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Ministry of Business, Innovation and Employment
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Telecommunications Act Review: Options Paper

1. This is Vector Limited's (Vector) submission to the Ministry of Business, Innovation and Employment (MBIE) Telecommunications Act Review: Options Paper (the Options Paper), released in July 2016. Vector's contact person for this submission is:

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2. No part of this submission is confidential and we are happy for it to be publicly released.

Criteria for the review

3. MBIE is required to review the telecommunications regulatory framework under section 157AA of the *Telecommunications Act 2001* (the Act). The purpose of the review is to determine whether the current regulatory framework is the most effective means of meeting the statutory criteria.
4. The statutory criteria require MBIE to consider, *inter alia*, the most appropriate regulatory framework for delivering innovation, promoting investment and competition for the long-term benefit of end-users.¹
5. The statutory criteria are comprehensive. Accordingly, MBIE is required to consider the full suite of regulatory tools for best achieving the criteria.

Current fixed line telecommunications services regulation

6. A clear focus of the MBIE discussion paper is the regulatory framework for fixed-line telecommunication services. Fixed line telecommunications regulation captures Chorus'

¹ Section 157AA(2)(a)-(b) *Telecommunications Act 2001*

regulated copper network services and ultra-fast broadband (UFB) rolled out by Chorus and local fibre companies (LFCs).

Regulated copper services

7. The Commerce Commission (the Commission) is responsible for administering the regulatory framework for access to Chorus' regulated copper network services, namely the unbundled copper local loop (UCLL) and unbundled bit-stream access (UBA). These services are regulated under the pricing principles specified by the Act.² The regulatory framework and the Commission's access price decisions for these services has been subject to intense debate over an extended period of time (since 2011 and recently settled in December 2015).
8. The application of this regulatory framework resulted in the Commission making multiple decisions for the terms of the UCLL and UBA. The sudden, significant and frequent changes to access terms for the UBA and UCLL reflected the shortcomings of the regulatory framework. The pricing principles in the Act required the Commission to make decisions that were often contentious and vigorously debated by industry. These frequent and highly publicised debates about copper network services undermined certainty and stability, created challenges for sustainable competition, and damaged investor confidence.

UFB compact

9. UFB services have been provided via a "compact" between Crown Fibre Holdings (acting on behalf of the government) and LFCs. The compact prescribed both non-price terms and a 10 year price-path for UFB services. In contrast to the highly charged debate for the UCLL and UBA, the 10 year compact has encouraged LFCs to roll-out of UFB infrastructure and customers to adopt UFB services. UFB is an international success with New Zealand achieving the highest annual growth rate of fibre-to-the-premises take-up in the OECD.³
10. The certainty of the 10 year compact has also encouraged LFCs to provide new innovative services.⁴ Chorus and other LFCs are offering higher grade throughput services, exceeding quality expectations conceived at the outset of the UFB programme.

² Pricing principles for the UBA and UCLL are found in Schedule 1 Part 2 of the *Telecommunications Act 2001*

³ OECD, Broadband Statistics, 1.11. Annual Growth of fibre subscriptions among countries reporting fibre subscriptions, Dec. 2014-2015

⁴ An example of this innovation was the Chorus "Gigatown" competition

The preferred option for future fixed-line telecommunications regulation

11. The Options Paper recommends regulating fixed-line services for both UFB and regulated copper services under a common framework post 2020. MBIE's recommended common framework is to replicate the regulation of "utilities" under Part 4 of the *Commerce Act 1986* (the Part 4 model). The Options Paper recommends replicating the Part 4 model in the Act. This includes developing input methodologies (IMs) for determining how assets should be valued and depreciated (such as a fixed regulated asset base) and other relevant service costs for determining reasonable access prices for fixed line services.
12. The preferred direction of the Options Paper appears to be addressing the well-publicised shortcomings of the fixed line copper regulatory framework. However, the Options Paper does not acknowledge the relative success of the 10 year UFB compact for driving investment, customer take-up of UFB services and service innovation. The success of the UFB compact is underscored by the Commission choosing not (and not being petitioned) to undertake an investigation to include UFB services as regulated services under the Act.
13. In this respect, MBIE's recommendation of moving to a Part 4 type regulatory framework without providing any further flexibility will potentially frustrate the gains achieved by UFB delivered by the UFB compact.

An undertaking regime will improve the long-term benefit of end-users

14. Vector is concerned with the light-handed dismissal of undertakings as a suitable regulatory reform for the regulatory framework.⁵ Vector recommends the inclusion of undertakings as an additional tool in the regulatory tool kit. An undertaking provides a vehicle to mirror the success of the UFB compact for copper services and allowing the success of the UFB compact to continue. We believe such a tool is consistent with the statutory terms for the review and will deliver for the long-term benefit of end-users.

The Options Paper assessment of undertakings

15. Vector does not agree with the "cons" identified by MBIE for including undertakings in the regulatory tool kit. MBIE has characterised an undertaking as a regulatory "short-cut" similar to "benchmarking" or "hypothetical cost-modelling" which could introduce regulatory uncertainty. Vector does not believe this analogy holds. This is due to the fact that an undertaking is supplier initiated. Therefore, the terms of the undertaking have an association with the regulated supplier's costs for delivering the service. It avoids the use of relying on overseas comparisons or unrealistic modelling assumptions resulting in perverse service terms.

⁵ MBIE, *Telecommunications Act Review: Options Paper*, p. 67

16. In this respect, an undertaking will elucidate information also necessary for specification in IMs (MBIE's preferred option) but avoid extensive consultation and potential litigation involved with getting the specificity right for IMs.
17. Vector also does not agree with the concern of the additional effort and resourcing involved with assessing an undertaking. While an undertaking will require resources to assess, the intellectual lens for assessing an undertaking application will have materially similar features to determining prices on the basis on IMs. The information supporting an undertaking is likely to encompass the characteristics of "building blocks" as a means of justifying that the proposed terms for the regulated service are efficient.
18. The effort involved with assessing an undertaking would be complementary to MBIE's preferred model as opposed to unnecessary additional effort. The Commission would still require supplier information when determining access prices under the MBIE preferred model. Therefore, assessing the reasonableness of an undertaking would assist the Commission's task of setting appropriate terms and conditions for the regulated service. This is a marked contrast to the diverse pricing methodologies and academic debate involved with the current regulatory framework for copper services.
19. Vector also does not agree with MBIE's concern that a revenue cap cannot be a feature of an access undertaking. The National Broadband Network Company (NBNco) undertaking⁶ for next generation communications services in Australia (discussed further in this submission) is a comprehensive document which covers in detail principles for governing expenditures, form of control, pricing principles, cost of capital, and other necessary information relevant to determining prices using building blocks.
20. There is no reason why an undertaking regime could not apply to a revenue cap form of control for multiple regulated services provided by a single supplier. The supporting information for an undertaking would still have to demonstrate the supplier is limited in their ability to earn excessive returns, will invest in supporting infrastructure of the regulated services and ensure services remain fit for purpose overtime.

Undertakings are an additional lever in the regulatory tool-kit

21. Vector recommends MBIE include within the regulatory tool kit an undertaking regime that delivers certain outcomes. This is in contrast to the current undertaking process in the Act for services which entitles the Commission to continue to consider prescriptive regulation

⁶ Referred to in the *Competition and Consumer Act (Cth) (Australia) 2010*, Part XIC, Division 5, Subdivision B – Special Access Undertakings

defined by the Commission. Vector recommends an accepted undertaking to be an additional regulatory instrument to be administered/overseen by the regulator rather than an alternative to regulation.

22. The flexible term of undertakings provide service providers the confidence to make significant investments supporting the delivery of more efficient and innovative telecommunications services, and enable the benefits from these services to be brought forward to end-users. The benefit of an undertaking is that it requires the service provider to initiate the “conversation” on fundamental concepts for determining the terms and conditions for the regulated service such as: the form of control, asset valuation, assessing forecast expenditures, customer engagement, service innovation, dispute resolution and high level service specifications.

Successful use of undertakings for delivering price-quality outcomes

23. Undertakings are a common tool internationally for delivering price-quality regulation outcomes. Vector recommends an undertaking regime similar to that found in different parts of the *Competition and Consumer Act (Cth) 2010* (CCA) for regulated services in Australia. This framework entitles a service provider to submit an undertaking to the regulator specifying the service terms for the regulated services and the duration for which the undertaking would apply. The regulator retains the power to accept or reject an access undertaking in accordance with statutory criteria designed to protect the long-term interests of end-users. However, upon accepting an undertaking from a supplier, the role of the regulator transitions from defining terms and conditions for the regulated service to ensuring the regulated service(s) are provided consistent with the undertaking.
24. Part IIIA of the CCA governs access to essential services (non-sector specific access regime) ensuring such services are provided on price-quality terms replicating a competitive market. This part includes provision for service providers to lodge an undertaking defining the terms for the regulated service.⁷ Access to the standardised rail-gauge service covering Western Australia, South Australia, Victoria and New South Wales is governed by the terms of a 10 year access undertaking.⁸
25. Undertakings are a key feature of the Australian telecommunications regulatory regime in Part XIC of the CCA.⁹ The undertaking regime has provided regulatory certainty for the

⁷ Section 44ZZA *Competition and Consumer Act 2010 (Cth)*(Australia)

⁸ Australian Rail Track Corporation Ltd (ARTC) Interstate Access Undertaking lodged 15 July 2008 found: <http://www.artc.com.au/library/2007%20ARTC%20Interstate%20Access%20Undertaking%20-%20clean.pdf>

⁹ *Ibid* n 6.

national NBNCo to roll out next generation communications infrastructure across Australia.¹⁰ The NBNCo special access undertaking will expire in 2040 embedding “fixed principles” upon which current and future NBN services will be governed by.

Recommendation

26. The MBIE preferred model will require most or all of this information to be specified in the form of IMs applying to fixed network service providers. Accordingly, there is greater risk of administrative rules being less fit for purpose than a process where the service provider undertakes the responsibility of putting forward the terms on which it anticipates to provide the service and justifying to the regulator that such terms are in the long-term benefit of end-users.

27. Vector recommends MBIE includes an option of an undertaking regime in the regulatory tool kit. An undertaking regime for fixed line regulation (for both UFB and regulated copper services) is consistent with the statutory criteria for the review. This tool will ensure the consumer benefits from UFB delivered under the UFB compact can continue and will provide another vehicle for fit for purpose regulation of copper services.

Yours sincerely
For and on behalf of Vector Limited

A handwritten signature in blue ink, appearing to read "Richard Sharp".

Richard Sharp
Head of Regulatory and Pricing

¹⁰ Details relevant to the NBNCo Special Access Undertaking can be found at: <https://www.accc.gov.au/regulated-infrastructure/communications/national-broadband-network-nbn/nbn-co-special-access-undertaking>