Submission

by

Business|NZ

to the

Commerce Commission

on the

Telecommunications Act 2001: Section 64 reviews into unbundling the local loop network and the fixed public data network

14 May 2003

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1. INTRODUCTION

1.1. Encompassing five regional business organisations (Employers' & Manufacturers' Association (Northern), Employers' & Manufacturers' Association (Central), Canterbury Employers' Chamber of Commerce, Canterbury Manufacturers' Association, and the Otago-Southland Employers' Association), Business New Zealand is New Zealand's largest business advocacy body. Together with its 50-member Affiliated Industries Group (AIG), which comprises most of New Zealand's national industry associations, Business New Zealand is able to tap into the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy.

1.2. In addition to advocacy on behalf of enterprise, Business New Zealand contributes to Governmental and tripartite working parties and international bodies including the ILO, the International Organisation of Employers and the Business and Industry Advisory Council to the OECD.

1.3. Business New Zealand's key goal is the implementation of policies that would see New Zealand retain a first world national income and regain a place in the top ten of the OECD (a high comparative OECD growth ranking is the most robust indicator of a country's ability to deliver quality health, education, superannuation and other social services). It is widely acknowledged that consistent, sustainable growth well in excess of 4% per capita per year would be required to achieve this goal in the medium term. Given the increasing need for businesses to receive information at a quicker pace than ever before, the telecommunications industry plays a vital role in ensuring businesses receive information immediately and effectively.

1.4. Business New Zealand therefore welcomes the opportunity to briefly make some general comment on the Telecommunications Act 2001 issues paper regarding unbundling of the local loop network.

2. GENERAL DISCUSSION

2.1. Section 64 of the Telecommunications Act requires that within 24 months after the commencement of the Act, an investigation be carried out into local loop unbundling (LLU) and access to, and interconnection with, Telecom's fixed Public Data Network (PDN). Section 19 of the Act states that the Commission must consider the purpose set out in section 18, which, among other things, *is to promote competition in telecommunications markets for the long-term benefit of end-users of telecommunications services within New Zealand by regulating, and providing for the regulation of, the supply of certain telecommunications services between service providers*. Competition provides benefits for both businesses (increased efficiency and innovation) and consumers (lower costs and a greater choice of goods and/or services).

2.2. Business New Zealand questions whether the developments of bottlenecks (key facilities that are unlikely to be duplicated in the short-medium term) should be remedied by regulatory actions. While there seems to be some ambiguity over defining LLU and in what form LLU should be considered, we believe that current technological changes, repercussions on investment through increased regulation, and the present status of broadband penetration are vital elements to consider when deciding if LLU by regulation, including access pricing, should be mandated.

3. TECHNOLOGY DEVELOPMENTS

3.1. Chapter 3 of the issues paper outlines a range of innovations in technology that is already occurring and being developed in New Zealand's fixed and wireless market segments. Various New Zealand and overseas companies have stated that data can be sent and received from satellite, fibre optic carriers and other backbone systems such as the power grid, thus by-passing the 'last mile' copper telephone lines of Telecom. Optus have stated that New Zealand's geography makes it an ideal place to use satellite communication services, as remote regions' communications needs can be met via satellites[1]. Broadband Internet access through power lines is already taking place in Auckland, while companies such as Walker Wireless have developed wireless modems, with the intention of spreading the technology throughout the country[2]. Competing local loops exist in Wellington and Auckland which, on a customer base, must rank among the best wired small cities in the world.

3.2. Although the issues paper discusses the advantage of increased competition through LLU, the existing development of current alternative forms of technology is already creating competition, which should benefit end users. There is no market reason why this process should not continue, and even accelerate given the existing regulatory framework and the number of regulatory interventions currently awaiting decision.

4. INVESTMENT IMPLICATIONS

4.1. New technology that is proven to work also brings in investment as investors see areas where new technology could phase out existing technology. Business New Zealand is concerned that LLU may contribute to a fall in investment because of placing another layer of regulation upon businesses. Telecom is currently New Zealand's biggest public company and largest investor of capital. While two years ago it invested $1.1 billion, last year this was reported to be down to $750 million, and this year investment has fallen further to $600 million[3].

4.2. Although the issues paper states that the OECD has found no evidence that LLU has slowed investment in new infrastructure or innovation, neither is there evidence offered of the effectiveness of transferring other regulatory models to the New Zealand setting; there are, however, a number of current infrastructural examples in New Zealand that call into question – even if only with hindsight – the shorter and longer term value propositions obtained by following either deregulatory or regulatory models derived elsewhere. These

[1] Optus Pushes Broadband Via Satellite in NZ, Optus media release, 28 January 2003.
[2] Wireless Undercuts Telecom, New Zealand Herald, 11th February 2003.
[3] Red Tape Worry as Firms Cut Investment, The Dominion Post, 5 May 2003.

examples must include energy and perhaps a number of transport sectors. None warrant repeating.

4.3. Consideration must also be given to the issue of property rights if the Government were to take regulatory steps through LLU. A requirement for a successful open-market economy is the need for clear specifications and enforcement of property rights, which are crucial for production as a company (and shareholders of the company) that invests in productive assets requires assurances that they receive suitable rewards for their investment. Ownership of property rights means that shareholders of the company have the right to use the asset, exclude others from using the asset, and transfer control of asset rights to others if they wish. Regulation would undermine these rights, and although regulatory measures are often introduced in pursuit of the public interest, they remove the incentive to invest because there are no assured rewards for incurring the costs of investment and ownership.

4.4. In the case of Telecom, shareholders would relinquish one of their property rights if LLU was mandated. If the Government set no form of compensation mechanism in place, LLU would lead to a fall in the value of one of the company's productive assets, as well as jeopardising the share value shareholders have in the company. The option of redeploying investment away from the local loop would also be lost, limiting future capital investment options for the company.

4.3 We are not surprised that the Telecom Chairman has recently been quoted as saying that increased regulation in areas such as telecommunications would continue to lower capital investment by the company with serious consequences for New Zealand's infrastructural development and economic growth. There is certainly evidence of the ambiguous positions adopted by some of the parties keen to promote LLU in New Zealand as compared to their parent companies' views on LLU in their base market.

4.4 This reinforces the critical importance of a credible evaluation of the benefits of mandated competition in the shorter and longer term respectively, taking into account the particular characteristics of a tiny and highly dispersed market that has demonstrated its appetite for and capacity to absorb rapid technological change. This is not the responsibility of the local loop incumbent whose assets have been acquired in different circumstances. Proponents of LLU need to assure business end users that in the medium to longer term they may still expect to access a globally competitive and efficient national telecommunications infrastructure that is the product of adequate investment and reinvestment over time. Alternatively, they must show that any short term price gains of LLU accruing to end users would significantly outweigh longer term outcomes that may be at risk to commercial decisions by incumbent operators that better returns on their capital may be obtained elsewhere.

5. BROADBAND PENETRATION

5.1. One of the main reasons unbundling is often mandated is to increase broadband penetration. Improving New Zealanders broadband access to the Internet is one of Business New Zealand's 20 key priorities for growth, as the Internet is an ideal way to facilitate trade markets for a remote country like New Zealand[4]. A fast and reliable Internet connection can provide businesses with increased productivity and be more responsive to customers needs.

5.2. One of the cases for LLU is that its absence puts up a barrier to the uptake of broadband usage. While New Zealand ranked 23rd out of 30 OECD countries in 2002 for broadband penetration (slipping from 16th in June 2001), New Zealand's broadband subscription ratio is still very close to countries it traditionally compares itself to, such as Australia and the U.K. Also, as the ranking is based on penetration per 1000 habitants, New Zealand's current population growth may result in a slide that does not relate to a genuine fall off in broadband use, given that other countries (especially in the European

[4] Twenty Priorities for Growth, Business New Zealand, January 2002.

Union) are experiencing population declines. Density of population is also a factor as New Zealand has a low density compared with countries such as South Korea and those in Europe that have a high population density, and therefore high penetration rates.

5.3. Customers using broadband has increased significantly in New Zealand over the last year. The number of residents and business customers subscribing to Telecom's current broadband Internet service, Jetstream, has more than doubled over the last year to 54,000, with around 50% of medium sized businesses across New Zealand using its service. Other companies such as CityLink have recently begun providing broadband access through Auckland's power lines, while RoamAD & Cisco, Walker Wireless and Optus are currently promoting wireless broadband access in New Zealand, which gives customers the added benefit of mobility.

5.4. In terms of increasing future broadband use, Telecom has announced plans to have broadband taken up by 100,000 households by the end of 2004, almost three times the current number of households (36,000)[5]. In addition, recently established companies providing broadband access would also seek out those currently not using broadband to establish a customer base. While there is no indication by companies providing broadband that they are also specifically targeting an increase in their business customer base, the make-up of New Zealand businesses means many small enterprises would have their business set-up at home, so we should also see an increase in the number of businesses using broadband, even if focus is solely aimed at increasing household broadband use.

5.5. Given the significant increase in those with broadband and future development of broadband penetration in New Zealand, Business New Zealand believes that positive steps are already being taken to improve New Zealand's broadband access. This includes Project Probe, promoted by the Government, under which three regions have already chosen an alternative

[5] Telecom Reports Solid Half Year Performance, Telecom Media Release, 4 February 2003.

provider to Telecom for broadband access. It is difficult to see how LLU would contribute to this process.

6. KIWI SHARE

6.1. The main purpose of the Government retaining a 'kiwi share' in Telecom when it was privatised in 1990 was to ensure universal service to residential users, and restrain increases in telephone line rentals. At that time, the Internet was hardly a factor, and the decision taken on the kiwi share issue has resulted in current local calls for standard dial-up Internet connections remaining free of charge. Given the relative differences in cost between dial-up and broadband connections within New Zealand, dial-up access looks the more attractive alternative if cost is the only issue that customers consider. In addition, the kiwi share may inhibit further entry into the market, as the existing provider cannot increase their charges, which would otherwise provide competitors with a viable opportunity to enter. Therefore, Business New Zealand recommends that a review of the issue of kiwi share take place in the near future, with specific focus on the current situation of local standard dial-up connections remaining free of charge.

7. CONCLUSION AND RECOMMENDATION

7.1. The telecommunications industry is presently one of the most rapidly changing industries in terms of technological development and innovation. As section 18 of the Act stipulates that the Act's purpose is to promote competition in telecommunications markets for the long-term benefit of end-users, the present rate of technological change, the possible harmful effects on investment, and the increased focus on raising broadband use means that LLU cannot be argued to be critical to effective competition or to the long term net benefit of end users. While the Government may wish to re-consider the issue in the future or keep the prospect under regular review, Business New Zealand recommends that for now LLU and access to, and interconnection with, Telecom's fixed PDN should not be mandated. Also, as the kiwi share may deter both broadband use and the entry of competitors into the market, we recommend that a review of the issue of kiwi share take place in the near future, with specific focus on the current situation of local standard dial-up connections being free of charge.