



**NEW ZEALAND INSTITUTE FOR THE STUDY
OF COMPETITION AND REGULATION**

FIT FOR PURPOSE?

Examining the Current State of Broadband Regulation in New Zealand

Bronwyn Howell,
General Manager
May 8 2013

CORPORATE MEMBERS

Contact Energy
Fonterra Co-Operative Dairy Group
Meridian Energy
Powerco
Telecom Corporation of New Zealand Ltd
Victoria University of Wellington
Westpac Institutional Bank

AGENDA

1. Some context
2. The problem(s)
3. The forthcoming Inquiry **must** address the problem(s)
4. What next?



1. SOME CONTEXT



“Chorus yesterday dodged a bullet from regulators only to step into the path of a rumbling tank.”

Tom Pullar-Strecker, Stuff, December 4 2012



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CONTEXT (cont)

3 December 2012

- draft wholesale bitstream prices from 1 December 2014 announced
 - fall from \$44.98 to \$32.45 per month
- Chorus shares fell 20% amidst feverish trading

It could have been worse

- simultaneous announcement of revision of draft (re-averaged) LLU price
 - revised upwards from \$23.52 from \$19.75 as announced on May 4
 - Chorus shares fell 15% following May announcement, with similarly large trading volumes



THE REACTION

“Prime Minister John Key has indicated the Government would change the law rather than see its ultra-fast broadband network compromised by a Commerce Commission decisionbecause consumers could be discouraged from switching from copper to fibre”

» Radio New Zealand, 3.10pm , 4 December 2012

Moody's put Chorus' "Baa2" issuer and senior unsecured ratings on review for possible downgrades.

Decision if implemented is “inconsistent with a Baa2 profilethe potential for a final adverse outcome on Chorus’ credit profile is meaningful”

» Maurice O’Connell, Senior Analyst, Stuff 4 December 2012



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THE REACTION (cont)

The Government's response, however, is unprecedented. It is a fundamental principle of our telecommunications regulatory regime that the regulator is independent, and is left to carry out its statutory role without interference or undue influence from the Government. The Government, by entering into the media debate, and criticising the draft determination in such clear terms that a rating agency has concluded the issue will be resolved politically, has crossed that line. “

- » Former Telecommunications Commissioner Dr Ross Patterson, Stuff, December 10 2013



THE REACTION (cont)

“I don't recall anyone voting for the Commerce Commission to deliver New Zealand superior infrastructure. It was John Key who was mandated by the public to deliver a step-change in New Zealand's infrastructure.

From a public policy perspective, it is wrong for government organisations like the Commerce Commission to be delivering changes that are hugely at odds with the government's desire to deliver on fibre, and where the government itself is spending huge sums of taxpayer money to deliver outcomes.

At the very least, the commission should seek some determinations from government ministers on taking into account how its operational framework works with mandated government flagship policies.”

» Investor Aaron Bhatnagar,
NBR December 4 1012



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THE REACTION (cont)

“The draft price would have come as no surprise to anyone who had read the legislation and understood the industry. The existing retail-minus price was set by reference to Telecom's retail price, and bore no relationship to the costs of providing the service. It was common knowledge in the industry that a cost-based UBA price would be substantially lower than the prevailing retail–minus price.....Chorus' response to the draft determination (that it could require Chorus to fundamentally rethink its business model, capital structure and approach to dividends) comes as no surprise.”

» Patterson (ibid)



THE RESPONSE

February 8 2013:

“I have decided to bring forward the wider regulatory framework review as regulatory certainty is an important factor in the ability of New Zealanders to have early access to high-quality communication services based on new technologies,”

» Communications and Information Technology Minister Amy Adams

Telecommunications Act s 157AA

Minister must review regulatory framework beginning no later than 30 September 2016



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RE-REACTION

Chorus share price rises 9%

– but still 7% below December 2

“Amy Adams is taking almost \$400 right out of the pockets of Kiwi households with her delaying tactics on the Commerce Commission’s suggested price cuts”

» Labour Communications and IT Spokesperson Clare Curran,
Media Statement * February 2013

“Extending the UBA review means we have a half-house regulatory regime in place until after this new review has been completed....The government has chosen in effect to freeze that process and to leave the industry in limbo.”

» TUANZ CEO Paul Brislen, Blog, February 8 2013



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2. THE PROBLEM(S)

A 'half-house' regulatory regime since 2010 (at least)

A new investor (Government)

- with conflicting interests (investor/regulator/policy-maker)
- and not subject to normal commercial imperatives

An incoherent broadband market competition policy



A (REGULATORY) HOUSE DIVIDED

Crown Fibre Holdings regulates fibre *networks*

Telecommunications Commission regulates copper *networks*

Who regulates the ***BROADBAND MARKET?***

- including satellite, mobile, wireless network provision

And what is NZ's ***BROADBAND MARKET COMPETITION POLICY?***



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CROWN FIBRE REGULATES FIBRE NETWORKS

“Crown Fibre Holdings monitors compliance with the terms of the Ultra-Fast Broadband Initiative while the network is being built. This includes oversight of price caps, products, network construction and operation (especially quality assurance testing), as well as the Government’s investment in shares, financial instruments and governance.”

» <http://www.crownfibre.govt.nz/publications/regulatory/>

“The Commerce Commission monitors and enforces the deeds of undertakings made by the government’s Ultra-Fast Broadband partners, as well as other aspects of the Telecommunications Act 2001”

» Ibid



TELECOMMUNICATIONS COMMISSION REGULATES COPPER NETWORKS

“We have no statutory role in promoting or protecting fibre,” says Gale. “Our task in this larger project is just to fix the price of copper-based services. Retail service providers will then compete on whatever network they find most profitable.”

- » <http://computerworld.co.nz/news.nsf/news/new-wholesale-price-for-access-to-copper-network>



THE ACT (in relation to UBA, UCLL)

Specifies

- that a firm, and not a market is the regulatory subject
- the specific products to be controlled
- the exact nature of remedies applied

Assumes

- enduring, intractable natural monopoly
- over a single nationwide market

Assumes away

- the possibility that the regulated firm might not be (or could cease to be) dominant in any given sub-markets



THE COMPETITIVE REALITY

Customers buy ‘broadband connections’ not ‘network access’ in multi-technology, oligopoly markets

For many consumers and applications, the current networks are perfectly substitutable

Copper has never been a ‘natural monopoly’ w.r.t. broadband in New Zealand

- 2nd, and even 3rd entrant in some markets (geographical, customer definitions)
- not even dominant in some markets



NZ COMPETITION POLICY

“The New Zealand policy is that copper will be a competitive constraint on fibre, with uptake determined by market forces. If copper prices are set above cost to encourage fibre uptake, they will no longer constrain fibre prices, and uptake will no longer be market driven.”

» Patterson, op. cit.

But fibre prices are not set by competitive forces in the first place

- subsidised by government to promote other policy objectives
- can (potentially) be changed at any time
 - e.g. government policy changes, renegotiating the Crown Fibre agreements
- Act offers no ability for a ‘copper response’ to fibre ‘market’ changes
 - without recourse to further regulation



AND WHAT SORT OF ‘COMPETITION’?

Services-based?

- competition between retailers ‘on the network’
- presumes enduring, intractable natural monopoly network

Infrastructure-based?

- between networks of different ownership/technology
- the ultimate objective of LLU ‘ladder of investment’ policies



GOVERNMENT FIBRE NETWORK INVESTMENT

Makes infrastructure competition inevitable

- fundamental change to competitive landscape

But regulation of copper network is largely unchanged

- identical products, identical remedies to 2006 reviews
- with minor adjustments to deal with Telecom structural separation
 - e.g. UBA price setting methodology changed from retail-minus to cost-plus



INCONSISTENT UFB, REGULATORY POLICIES

What is the purpose of the fibre investment?

To provide infrastructure competition to copper?

- because existing policies have failed to deliver it?
 - then why persist with ‘failed’ copper regulation?
- but if infrastructure competition actually exists, then regulation to promote its creation is redundant
 - ‘old’ regulation cannot satisfactorily govern new competitive realities

To accelerate the rate of substitution from (legacy) copper to (frontier) fibre?

- then why persist with pretence that ‘competition’ and ‘market forces’ will drive substitution?



THE EVIDENCE

(in the absence of a single, clearly-articulated policy objective)

Accelerating infrastructure competition?

- appears supported by letting fibre contracts to non-Chorus partners in Northland, Central North Island, Christchurch
- but then why let the Auckland fibre contract to Chorus?
 - most likely region where LLU might lead to full infrastructure competition (if the ‘ladder of investment actually’ works)

Accelerating fibre substitution?

- appears supported by letting the Auckland contract to Chorus
- but then why introduce competition to Chorus in Northland, Central North Island, Christchurch?



THE PRESENT REALITY

Infrastructure competition prevails

- the mobile ‘challenge’

With different effects in different geographical markets

The Act is unfit for the purpose of regulating this reality

- backward-looking, not forward-focused
- regulates firms and networks, not markets
- takes a single nationwide approach to what are increasingly regional markets
- cannot cope with rapid changes in the commercial and political environment



3. THE INQUIRY

The LAST CHANCE to get the telecommunications regulatory framework settings right before fibre uptake 'takes off'



157AA Minister must review regulatory framework

(1)The Minister must, not later than 30 September 2016, commence a review of the policy framework for regulating telecommunications services in New Zealand, taking account of the market structure and technology developments and competitive conditions in the telecommunications industry at the time of the review, including the impact of fibre, copper, wireless, and other telecommunications network investment.

(2)The review must—

(a)consider whether the existing regulatory framework under the [Telecommunications Act 2001](#) is the most effective means to—

- (i)promote competition for the long-term benefit of end-users; and
- (ii)promote the legitimate commercial interests of access providers and access seekers; and
- (iii)encourage efficient investment for the long-term benefit of end-users, by—
 - (A)providing investors with an expectation of a reasonable return on their investment; and
 - (B)providing sufficient regulatory stability, transparency, and certainty to enable businesses to make long-term investments; and
- (iv)support innovation in telecommunications markets, or deregulation where sufficient competition exists; and

(b)assess whether alternative regulatory frameworks, including (without limitation) generic price control, would be a preferable and more effective means of achieving these outcomes.



A 'CLEAN SWEEP'

Future-focused, not backward-looking

- regulating for 2014 and beyond, not 1990s
- for broadband access and not fixed-line voice telephony services

Competition-focused

- a dynamic, interactive process where markets are central
- structures, technologies, the identity of the players constantly change in response to changes in competitive forces
- tests the boundaries between competition law and regulation

Technological, operator neutrality is imperative



A 'CLEAN SWEEP' (cont)

Clarity

- Government objectives for fibre investment, competition policy intentions must be made clear

Consistency matters

- consistent policy principles
 - more important than adherence to specific industry structures or persistence with particular regulatory instruments
- consistency across policies; between policy intentions and implementation of them is **VITAL**
 - TSO review cannot be separated from review of other regulatory principles and processes



OTHER ISSUES

Exemplars are difficult to find

- NZ's substantial government funding makes it 'different'

Political oversight of processes, network ownership leads to ongoing risks

- a case for a bipartisan approach?



THE INQUIRY PROCESS

Discussion documents circulated by MoBIE in mid June, with six week response horizon

ISCR's contribution:

Half-day workshop/seminar Friday July 12, Wellington

- New Zealand and international presenters with industry, policy and academic perspectives
- opportunity for discussion and debate to inform submissions and policy formulation processes
- register interest by emailing iscr@vuw.ac.nz, with 'Telco Seminar' in subject line
- details to follow on www.iscr.org.nz



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WE LIVE IN INTERESTING TIMES

Thank you



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FOR FURTHER REFERENCE

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