

Regulating communications for the future



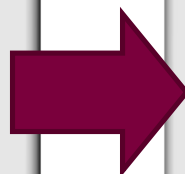
Summary of Chorus' response to MBIE Discussion Paper

Fundamental change is needed to support a sustainable policy environment that delivers better broadband to NZ

- > **Broadband is a critical enabler** of economic growth and social wellbeing. New Zealanders' reliance on being online is ever increasing. Broadband has become an essential facility much like water, electricity, gas.

TODAY: Complexity

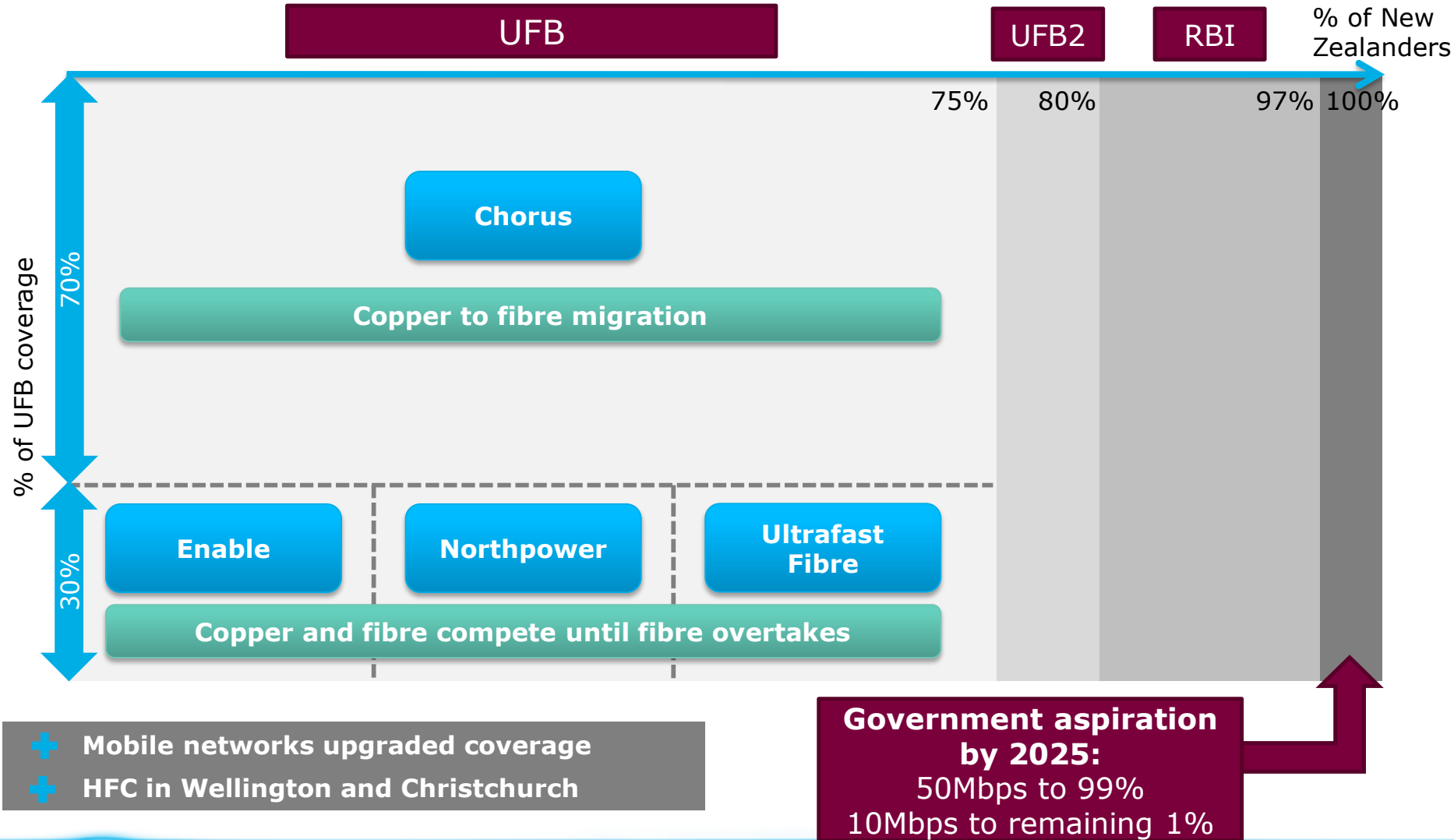
- ✗ There hasn't been a single year since 2007 that the industry hasn't been in a **complex regulatory process**
- ✗ **Multiple instruments**, many with high prescription
- ✗ **Ambiguity** as to how policy objectives should be weighed, and how the purpose statement should guide regulatory discretion
- ✗ Designed for a **vertically integrated operator** that no longer exists
- ✗ **Isolated (but fundamental) debates** about wholesale access prices
- ✗ **Price shocks** are a feature – real costs are not used so it is impossible to predict price outcomes



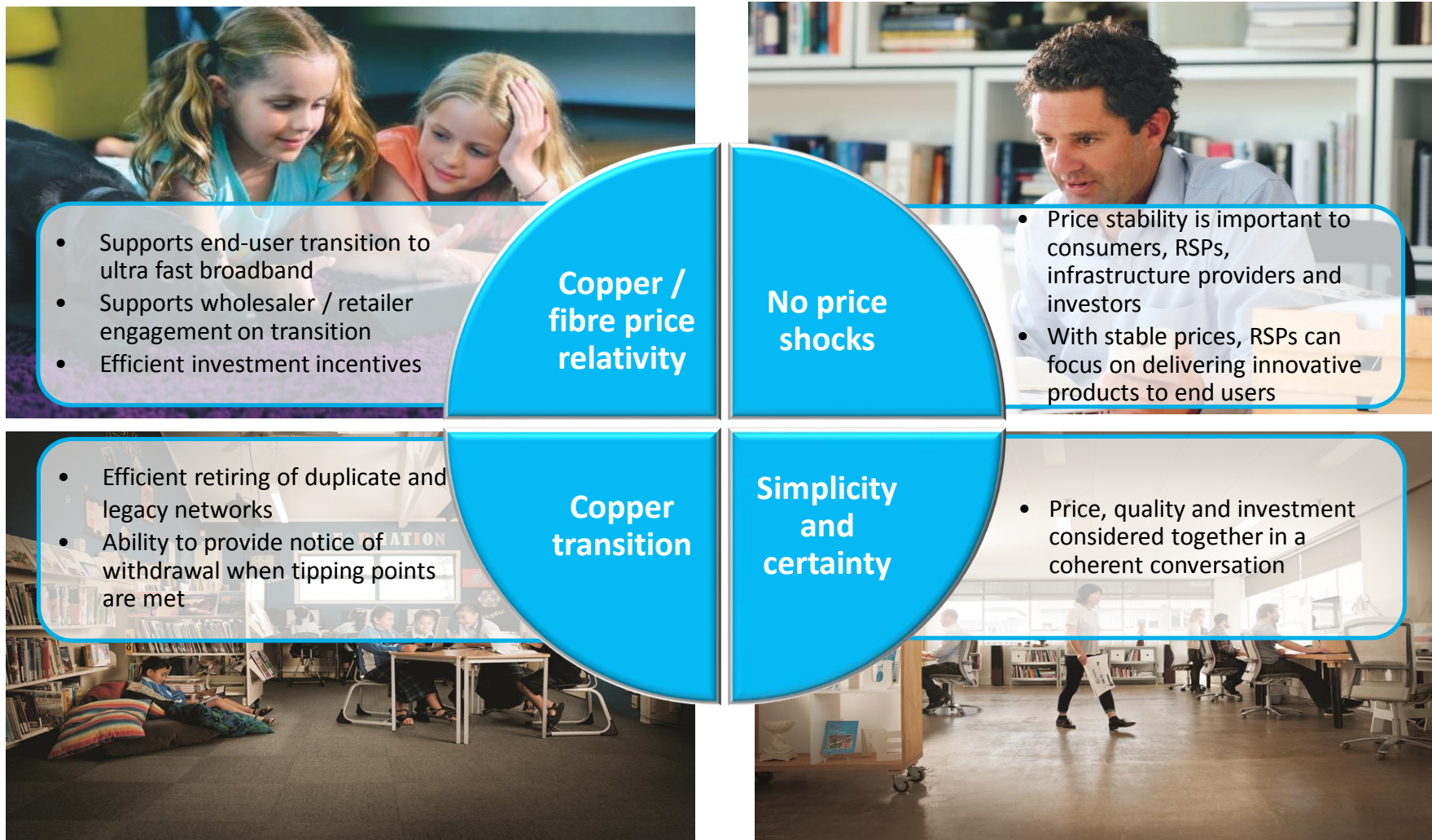
TOMORROW: Simplicity

- ✓ Scope for **industry solutions** where possible
- ✓ Opportunity to **simplify and rationalise**, bringing regulatory instruments into one place
- ✓ Duplication of fibre to the home infrastructure isn't efficient, but **ongoing investment and open access** to the upgraded infrastructure and wholesale services is
- ✓ A **utility-style model** ensures regulatory commitment, fair pricing, and a fair return – all in the long-term interests of consumers
- ✓ **Price, quality and investment** to be considered together in a single conversation
- ✓ **Price shocks are in no-one's interests** – a utility-style model can enable more stable and predictable prices

Infrastructure upgrades: Substantial investments are underway across New Zealand



Enablers to support the better broadband ambition



Type of regulation: We support a utility-style Building Block Model (BBM) framework

	TSLRIC	BBM	Anchor products
Price stability	✗	✓	✓
Fair return for investors	✗	✓	✓
Copper to fibre transition	✗	✓	✓
Simplicity	✗	✓	✓
Common approach to regulation in NZ	✓	✓	✗

A BBM framework is able to **align the interests of end-users, RSPs and network providers**, and can be designed flexibly to meet the **Government's objectives** for the sector

Active consideration should be given to **anchor product regulation** - preferred approach to **managing copper to fibre transition** in EU & UK

Choosing the point of regulation: The case for fibre bitstream differentiation

Fibre bitstream differentiation aligns consumer and investor interests:

- ✓ It supports **digital inclusion**, enabling low cost entry level products
- ✓ It **boosts uptake, revenue and investment** at wholesale and retail
- ✓ It enables **copper to fibre migration**

Fibre unbundling could undermine differentiated product ranges at both wholesale and retail

"if an unbundled product is available which offers the full capability of fibre at a single wholesale price, then any retailer who attempts to charge a premium for the highest possible speed will be undercut and one who charges less for a lower speed value package will not find it viable"

Plum Consulting

"Layer 1 unbundling would... involve a significant trade-off in terms of weakened investment incentives since overall demand and revenue will be lower, and reduced scope to offer entry level packages which would support digital inclusion."

Plum Consulting

Choosing the point of regulation: fibre bitstream differentiation, fibre unbundling and pricing flexibility

- > There's a choice to be made around the appropriate point of regulation. It will either be regulation at: layer 1 or layer 2.
- > Plum consulting argue that speed-price differentiation must exist at the wholesale level to be sustainable at retail.

Active wholesale products



Source: Plum Consulting

Passive wholesale product



Source: Plum Consulting

"Pricing flexibility at wholesale level is necessary to allow both the access seeker and the SMP operator's retail business to introduce price differentiation on the retail broadband market in order to better address consumer preferences and foster penetration of very high-speed broadband services"

September 2013 EC Recommendation on costing and non-discrimination

Choosing the point of regulation: Unbundling if the benefits outweigh the costs

Metric	Fibre bitstream	Fibre unbundling
Innovation	Innovation by open access network operator	RSP innovation – scale may be unclear
Differentiation	Differentiated bitstream products enabling differentiation at the retail level	Single unbundled product could collapse differentiation at the retail level
Pricing	> A range of price points across differentiated products > Enables low cost entry level product	> Based on Chorus's avoided cost > Entry level products may no longer be viable
Nationally averaged prices	Consistent with nationally averaged prices	Could be inconsistent with national averaging due to prices based on avoided costs - unbundling likely to be concentrated in urban areas
Competition	> No unbundling > Bitstream services would offer an open and level playing field	> Introduces competition at layer 2 > May impact competition at the retail level due to economies of scale in unbundling and likely switching costs for end-users
Investment incentives	Increased incentives for investment due to: > Higher uptake > Relative simplicity and predictability of framework	> May stimulate investment from RSPs > But investment incentives could decrease overall due to falling demand and difficulty in predicting demand for unbundled access

Transition to a fit for purpose framework: Scope for commercial solutions where possible

The TCF supports a utility-style model for fibre and more scope for commercial solutions where possible.

- > Building on that alignment our submission outlines our proposals for how to transition to utility-style regulation.
- > Our proposals take into account the policy objectives outlined in the discussion document, including the aspirations for future investment and the need for competition and innovation at the retail level.
- > We see **two credible options** for transition to a BBM:
 - **Option 1:** Special Access Undertaking (SAU) to implement a BBM from 2020
 - **Option 2:** Transitional arrangement for 2020 – 2030 with a BBM implemented by SAU thereafter
- > Our proposals are outlined in the following slides.

Option 1: SAU to implement a BBM from 2020

The process

Establish combined copper and fibre RAB

- > Initial RAB value could be set using 'line in the sand' approach, moving forward from today's prices

Chorus is subject to a revenue cap: MAR calculated based on building blocks

- > Maximum allowable revenue (MAR) calculated based on return on and of capital, opex and depreciation

Translate MAR into prices

- > Differentiated anchor products
- > Freedom on additional products

The benefits

- > Allows copper / fibre price relativity to be managed to support migration
- > Minimises price shocks in the transition to a BBM
- > Has regulatory precedent
- > Avoids complex regulatory debate

- > Provides constraint on cost recovery overall
- > Ensures revenue sufficiency and a fair return on efficient investment but not more

- > Differentiation enables low cost entry level products
- > Complex cost allocation/lengthy processes avoided
- > RSP consultation and input

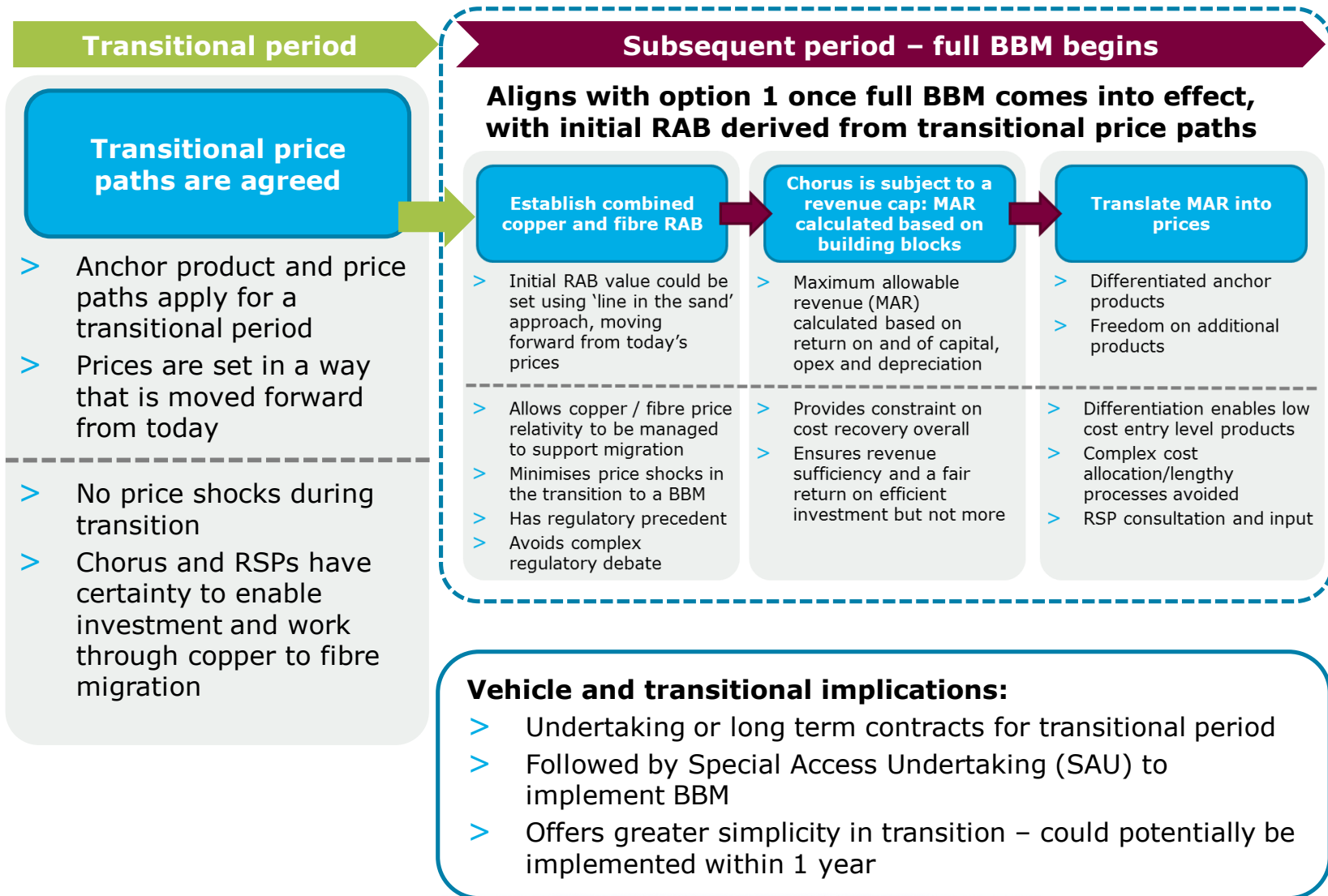
Vehicle and transitional implications:

- > Implemented through a Special Access Undertaking (SAU)
- > Timeframe to implement – 1 to 2 years (compared to around 4 years without an SAU)
- > But less complexity in agreeing design parameters than in a regulator led process

Option 2: Transitional arrangement for 2020 – 2030 with a BBM implemented by SAU thereafter

The process

The benefits



We're all committed to bringing NZ better broadband: How do we get there in a way that works for all kiwis?

New Zealand will need...

Investment

Investment and innovation supported by a stable, predictable and proportionate utility-style regulatory framework

Fair prices

Anchor products with a BBM mechanism to ensure fair prices. Efficiency secured by BBM to keep costs and prices down

The same urban and rural prices

Delivered by addressing copper and fibre in one framework with a commitment to nationwide anchor products

Stable prices as we transition

Proposed price paths for anchor products provides stability and revenue could be used to determine a RAB

Products that match demand

Involving consumers in decisions on new investment and new products

To keep up with change

An undertaking provides flexibility and allows industry input

To have a plan to move off copper

Kiwis ready for the migration through clear milestones (e.g. uptake thresholds)

To keep it simple

A regulatory undertaking with industry input will reduce complexity

A coherent foundation

Grounding the framework in legislation to consider price, product and investment collectively