



Response to Telecom's Submission

on the

MED Consultation Document

“Development of Requirements for the Operational
Separation of Telecom”

15 May 2007

Public Version
(there is no confidential version)

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1. Introduction	2
2. Executive Summary	3
3. Telecom’s proposal	4
4. Discussion	6
5. Conclusion	11
Appendix I: Legislative change required by Telecom’s proposal	12

1. Introduction

- 1.1 InternetNZ welcomes the opportunity to comment on Telecom’s submission in response to MED’s Consultation Document; specifically, “Telecom’s proposal to establish a structurally separate network company, and their request to make other changes to the regulatory framework for telecommunications.”¹
- 1.2 Telecom is proposing to create a stand alone, structurally separated company, “Netco”, which would own the fixed line local access bottleneck assets.² Integral to the package is considerably weakened operational separation within the remaining parts of Telecom. This is a major and significant departure³ from Telecom’s previously stated position on operational separation (Note: the “BT Model”).
- 1.3 Equally significant in Telecom’s proposal is a call for a “new regulatory framework” based on “regulatory contracts” to be negotiated directly with the Government.
- 1.4 Regulatory contracts would be the legal mechanism to establish rates of return for both Netco and Telecom Wholesale in which agreements would be negotiated for pricing of regulated services under the proposed new regulatory framework. (Price setting of regulated services is currently a role delegated to the Commerce Commission under the Telecommunications Amendment Act 2006.)
- 1.5 In previous submissions InternetNZ has endorsed the principle of structural separation in preference to operational separation, a position based on the added net benefits over the medium to long term. These benefits are outlined in our previous submissions (particularly our August 2006 submissions to the Commerce Select Committee on the Telecommunications Amendment Bill).
- 1.6 InternetNZ does note that its proposals to include structural separation provisions in the legislation last year was firmly rejected by Telecom.

¹ Minister of Communications Media Statement 1 May 2007.

² Telecom April 2007 submissions, paras 19 and 68.

³ Telecom April 2007 submissions, para 36.

- 1.7 InternetNZ will continue to encourage discussions concerning options to facilitate the structural separation of Telecom's network assets but not in the context of the Telecom proposal.

2. Executive Summary

- 2.1 Telecom's proposal is essentially unworkable given the current context and process that the Government and industry stakeholders are committed to (operational separation and also the implementation of LLU, UBA and associated services).
- 2.2 Telecom's proposal is predicated on a "new regulatory framework" that would require additional legislation to allow for its implementation. The required legislative changes would be substantial and complex. This would represent significant departures from existing policy settings.⁴
- 2.3 A more detailed assessment is contained in **Appendix I**.
- 2.4 Moreover, given the controversial aspects of the proposed "new regulatory framework", a further complicating factor beyond the legislative requirements will be the considerable difficulty in achieving industry-wide agreement and support. Even if agreement could be reached with Government and industry stakeholders, the timeline needed to support a process to develop and pass such legislation would take at least a year or longer resulting in additional and unacceptable further delays.
- 2.5 Consequently InternetNZ shares industry concerns that the momentum driving the current process cannot be delayed or compromised through any undue consideration of Telecom's structural separation proposal (which is seen by many in industry as nothing more than an 11th hour delaying tactic).
- 2.6 Also noted in Telecom's proposal is the inclusion of "a solution" to provide unbundled DSL ports as an alternative to subloop unbundling⁵. This proposal requires further clarification as well as industry input. Telecom maintains that each cabinet can hold only one DSLAM.⁶ Assuming that is so, Telecom incorrectly state that DSLAMs are not bottleneck assets.⁷ Telecom can consent to a Schedule 3 addition of unbundled DSL ports⁸ to the existing Schedule I services.
- 2.7 InternetNZ does share concerns raised by Telecom in their proposal regarding investment shortfalls in next generation access networks and the potential for negative impact on Government's Digital Strategy Broadband targets.
- 2.8 Investment related issues concerning next generation access networks do merit closer examination and need to involve all industry players equally.

⁴ See footnote 3.

⁵ Telecom Submissions April 2007, para 49.

⁶ Telecom Submissions April 2007, para 91.

⁷ Telecom Submissions April 2007, para 89.1

⁸ Telecom Submissions April 2007, para 93

- 2.9 InternetNZ further recommends that any study that might be undertaken by MED and/or the Commission in this regard include an assessment of the UK Industry and regulatory NGAN initiatives.
- 2.10 It needs to be further noted that Telecom has chosen not to respond directly to the operational separation discussion document. Rather, Telecom presented an “all-or-nothing” structural separation package.
- 2.11 The consequence is that, if Government does not accept Telecom’s proposal in its entirety, Telecom accepts the MED operational separation plan in full. The Minister can issue his determination based on the MED plan, as varied by other parties’ submissions, to the extent that he accepts them. Telecom’s approach enables Government to expedite achievement of optimal outcomes⁹.
- 2.12 The proposed asset and service split between Telecom’s Netco and the Ministry’s access services division are nearly the same: this illustrates that structural separation remains an option later, as irreversible investment decisions won’t have been made (and the Act allows amendment of the operational separation undertakings to cater for such developments).

3. Telecom’s proposal

- 3.1 Telecom’s proposal seeks the following outcomes :
- 3.1.1 A structural separation of their network assets (“Netco”) as a means to ensure a clearer equality of access to bottleneck assets.
 - 3.1.2 Diluted operational separation between Telecom Wholesale and Telecom Retail.
 - 3.1.3 Development of a “new regulatory framework” to incent investment in next generation access network infrastructure.
- 3.2 One of the reasons given for embracing structural separation (a reversal of Telecom’s earlier position in 2006) is the incorrect assertion that the MED operational separation proposal goes further than the BT Undertakings i.e. the “BT Model”. Telecom, from 2006, frequently promoted an operational separation plan for New Zealand which was largely the same as the BT Model. For example, Mark Ratcliffe, Chief Operating Officer Technology & Enterprise, said (on 11 August 2006):

*“We also believe in the interests of being transparent that we should point out that there are differences to what we are proposing in terms of a model and the one that British Telecom there. **We believe these are relatively minor characteristics that don’t impact on any of the outcomes that we are looking to get or that our stakeholders are looking to get from the models we are proposing.**”* (emphasis added)

⁹ See paragraphs 3.6-3.8 below.

- 3.3 Telecom claims that MED's proposal outlines "*a very rigid and invasive operational separation of Telecom on an aggressive timetable and is silent on the key investment and network renewal issues*"¹⁰.
- 3.4 This is not correct. Particularly notable is that the MED model is much less intrusive than the baseline model that Telecom has promoted and accepted: the BT model. In this regard TelstraClear's April 2007 careful and comprehensive submissions on the MED Consultation Paper are further illustration of the considerable shortfall between the BT Model and the MED model.
- 3.5 InternetNZ endorses the April 2007 submissions by TelstraClear, and recommends them for careful consideration. Telecom has chosen not to respond directly to the operational separation discussion document. The fact that Telecom has submitted on its separate "all-or-nothing" structural separation proposal, rather than providing direct suggested changes to the MED model, may be explained by its recognition that the MED model is favourable to Telecom compared to what could otherwise have been the case (a much more intrusive model, nearer the benchmark it promoted: the BT model).
- 3.6 In those circumstances, assuming the "all-or-nothing" structural separation proposal is rejected, Telecom can be taken to have accepted the MED Model. That is an outcome that Telecom will have expected, in light of well-known long standing practice. To illustrate the point, in 1993, the Wellington Airport company was updating the landing fees it charged to airlines. It consulted stakeholders including heavily-affected Air New Zealand. For tactical reasons, Air New Zealand chose not to make submissions when they were given the opportunity. The airport went ahead and set the charges. The airline complained to the Court that the airport company had not consulted. The Court of Appeal confirmed¹¹ – in a judgment quoted numerous times since – that the airport had done what it needed to do by giving the opportunity to submit to Air New Zealand.
- 3.7 This requirement to submit when the opportunity is given is very well known to parties such as Telecom.
- 3.8 The significance here is that the Minister can now move quickly to a determination, based on the MED model, varied to the extent that the Minister accepts submissions by other parties. The Ministry does not need to get further submissions (indeed it should not do so, for that would be unfair to stakeholders, other than Telecom, which have considerable interests at stake as well). This is neither unfair nor unreasonable and to do otherwise leads to unbalanced consultation.

¹⁰ Telecom April 2007 submissions, Para 32.

¹¹ *Wellington International Airport v Air New Zealand* [1993] 1 NZLR 671

- 3.9 Some of the more detailed elements of Telecom's proposal are as follows:
- 3.9.1 A proposed structural separation of the access and regional backhaul networks into a "NetCo" along similar (but not identical) boundaries to the Ministry's proposed operationally-separated "ANS division".
 - 3.9.2 A "wholesale product roadmap" showing when various services will be developed and to what standards of equivalence.
 - 3.9.3 An unspecified commitment to invest funds in a fibre-to-the-cabinet rollout, timelines and costs unstated.
 - 3.9.4 Much less rigorous operational separation requirements on the remaining Telecom business.
 - 3.9.5 Delivery of equivalence of inputs on a partial and slower basis than proposed by the Ministry.
 - 3.9.6 A 'regulatory contract' between NetCo and the Crown which restricts the future options available to the Commerce Commission in regulating yet-to-be-launched services, and removes the pricing role from the Commission.
 - 3.9.7 Different but largely unspecified regulation of pricing.
 - 3.9.8 Unspecified 'coordination' of regulatory functions in respect of separation, regulated services and the TSO.
 - 3.9.9 A roadmap towards removal of regulation requiring resale of retail and then wholesale services.
 - 3.9.10 A rejection of the Ministry's proposed operational separation plan.

4. Discussion

Regulatory Contract between the Crown and Netco

- 4.1 Telecom proposes to shift the responsibility for the pricing of regulated services from the Commerce Commission directly to Government by way of regulatory contracts and/or other means.
- 4.2 The proposal for a regulatory contract is closely coupled with the establishment of a "new regulatory framework", a major component that would form the basis of negotiated agreement with Government.
- 4.3 As outlined by Telecom, a regulatory contract together with the notion of a "new regulatory framework" presents significant difficulties insofar that it would require substantial changes to the Telecommunications Act 2001 (and as amended in 2006). (Tax and corporate structure legislation may need amendment too.) This is detailed in **Appendix I**. For example:
 - 4.3.1 Government would require access seekers to pay a higher price for LLU, UBS, UBA and other services, than Telecom considers would be determined by the Commission.¹²
 - 4.3.2 Government would effectively set the pricing of, at least, LLU, UBS and UBA, overriding the current statutory Commission Standard Terms Determination process (which will have to be reversed). It

¹² That is the effect of Para 25 of Telecom's submissions.

probably would have to set the complex non-price terms as well (for a service such as LLU, this stretches to numerous pages of specification). It's hard to see how price can be handled in isolation from other components of the service. There are mechanisms for Parliament to devolve sorting out the detail in each of these examples (for example, for the Minister to fix price and non-price terms instead of the Commerce Commission). However this, like the other examples, is a considerable leap, not only away from existing policy settings, but also away from international standard practice.

4.3.3 Government would override the process by which the Commission recommends (to the Minister, who decides whether to regulate) addition and deletion of regulated services. Instead, Government would legislate, in advance, stated timeframes within which various regulated services would be removed from regulation.

4.3.4 Government would give a regulatory holiday (it is not clear whether this applies to Netco and/or Telecom (including Telecom Wholesale)). In other words, Parliament would agree that certain services will not be regulated (i.e.: made available to other carriers), so that the provider has incentive to invest. This contravenes the BT Undertakings model (and thus contravenes Telecom's commitment last year). UK regulator, Ofcom, and the European Commission, are opposed to regulatory holidays: there are other solutions.

4.3.5 Government would also add (and price) a new service: Unbundled DSL ports. This bypasses the Schedule 3 process by which the Commission considers whether to add the service, makes a recommendation, and the Minister then decides whether to regulate. The Commission then determines price and non-price terms.

4.3.6 Government would be likely to give Telecom tax relief to effect this change.

4.4 If there is to be change of this magnitude, careful policy review is required, followed by a careful parliamentary process, all of which would take over a year (assuming a fast-track). InternetNZ does not support the current operational separation process being derailed in this way.

Investment Issues

4.5 Telecom's proposal contains a wide range of comments concerning the need for a regulatory environment that ensures a suitable rate of return, thereby providing for adequate incentives to invest in next generation access networks.

4.6 If structural separation was to be seriously considered, InternetNZ accepts that alternative models may need investigation to ensure continued investment in the access network.

4.7 It is possible that this review will show that the pricing mechanisms under the Telecommunications Act for regulated services are constructed with this constraint in mind. TSLRIC pricing is specifically designed to take the risks of the business and the cost of capital in mind, to ensure that there is a viable

long-run future for the relevant services. Retail-minus pricing has this effect even more.

- 4.8 Structural separation could be seen as a way to help resolve this problem, as it provides a separate legal entity with its own dividends policy, RoI and cost of capital requirements separate to those of the Telecom Group. This might incent long term, low-return infrastructure investors to provide the capital required for network investment.
- 4.9 That is the basis on which InternetNZ continues to support structural separation as a preferred long term option.
- 4.10 Many other countries are grappling with the challenges of providing incentives for NGN Access roll-out. The UK experience in particular demonstrates that there are complex issues involved that require careful scrutiny, and that care must be adopted to take steps (e.g.; whether or not to regulate) too soon or too late.¹³ The Telecom proposal is sparse on important detail, ranging from the profit gains it can achieve from selling Netco in this market in which infrastructure sales attract considerable interest¹⁴, through to the complexities of separation illustrated in the TelstraClear April 2007 submissions.

Equivalence of Inputs

- 4.11 InternetNZ has supported the implementation of Equivalence of Inputs for a range of services on the access network in all its submissions relating to the telecommunications regime. It continues to do so, as set out in its April submissions.
- 4.12 Telecom's proposal supports more narrowly focused EOI requirements on a narrower range of services.
- 4.13 Equivalence of Inputs is the only effective basis to give long-run equivalent access to bottleneck infrastructure. It is the only sustainable manner to deliver services that can give government or regulators the confidence to contemplate deregulation of services on the retail or wholesale side of the business in future.
- 4.14 InternetNZ rejects Telecom's assertion in paragraph 120, that in the context of a structurally separated Netco:
- "At that point, there will be no issue of principle that justifies singling out Telecom from its competitors by imposing regulations on Telecom to provide Wholesale services or to resell retail services."*
- 4.15 This suggests a reversion to Telecom's preference for a two-way split as outlined in their submissions to the Commerce Select Committee in August 2006.

¹³ See for example the April 2007 Broadband Stakeholder Group report *Pipe Dreams? Prospects for next generation broadband deployment in the UK*, and Ofcom, *Regulatory Challenges posed by next generation access networks* (November 2006).

¹⁴ Bear Sterns and other commentators report the "significant release of capital" from sale of last mile assets. See for example Para 8.29 in example the April 2007 Broadband Stakeholder Group report *Pipe Dreams? Prospects for next generation broadband deployment in the U.K.*

- 4.16 Telecom's structural separation-based proposal seeks a weakening of equivalence obligations and a more focused application of them. InternetNZ reiterates the points it made in its April submissions, that full equivalence of inputs should become the basis of all new services in the access network business, and that it should (for other than minor legacy services) be broadly, not narrowly, applied. In this context, the TelstraClear April 2007 submissions are endorsed by InternetNZ.

Regulatory certainty and coherence

- 4.17 The current regulatory framework provides sufficient regulatory certainty and coherence. The Commission sets pricing and service specifications for regulated services. The Ministry of Economic Development is managing the operational separation process, and the TSO review process. All are conducted with the need to create an investment-friendly regulatory framework.
- 4.18 Structural separation along the lines of a Netco could add to certainty in the long run, by removing any ability for the industry to call for such separation as a further remedy, and by definitively separating the network from the rest of Telecom.
- 4.19 Telecom's proposal however could create further regulatory uncertainty. By proposing to remove the power to regulate services from the Commission into a rigid regulatory contract, there is no way to ensure that new situations where market power is being used in an anticompetitive manner is able to be dealt with by regulation. Instead, participants would have an incentive to lobby the Government of the day to change the contract which, given it is a political process, provides less certainty than a regulatory process.

Long run deregulation

- 4.20 InternetNZ accepts as a general proposition that regulation providing for equality of access for bottleneck assets provides scope for future deregulation further up the value chain. That is why InternetNZ supports the regulatory framework currently in force rather than the previous regime which was focused on the regulation of specific services after competition problems had emerged.
- 4.21 Deregulation is a prospect. It is not and cannot be guaranteed. Telecom's proposal seeks to bind the Crown to a path of deregulation for retail and wholesale services¹⁵ which can be agreed to at this time.
- 4.22 If the Crown offered such a guaranteed path to deregulation, the incentive on Telecom would be perverse: the incentive would be to make the equality of access regime fail, because in time retail regulation would be guaranteed to be removed and so the historic pattern of anti-competitive behaviour could be resumed.

¹⁵ Telecom Submissions April 2007, para 123 onwards.

- 4.23 InternetNZ therefore reiterates its opposition to deregulatory paths being administered outside the Commission and being guaranteed in advance. The existing processes in the Act are more suitable, and providing a guaranteed deregulatory path would provide Telecom with strong incentives to make the equality of access regime currently being implemented, fail.

Telecommunications Service Obligation

- 4.24 There are strong interactions between the nature of the universal service obligations set out in the TSO review, and the shape of the regulatory framework applying to the telecommunications industry.
- 4.25 MED are currently working on a review of TSO. The only coordination that is required is that the review considers investment issues, and that if major changes are proposed to the obligations falling on Telecom – or on how the TSO obligations are funded – then there may be consequent changes required either to the operational separation undertakings, or to the broader regulatory framework.
- 4.26 The nature of universal service obligations is a public policy debate for Government to consider, as it involves issues of social inclusion and infrastructure delivery that are by definition not within the ambit of market investment and provision.
- 4.27 The current proceedings are, and should remain, focused on making access to Telecom's existing local access network fairer, to allow other access seekers to develop their networks, invest in plant in the deepest possible levels of the network, and deliver new and innovative services to consumers.

5. Conclusion

- 5.1 On balance InternetNZ recommends that the Telecom proposal be rejected at this time, because:
- 5.1.1 It cannot be accommodated within the Telecommunications Act, so would require slow and fundamental changes to the regulatory framework adopted in 2006.
 - 5.1.2 It would weaken the application of equality of access principles, and mark a significant departure from the model of separation agreed after extensive discussion last year – to the detriment of consumers and the industry more generally.
 - 5.1.3 It inappropriately attempts to conflate debates about the application of equality of access to the existing access network with debates on how to promote investment in next generation access networks.
- 5.2 The Government should proceed forthwith with operational separation as set out in the Ministry's consultation document, amended by appropriate consideration of the submissions received.
- 5.3 Operational separation of Telecom, into three parts (network, wholesale and retail) will be required regardless of whether the access network remains within Telecom or is structurally separated at some future time.
- 5.4 Rejection of Telecom's proposal does not rule out the option of structural separation going forward in the future. InternetNZ supports that option, properly proposed, for the reasons outlined above. The current process of operational separation involves no decisions on investment that cannot be later reversed. The Minister can employ his powers to vary the undertakings if the benefits in terms of efficient governance and capital management / investment opportunities make Netco a viable option.

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Appendix I: Legislative Change required by Telecom's Proposal

No.	Legislation Changes that are required by Telecom Proposal (for example, to enable Government to enter a regulatory contract with Telecom)	Existing Law affected by legislation changes, and comments	Position in the UK
1	The legislation will need to address "the possibility that the Government's Digital Strategy Objectives might imply network investment that is uneconomic in current market arrangements." ¹⁶	The handling of this issue, like much of the Telecom submission, is opaque, short on detail, and does not provide specific solutions. There are many oblique and undefined references in the Telecom submissions.	
2	<p>Netco and Telecom Wholesale will require new legislation that ensures they receive an adequate rate of return so that they can continue to invest¹⁷.</p> <p>While this and other steps can be achieved by legislative delegation (e.g.; to the Minister), ultimately, legislation is required to override the existing regime (in this instance, to take responsibility for fixing prices away from the Commission and give it to Parliament or</p>	<p>The Telecom proposal requires new legislation as to both for both Netco and Telecom Wholesale.</p> <p>The current legislative position is that there are 2 main pricing models by which the Commission sets regulated prices.</p> <ul style="list-style-type: none"> • Retail-minus. This produces high returns for the access provider and is specifically designed to protect the access provider. These returns are so high that there is an increasingly strong view that retail-minus, as applied in NZ, fails as the price paid to the access provider is too high (ie the problem is contrary to that claimed by Telecom). For detail, see the Commerce Commission's submissions to the Finance and Expenditure Select Committee in respect of the Telecommunications Amendment Bill and also the Appendix in the submissions to the Commission on the Mobile Services Review lodged by Econet. • TSLRIC is sufficiently flexible to reflect incentives to invest. For example, the WACC component of the calculation reflects risk. 	<p>Ofcom rarely uses retail-minus without imputation test.</p> <p>Cost-based pricing prevails.</p> <p>Ofcom not Government sets price.</p>

¹⁶ Paras 24 and 51-52 Telecom April 2007 Submissions

¹⁷ Paras 24 and 50, Telecom April 2007 Submissions

¹⁸ Paras 25 and 51, Telecom April 2007 Submissions

	<p>the Minister via delegated legislation).</p> <p>The proposal also requires removal of what Telecom calls the current regulatory bias to lower returns. Government will set all regulated prices to deliver reasonable rate of return¹⁸ This means that the legislation will require access seekers to pay higher prices for services than, according to Telecom, would be paid if the Commerce Commission made the decision.</p>	<p>Significantly, in its structural separation submission, Telecom gives no reason for its claim that there is regulatory bias in favour of lower returns. It's a mere claim without stated support, on which it expects major changes to the existing regulatory settings.</p> <p>The Telecom proposal will take determination of the price of services away from the Commission and give it to Government (possibly by delegation to the Minister). That is contrary to the policy settings in the Act, and contrary to standard international practice.</p>	
<p>3</p>	<p>Fix propensity to change what is regulated after investments are made¹⁹</p> <p>Remove ability to add regulated services later (Telecom are requiring regulatory holidays).²⁰</p>	<p>The present position under the Act is as follows:</p> <ul style="list-style-type: none"> • There is a Schedule 3 Commission investigation as to whether to add a service • Minister then decides whether to regulate • Commission and Minister always consider, as a key issue, incentives to invest (dynamic efficiencies). They always carefully consider whether adding services will adversely impact on investment incentives. The Commission devotes considerable attention and priority to incentives to invest and dynamic efficiencies. <p>The Telecom proposal takes the decisions away from the Commission.</p> <p>Telecom, in its submission, gives no analysis for its conclusion that there is a propensity (implicitly, on the part of the Minister, after recommendation from the Minister) to regulate after investments are made. The history of light-handed regulation so far shows the opposite has happened (eg; the introduction of LLU</p>	<p>The BT Undertakings do not stop addition of regulated services. The opposite is the position. It is recognised that this may in fact happen. A key component of the model is that new services may be regulated where there is SMP</p> <p>In particular, express in the undertakings is that NGN-based services may be regulated if there is SMP (that's a key expectation in the Undertakings).</p> <p>Ofcom has made it clear that it will not allow regulatory holidays as a solution. (the European Commission is also opposed, and is reviewing the Deutsche Telekom regulatory holiday).</p> <p>The BT Undertakings (which, last year,</p>

¹⁹ Para 25, Telecom April 2007 Submissions

²⁰ Para 66, Telecom April 2007 Submissions

		<p>years after other OECD countries).</p> <p>The regulator needs flexibility to add new services, taking into account the factor that the ability to add regulated services later may be a disincentive to invest. This requires a balanced approach, weighing up all factors, and that is safer than a blanket restraint on regulation of new services. Incentive to invest can be addressed by other factors including how the price is set (in particular by setting the price sufficiently high that incentives to invest remain). The Commission has sent out frequent signals that it takes real care to facilitate incentive to invest.</p> <p>Regulatory holidays, as proposed by Telecom, are highly controversial and generally opposed by regulatory bodies as being a sub-optimal solution.</p> <p>Successful operational separation is expected to lead to less services being regulated. But this cannot be pre-ordained (and it is not pre-ordained under the model proposed by Telecom: the BT Undertakings).</p>	<p>Telecom pushed as the model for NZ, with modest changes) do not allow for regulatory holidays. Yet Telecom now reverses the position it promoted in 2006.</p> <p>There is an expectation that Ofcom will not regulate some services, if the BT Undertakings are successful. However options have been left open by the Commission.</p> <p>The careful regulatory approach to facilitate incentives to invest is outlined in Ofcom's 2 main papers on NGN.²¹ This is an excellent illustration of regulatory caution.</p>
4	Coordinated regulation is required (between MED operational separation, Commerce Commission determinations and TSO Review) ²²	The Consultation Paper contains regulatory coherence with the approach by the Commission (InternetNZ has said coherence should be achieved in a different way). MED is dealing with both TSO and operational separation: coordination to the extent needed seems achievable.	The BT Undertakings preserve the existing regulatory settings (eg Ofcom's mechanisms for determining SMP, price, etc).
5	Government must legislate for a pre-ordained roadmap for removing regulation of resale of Telecom's retail services, wholesale services, UBS (in areas where LLU services are provided by access seekers) ²³	<p>The current position:</p> <ul style="list-style-type: none"> • Schedule 3 – Commerce Commission can recommend to Minister to remove services from Schedule 1 • Schedule 3 review by Commerce Commission as to whether to recommend to Minister that Schedule 1 services should continue to be regulated beyond 5 years <p>This preserves appropriate flexibility and has regard to incentives to invest. For the new position that overrides the existing position, see comments at 3 above.</p>	No pre-ordained roadmap. Ofcom provides indications that regulation may be removed depending on the success of operational separation Ofcom waits to see what happens.
6	Government introduces new service (unbundled DSL	The current position is that there is no such service in Schedule 1. If added to Schedule 1, this would require a Schedule 3 investigation, the Minister must	BT Undertakings apply to services where there is SMP and with provisions

²¹ See Ofcom, *Regulatory Challenges posed by next generation access networks* (November 2006), and its predecessor NGN paper.

²² Para 28, Telecom April 2007 Submissions

²³ Paras 29 and 123-128, Telecom April 2007 Submissions

	<p>ports) as a regulated service, with price fixed by legislation²⁴.</p> <p>It appears this would require legislation to fix non-price terms as well.</p>	<p>accept the Commerce Commission recommendation, followed by Commerce Commission determination of price and non-price terms.</p> <p>InternetNZ and TelstraClear submitted in their April 2007 submissions that operational separation permits non-regulated services and inputs to be included as EOI services covered by the operational separation undertakings, and that this should happen. If necessary, InternetNZ would support rapid addition of this new service under Schedule I, but not as a substitute for existing services.</p>	<p>applicable prior to determination there is SMP (eg; as to NGN-based services)</p>
7	<p>Government fixes LLU price, to allow for reasonable rate of return on assets and changing market considerations²⁵</p> <p>While not stated by Telecom, complex non-price terms would need to be legislated too unless a complicated dual model (one for price and the other for non-price terms) can be constructed.</p> <p>All other Netco pricing is to be determined in advance too.²⁶</p>	<p>LLU is currently being handled by the Commission in its Standard Terms Determination process. Likewise for the other services</p> <p>The pricing model (TSLRIC) is sufficiently flexible to meet Telecom concerns (retail-minus even more so). See 2 above.</p> <p>The new legislation would reverse this process, which overrides the existing policy settings in the Act. Government would determine price (and non-price terms) not the Commission.</p>	<p>Ofcom set the price.</p>
8	<p>Legislation by which Government decides between averaged and de-averaged LLU price (instead of the Commission)²⁷</p>	<p>Currently, the Commerce Commission decides this complex and controversial issue, as part of Standard Terms Determination.</p> <p>Under the new legislation, Government would decide instead, and the current Standard Terms Determination is reversed.</p>	<p>Ofcom decides, applying regulatory principles</p>
9	<p>Government sets relativities between Netco and</p>	<p>Current position: Schedule I – Commerce Commission sets prices of LLU and UBS/UBA taking into account relativities and ladder of investment.</p>	<p>Ofcom role</p>

²⁴ Para 49, Telecom April 2007 Submissions

²⁵ Paras 52 and 82, Telecom April 2007 Submissions

²⁶ Par 68 Telecom April 2007 Submissions

²⁷ Para 26, Telecom April 2007 Submissions

	wholesale products instead of the Commission ²⁸	<p>The model favours Telecom as Telecom has control of the UBS/UBA price and can move UBS/UBA price to its advantage. This problem is outlined in the Commerce Commission's submissions to the Finance and Expenditure Select Committee, on the Telecommunications Bill.</p> <p>InternetNZ would support an amendment to remove this anomaly, but not as part of a structural separation package.</p>	
10	Government sets UBA and UBS prices instead of Commission ²⁹ . This is likely to require setting of non-price terms as well.	<p>Commission's Standard Terms Determinations are dealing with this. Pricing principles (retail-minus) are highly favourable to Telecom (see 2 above).</p> <p>This proposal involves a major departure from current legislation.</p>	Ofcom sets prices
11	Legislation to effect split needed? ³⁰	As Telecom note, unless Companies Act mechanisms are adequate, special legislation is required. If this is a simple mechanism, this seems uncontroversial apart from the delays involved.	N/A
12	Legislation to address tax liabilities? ³¹	Telecom's initial scoping shows tax liabilities created by the structural separation may need to be legislated (presumably the tax liability is exonerated). That may be controversial.	N/A

²⁸ Para 51.3, Telecom April 2007 Submissions

²⁹ Para 62 & 63, Telecom April 2007 Submissions

³⁰ Para 109, Telecom April 2007 Submissions

³¹ Para 109, Telecom April 2007 Submissions