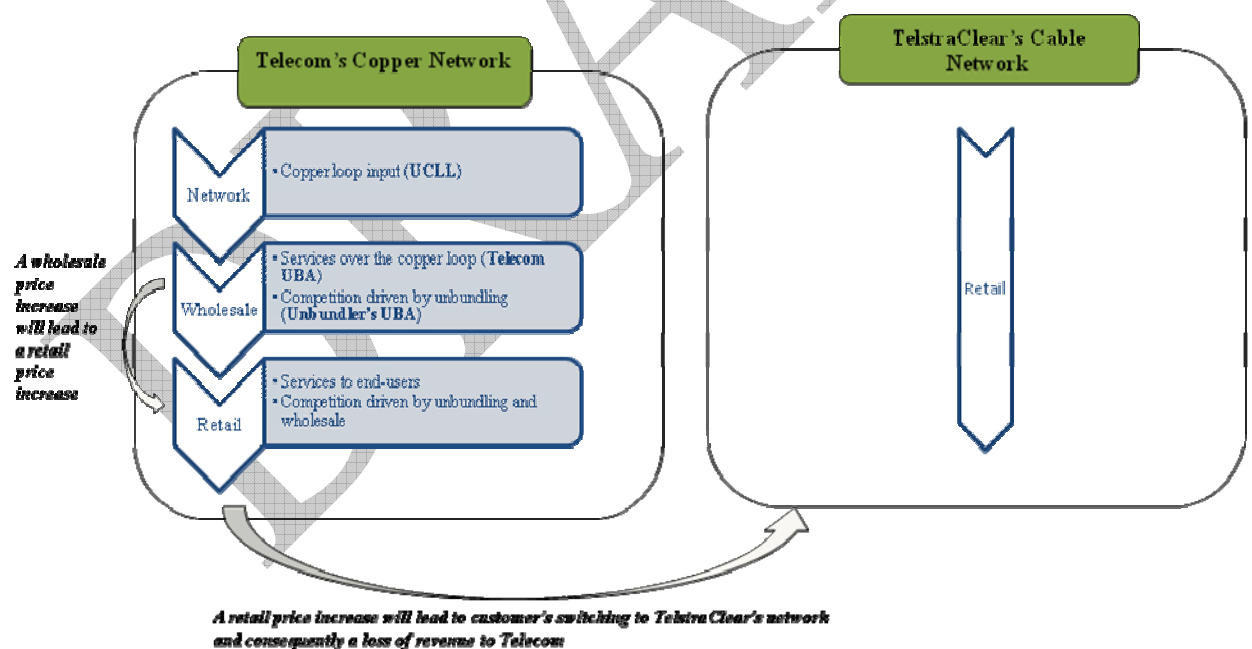
Market Definition

11. The Commission's preliminary view in the Draft Review was that the relevant product dimension of the market was broadband access over copper, cable and fibre (but excluding fixed-wireless, satellite and 3G mobile services). The Commission also considered that, in defining the geographic scope of the market, cabinetised areas were a distinct market from ESAs.
12. The Commission has reconsidered its view based on the submissions received. For the reasons discussed below, the Commission's current view is that:
 - the product dimension of the market includes both cabinetised lines and non-cabinetised lines
 - the geographic dimension of the market remains ESAs.
13. The Commission's preliminary view was that the functional dimension of the market in which bitstream access is supplied was the wholesale level of the market. The Commission's preliminary view was also that separate customer dimensions of the market were not required for the purposes of this Review. The Commission has not changed its views regarding the functional and customer dimensions of the market.

Product dimension

14. The Commission's current view is that cabinetised lines and non-cabinetised lines are in the same relevant product market, as Telecom could be constrained not only by direct wholesale supply but also by competition at retail level over cabinetised and non-cabinetised lines.
15. Competition at the retail level can provide some price constraint at the wholesale level, due to the possibility of switching by end-users in the downstream retail market. This is referred to as an indirect constraint. This indirect price constraint is relevant as long as that retail competition is not dependent on an exclusive input provided in the upstream market.
16. Figure 1 considers competition between Telecom's copper network and TelstraClear's cable network and provides an example of the indirect constraint placed on Telecom's copper network by TelstraClear's cable network.
17. Whilst TelstraClear does not offer access at the input or wholesale level, it can still constrain Telecom's wholesale broadband prices. This is because an increase in wholesale prices would make Telecom's network less attractive to customers, as it would likely lead to retail broadband price increases. A retail broadband price increase would in turn lead to customers switching from Telecom's network to TelstraClear's network, and consequently a loss of revenue to Telecom.

Figure 1: indirect constraint placed on Telecom's copper network by TelstraClear's cable network



18. The same argument can be applied to cabinetised and non-cabinetised lines. Telecom does not currently differentiate its retail broadband prices between cabinet-fed and

non-cabinet fed customers.³ Telecom's wholesale price is therefore constrained by the retail broadband prices of UCLL providers in non-cabinetised areas.

19. In light of the above, the Commission is of the view that cabinetised and non-cabinetised lines are in the same relevant product market because Telecom is constrained in its ability to price discriminate between cabinetised and non-cabinetised lines and Telecom's behavior to date illustrates this practice. The relevant constraints on Telecom are:
- the indirect price constraint imposed by non-cabinetised lines on cabinetised lines
 - the indirect price constraint imposed by TelstraClear's cable network (in the areas covered by TelstraClear's network).
20. The product dimension of the market is therefore broadband access over copper, cable and fibre, including both cabinetised lines and non-cabinetised lines.

Geographic dimension

21. The Commission's preliminary view in the Draft Review was that the geographic dimension of the market was ESAs.
22. The implication of an effective indirect pricing constraint is that the scope of the wholesale market would likely to be wider. For example, if an indirect constraint is effective in ESAs such as Blockhouse Bay and Devonport, the geographic scope of the market is likely to be Auckland (the boundaries of the retail market).
23. However, the Commission considers that for purposes of this Review it is appropriate to delineate a narrow market according to ESAs because it is likely that there will be different levels of competition (and market power) in different ESAs. The Commission therefore considers that the markets in which UBA services are supplied are the wholesale markets for broadband access in each of Telecom's ESAs.

Is mobile broadband a competitive constraint on the UBA service?

24. In the Draft Review, the Commission's preliminary view was that 3G mobile services do not represent a sufficiently close substitute to be included in the market for broadband access. The Commission remains of this view for the reasons discussed below.
25. Mobile broadband is now becoming a viable consumer proposition with all three mobile operators in New Zealand rolling out High Speed Packet Access networks which have enabled them to offer internet access at headline speeds comparable to those available on fixed networks.
26. In considering this matter, the Commission has had regard to the position taken by Ofcom. Ofcom has noted that despite the high rate of take up of mobile broadband in the UK, mobile broadband is largely seen as complementary to existing fixed broadband access as most mobile broadband customers also purchase fixed access rather than as a substitute. According to Ofcom, this is likely to be a result of constraints associated with the speed and capacity of mobile broadband making it less

³ If this non-discriminatory practice changes and Telecom does price discriminate between cabinetised and non-cabinetised lines, the Commission will need to review the market definition and competition assessment under section 30R of the Act.

appropriate for in-home use where users may be more inclined to use data hungry services.⁴

27. Ofcom also noted that in the short term, it is unlikely that the capacity of existing mobile networks will be able to support larger take-up of mobile broadband to compete with existing fixed broadband demand.⁵
28. A recent survey by Analysys Mason of 6000 European and US customers in 2010, found that interest in mobile broadband among non-subscribers declined slightly in all markets between 2009 and 2010, leading them to conclude that mobile broadband is a complement, rather than a substitute for fixed line broadband. Notably, the survey found that:⁶
 - 84% of mobile broadband subscribers also have a fixed broadband connection, and that there is little evidence that these subscribers will drop their fixed line contracts
 - the number of customers who said they were not interested in mobile broadband because they are happy with their fixed line service increased by 7% from 65% in 2009 to 72% in 2010.
29. The Commission considers that product substitutability between mobile and fixed broadband is likely to increase over time as technology improves, service innovation and competition in mobile broadband continues to develop, and mobile broadband prices fall. Improvements in these factors may lead to an environment where mobile broadband services provide an effective substitute to fixed broadband services in the future.
30. The Commission however, considers that mobile broadband is not currently an effective substitute in the current environment for the following reasons.
 - The relatively high pricing for mobile broadband services, coupled with relatively low speeds compared to fixed-line broadband, limit the substitutability of mobile broadband services for fixed-line broadband services.⁷
 - The price differential is likely to reflect a premium for the mobility feature that is available through mobile broadband services. However, this pricing differential is significant, and in the face of a small but significant increase in the price of a fixed broadband service, it is unlikely that a material proportion of customers would sufficiently value mobility to switch services.
 - There is a strong perception among consumers that mobile broadband is more unreliable, more expensive and is not as fast as fixed broadband.⁸
 - The difference between fixed and mobile broadband will become increasingly apparent as fixed operators deploy more fibre and double digit Mb/s speeds become increasingly available and more commonly used.

⁴ Ofcom, Review of the wholesale broadband access markets: 23 March 2010, paragraph 3.106 page 30

⁵ Ofcom, Review of the wholesale broadband access markets: 23 March 2010, paragraph 3.114 page 31

⁶ Analysis Mason, Mobile Insight and the Connected Consumer, Mobile World Congress, 2011, p4

⁷ According to Telecom's website, the standard monthly price of the 'Mobile Broadband 2GB' plan is \$61.06 and the charge for an additional 2GB is \$29.95

⁸ Analysis Mason, Mobile Insight and the Connected Consumer, Mobile World Congress, 2011, p4

Conclusion on relevant market

31. The Commission concludes that the relevant market is the provision of wholesale broadband services within each of Telecom's exchange service areas including cabinetised lines.
32. The Commission does not consider that mobile broadband is currently an effective substitute.

Competition Assessment

33. The Commission's preliminary conclusions in the Draft Review were that Telecom does not face limited, and is unlikely to face lessened, competition in exchange service areas (excluding lines that are cabinetised) where either:
 - two or more Competing Providers are present, or
 - one UCLL-based Competing Provider is present and the exchange will serve at least 6,500 non-cabinetised lines (after the cabinetisation deployment is completed).
34. The Commission also concluded in the Draft Review that Telecom faces limited competition in all other exchange service areas and all cabinetised lines.
35. The Commission has reconsidered its conclusions from the Draft Review based on the submissions received for the reasons discussed below.

Commission's view

36. Ofcom, in its assessment of competition in the Wholesale broadband market in the UK, defined a number of markets and used a combination of the number of competing providers present and the market share of the incumbent to define the markets.
37. In Australia, when considering whether to grant Telstra exemptions in respect of the local carriage and wholesale line rental services, the Australian Competition and Consumer Commission (ACCC) conducted its market analysis on an ESA basis.⁹ This was subsequently appealed¹⁰ to the Australian Competition Tribunal (ACT).¹¹
38. The ACT introduced a market share threshold, which is applied by the ACCC to each ESA as applicable. The Tribunal decided that absent a market share threshold, it would be difficult to ascertain whether competitors who had entered an ESA are likely to be commercially meaningful competitors who can constrain the incumbent (Telstra) in the long run.
39. Telecom has reduced its prices in certain areas in response to the competitive constraint provided by competing networks. These are the areas where competing infrastructure has been deployed, whether by UCLL operators (primarily in Auckland), or TelstraClear's network in Wellington and Christchurch.
40. However, in those areas within Auckland, Wellington and Christchurch where there is little or no competing infrastructure the Commission expects that the intensity of competition will be reduced. These areas are, for example, ESAs in Auckland that

⁹ ACCC, *Telstra's local carriage service and wholesale line rental exemption applications: Final Decision and Class Exemption*, August 2008

¹⁰ Application by Chime Communications Pty Ltd (No 3)[2009] AcompT 4 (24 August 2009).

¹¹ The ACT decision was subsequently appealed to the Federal Court and referred back by that Court to the ACT for further consideration. The ACT's decision the Commission is relying on is the one released on 1 September 2009.

have not been unbundled, and those areas in Wellington and Christchurch not covered by TelstraClear's network.

41. Vodafone¹² suggested that the Commission should consider an equivalent approach to that used in Australia, given the relative infancy of UCLL and the continuing reduction of the UCLL addressable market due to Telecom's cabinetisation programme.
42. In Australia, the ACT has mandated that a 70/30 percent market share threshold should apply as one factor to assess whether Telstra should be exempt from delivering the local carriage services within an ESA. The Tribunal found that Telstra would only be exempted in ESAs where access seekers have an aggregate market share equal to or greater than 30% of the total services in operation (SIO) in each ESA.
43. The Commission has run a sensitivity analysis of different Telecom market shares to see what the effect of the different market shares would be on competition. The Commission has used geospatial mapping data to overlay the coverage of TelstraClear's network with Telecom ESAs including unbundled exchanges to determine the appropriate market share.
44. The Commission considers that a market share threshold that aligns with the areas in New Zealand where retail competition has been observed is more appropriate. The Commission observed that when a market share of 80/20 percent is applied, this closely aligns with the areas where Telecom has reduced its broadband price due to competition from competing providers. This is likely to combine actual and potential competition which in combination acts as a competitive constraint.¹³
45. The Commission therefore considers that a market share threshold that should apply is 80/20 percent. This implies that deregulation will only be considered in ESAs where Telecom's market share is less than 80% and access seekers have an aggregate market share greater than 20%.
46. This market share threshold, in combination with the competing provider assessment, will be applied to assess competition levels in the relevant wholesale broadband markets.

What are the conditions under which alternative operators are to be considered a competitive constraint?

47. In the Draft Review, the Commission's view was that the relevant product market included broadband provided over copper, cable and fibre. The Commission concluded that due to the lack of uptake of fibre broadband connections, and barriers to customers switching to fibre services, the Commission was not satisfied that FTTP networks provide a material constraint on Telecom in terms of the UBA service at the present time.
48. The Commission also noted that although TelstraClear does not currently provide wholesale access to its HFC network,¹⁴ competition provided by TelstraClear's cable network in the retail market is likely to act as an indirect constraint on Telecom in the wholesale market for broadband services. The Commission used TelstraClear's

¹² Vodafone, response to Telecom's Request for Clarification, 30 March 2011

¹³ The two areas do not precisely match. This reflects the Commission's preliminary view that observed price reductions by Telecom provides some but not conclusive evidence of effective competition.

¹⁴ TelstraClear, *Letter to Commission re UBA Competition Review*, 6 August 2010, paragraph 11.

coverage maps¹⁵ to determine whether TelstraClear had cable coverage in Telecom ESAs located in the Wellington, Kapiti and Christchurch regions.

49. Telecom¹⁶ submitted that a clear framework is needed for assessing when a fibre provider is considered a competing provider and suggested applying the same criteria that is used for cable.
50. Vector¹⁷ submitted that it was unclear how the Commission will address partial coverage scenarios where ESAs are only partly covered by the competing networks. Vector proposed that a pragmatic approach is to assess the number of premises in an ESA that are passed by a competing network and deregulate where this coverage exceeds a minimum threshold.
51. The Commission considers that in order for a Competing Provider in a given ESA to provide a competitive constraint it must be able to supply, or be capable of supplying, a broadband service to a significant part of that ESA.
52. As the Commission has added a market share threshold to the competition test, it is of the view that there is no need to include an explicit infrastructure coverage threshold. The market share test is likely to provide an accurate representation of market dynamics in ESAs in combination with an assessment of the constraint provided by Telecom's competitors in ESAs.

Cabinetisation

53. In the Draft Review the Commission's view was that the challenging economics of sub-loop unbundling in general meant that Telecom faces limited competition in respect of cabinetised lines.
54. Vector¹⁸ submitted that the Commission needs to explicitly consider the level of competitive constraint placed on UBA cabinet services directly from competing networks separate of that stemming from UCLL.
55. The Commission has altered the market definition to include cabinet-fed lines and exchange fed lines in the same market as discussed in paragraphs 14 to 20 above.
56. The Commission considers that the introduction of a market share test would ensure that deregulation occurs only when there is effective competition in an ESA.

Conclusions on competition assessment

57. The Commission's current view is that Telecom does not face limited competition in an ESA when two or more competing providers are present and Telecom has a market share less than 80% in that ESA. Based on this current view, Appendix 1 lists the exchanges where Telecom does not face limited competition.

What is the appropriate approach for calculating the regulated UBA price?

58. In response to Telecom's submission that it was appropriate to amend the UBA Price List so that pricing data from deregulated ESAs is not considered when calculating the

¹⁵ <http://www.telstraclear.co.nz/residential/network-maps.cfm>

¹⁶ Telecom Submission, pages 6-7.

¹⁷ Vector, -*Submission to the Commerce Commission on the 1st UBA Competition Test Draft Decision*, 25 November 2010, page 2.

¹⁸ Vector, *Submission to the Commerce Commission on the 1st UBA Competition Test Draft Decision*, 25 November 2010 Para 7

UBA price for regulated ESAs, the Commission has considered arguments for including and excluding deregulated ESAs in the calculation.

59. The Commission's preliminary view is that deregulated ESAs should be excluded from the calculations.

Arguments for excluding retail prices in competitive ESAs

60. The retail minus pricing methodology is meant to achieve specific objectives. One of these is that it provides 'economic headroom' for wholesale competitors to compete. In calculating this it is the Telecom retail prices which wholesalers compete against which are most relevant.
61. The retail minus pricing methodology also sits under a wider Ladder of Investment (LOI) framework. UBA is the step on the ladder prior to unbundling exchanges (and purchasing the UCLL product). To maintain incentives for Access Seekers to climb the LOI, the price differential between UBA and UCLL is important.¹⁹ Over time, including wider retail prices could reduce the margin between UCLL and UBA to the point where UCLL is no longer economically viable.
62. In deregulated areas the Commission expects price competition to be more effective and retail prices to be lower over time. Including these areas in the calculation of the UBA price is likely to lower the price of UBA and by doing so lower the incentives for Access Seekers to move up the ladder to unbundling and the more effective infrastructure based competition that brings. This would occur in those areas which would most benefit from enhanced competition through additional investment in network infrastructure.
63. Including deregulated areas in the UBA price calculation may also weaken incentives for Telecom to compete aggressively on price in deregulated areas. They will take into account lost wholesale revenues in regulated areas in pricing in deregulated areas and that could lead to their retail prices to end-users being higher than it otherwise would be.²⁰

Arguments for including retail prices in competitive ESAs

64. The retail minus pricing principle allows Telecom to recoup revenues above their costs to the extent their retail prices are above competitive levels. Given that lower retail prices from Telecom have been observed in areas with greater competition, it is likely that retail prices are likely to be above competitive levels elsewhere.
65. As competition develops it is to be expected that Telecom's retail prices will fall and the UBA price to become more cost reflective. By including deregulated areas in the calculation of the UBA price, end-users in regulated areas would benefit from competitors to Telecom having greater margin to pass-through to them. At the same time the UBA price should still allow Telecom to make a return on this wholesale product. The result would be that the benefits of competition would be spread more widely across end-users in New Zealand.

¹⁹ This is also reflected in the Schedule 1 of the Act where the Commission is required to consider the relativities between UCCL and UBA pricing. "The Commission must consider relativity between this service and Telecom's unbundled copper local loop network service..."

²⁰ For example Telecom Wholesale's decision to cut the UBA price in deregulated areas would take into account the likelihood Telecom Retail passes this through to end-users which will lead to UBA price cuts elsewhere and consequential lost revenue.

66. As noted above, this may come at a cost of lower levels of unbundling. For some parts of New Zealand, the size of exchanges and costs of backhaul may make unbundling prohibitively expensive. In these areas maintaining a higher UBA price incurs a cost to end-users but does not reward them with more effective infrastructure based competition in the longer term.
67. CallPlus and Kordia²¹ have argued that de-averaging the calculation of retail price would be contrary to the Act and would be detrimental to the market. The Commission's view is that the Act does not prohibit the exclusion of de-regulated areas from the UBA price calculation.
68. Vodafone²² have also raised concerns that Telecom may raise retail prices in deregulated areas whilst pricing wholesale services in de-regulated areas to the detriment of unbundlers. The Commission's analysis is that competition will act as a constraint on UBA prices in deregulated areas.

Conclusion

69. The analysis above suggests that there are end-users who would benefit and those that would lose out from a decision to exclude de-regulated areas from the UBA calculations.
70. While the UBA initial pricing principle does not expressly state that a different pricing approach is required in markets where Telecom faces limited competition in comparison with those where Telecom does not face limited competition and a decision to regulate is made, the final pricing principle requires a different pricing approach to be used in those different circumstances.
71. The Commission believes that the price determined using the initial pricing principle should provide a proxy for the bitstream price which would be likely if the Commission were to proceed to a final pricing principle. This is more likely to occur and give effect to section 18 if the retail prices used in the calculation of the imputed retail price are calculated from the available retail prices of Telecom's DSL enabled plans within regulated ESAs.
72. The Commission's current view is that the UBA price should only be calculated from UBA prices in regulated ESAs. The Commission has reviewed the UBA Price List to incorporate this current view. The changes made to the UBA Price List appear as tracked changes in Appendix 4.

²¹ CallPlus Kordia, UBA Price Calculation, Telecom request for clarification, 29 March 2011

²² Vodafone, response to Telecom's Request for Clarification.

APPENDIX

Review Process

73. In the Draft Review the Commission's view was that the six monthly reviews should be undertaken with the potential for ad hoc reviews on an exchange by exchange basis. The Commission remains of that view.
74. In the six monthly reviews the Commission intends to refresh the analysis that underpins the competition assessment. The six monthly reviews will also allow the Commission to take into consideration new market developments, such as the further unbundling undertaken by access seekers.
75. Telecom noted that the Draft Review suggests that an increase in price in an ESA is likely to warrant an ad hoc review. Telecom requested that the Commission clarify its intention regarding this as there may well be legitimate reasons why prices may rise in a competitive market.²³
76. The Commission acknowledges that there may be cases for legitimate price increases and does not consider that any price increase would require a review of the competition status in an ESA that has been deregulated. The Commission will only undertake a review of the competition status in an ESA if there are material grounds to do so.
77. The Commission anticipates that it will go through a process to establish whether there are grounds for a review before commencing a review.

THE COMMISSION'S DECISION

Market definition

78. The relevant market in which the UBA service is supplied is the wholesale markets for broadband access in each of Telecom's exchange service areas (including cabinetised lines).

Competition assessment

79. Telecom does not face limited competition or is likely to face lessened competition in exchange service areas (including lines that are cabinetised) where two or more Competing Providers are present and Telecom has a market share of less than 80%. Appendix 1 lists the exchanges where Telecom does not face limited competition.

Frequency of future reviews

80. The Commission concludes that six monthly reviews will be undertaken and in these reviews, the Commission will refresh the analysis that underpins the competition assessment.

Additional amendments to UBA STD Schedules to give effect to the application of the competition condition following this Review

81. As a consequence of applying the competition conditions outlined in Schedule 1, Part 2 of the Act, amendments to the UBA STD Schedules are required. The Commission has made amendments to the UBA Price List given that the UBA price calculations

²³ Telecom, *Submission on the draft review of UBA STD – The competition assessment*, 25 November 2010, page 11

must only have regard to Telecom's retail broadband plans in regulated ESAs. A revised version of the UBA Price List is attached (see

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APPENDIX 4).

82. The Commission has also made amendments to the UBA Service Description to carve out areas of Telecom's network where the regulated UBA Service is not available. A revised version of the UBA Service Description setting out these proposed amendments is attached in Appendix 3.
83. The Commission has inserted new clauses into the UBA Service Description explaining the areas where the UBA Service is available.
84. The UBA Service connects the end-user's building (or, where relevant, the building distribution frames) to Telecom's first data switch (**FDS**). However, in many cases the local telephone exchange used to supply broadband services to end-users does not contain an FDS, so UBA traffic is handed over to the access seeker at another exchange in which an FDS is located.
85. The Commission has added a new clause to the UBA Service Description (clause 2.9) to clarify the impact of deregulation of the wholesale broadband market in an ESA where the Handover Point in that ESA is required to remain available for DSLAMs that remain within a regulated Coverage Area.

APPENDIX 1

ESAS where the terms of the UBA STD will not apply

86. As a result of applying the competition test outlined in this review, the ESAs in Table 1 have been determined as markets where Telecom does not face limited competition and is not likely to face lessened competition. A graphical representation of the deregulated ESAs is shown in Appendix 5. Table 2 shows all ESAs where two or more Competing Providers are present.

Table 1: ESAs where the terms of the UBA STD will not apply²⁴

Auckland (Akcen)	Courtenay Place	Linwood	Riccarton
Avondale	Devonport	Mt Eden	Takapuna
Beckenham	Ellerslie	Mt Roskill	Te Atatu
Birkdale	Forrest Hill	New Brighton	Titirangi
Birkenhead	Glen Eden	New Lynn	Torbay
Blockhouse Bay	Glenfield	Pakuranga	Wellington
Christchurch	Hillmorton	Ponsonby	

Table 2: ESAs where two or more Competing Providers are present

Albany	Frankton	Maxwells Line	Remuera
Auckland (Akcen)	Glen Eden	Mt Albert	Riccarton
Avondale	Glendowie	Mt Eden	Rotorua
Beckenham	Glenfield	Mt Roskill	St Heliers
Birkdale	Hamilton	Napier	Takapuna
Birkenhead	Hamilton East	Nelson	Tamaki
Blenheim	Hastings	New Brighton	Taradale
Blockhouse Bay	Havelock North	New Lynn	Tauranga
Browns Bay	Henderson	New Plymouth	Tawa
Christchurch	Hillmorton	Onehunga	Te Atatu
Claudelands	Howick	Otahuhu	Te Rapa
Courtenay Place	Linwood	Otumoetai	Three Kings
Devonport	Mangere	Pakuranga	Titirangi
Dunedin	Manukau City	Palmerston North	Torbay
Ellerslie	Manurewa	Papakura	Wanganui
Fendalton	Marewa	Papatoetoe	Wellington
Forrest Hill	Massey	Ponsonby	

87. The Commission has used the following approach to determine the relevant market share for this Review.
88. TelstraClear has provided the Commission with its total number of cable broadband customers. The total number of cable broadband subscribers has been divided by the total number of premises within TelstraClear's network coverage area in order to estimate the proportion of households that subscribe to TelstraClear's cable network (the 'TelstraClear customers to houses passed ratio').

²⁴ Where two or more competing providers are present and have 20% or more market share.

89. The Commission has mapped TelstraClear's network coverage areas to Telecom's ESA boundaries to calculate the number of houses passed by TelstraClear's network in each ESA. The TelstraClear customers to houses passed ratio has then been applied to estimate the number of TelstraClear subscribers in each ESA.
90. The Commission understands that TelstraClear uses fibre to deliver services to inner city areas in Wellington and Christchurch where its cable network does not reach. The Commission has included this in its analysis.
91. The Commission has set the market size in each ESA equal to 'active' broadband lines in the relevant ESA. Telecom has provided the Commission with the number of active copper broadband lines²⁵ in each ESA and the Commission has estimated the number of active cable broadband lines in each ESA based on the method outlined in paragraphs 87 to 90 above.
92. Telecom has provided the Commission with the number of active copper broadband lines that are provided by Telecom Group and the number of active copper broadband lines provided by UCLL. Both sets of data are broken down by ESA.²⁶
93. Some of the data provided by Telecom relates to different time periods, however, the Commission does not expect this to have a material effect on the outcome of the competition assessment. The Commission will ask Telecom to update all the data so that the data relate to the same time period for the Final Report.
94. Where TelstraClear has coverage, the number of active copper broadband lines has been added to the estimated number of TelstraClear customers in the relevant ESA. This gives the total number of active broadband lines.

²⁵ This number includes UCLL lines and lines used by Telecom Wholesale.

²⁶ Not all Telecom data relates to the same time period, however, because the incremental changes in the data is not expected to be significant, the Commission does not expect this to have a material effect on the outcome of the competition assessment. The Commission will ensure that this inconsistency is remedied in the Final Report.

APPENDIX 2

Summary of Submissions

95. This appendix summarises the key issues raised in submissions and cross submissions on the Draft Review.

Market Definition

96. Telecom²⁷ agreed that the ESA market is the most appropriate unit of measurement. However Telecom noted that if UCLL operators continue to provide broadband services from the exchange (albeit at slower speeds) on cabinetised lines, the Commission's draft view to have cabinetised lines in a separate market would need to be revisited.
97. Vector²⁸ agreed that the appropriate geographic unit to conduct the assessment of competition for UBA is at the ESA level. Vector however noted that this would only be appropriate while there exist equivalence of inputs between UCLL and UBA.
98. Vector noted that the Commission needs to consider the level of competitive constraint placed on UBA cabinet services directly from competing networks separate from that stemming from UCLL. Vector noted that the economics of unbundling cabinets will not matter to a competing network and it was also irrelevant to the competition assessment as to whether a competing network covers a cabinet area or an ESA.²⁹
99. Vodafone³⁰ submitted that clarification of the UBA STD to cater for the provision of regulated UBA in conjunction with the commercial sub loop extension service, has meant that access seekers are now looking at expanding their unbundling footprint to geographic areas and exchanges that have been cabinetised and were previously not economic.

Is mobile broadband a competitive constraint on the UBA service?

100. Telecom³¹ submitted that mobile broadband was becoming a closer substitute for fixed broadband for New Zealand consumers and that the Commission should consider mobile a close substitute for standard speed broadband. In their cross-submission, Telecom³² stated that further analysis and consultation was needed on the level of which wireless represents a close substitute and proposed that this be consulted on prior to the next review.
101. Vodafone³³ agreed that the relevant product market should, for the purposes of this current review, exclude 3G mobile services.

²⁷ Telecom, *Submission on the draft review of UBA STD – The competition assessment*, 25 November 2010, page 7.

²⁸ Vector, *-Submission to the Commerce Commission on the 1st UBA Competition Test Draft Decision*, 25 November 2010, page 6

²⁹ Ibid

³⁰ Vodafone, *Re: Draft Review of the Standard Terms Determination for Telecom's unbundled bitstream access service*, 25 November 2010, page 3

³¹ Telecom, *Submission on the draft review of UBA STD – The competition assessment*, 25 November 2010, pages 5-6.

³² Telecom, *Cross Submission on the Draft Review of the UBA STD – The Competition Assessment*, 21 December 2010

³³ Vodafone, *Re: Draft Review of the Standard Terms Determination for Telecom's unbundled bitstream access service*, 25 November 2010, pages 1-2.

102. Vector³⁴ submitted that the relevant product definition should be technology agnostic and should include wireless and 3G mobile broadband where the products use technologies that provide a comparable bandwidth service to the UBA Service. To that end, Vector proposed that the Commission should consider the merits of defining the product market with reference to bandwidth characteristics.
103. Vector submitted that while mobile is unlikely to be a perfect substitute for fixed line services, it is increasingly becoming a near substitute.

Competition Threshold

104. Vector³⁵ submitted that it had concerns over the robustness of the Commission's threshold approach in the competition assessment in the Draft Review.
105. Vector noted that the threshold does not:³⁶
- provide for an ex-post assessment of the impact of competition in a particular ESA to supplement the threshold based competition test. Vector submitted that a supplementary analysis of the ex-post impact of competition will bolster a simple threshold test – reducing the likelihood of false positive decisions – and will also act as a bellwether to reveal the extent and ferocity of competition at a particular ESA or cabinet
 - take account of the extent of unbundling or competitive network coverage. Vector noted that there could be only a handful of lines unbundled in a particular ESA, but all customers will be deregulated by the threshold test
 - take account of the intentions of competing businesses to invest further in unbundling or competing networks
 - take into account Telecom's national scale and its ability to subsidise competitive ESAs from its national activities. Vector suggested that a supplementary test as to whether Telecom's national scale provides it with significant market power (**SMP**) should be undertaken
 - provide evidence of the level of competitive constraint provided by competing networks
 - effectively assess the impact of competition directly from competitive networks on UBA cabinet services.
106. Vodafone³⁷ in response to Vector's submission, cross-submitted that it would be very difficult to prove that Telecom had SMP in a particular market and that the Commission would be required to gather tangible information, facts and evidence in order to undertake the analysis. Vodafone concluded that including SMP in the Commission's consideration will deliver a significantly different outcome and it could delay the Commission's final decision.
107. Telecom³⁸ cross-submitted that they disagreed with Vector's submission and that there are sufficient safeguards such as the regular competition reviews proposed by the

³⁴ Vector, *Submission to the Commerce Commission on the 1st UBA Competition Test Draft Decision*, 25 November 2010), pages 4-5

³⁵ Vector, *Submission to the Commerce Commission on the 1st UBA Competition Test Draft Decision*, 25 November 2010), page 8

³⁶ *Ibid* pages 8-10

³⁷ Vodafone, *Cross Submission*, 21 December 2010, pages 2-3

³⁸ Telecom, *Cross Submission on the Draft Review of the UBA STD – The Competition Assessment*, 21 December 2010, page 5

Commission, Telecom's Separation Undertakings and provisions of the Commerce Act to mitigate any risk of a "false positive".

Alternative operators are to be considered a competitive constraint

108. Telecom³⁹ submitted that a clear framework is needed for assessing when a fibre provider is considered a competing provider and suggested applying the same criteria that is used for cable.
109. Vector⁴⁰ submitted that it was unclear how the Commission will address partial coverage scenarios where ESAs are only partly covered by the competing networks. Vector proposed that a pragmatic approach is to assess the number of premises in an ESA that are passed by a competing network and deregulate where this coverage exceeds a minimum threshold.

Cabinetisation

110. Telecom⁴¹ submitted that cable imposes a significant constraint on Telecom and the assessment for exchange fed lines should also be applied for cabinetised lines in competitive ESAs.
111. Vector⁴² submitted that the Commission needs to explicitly consider the level of competitive constraint placed on UBA cabinet services directly from competing networks separate of that stemming from UCLL.
112. Vodafone⁴³ requested that the Commission clarify how the 6500 non-cabinetised lines threshold will apply.
113. Telecom⁴⁴ considered that the figure of 6500 non-cabinetised lines served from an exchange should be revisited as part of an annual review process as they consider that the average size of unbundled exchanges will decrease as operators start to unbundle less dense ESAs.

Appropriate approach for calculating the UBA Price

114. Telecom⁴⁵ submitted that it was appropriate to amend the UBA Price List so that pricing data from deregulated ESAs is not considered when calculating the UBA price for regulated ESAs.
115. In response to a request for clarification, Telecom⁴⁶ noted that while maintaining a link between regulated and deregulated ESAs may have some superficial attraction, such a link is more likely to be harmful to competition and work contrary to the long term interests of end-users.

³⁹ Telecom Submission, pages 6-7.

⁴⁰ Vector, *-Submission to the Commerce Commission on the 1st UBA Competition Test Draft Decision*, 25 November 2010, page 2.

⁴¹ Telecom, *Submission on the draft review of UBA STD – The competition assessment*, 25 November 2010, page 7

⁴² Vector, *Submission to the Commerce Commission on the 1st UBA Competition Test Draft Decision*, 25 November 2010 Para 7

⁴³ Vodafone, *Re: Draft Review of the Standard Terms Determination for Telecom's unbundled bitstream access service*, 25 November 2010, page 3

⁴⁴ Telecom, *Submission on the draft review of UBA STD – The competition assessment*, 25 November 2010, page 11

⁴⁵ Telecom, *Submission on the draft review of UBA STD – The competition assessment*, 25 November 2010, paragraph 41, page 11

⁴⁶ Telecom, UBA Price Calculation: request for Clarification, 22 March 2011

116. Telecom further noted that de-linking the UBA price from the price set in competitive markets is likely to:⁴⁷
- promote efficient competition in regulated ESAs and avoid skewing Telecom's pricing incentives in competitive markets
 - promote further efficient competition in deregulated ESAs
 - increase the transparency and fairness of the UBA regulation
 - be more consistent with economic / regulatory best practice.
117. Telecom however noted that if the UBA price is calculated to reference all ESAs, this would be likely to:⁴⁸
- promote inefficient investment and distort competition by:
 - weakening competition in deregulated ESAs
 - weakening incentives for further entry in regulated ESAs where pricing is affected by market dynamics in non-regulated areas
 - stymie competition leading to higher average prices in the long run.
118. Vodafone⁴⁹ submitted that adopting Telecom's changes to the UBA retail minus methodology will discourage further UCLL competition. According to Vodafone, UCLL has brought significant benefits to end-users in terms of competitive pricing and service innovation. Telecom's proposal, according to Vodafone, will damage UCLL competition and will not promote competition in markets for the long-term benefit of end-users.
119. TelstraClear⁵⁰ submitted that if Telecom's proposed approach is adopted, there is a risk that it will increase the broadband prices in regulated ESAs.
120. Network Strategies⁵¹, in a report commissioned by TelstraClear noted, that it is essential to ensure that the application of the initial pricing principle does not have the opposite of the desired effect – namely to ensure consumers in regulated areas reap the benefits of competition. Network Strategies also submitted that there was a risk that Telecom might inflate retail prices in regulated areas either as a barrier to competition in those areas or cross-subsidise low prices in deregulated areas.
121. CallPlus and Kordia⁵² do not support the proposed de-coupling of retail prices in deregulated areas from regulated areas. CallPlus and Kordia requested that the competition test be deferred until cost based UBA is introduced.

Review process

122. Telecom⁵³ submitted that the Commission should refresh its market data quarterly according to the predefined methodology and that the underlying policy should be

⁴⁷ Ibid

⁴⁸ Ibid

⁴⁹ Vodafone, response to Telecom's Request for Clarification.

⁵⁰ TelstraClear, Comments on Telecom's additional submission, 30 March 2011

⁵¹ Network Strategies, UBA Price Calculation: Comment on Telecom's proposed changes. Report for TelstraClear, 28 March 2011

⁵² CallPlus Kordia, UBA Price Calculation, Telecom request for clarification, 29 March 2011

⁵³ Telecom, *Submission on the draft review of UBA STD – The competition assessment*, 25 November 2010, page 13

reviewed annually. This was a position that Vector⁵⁴ supported in its cross submission.

123. Vodafone⁵⁵ however were of the view that a six monthly review was more appropriate as the competition assessment is dependent on investment in infrastructure, evolution of the regulatory regime and emergence of new competitors and new technologies. A quarterly review, in their opinion, would generate additional costs and would certainly be an unnecessary distraction.

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⁵⁴ Vector, Cross submission, 21 December 2010, page 3.

⁵⁵ Vodafone, Cross Submission, 21 December 2010, page 2

APPENDIX 3

UBA Service Description

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APPENDIX 4

UBA Price List

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APPENDIX 5

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