



COMMERCE COMMISSION

**Summary and Analysis of  
Telecom Corporation of New Zealand Limited's  
Regulatory Financial Statements  
for the year ended 30 June 2009**

Date: 14 April 2010  
Filesite: 989669v8

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## **An appropriate citation for this report is:**

Commerce Commission, Summary and Analysis Report on Telecom Corporation of New Zealand Limited's Regulatory Financial Statements for the year ended 30 June 2009.

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## 1. Introduction and Background

1. The Commerce Commission (**Commission**) is responsible for monitoring competition in telecommunications markets, and for making information publicly available regarding the industry, industry activities and specific products and services.
2. The Telecommunications Act 2001 (the **Act**) requires Telecom Corporation of New Zealand Limited (**Telecom**) to publish financial and other information about its network, wholesale and retail business activities and services. The Act also requires the Commission to publish a summary and analysis of the information under the Telecom Accounting Separation Information Disclosure Requirements for Financial Years Ending 2009 and 2010 (the **Requirements**)<sup>1</sup>. The Requirements were implemented following a period of public consultation.
3. Telecom released its first set of audited regulatory financial statements for the financial year ended 30 June 2009 on 18 December 2009<sup>2</sup> in compliance with the Requirements. These set out the specific accounting information and reports that Telecom was required to disclose, as well as a regulatory reporting manual covering its approach to attribution, asset valuation and accounting policies.<sup>3</sup>
4. The Commission's summary and analysis of Telecom's regulatory financial statements is intended to promote greater understanding of Telecom's operations and behaviour, and any changes in its operations and behaviour over time<sup>4</sup>. The key background concepts for regulatory financial reporting are discussed in the Commission's 25 March 2009 Companion Paper<sup>5</sup>.
5. Telecom's regulatory financial statements aim to inform a wide range of people about the company's operations and behaviour. In preparing the regulatory financial statements, Telecom must attribute revenues, expenses, assets and short-term liabilities across business activities, as well as across products and services.
6. In contrast, the main purpose for the financial information contained in Telecom's Annual Report is to meet statutory reporting obligations as well as to inform shareholders, amongst others, about the historical financial performance and position of the company overall. While Telecom does provide limited information in its Annual Report on disaggregated parts of its business,<sup>6</sup> it is not reported in a manner, or in sufficient detail, to meet the purposes of Part 2B of the Act.
7. Telecom's 2009 regulatory financial statements include reporting for Services Groups defined by the Commission, and which include the Telecom's operationally separated business units:
  - The Access Services Group includes the activities of Chorus.

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<sup>1</sup> The Commission issued the Telecom Accounting Separation Information Disclosure Requirements for Financial Years ending 2009 and 2010 under Part 2B of the Act on 25 March 2009.

<sup>2</sup> <http://www.telecom.co.nz>

<sup>3</sup> Attribution is the process of assigning revenues, expenses, assets and short-term liabilities across business activities. Valuation is the process of determining the value of an asset.

<sup>4</sup> S69ZG of the Act.

<sup>5</sup> A copy of this paper can be found at

<http://www.comcom.govt.nz/IndustryRegulation/Telecommunications/AccSepofTelecom/ContentFiles/Documents/Final%20Companion%20Paper%20issued%20March%202009.pdf>

<sup>6</sup> Telecom's Annual Report contains a segmental analysis of operating revenue by segment but does not include a breakdown of expenses or capital employed by segment.

- The Wholesale Services Group includes the activities of Telecom Wholesale but excludes International activities.
  - The Retail Services Group includes the activities of Telecom Retail and Gen-I.
  - The Other Services Group includes the activities of the international business group and overseas operations.
8. Telecom prepared its regulatory financial statements using two asset valuation methodologies. The first method, historical cost accounting (HCA),<sup>7</sup> uses the same New Zealand generally accepted accounting practices (NZ GAAP) principles to value fixed assets as are used by Telecom when preparing its Annual Report. The second method, current cost accounting (CCA),<sup>8</sup> values fixed assets using techniques intended to reflect the current cost of those assets.
9. The use of two different asset valuation methods results in two sets of regulatory financial statements which report different earnings before interest and taxation (EBIT).

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<sup>7</sup> HCA is the conventional accounting method where assets are typically valued at cost at time of purchase.

<sup>8</sup> Under CCA fixed assets are valued using their replacement cost values at current market prices.

## 2. Commission's Key Observations

10. Telecom's 2009 financial year was a transitional year where revenues, expenses, assets and short-term liabilities were allocated to Telecom's Services Groups<sup>9</sup>, but not at a product level.
11. The Commission identified a number of issues with the reliability of the published regulatory financial statements:
  - The implementation of the Requirements is a complex process. As the 2009 financial year is the first year of the accounting separation information disclosure regime, it was anticipated that there might be a need for substantive revisions after the first year to improve reliability.
  - The Commission was unable to assess the significant internal transfer charges between Services Group. These internal transfer charges have a material impact on the financial performance reported for the Services Groups, and the EBIT position for each Services Group can change markedly depending on the nature and flows of the transfer charging arrangements.
  - Much of the non-financial data used as the basis for attributing costs and assets is not independently verified, which results in uncertainty regarding the reliance that can be placed on the regulatory financial statements. The Commission has proposed in its draft decision on changes to the Requirements that the reliability of key material non-financial data is addressed, at least in part, for the introduction of specific product statements in 2010.
  - The fixed asset value difference between the HCA and CCA valuation approaches is significant, which has a material impact throughout the regulatory financial statements. Under the CCA approach, the valuation of the passive network is more than twice its value under HCA. The valuation methodologies of Telecom's network can have an impact on the estimated cost of providing services such as access and backhaul services to other providers; therefore, to the extent that the CCA Statement of Financial Performance is impacted by the increases to the value of fixed assets through net revaluation gains and the resulting increase in depreciation expense, this will flow through to product statements in the 2010 financial year. The Commission will review and verify the asset valuation methodologies used in the regulatory financial statements for the 2010 financial year.
12. The Commission considers that parties should take these issues into account when making an assessment of the reliability and usefulness of the published financial reports.
13. The Commission will address these observations in the proposed changes to the Requirements.

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<sup>9</sup> Services Group is defined in the Telecom Information Disclosure Requirements dated 25 March 2009, being the Access Services Group, the Other Services Group, the Wholesale Services Group and the Retail Services Group.

### **3. Regulatory Reporting**

#### **3.1 Regulatory Reporting Objectives**

14. The regulatory financial statements are intended to provide information regarding the financial performance of Telecom's network, wholesale and retail business activities and services as if they were operated by independent entities.
15. The main priorities for the 2009 regulatory financial statements were to have regulatory financial statements prepared for each Services Group and to have regulatory statements produced using the CCA and HCA methodologies.
16. The priorities for the 2010 and 2011 years are the preparation of product statements for significant regulated products (such as UCLL) and the refinement of Telecom's regulatory processes and methodologies. Particular attention will be given in 2010 to improvements in the documentation of the regulatory processes and to ensuring that Telecom's attribution and valuation methodologies deliver useful regulatory financial and product statements.

#### **3.2 Regulatory Reporting vs. Statutory Financial Reporting (Annual Report)**

17. Regulatory reporting uses methodologies that are different from those used for statutory financial reporting. Unlike Telecom's Annual Report, the regulatory financial statements show the attribution of revenues, expenses, assets and short-term liabilities across Telecom's business activities, processes and services, so that readers have a more informative view of Telecom's operations and behaviour.
18. Statutory financial reporting focuses on the historical financial performance and position of an entity as a whole for the benefit of investors and shareholders. Statutory financial reports provide limited information at a disaggregated level.
19. Key areas where Telecom's regulatory financial statements differ from its statutory financial statements are:
  - The regulatory financial statements include detailed statements at a disaggregated level (i.e., Services Groups) as if they were independent unrelated entities, as opposed to providing detailed reports at an aggregated corporate level<sup>10</sup> with limited reporting at the segment level<sup>11</sup>. The regulatory financial statements require, commencing financial year ending 30 June 2010, the disclosure of product statements for specific products and services. Statutory financial statements do not disclose financial statements for products or services.
  - The Regulatory Statement of Financial Performance is assessed before taxation. In addition, it is not concerned with how assets are funded and it does not include the costs of servicing long term debt (i.e., interest).
  - The regulatory financial statements include the use of CCA in the valuation of the fixed assets. The CCA Regulatory Statement of Financial Performance also includes adjustments (i.e., supplementary depreciation and revaluation gains and losses) resulting from the use of CCA asset valuation methodologies.

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<sup>10</sup> Telecom's Annual Report provides detailed information at the group level (including subsidiaries and interests in associates) and parent company level (Telecom Corporation of New Zealand Limited).

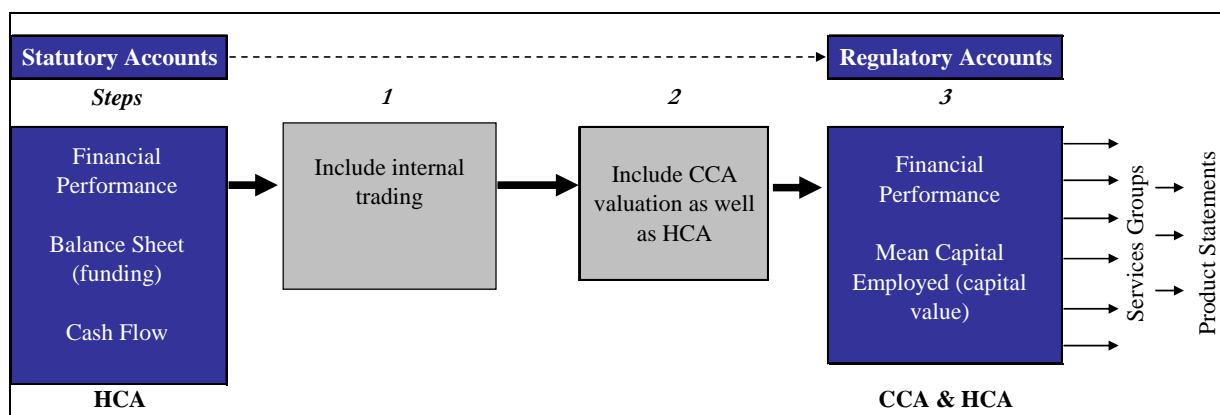
<sup>11</sup> The segmental analysis in Note 2 to the Financial Statements in Telecom's Annual Report analyses operating revenue by segment but does not include breakdown of expenses or capital employed by segment. In 2009, Telecom reported on six operating segments in its Annual Report.

- The categories and layout of the regulatory financial statements differ from their statutory counterparts. In particular, the Statement of Mean Capital Employed,<sup>12</sup> which is the regulatory equivalent of the statutory Balance Sheet, is only concerned with the value of the net operating assets used to provide products and services, and is not concerned with how they are funded. Therefore, funding components such as debt and equity, and asset items such as goodwill are excluded from the Regulatory Statement of Mean Capital Employed.
- If the Commission were to look at the funding components, it would need to derive an appropriate cost of capital<sup>13</sup> for Telecom. Given the transitional nature of the regulatory financial statements, the Commission has chosen to place emphasis on attribution, internal transfer charges, and asset valuation. Once the Commission is satisfied that the appropriate methodologies for these are in place, it will look at an appropriate cost of capital for Telecom's regulatory financial statements.

20. In preparing regulatory financial statements, the financial records used for preparing the statutory financial statements are augmented by three major steps as shown in the illustration below.

- The first step is to include all transactions which reflect internal trading where one business group supplies another business group with the inputs necessary for the supply of products and services.
- For CCA regulatory financial statements, the second step is the introduction of potential CCA revaluations, and the subsequent changes to depreciation and the impact of revaluation gains and losses.
- The third step is the disaggregation of the financial statements into Services Groups, and ultimately product statements through the attribution process.

### Statutory Reporting Compared to Regulatory Reporting



<sup>12</sup> The Mean Capital Employed is the average of the opening value and closing value of the Capital Employed over the relevant regulatory reporting period.

<sup>13</sup> The cost of capital would require an estimate of the appropriate weighted average cost of capital (WACC).

21. Telecom prepared its regulatory financial statements using both HCA and CCA asset valuation methodologies, which is consistent with regulatory financial disclosures in Europe jurisdictions<sup>14</sup>.
22. HCA is the conventional accounting method where fixed assets are valued at cost at the time of their purchase and subsequently depreciated. Telecom's Annual Report is prepared applying HCA methodologies to the valuation of fixed assets.
23. Under CCA, certain fixed assets are valued at their replacement cost. Telecom applied a range of techniques to value its fixed assets for its regulatory financial statements, all of which are documented in Telecom's regulatory reporting manual<sup>15</sup>.
24. Preparation of Telecom's regulatory financial statements also required the attribution<sup>16</sup> and allocation<sup>17</sup> of revenue, expenses, assets and short-term liabilities to the Services Groups. These processes are recorded in Telecom's regulatory reporting manual.

### 3.3 Regulatory Services Groups

25. The regulatory financial statements include reporting for each of the Services Groups as noted below:
  - The Access Services Group includes the activities of Chorus.
  - The Wholesale Services Group includes the activities of Telecom Wholesale but excludes international activities.
  - The Retail Services Group includes the activities of Telecom Retail and Gen-I, including all of Telecom's mobile assets and services.
  - The Other Services Group includes the activities of the international business group and overseas operations (including AAPT and Southern Cross).
26. The Services Groups include a share of Corporate and T&SS expenses and assets.<sup>18</sup>
27. The Services Groups are intended to reflect the arrangement that would occur if Telecom's business activities were performed by independent unrelated entities, and is consistent with Telecom's operational separation undertakings. The use of Services Groups ensures consistency over time.

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<sup>14</sup> ERG, *ERG Report: Regulatory Accounting in Practice* 2008, September 2008, page 18, available at: [http://www.erg.eu.int/doc/publications/erg\\_08\\_47\\_final\\_ra\\_in\\_practice\\_081016.pdf](http://www.erg.eu.int/doc/publications/erg_08_47_final_ra_in_practice_081016.pdf).

<sup>15</sup> A copy can be found on Telecom's website at [www.telecom.co.nz/binarys/2009\\_regulatory\\_reporting\\_manual.pdf](http://www.telecom.co.nz/binarys/2009_regulatory_reporting_manual.pdf)

<sup>16</sup> Cost attribution charges a specific cost directly to a cost unit. It involves a causal relationship.

<sup>17</sup> Cost allocation splits costs across two or more cost units. That is, there is allocation of those costs across units where a causal relationship cannot be established and the costs are not directly attributable.

<sup>18</sup> T&SS (Technology and Shared Services) is the Telecom business unit that includes the core network and the business activities that are common to all the customer facing units.

## 4. Roles of the Independent Regulatory Auditor and the Commission

### 4.1 Independent Regulatory Auditor's Role

28. The Commission required Telecom to engage an independent regulatory auditor to assess whether Telecom's regulatory financial statements were prepared in accordance with its regulatory reporting manual, which describes the procedures Telecom is to follow when preparing its regulatory financial statements. The regulatory auditor is not required to form an audit opinion or professional view on the regulatory reporting manual or the regulatory methodologies. As such, the audit focuses on the processes rather than methodologies.
29. The audit opinion was required to be at the "*prepared in all material respects in accordance with*" standard. This standard of audit assurance provides a significant level of assurance, but is not as high as the "*present fairly, in all material respects*" standard which applies to the audit of Telecom's statutory financial statements in its Annual Report.<sup>19</sup>
30. Telecom engaged KPMG to audit the regulatory financial statements. KPMG gave an unqualified audit opinion<sup>20</sup> with an explanatory paragraph which discussed the implication of the fundamental uncertainty in relation to network inventory data<sup>21</sup>. KPMG noted that future verifications of this data may result in material variances in the regulatory financial statements:

Whilst this network inventory data is sufficiently reliable for the effective operation of the Company's telecommunication network, without completing a physical verification of the network, it is uncertain as to whether the network data is sufficiently reliable for the purposes of the preparation of the Regulatory Financial Statements.

Although it was not possible to complete a physical verification of the network inventory data, we have obtained and evaluated other available sources of evidence to enable us to form our opinion. However, any further physical verification of the network inventory data may result in material variance, either positive or negative, in the Regulatory Financial Statements.<sup>22</sup>

### 4.2 Commission's Role

31. The Commission's review focused on assessing whether Telecom's regulatory financial statements were prepared, for the Services Groups, in accordance with the Requirements.
32. To assess Telecom's compliance with the Requirements and to prepare this summary and analysis, the Commission reviewed Telecom's regulatory reporting manual and regulatory financial statements. The Commission also used compliance monitoring information to inform its assessment.<sup>23</sup>
33. As the Commission is separately proposing changes to the Requirements, material differences may occur in the attribution and valuation of Telecom's fixed assets and expenses between the 2009 and 2010 regulatory financial statements.
34. After public consultation on the proposed changes, the Commission anticipates issuing revisions to the Requirements.

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<sup>19</sup> Neither of these audit opinions guarantees that the audited information is error free.

<sup>20</sup> An unqualified audit opinion indicates that the auditor did not identify any material errors or limitations of scope.

<sup>21</sup> One example of the limitations of the network data which the Commission identified is that the volume data for attributing network component costs is not always available.

<sup>22</sup> KPMG's Auditor's Report is on page 7-8 of Telecom's published regulatory financial statements.

<sup>23</sup> Under the Act, the Commission may request additional information from Telecom to monitor Telecom's compliance with the Requirements.

## 5. Summary - Financial Performance

35. The Regulatory Statement of Financial Performance summarises the operating performance of Telecom as a whole entity as well as the separate Services Groups. It is similar in structure to the statutory Income Statement in Telecom's Annual Report where it reports revenues, and expenses including depreciation.
36. A major difference, however, is that the Regulatory Statement of Financial Performance is pre taxation, and is also not concerned with how assets are funded. It does not include the costs of servicing long term debt (i.e., interest). Another difference is the CCA Regulatory Statement of Financial Performance includes adjustments resulting from the use of CCA valuation methodologies.

### 5.1 Consolidated Statement of Financial Performance

37. The Regulatory Statement of Financial Performance records the revenue, expenditure including depreciation, and the resulting surplus or deficit. It portrays the operational performance of the entity in financial terms.
38. The table below compares the consolidated Regulatory Statement of Financial Performance in Telecom's 2009 regulatory financial statements with the corresponding statutory Income Statement contained in Telecom's 2009 Annual Report.

<b>Consolidated Statement of Financial Performance Comparison</b>			
<b>Year ended 30 June 2009</b>	HCA	HCA	CCA
<b>\$million</b>	Statutory <sup>1</sup>	Regulatory	Regulatory
Revenue	5,599	7,157	7,157
Expenses	3,920	5,503	5,503
EBITDA <sup>2</sup>	1,679	1,654	1,654
Depreciation and amortisation	917	917	917
CCA adjustments	0	0	175
<b>Earnings before interest and taxation</b>	<b>762</b>	<b>737</b>	<b>562</b>

<sup>1</sup> HCA statutory financial statements are contained in Telecom's 2009 Annual Report

<sup>2</sup> Earnings before interest, taxation, depreciation, and amortisation

39. The revenues and expenses reported in both the regulatory columns are derived from both internal and external transactions, whereas the statutory column reports must exclude internal transactions. The main difference between statutory and regulatory financial performance is that the regulatory revenues and expenses both include internal transactions by way of transfer charges of \$1.6 billion.<sup>24</sup>
40. The other difference of note is the inclusion of CCA adjustments in the CCA regulatory column. Where CCA financial statements are reported, the changes to the value of the fixed assets will have a flow-on effect in the Statement of Financial Performance, as either an increase or decrease to the value of the fixed assets (valuation gain or loss) and a resulting increase or decrease in the depreciation expense. For 2009, the CCA adjustments totalled a net \$175 million (the major component of the adjustments being additional depreciation), which result in the CCA regulatory financial statements reporting

<sup>24</sup> Each internal transfer charge will appear as revenue for one Services Group and an expense for another Services Group.

a lower EBIT of \$562 million compared to the HCA regulatory financial statements EBIT of \$737 million (and the EBIT of \$762 million in the statutory financial statements).

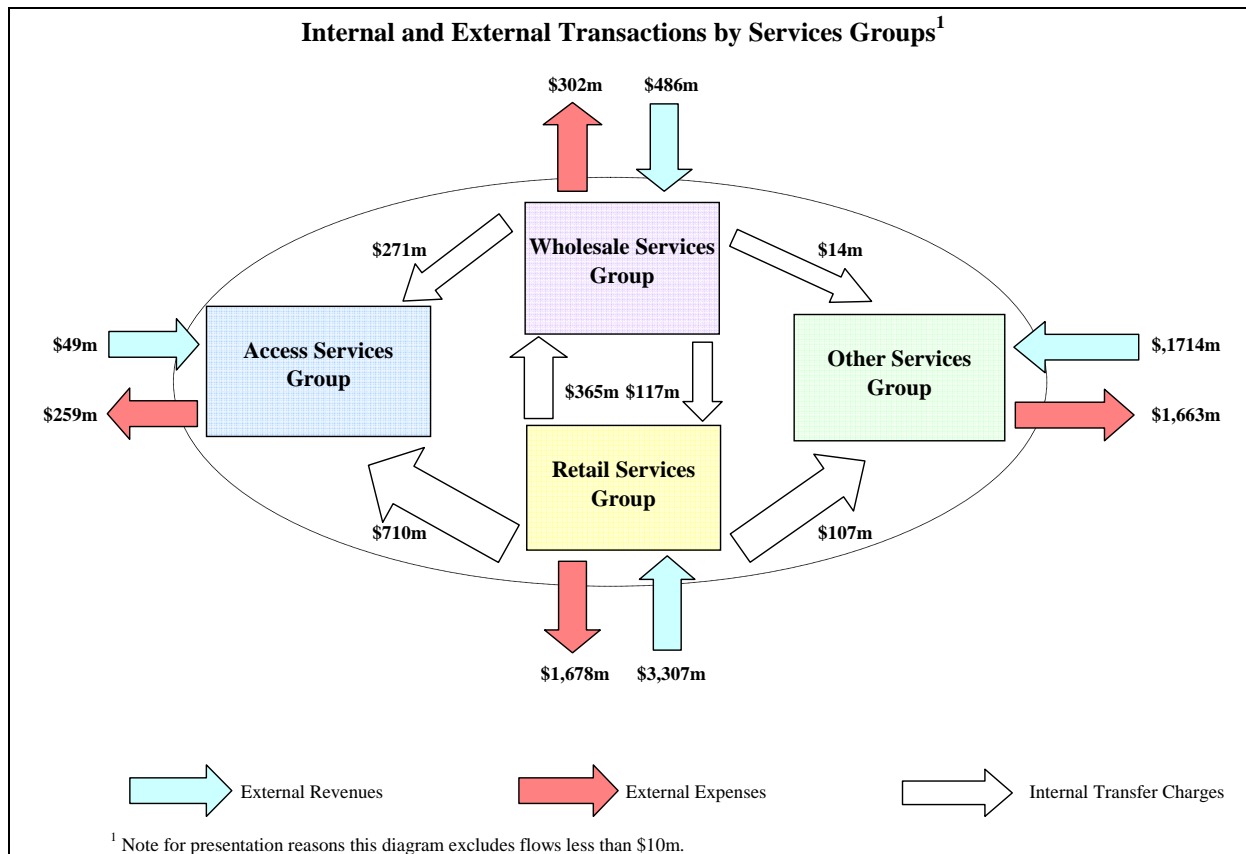
## 5.2 Services Groups – Statement of Financial Performance

41. The Act obligates the Commission to implement Requirements that report on any and all of Telecom’s network, wholesale and retail activities as if operated as independent entities. The internal transfer charges are the revenues and the corresponding expenses which would be paid and received by the Services Groups from each other.
42. The table below summarises the HCA Regulatory Statement of Financial Performance for the four Services Groups from Telecom’s regulatory financial statements section.

<b>Services Group HCA Regulatory Statement of Financial Performance</b>						
<b>Year ended 30 June 2009</b>	Access	Wholesale	Retail	Other	Total	%
<b>\$million</b>	Services	Services	Services	Services		
	Group	Group	Group	Group		
<b>Revenue</b>						
Revenue - Internal	983	377	120	121	1,601	22%
Revenue - External	49	486	3,307	1,714	5,556	78%
<b>Total revenue</b>	<b>1,032</b>	<b>863</b>	<b>3,427</b>	<b>1,835</b>	<b>7,157</b>	<b>100%</b>
<i>Internal revenue %</i>	<i>95%</i>	<i>44%</i>	<i>4%</i>	<i>7%</i>	<i>22%</i>	
<b>Expenses</b>						
Expenses - Internal	12	402	1,182	5	1,601	29%
Expenses - External	259	302	1,678	1,663	3,902	71%
<b>Total expenses</b>	<b>271</b>	<b>704</b>	<b>2,860</b>	<b>1,668</b>	<b>5,503</b>	<b>100%</b>
<i>Internal expenses %</i>	<i>4%</i>	<i>57%</i>	<i>41%</i>	<i>0%</i>	<i>29%</i>	
EBITDA	761	159	567	167	1,654	
Depreciation and amortisation	167	122	382	246	917	
Earnings before interest and taxation	594	37	185	(79)	737	
<i>Earnings before interest and taxation %</i>	<i>81%</i>	<i>5%</i>	<i>25%</i>	<i>-11%</i>	<i>100%</i>	

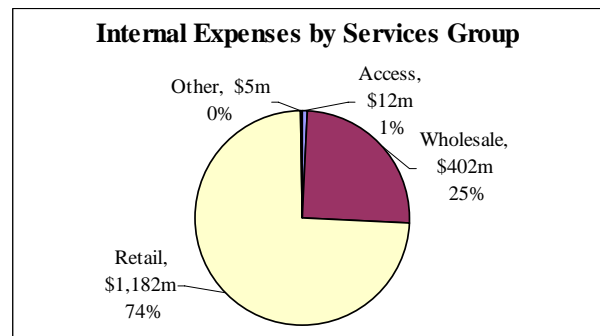
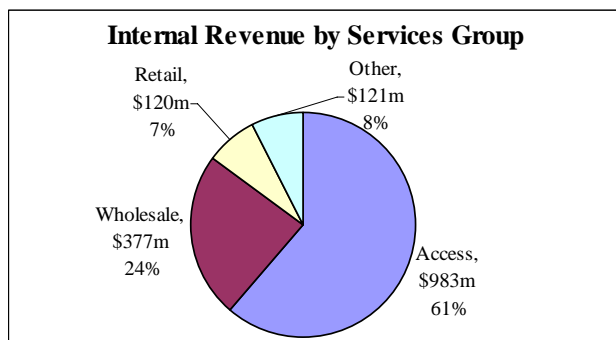
43. The illustration below describes the nature and magnitude of both the internal flows between the Services Groups, and the external revenue and expense flows between the Services Groups and its external customers and service providers.
44. In 2009, Telecom’s total of \$1.6 billion of internal services was provided by Services Groups to other Services Groups. These consist of transactions under structured trading arrangements and transactions where the value of the services provided has been estimated by management, with the total being collectively known as internal transfer charges<sup>25</sup>. The internal transactions are significant, making up 22% of the \$7.2 billion of total revenue for regulatory purposes as reported by Telecom in the regulatory financial statements. This quantifies the significance of Telecom’s structure as a vertically integrated telecommunications operator.

<sup>25</sup> Internal transfer charges are those transactions that take place between Telecom owned or managed business units. External transactions take place between Telecom business units and outside suppliers and customers.



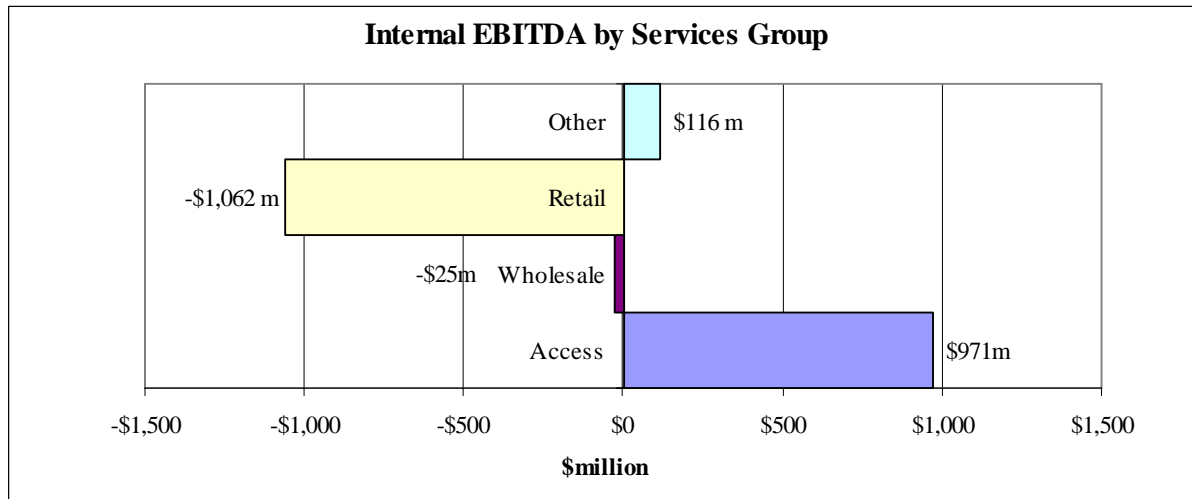
### 5.2.1 Internal Financial Performance

45. The two charts below show the shares of Telecom's internal revenue and internal expenses for which each Services Group is responsible. The internal expenses chart excludes depreciation.



46. The internal revenue chart shows the Access Services Group receives the highest share of the internal revenue at 61% (\$983 million), followed by the Wholesale Services Group at 24% (\$377 million). The Retail Services Group and the Other Services Group receive the lowest share at 7% (\$120 million) and 8% (\$121million) respectively.
47. The internal expenses chart shows the Retail Services Group incurs the highest share of internal expenses at 74% (\$1.2 billion), the Wholesale Services Group follows at 25% (\$402 million), the Access Services Group is third at 1% (\$12 million), and the Other Services Group incurs the smallest share at \$5 million.

48. The net impact of internal revenue less internal expenses at Services Group level is described in the graph below. This graph shows whether the internal earnings before interest, taxation, depreciation and amortisation (EBITDA) is a surplus or deficit and which Services Groups are net suppliers, and which are net consumers of internal services.<sup>26</sup>



#### Retail Services Group

49. The Retail Services Group is a net consumer of internal services. The major portion of the internal expenses is for the access services they purchase (i.e., UCLL and MPF) from the Access Services Group. The Retail Services Group conducts the majority of its business with external customers, indicated here by the negative net internal revenue of \$1.1 billion. They do, however, receive a small amount of internal revenue from the Wholesale Services Group, which resells a number of Retail services (mainly local phone service and broadband).

#### Wholesale Services Group

50. The largest portion of the Wholesale Services Group's expenses is also for services that they purchase from the Access Services Group (eg, UCLL, used to provide the Wholesale Services Group with bitstream services). The Wholesale Services Group's internal revenue is nearly all from the provision of broadband services to the Retail Services Group for resale to the end-user.

#### Access Services Group

51. The Access Services Group is a net supplier, providing most of its services to the Retail Services Group. In 2009, the Access Services Group received \$710 million of internal revenue from the Retail Services Group. The Access Services Group also supplies services to the Wholesale Services Group. The main services consumed being UCLL, MPF, backhaul and field services. The Access Services Group consumes only a small amount of internal services resulting in a net internal revenue surplus of \$971 million.

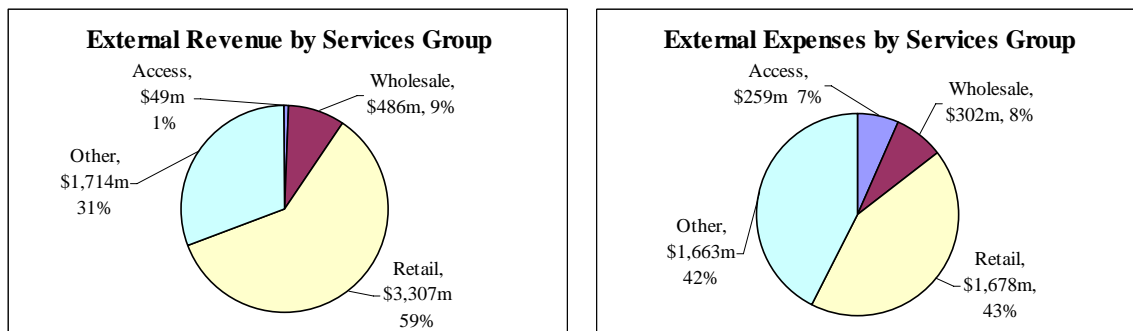
<sup>26</sup> In order to review and assess the detail of the internal transfer charges, the Commission requires product statements, which will be available in Telecom's 2010 regulatory financial statements.

### Other Services Group

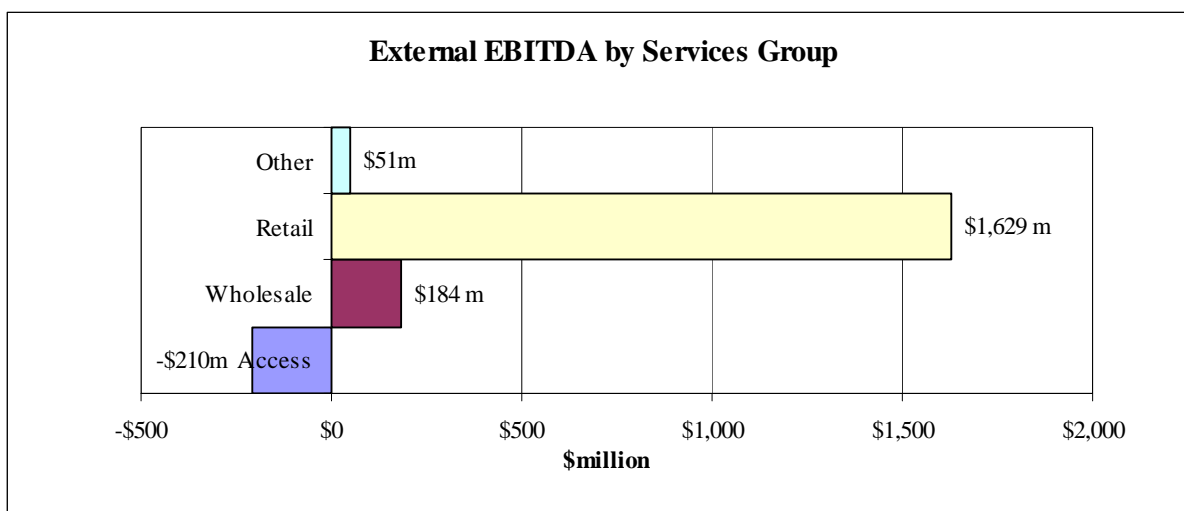
52. Internal transactions within the Other Services Group are very small in comparison to the other three Services Groups.

#### **5.2.2 External Financial Performance**

53. The two charts below show the split of Telecom's external revenue and external expenses across the Services Groups. The external expenses chart excludes depreciation.
54. These charts describe the shares of Telecom's total external revenue and expenses for which each Services Group is responsible. It shows that the Retail Services Group has the highest share of Telecom's external revenue at 59% (\$3.3 billion), followed by the Other Services Group at 31% (\$1.7 billion), the Wholesale Services Group at 9% (\$486 million), and the Access Services Group at 1% (\$49 million).



55. The external expenses chart shows that the Retail Services Group also incurs the highest share of Telecom's external expenses at 43% (\$1.7 billion), followed by the Other Services Group at 42% (\$1.7 billion). The Wholesale Services Group and the Access Services Group receive the lowest share at 8% (\$302 million) and 7% (\$259 million) respectively.
56. The net impact of external revenue less external expenses at Services Group level is summarised in the graph below, which provides a view as to which Services Groups are net suppliers and which are net consumers of external services.



### Retail Services Group

57. The Retail Services Group's external revenue, at \$3.3 billion, is generated mainly from the sale of retail mobile and fixed line products for voice and broadband services. At 30 June 2009, Telecom had a 47% share of the retail mobile connections market, 75% of retail fixed lines and 61% of the retail broadband connections market<sup>27</sup>.
58. The Retail Services Group's external expenses are, in part, for personnel costs and other external costs, but the largest single portion is for external cost of sales. The Retail Services Group's business is nearly all external, which shows in the external EBITDA surplus of \$1.6 billion.

### Wholesale Services Group

59. For the Wholesale Services Group, external customers generate \$486 million of revenue from the purchase of services such as bitstream products, fixed line rental, and voice interconnection. These services are the inputs that the Wholesale Services Group's customers need to provide products to their own customers. The Wholesale Services Group's external expenses are a mix of management and network expenses with the most significant item being external interconnection charges from other networks. The Wholesale Services Group generates an external EBITDA of \$184 million.

### Access Services Group

60. The Access Services Group is the supplier of access copper lines (UCLL and Sub-Loop) and other products such as co-location, field services, and UCLL backhaul to external customers. All of these products are necessary inputs to allow the Access Services Group's external customers (i.e. access seekers) to provide service to its own customers. The Access Services Group's revenue from external customers is the smallest of the Services Groups at \$49 million, but is consistent with the take-up by access seekers observed since the introduction of unbundled copper lines. The Access Services Group's external expenses are dominated by charges for field services while there are also a small amount of management expenses. The Access Services Group's external business reports a negative EBITDA of \$210 million.

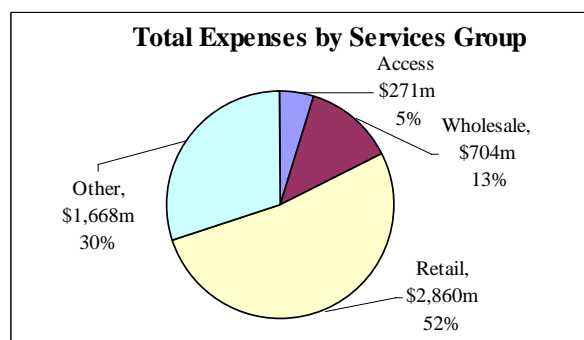
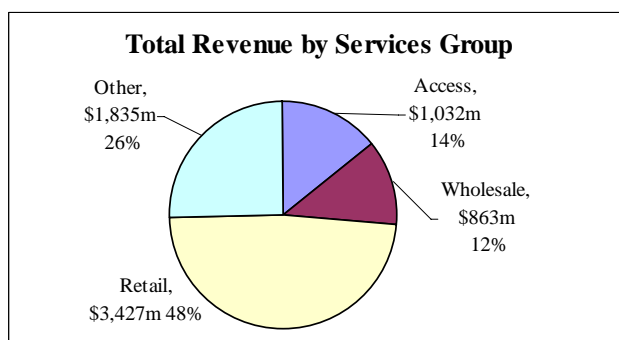
<sup>27</sup> Source: Commerce Commission.

### Other Services Group

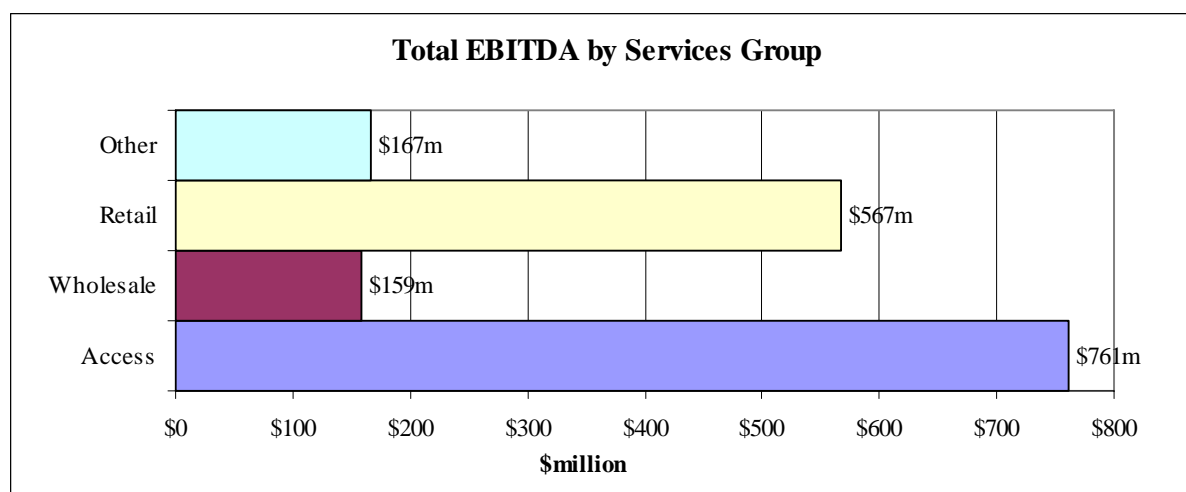
61. The Other Services Group receives \$1.7 billion of external revenue from external customers, largely for international services, corporate financial transactions and overseas activities. The Other Services Group's external expenses are a mixture of cost of sales, and (significantly) for intercarrier costs in Australia. Like the Wholesale Services Group, the Other Services Group has a mix of internal and external business, though it generates only a small external EBOTDA of \$51 million.

### ***5.2.3 Total Financial Performance***

62. The two charts below show the total of the internal and external revenues and expenses across the Services Groups. Total financial performance is the sum of internal and external EBITDA and as such it excludes each Services Group's share of depreciation which is reported in the Services Group HCA Financial Performance in section 5.2.



63. The total revenue chart shows the Retail Services Group has the largest absolute share of total revenue at 48% (\$3.4 billion) and, correspondingly, the largest absolute share of total expenses at 52% (\$2.9 million).
64. The Access Services Group and the Wholesale Services Group both have smaller shares of total revenue and total expenses. The Access Services Group has 14% (\$1.0 billion) of total revenue and 5% (\$271 million) of total expenses; the Wholesale Services Group has 12% (\$863 million) of total revenue and 13% (\$704 million) of total expenses.
65. The Other Services Group has the second highest share of total revenue at 26% (\$1.8 billion) and total expenses at 30% (\$1.7 billion).
66. The net impact of total revenue less total expenses before depreciation expense<sup>28</sup> (EBITDA) is summarised in the graph on the following page for the Services Groups.



67. The Access Services Group shows the highest total EBITDA at \$761 million, followed by the Retail Services Group at \$567 million, the Wholesale Services Group \$159 million, and the Other Services Group \$167 million.

<sup>28</sup> The absence of product reporting in 2009 does not allow depreciation to be allocated to internal and external services. As a consequence, depreciation is excluded from the total financial performance.

68. This EBITDA result is the combination of internal and external performance but does not include depreciation expense. The impact of deducting depreciation for each Services Group is reported in the table on page 13 (see Services Group HCA Regulatory Statement of Financial Performance). This table shows the Access Services Group reporting the highest EBIT of \$594 million and the Retail Services Group at \$185 million (after deducting depreciation and amortisation).

### 5.3 Services Group CCA Regulatory Statement of Financial Performance

69. The CCA Regulatory Statement of Financial Performance for the Services Groups reports the same internal and external revenues and expenses as reported under HCA with the (important) exception of revaluation gains/losses and depreciation. Accordingly, the revenue and expense analyses discussed previous to this section do not change for CCA above EBITDA in the Statement of Financial Performance.
70. The impact on financial performance of the CCA revaluations is reported in the table below as CCA adjustments which include increases in reported depreciation expense and any revaluation gains or losses<sup>29</sup> due to the CCA revaluation over HCA.
71. The CCA adjustments lead to either an increase or decrease in reported EBIT. The table below summarises the CCA Regulatory Statement of Financial Performance by Services Group.

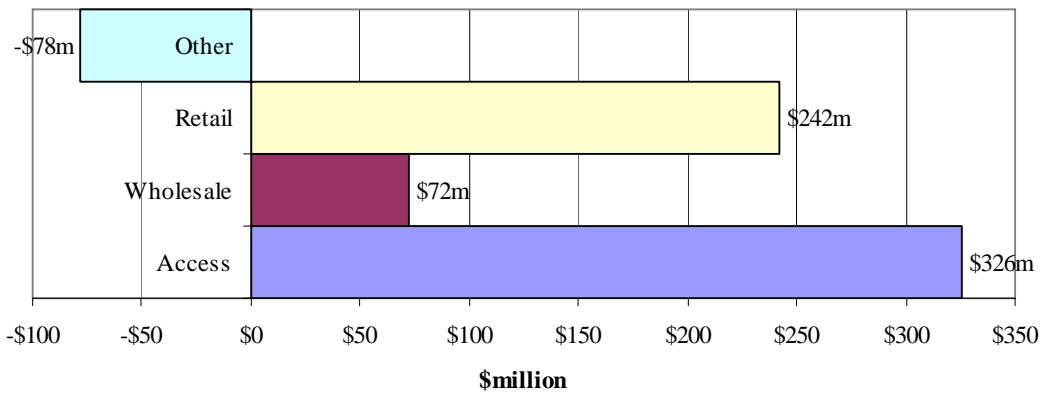
#### Services Group CCA Regulatory Statement of Financial Performance Comparison

<b>Year ended 30 June 2009</b>	Access	Wholesale	Retail	Other	Total
<b>\$million</b>	Services	Services	Services	Services	
	Group	Group	Group	Group	
Earnings after depreciation and amortisation	594	37	185	(79)	737
CCA adjustments	268	(35)	(57)	(1)	175
Earnings before interest and taxation	326	72	242	(78)	562
<i>Earnings before interest and taxation %</i>	<i>58%</i>	<i>13%</i>	<i>43%</i>	<i>-14%</i>	<i>100%</i>

72. The Access Services Group has a significant CCA adjustment expense of \$268 million, made up of an additional \$382 million in reported depreciation expense but offset by \$114 million in revaluation gains. These adjustments largely relate to the increased revaluation of the passive network.
73. The CCA adjustments in the other three Services Groups result in increases to the EBIT, predominantly driven from gains in the revaluation of its respective fixed assets. The Wholesale Services Group's revaluation gain of \$31 million (plus a \$4 million depreciation recovery) is mainly attributable to a revaluation of the legacy PSTN platform and the active transmission equipment.
74. The Retail Services Group's revaluation gain of \$86 million (less \$29 million depreciation expense) is mainly attributable to the legacy PSTN platform and to mobile assets.
75. Under CCA financial performance, the Access Services Group reports the highest EBIT at \$326 million. The Retail Services Group reports \$242 million, the Wholesale Services Group \$72 million, and the Other Services Group shows a loss of \$78 million.

<sup>29</sup> A revaluation gain (or loss) is the increase (or decrease) in the value of an asset due to the asset being revalued under CCA.

### CCA EBIT by Services Group



## 6. Summary - Financial Position

76. The Regulatory Statement of Mean Capital Employed summarise the operating capital employed; that is, the net operating assets for Telecom as a whole entity, as well as for the separate Services Groups.
77. The Regulatory Statement of Mean Capital Employed is similar to, but is not the same as, the statutory Balance Sheet in Telecom's Annual Report. The primary differences are that:
- The Regulatory Statement of Mean Capital Employed describes the operating capital used to provide products and services to customers. As such it does not try to describe how the operating capital is funded and therefore debt funding components such as debt and equity are excluded from the Regulatory Statement of Mean Capital Employed.
  - Operations are reported without distinguishing whether they are funded by debt or equity or accounting for interest payments, whereas the statutory financial statements account for interest payments and present opening and closing equity positions. Regulatory financial statements report the average or mean capital figure over the financial year.
  - In relation to net assets, the statutory balance sheet records shareholder funds as net total assets. This compares to regulatory reporting which only records the value of operating assets, and is not concerned with non-operating assets such as goodwill.

### 6.1 Consolidated Statement of Mean Capital Employed

78. The table below compares the consolidated Regulatory Statement of Mean Capital Employed in Telecom's 2009 regulatory financial statements with the corresponding statutory Balance Sheet contained in Telecom's 2009 Annual Report.

<b>Consolidated Statement of Capital Employed Comparison</b>			
<b>Year ended 30 June 2009</b>			
	HCA Statutory <sup>1</sup>	HCA Regulatory	CCA Regulatory
<b>\$million</b>			
Current assets	1,188	1,266	1,266
Non-current assets	5,848	5,135	9,698
<b>Total assets</b>	<b>7,036</b>	<b>6,401</b>	<b>10,964</b>
Current liabilities	1,483	1,159	1,159
Non-current liabilities	2,837	0	0
<b>Total liabilities</b>	<b>4,320</b>	<b>1,159</b>	<b>1,159</b>
<b>Capital Employed</b>	<b>2,716</b>	<b>5,242</b>	<b>9,805</b>

<sup>1</sup> HCA statutory financial statements are contained in Telecom's 2009 Annual Report

79. Current assets, included in both the regulatory columns, consist of cash and short-term investments, receivables and prepayments. The 2009 statutory current assets are lower than the current assets reported in the 2009 regulatory columns due to the exclusion of inter-business receivables and inclusion of tax recoverable in the statutory total.

80. The current liabilities consist of accounts payable and accruals, short-term provisions and short term liabilities. The statutory current liabilities are higher due to the inclusion of \$385 million of debt due within one year, while it should be noted that the statutory total also excludes internal inter-business payables.
81. Non-current assets in the statutory column include both fixed assets and long-term financial assets, while both regulatory columns include only fixed assets.
82. The statutory non-current liabilities of \$2.8 billion consist of long-term debt and other liabilities. This is not included in the regulatory columns for the reasons noted above.

## 6.2 Services Groups Statement of Mean Capital Employed

### 6.2.1 Services Group HCA Regulatory Statement of Mean Capital Employed

83. The table below summarises the HCA Regulatory Statement of Mean Capital Employed for the four Services Groups from Telecom's regulatory financial statements.

<b>Services Group HCA Regulatory Statement of Mean Capital Employed Comparison</b>					
<b>Year ended 30 June 2009</b>	Access	Wholesale	Retail	Other	Total
<b>\$million</b>	Services	Services	Services	Services	
	Group	Group	Group	Group	
Current assets	222	115	583	346	1,266
Non-current assets	1,747	609	1,797	982	5,135
Total assets	1,969	724	2,380	1,328	6,401
Total assets %	31%	11%	37%	21%	100%
Current liabilities	69	124	602	364	1,159
Total liabilities	69	124	602	364	1,159
Mean capital employed	1,900	600	1,778	964	5,242
Mean capital employed %	36%	11%	34%	18%	100%

84. The Access Services Group records the highest HCA mean capital employed at \$1.9 billion. The Retail Services Group is next at \$1.8 billion, followed by the Other Services Group at \$1.0 billion, and the Wholesale Services Group at \$0.6 billion.
85. Mean capital employed is largely represented by fixed assets that are attributed to the Access Services Group and the Retail Services Group, which have the largest asset values at \$1.7 billion and \$1.8 billion respectively. Their fixed assets mainly comprise network plant and equipment and network systems.
86. The Retail Services Group and the Other Services Group show higher current assets and liabilities than either the Access Services Group or the Wholesale Service Group simply because of their higher volume of internal and external business than those Groups.

### 6.2.2 Services Group CCA Regulatory Statement of Mean Capital Employed

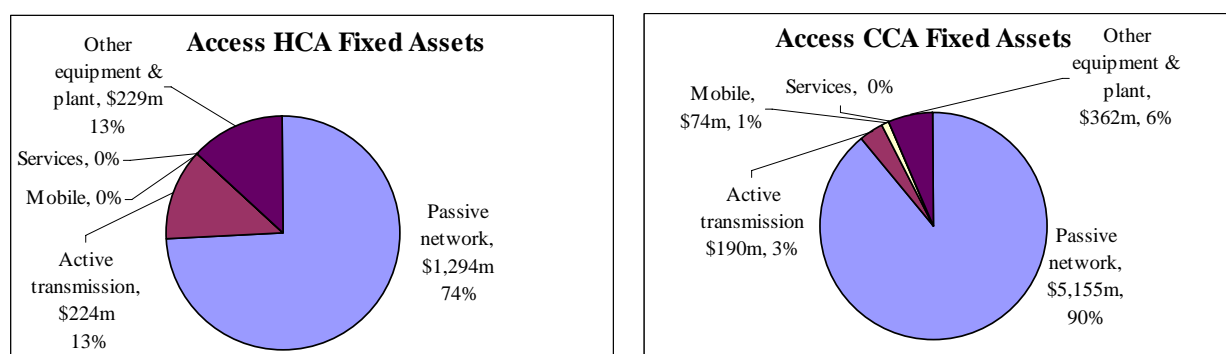
87. Telecom was required to provide regulatory financial statements using CCA. Under this requirement, both current assets and current liabilities are the same in the CCA Regulatory Statement of Mean Capital Employed for the Services Groups as those reported in the HCA Regulatory Statement of Mean Capital Employed.
88. The table below summarises the CCA Regulatory Statement of Mean Capital Employed for the four Services Groups from Telecom's regulatory financial statements.

<b>Services Group CCA Regulatory Statement of Mean Capital Employed Comparison</b>					
<b>Year ended 30 June 2009</b>	Access	Wholesale	Retail	Other	
<b>\$million</b>	Services	Services	Services	Services	Total
	Group	Group	Group	Group	
Current assets	222	115	583	346	1,266
Non-current assets	5,781	714	2,188	1,015	9,698
<b>Total assets</b>	<b>6,003</b>	<b>829</b>	<b>2,771</b>	<b>1,361</b>	<b>10,964</b>
<i>Total assets %</i>	<i>55%</i>	<i>8%</i>	<i>25%</i>	<i>12%</i>	<i>100%</i>
Current liabilities	69	124	602	364	1,159
<b>Total liabilities</b>	<b>69</b>	<b>124</b>	<b>602</b>	<b>364</b>	<b>1,159</b>
<b>Mean capital employed</b>	<b>5,934</b>	<b>705</b>	<b>2,169</b>	<b>997</b>	<b>9,805</b>
<i>Mean capital employed %</i>	<i>61%</i>	<i>7%</i>	<i>22%</i>	<i>10%</i>	<i>100%</i>

89. The Access Services Group reports the highest mean capital employed under CCA valuation totalling \$5.9 billion, followed by the Retail Services Group at \$2.2 billion, the Other Services Group at \$1.0 billion, and the Wholesale Services Group at \$0.7 billion.
90. This is largely represented by fixed assets with the Access Services Group and the Retail Services Group having the larger asset values of \$5.8 billion and \$2.2 billion respectively. The large difference between the Access Services Group's HCA and CCA fixed assets valuations is analysed below.

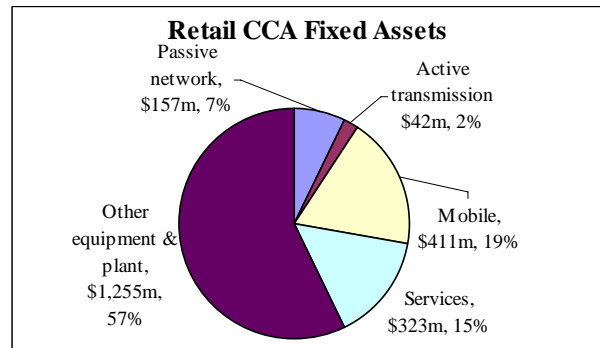
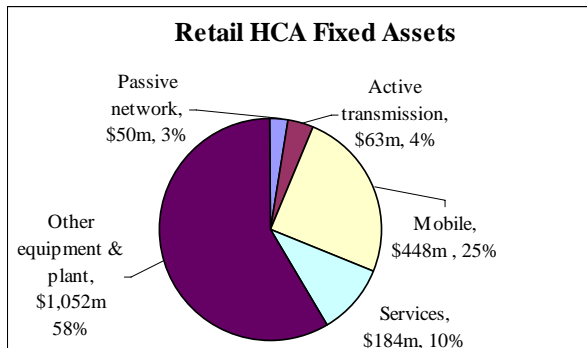
### 6.3 Fixed Assets

91. Telecom prepared regulatory financial statements using two fixed asset valuation methodologies. HCA is the conventional accounting method, where fixed assets are valued at cost recorded at the time of their purchase and subsequently depreciated. In contrast, CCA methodologies value fixed assets at current cost, which is then depreciated.
92. The two charts below give a comparison between the HCA and CCA values of the Access Services Group's fixed assets, as the Access Services Group's fixed assets are the largest contributor to the total mean capital employed.
93. Both charts show that the largest share of the Access Services Group's fixed assets for both HCA and CCA is in the value of the passive network. The passive network valuations are significantly different between HCA at \$1.3 billion (74% of the total), and CCA at \$5.2 billion (90% of total fixed assets).

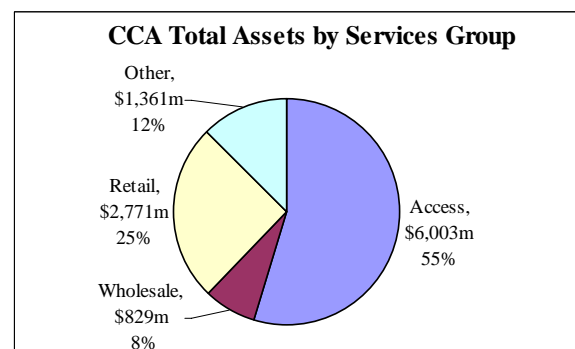
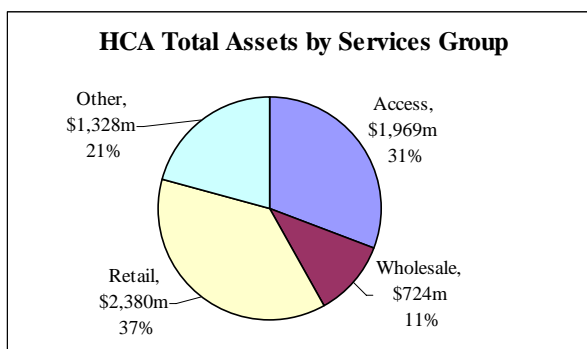


94. In a similar manner, the two charts below give a comparison between the HCA and CCA values of the Retail Services Group's fixed assets. In the Retail Services Group, the

largest share is in ‘other plant and equipment’, which includes systems hardware and software. Both valuations are relatively close, with HCA at \$1.1 billion (58% of total) and CCA at \$1.3 billion (57%). The Retail Services Group fixed assets include newer mobile XT network assets, as well as other new software and systems related assets.



95. The comparison of Services Groups total assets in the two charts below emphasises the significance of the valuation uplift in the Access Services Group. Excluding this uplift, the HCA and CCA valuations are similar.



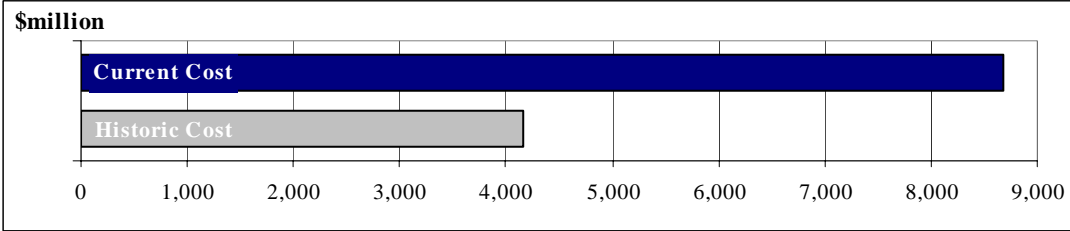
### 6.3.1 Fixed Asset Valuations

96. Telecom prepared regulatory financial statements using two asset valuation methodologies. HCA is the conventional accounting method, where fixed assets are valued at the cost recorded at the time of their purchase and subsequently depreciated. In contrast, CCA methodologies prescribe the valuation of fixed assets at current cost with the appropriate level of depreciation. Both approaches have advantages and disadvantages associated with them.<sup>30</sup>
97. The net replacement CCA asset valuation applied by Telecom is more than twice the HCA net book value of the same fixed assets: HCA of \$4.2 billion (excluding Other Services Group) increases to CCA of \$8.7 billion, resulting in a 107% uplift<sup>31</sup> of \$4.6 billion.

<sup>30</sup> The specific applications of HCA and CCA are discussed further on pages 22-26 of the Commission’s Companion Paper to the Requirements.

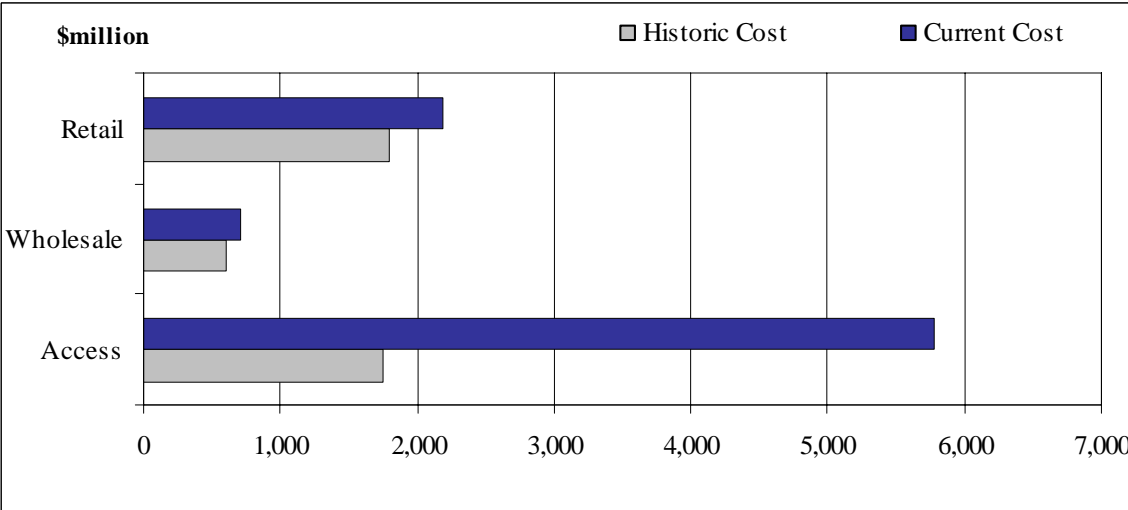
<sup>31</sup> The valuation uplift is the increase in the asset valuation base over HCA resulting from the application of CCA valuation methodologies.

**Comparison of Asset Valuation Methodologies (HCA vs. CCA)**



- 98. Telecom’s total valuation uplift is high compared to telecommunications companies such as BT in the United Kingdom where the equivalent uplift is approximately 10%<sup>32</sup>. Thus size of Telecom’s total valuation uplift through revaluation is significantly higher than would be expected based on overseas experience. In its draft decision on proposed changes to the Requirements, the Commission has recommended introducing a number of changes to Telecom’s valuation methodologies in order to remove from the reported CCA valuation any excess capacity, additional functionality and fully written down assets. If the latter proposed change had been implemented in 2009, it would have resulted in a devaluation of Telecom’s CCA fixed asset values by \$711 million. It is unknown at this stage the impact of the other proposed changes.
- 99. A breakdown of the uplift (see graph below) shows that 89% (\$4.0b) of the \$4.6 billion asset valuation uplift is in the Access Services Group. Any CCA valuation uplift for the Access Services Group will increase the reported regulatory costs for that Services Group, and is likely to result in lower reported earnings compared with that reported under HCA valuation. This effect will be significant at the Services Group level, and also at product statement level, for which Telecom is required to publish Product Statements in 2010.

**Services Group Valuation Uplift Comparison**



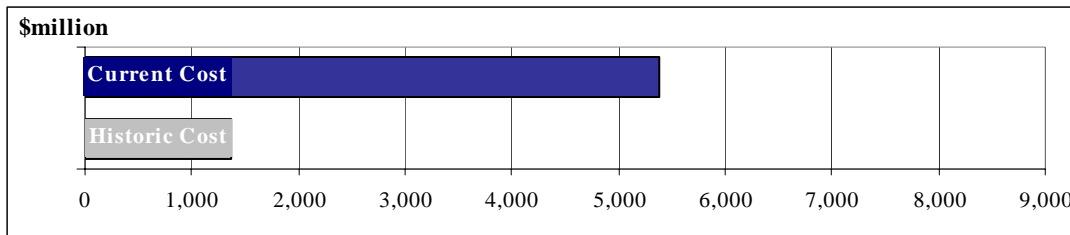
- 100. The majority of the uplift in the Access Services Group is in the passive network. The passive network contains trenches with ducts, trenches without ducts, ducts, copper cables, copper joints, fibre cables and fibre joints. It is an essential input to deliver all fixed line

<sup>32</sup> BT reported a CCA adjustment in the 2008 MCE reconciliation statement of \$1.6b compared with BT’s HCA fixed asset (property, plant and equipment) total in their annual report of \$15.3b.

based services such as voice and broadband services to customers. Telecom Retail and other wholesale customers use parts of the passive network such as UCLL as an input to provide their services.

101. Under HCA, the value of the passive network is \$1.4 billion, 33% of the total fixed assets value of \$4.2 billion (excluding Other Services Group). In contrast, CCA shows the passive network is \$5.4 billion, 62% of the total fixed assets value of \$8.7 billion.
102. The absolute size of the value uplift of the passive network elements can be seen in the following illustration.

### Impact of Asset Valuation Methodology on Value of Passive Network



## 7. Analysis - Financial Performance

103. The Commission conducted a review of Telecom's Regulatory Financial Statements, including the supporting manuals that describe the policies and methodologies that Telecom used in preparing the statements.
104. HCA regulatory financial statements provide an indication of the relative performance of each Services Group compared to the statutory financial statements (as shown below in the HCA columns).

<b>The Relative Regulatory Financial Performance by Service Group</b>					
<b>Year ended 30 June 2009</b>	HCA Total External Revenue	HCA Total Revenue	HCA Earnings before Depn (EBITDA)	HCA Earnings after Depn (EBIT)	CCA Earnings after Depn (EBIT)
Access	1%	14%	46%	81%	58%
Wholesale	9%	12%	10%	5%	13%
Retail	60%	48%	34%	25%	43%
Other	31%	26%	10%	-11%	-14%
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

105. However, the value of Telecom's internal transfer charges is significant at \$1.6 billion, and has a direct and material effect on the reported financial performance of the Services Groups.

### Access Services Group

106. The Access Services Group generates only 1% of external revenues as would be expected given that it largely supplies the other Services Groups with services to sell at retail and wholesale.
107. However, when internal transfers are taken into account, the Access Services Group's share of total revenue for regulatory purposes is 14% of the Telecom's reported revenue. As previously discussed and in the Commission's draft decision on proposed changes to the Requirements, the Commission does not have sufficient documentation regarding Telecom's internal trading arrangements to assess whether this level of revenue is reasonable.
108. From total revenue, the Access Services Group returns 46% of Telecom's EBITDA, whilst after HCA depreciation is removed, it returns 81% of Telecom's EBIT. This improvement in financial performance after depreciation may be explained by the fact that much of the passive network is old and written down for HCA, and as such the depreciation charge is relatively low compared, for example, to the new assets in the Retail Services Group.
109. This can be seen in the CCA column, where the application of the CCA valuation increases the depreciation expense, with a corresponding drop in the Access Services Group's relative EBIT contribution to Telecom's EBIT, from 81% under HCA to 58% under CCA. Both EBIT contributions are high, which may simply reflect the higher valuation of the passive network. However, as previously discussed and in the Commission's draft decision on proposed changes to the Requirements, the Commission does not have sufficient information regarding Telecom's internal trading arrangements

and attribution and valuation processes to assess whether this level of EBIT is reasonable. This is intended to be addressed with changes to the 2010 Requirements.

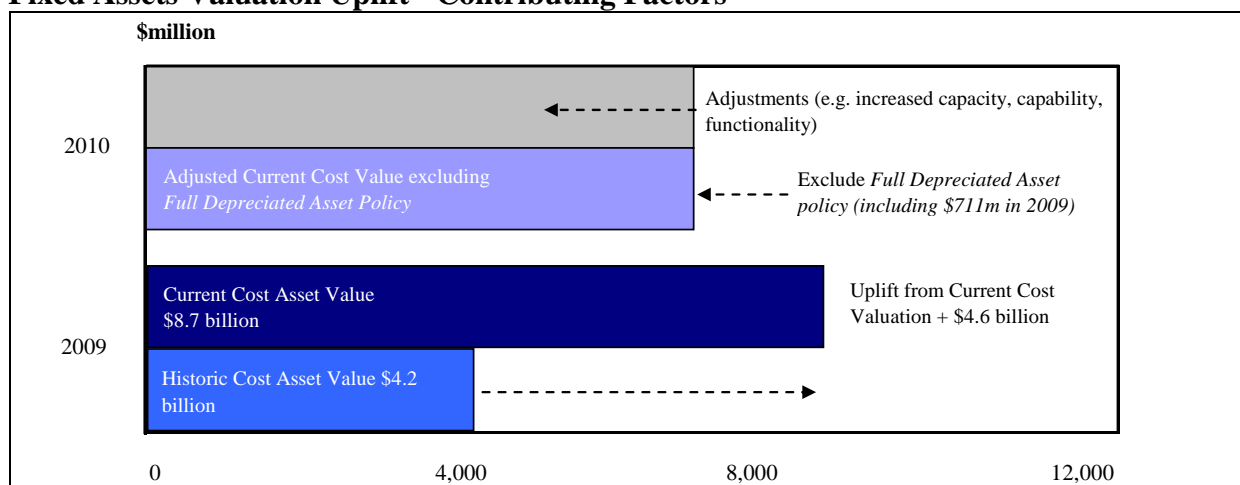
#### Retail Services Group

110. Retail receives 60% of external revenues, which reduces to 48% of Telecom's revenue when the internal trading arrangements are included for regulatory purposes. As discussed above, the Commission does not yet have sufficient information regarding Telecom's internal trading arrangements to assess whether this level of revenue is reasonable.
111. The Retail Services Group records EBITDA of 34% and EBIT of 25% on 48% of Telecom's earnings. The Retail Services Group's EBIT increases to 43% after the CCA adjustments are made. This appears to be a relatively high contribution for the Retail Services Group. However, as raised above, the Commission does not have sufficient information regarding Telecom's internal trading arrangements and attribution and valuation processes to assess whether this level of EBIT is reasonable. The Commission has proposed changes to address this issue in its draft decision on the 2010 Requirements.

## 8. Analysis - Financial Position

112. The valuation uplift to the passive network in the Access Services Group at \$4.6 billion is reported in the Regulatory Statement of Mean Capital Employed.
113. The passive network is used to provide fixed telecommunications services, and in particular regulated services such as UCLL. As a result, the CCA valuation adjustments will have a direct impact and will increase reported regulatory costs in the Access Services Group's product statements over and above reported HCA costs.
114. The Commission review has revealed a number of factors that have caused the valuation uplift. The following chart illustrates the impact that various factors within Telecom's CCA valuation methodology can have on the overall fixed asset valuation.

### Fixed Assets Valuation Uplift - Contributing Factors



115. In the 2009 regulatory financial statements, fixed assets that were fully depreciated under HCA were re-valued under CCA (referred to as the "fully depreciated asset policy"). These assets contributed to the large difference between the CCA and the HCA values. The Commission has proposed changes to the Requirements for regulatory reporting whereby this policy is not used for CCA in the future. This would have resulted in a CCA value that is \$711 million lower in 2009.
116. A second area leading to the higher valuation uplift for CCA may be explained by the application of methodologies where CCA fixed asset values have been valued at replacement cost that do not correspond to the actual functionality of the existing network. Where existing and used fixed assets have been valued on the basis of modern technologies (for example, using the Modern Equivalent Asset valuation methodology) efficiency adjustments have to be made to take into account the additional functionality or capability associated with these equipment. For example, new equipment may be longer lived, and able to handle higher volumes of a service or an increased number of services.
117. A third area leading to a higher-than-expected CCA valuation is the inclusion of excess capacity that is not being utilised in the existing network. The current value of the underlying assets should reflect the efficient cost of providing telecommunications services, and to the extent that assets are not being utilised, valuations that fail to adjust for overcapacity may represent a level of overinvestment.
118. For fixed assets that are not subject to significant technological change (i.e. the passive elements of a network such as trenches), replacement techniques may lead to an over-estimation of costs an entity is facing and therefore HCA values may better reflect the

underlying cost. Where Telecom has replaced its fixed assets before the end of their useful life, and is able to demonstrate the appropriateness of the investment (i.e. taking into account excessive capacities), replacement values can be used.

## 9. List of Terms and Abbreviations

<b>Access Services Group</b>	<p>The Services Group consisting of all business activities and services provided by Telecom's ANS Unit as if it was operated as an independent or unrelated company, including –</p> <ul style="list-style-type: none"><li>(i) all Relevant Network Access Services;</li><li>(ii) any services provided over Telecom's Local Access Network;</li><li>(iii) that portion of Shared Services activities provided in support of any of the foregoing.</li></ul> <p>but excluding any activities or services attributable to another Services Group.</p>
<b>Annual Report</b>	<p>The report prepared by Telecom under section 208 of the Companies Act 1993.</p>
<b>Business Unit</b>	<p>The internal structure that Telecom is organised into for its day to day operations. There are five customer facing business units: Chorus, telecom Wholesale (including International), Telecom Retail, Gen-I Australasia and AAPT and two support centres: Shared services and Corporate.</p>
<b>Commission</b>	<p>The Commerce Commission established by section 208 of the Companies Act 1993.</p>
<b>Compliance Monitoring Information</b>	<p>Information Telecom provided to the Commission for the purpose of monitoring Telecom's compliance with the Accounting Separation Requirements.</p>
<b>Financial Year</b>	<p>The period of 12 months commencing on 1 July in any year and ending with 30 June in the following year.</p>
<b>Current Cost Accounting</b>	<p>Assets are valued at their replacement cost using current market prices.</p>
<b>Historical Cost Accounting</b>	<p>Assets are valued at cost at the time of their purchase.</p>
<b>Independent Auditor</b>	<p>A person who –</p> <ul style="list-style-type: none"><li>(i) is qualified for appointment as auditor of a company under the Companies Act 1993;</li><li>(ii) has no relationship with, or interest in, Telecom that is likely to involve the person in conflict of interest;</li><li>(iii) has not assisted with the compilation of the information or provided advice or opinions (other than in relation to audit reports or in respect of the interpretation of the Requirements) on the methodologies or processes used in compiling the information; and</li><li>(iv) is not associated with nor directed by any person who has provided any such assistance, advice or opinion.</li></ul>
<b>Manuals</b>	<p>The documents prepared by Telecom which set out the methodologies used to prepare the regulatory financial statements.</p>
<b>NZ GAAP</b>	<p>Generally Accepted Accounting Practice as defined in section 3 of the Financial Reporting Act 1993.</p>

<b>Other Services Group</b>	The Services Group consisting of – <ul style="list-style-type: none"> <li>(i) all activities and services provided outside New Zealand; and</li> <li>(ii) all activities and services provided (or necessary for the provision of) all services provided by Telecom but not provided by the Access Services Group, Wholesale Services Group, or the Retail Services Group, including Telecom’s corporate management and international services.</li> </ul>
<b>Part 2B</b>	Part 2B of the Telecommunications Act 2001.
<b>Product Statement</b>	Financial Statement summarising revenues, expenses and supporting information in accordance with the form of the report in the Requirements.
<b>Regulatory Financial Statements</b>	The Regulatory Statements of Financial Performance, the Regulatory Statements of Fixed Assets, and the Regulatory Statements of Mean Capital Employed, and any consolidated version of these statements.
<b>Regulatory Statement of Financial Performance</b>	Financial statement summarising revenues and expenses for the applicable financial year in accordance with the form of report in the Requirements.
<b>Regulatory Statement of Mean Capital Employed</b>	Financial statement of the mean capital employed being the sum of the fixed assets, intangible assets, inventories and debtors less creditors, and any short term provisions; calculated as the average of the start capital employed and the end value for the financial year but excluding taxation provisions, dividends payable, short and long-term debt and goodwill for the financial year.
<b>Regulatory Statement of Fixed Assets Movements</b>	Financial statement describing the movement of fixed assets including the opening assets, the additions to assets including capital investments, the deductions from assets including depreciation and the closing assets.
<b>Requirements</b>	The Telecom Accounting Separation Information Disclosure Requirements for Financial Years ending 2009 and 2010 as issued by the Commission on 25 March 2009.
<b>Retail Services Group</b>	The Services Group consisting of all business activities and services provided by Telecom directly to end-users in New Zealand, including – <ul style="list-style-type: none"> <li>(i) those provided by Telecom’s Retail Unit;</li> <li>(ii) retail mobile services;</li> <li>(iii) those provided under the Gen-I brand; and</li> <li>(iv) those that would be provided by telecom’s Retail unit if it was operated as an independent or unrelated company, including that portion of Shared services activities provided in support of any of the foregoing;</li> </ul> but excluding any activities or services attributable to another Services Group.
<b>Services Group</b>	Any of the four categories in or to which all business activities and services of Telecom must be allocated and/or attributed; being the Access

Services Group, the Wholesale Services Group, the Retail Services Group and the Other Services Group.

**Telecom** Telecom Corporation of New Zealand Limited and any of its subsidiaries.

**Wholesale Services Group** The Services Group consisting of all business activities and services provided by Telecom on a wholesale basis, whether internally to Telecom or externally to another service provider, including –

- (i) relevant Wholesale Services; and
- (ii) any activities or services that would, if the Wholesale Unit was operated as an independent or unrelated company, be attributable to the Wholesale Unit, including wholesale mobile services and that portion of Shared Services activities provided in support of any of the foregoing.