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Filomena Autunes  
Commerce Commission  
44 The Terrace  
P O Box 2351  
WELLINGTON 6140

Trustpower Limited

Head Office  
108 Durham Street  
Tauranga

Postal Address:  
Private Bag 12023  
Tauranga Mail Centre  
Tauranga 3143

F 0800 32 93 02

Offices in  
Auckland  
Wellington  
Christchurch  
Oamaru

Freephone  
0800 87 87 87

[trustpower.co.nz](http://trustpower.co.nz)

By email: [telco@comcom.govt.nz](mailto:telco@comcom.govt.nz)

## TRUSTPOWER SUBMISSION: DRAFT REPORT ON WHETHER SPARK'S RESALE VOICE SERVICES SHOULD BE OMITTED FROM SCHEDULE 1

### 1 Introduction and overview

- 1.1.1 Trustpower Limited (Trustpower) welcomes the opportunity to provide a submission to the Commerce Commission on its *Draft report on whether Spark's Resale Voice Services should be omitted from Schedule 1 of the Telecommunications Act 2001* (the Draft report).
- 1.1.2 We understand that the Commission's preliminary view is to recommend to the Minister of Communications that Spark's resale voice services be omitted from Schedule 1 of the Telecommunications Act 2001 (the Act), with a transition period to allow Retail Service Providers (RSPs) to consider their wholesale options, and to give them time to mitigate any disruptive effects, including the development of necessary business systems.
- 1.1.3 We have a number of concerns with this approach, including:
  - a) RSPs ability to negotiate a fair and reasonable contract with Spark;
  - b) That there are not currently effective competitive constraints on Spark;
  - c) That the cited benefits of deregulation do not appear to outweigh the associated costs; and
  - d) That the proposed transition period of 12 months is not long enough.
- 1.1.4 Accordingly, we do not believe that Spark's resale voice services should be omitted from Schedule 1 of the Telecommunications Act. If the Commission decides to that these services should be omitted from Schedule 1, then we believe that a transition period of 2-3 years would be appropriate.

### 1.2 Concerns about our ability to contract with Spark

- 1.2.1 We are concerned about our ability to contract with Spark while migrating to alternative services. The Commission has noted concerns from parties about proposed reductions in existing volume-based rebates. We share these concerns, and are also concerned about other margin-increasing tactics Spark may use in contract negotiation.
- 1.2.2 We already have concerns with our existing ability to contract with Spark, and note the following:

- a) Although the Commission states that the PSTN wholesale margin declined by -17% between 2014 and 2015, we conservatively estimate that Spark's wholesale PSTN margin is almost 30%. This is significantly more than the margin for retailers.
- b) Further, in February 2015, Spark increased both its wholesale and retail prices for its voice services, citing uncertainty around backdating of the Commission's final pricing principle (FPP) decision. Following the Commission's decision not to backdate, Spark has made a reimbursement offer to some of its customers<sup>1</sup>, however, it did not reimburse Trustpower even when requested to do so.

This was despite Spark's assurances that it would reimburse its customers if backdating did not occur. Spark stated in its 20 February 2015 submission on the draft determinations for UBA and UCLL services:<sup>2</sup>

We are willing to make a commitment here that, if the Commission decides not to backdate the costs of any UCLL price increase, we will pass the value of our related retail price increases (during the period from 1 February until the Commission's final determinations) back to our customers in a fair and transparent way. We challenge all other RSPs to make the same commitment.

We did not increase our retail prices until March 2016, after the Commission's final determination.

We estimate that Spark likely increased its wholesale margin by over \$10 million between February 2015 and December 2015 as a result. We have concerns that Spark will start engaging in similar behaviour while it still has monopoly power as its resale voice services are not truly constrained by competitive alternatives.

### 1.3 Lack of effective competitive constraints

1.3.1 The Commission states that "[f]or over 99% of commercial and residential addresses, RSPs have at least one alternative wholesale input provided by either Chorus, Local Fibre Companies or fixed wireless operators".<sup>3</sup> The Commission outlines those alternatives as wholesale broadband services offered by Chorus (UCLL and UBA), wholesale voice services offered by Chorus (Baseband copper, Baseband IP, and Baseband IP Extended), wholesale broadband services offered by the local fibre companies, wholesale services offered by Vodafone (FWA and RBI services), and providers who have deployed their own networks, such as Vodafone's cable service and FWA operators.

1.3.2 While we agree that there are emerging technologies and we are starting to see alternative services becoming available, we note that:

- a) The strength of these alternative services is not yet sufficient to constrain Spark's market power. Spark summarised our sentiment to wholesale voice services in its submission on the Schedule 1 review in relation to backhaul. Spark stated:<sup>4</sup>

While there is nascent competition from LFCs and wireless technologies in broadband markets, the strength of these alternatives are not yet sufficient to constrain Chorus' power in broadband infrastructure markets and it would be premature to undertake an investigation at this stage. RSPs rely heavily on Chorus inputs and to remove them from the Act would have a significant adverse impact on the market and end users.

This is our view in relation to Spark's resale voice services; and

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<sup>1</sup> See <http://www.stuff.co.nz/business/industries/77417090/Spark-offers-33-rebate-or-free-upgrade-but-customers-must-claim>.

<sup>2</sup> Spark New Zealand, Submission on draft determinations for UBA and UCLL services, 20 February 2015, [26].

<sup>3</sup> Commerce Commission, Draft report on whether Spark's Resale Voice Services should be omitted from Schedule 1 of the Telecommunications Act 2001, [X9].

<sup>4</sup> Spark New Zealand, Submission on Review of Designated and Specified Services under Schedule 1, 23 May 2016, [7].

- b) There is not open and non-discriminatory wholesale access to fixed wireless and cable services, so we question the effectiveness of relying on these services to constrain Spark's wholesale market power. At best, they constitute only a limited constraint.

#### **1.4 The benefits of deregulation do not outweigh the associated costs and risks**

- 1.4.1 The Commission states that the net benefits of omitting the Resale services are small, but that deregulating Spark's resale voice services will best give effect to Section 18. The Commission cites the following benefits of deregulating Spark's resale voice services: avoided costs of regulation, and avoiding distortions due to the price and non-price terms of the resale services. Neither of these benefits have been quantified.
- 1.4.2 The Commission has indicated that it expects the regulatory costs will be the same whether the resale services are deregulated or not.<sup>5</sup> There is no real benefit.
- 1.4.3 The Commission further states, looking at the lower prices of voice services in other countries, that backstop regulation "gives RSPs the confidence that they will always be able to compete with Spark at the retail level, but it may also limit Spark's incentives to drop prices."<sup>6</sup> We do not believe that existing backstop regulation is limiting Spark's incentives to drop prices. Rather, this is more indicative of a lack of price regulation of a monopoly service. If there were real competitive constraints on Spark's resale voice services, its price would have decreased further than it has, and likely be closer to that of other countries.
- 1.4.4 The Commission cites the following costs of deregulating Spark's resale voice services: costs to RSPs of bringing forward the development of the business systems needed to use other wholesale inputs, and costs to the small number of customers whose choice of telecommunications suppliers may be reduced. Again, these have not been quantified.
- 1.4.5 The Commission's approach, at face value, seems to favour benefits to Spark over detriments to other RSPs and end users. We question how this best gives effect to section 18.
- 1.4.6 The Commission states, with respect to the costs to RSPs of bringing forward the development of business systems required, that "RSPs are already migrating from resale to other wholesale inputs in any event because of their greater potential in terms of functionality, so this effect largely relates to the bringing forward of costs that are likely to be incurred anyway."<sup>7</sup>
- 1.4.7 This does not take into account the risks to consumer experience of fast-tracking these processes. Time is required to ensure adequate testing of the new systems and staff training. The risk of errors, and therefore the likelihood of poor customer experience, increases if there is inadequate time. This adds additional expense, and has the potential to be particularly costly to business models based on superior customer service and experience, such as Trustpower's.
- 1.4.8 We are also concerned that the Commission's approach does not take into account the following:
- a) Adequate time will be required to allow for migration from Spark's resale voice services on to alternatives, such as Baseband services. Chorus is currently only able to connect 2000-4000 end-users per month to its Baseband services. Chorus is currently undertaking improvements to its existing processes, however, even after such improvements, it will not be capable large-scale migration. Incremental migration will be required; and

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<sup>5</sup> Commerce Commission, Draft report on whether Spark's Resale Voice Services should be omitted from Schedule 1 of the Telecommunications Act 2001, [130].

<sup>6</sup> Commerce Commission, Draft report on whether Spark's Resale Voice Services should be omitted from Schedule 1 of the Telecommunications Act 2001, [131].

<sup>7</sup> Commerce Commission, Draft report on whether Spark's Resale Voice Services should be omitted from Schedule 1 of the Telecommunications Act 2001, [136].

- b) Spark has previously exercised its market power to increase its margin on its wholesale voice services, as outlined in section 1.2 above. We do not believe that this would have been possible if its services were constrained by competition. We also have concerns about our ability to negotiate a fair agreement with Spark in the absence of a backstop regulatory regime.

## **1.5 The Commission's preliminary recommendation**

- 1.5.1 The Commission's preliminary recommendation is that Spark's resale voice services should be deregulated because retail competition is now established, and that the number of end users that will not benefit from competitive constraints is small and will have a price capped by Spark's Telecommunications Service Obligations.<sup>8</sup> As outlined above, we disagree with this preliminary recommendation.
- 1.5.2 We do not believe that there is evidence to show that wholesale competition is firmly established. While wholesale competition is developing, backstop regulation will be required to ensure competition strengthens without affording Spark the ability to make monopoly profit in the interim. As explained in section 1.2, Spark has collected monopoly profit of around \$10 million over the period from February 2015 to December 2015. Further, we do not believe the benefits of deregulation outweigh the potential costs.

## **1.6 There should be a transition period of 2-3 years if Spark's resale voice services are deregulated**

- 1.6.1 The Commission is recommending a transition period of 12 months from the date on which the Order in Council is made for deregulating Spark's resale voice services. It states that this period is to allow RSP's time to bring forward investments in business systems required to use other wholesale inputs, adapt to the use of new inputs, migrate customers, and renegotiate new commercial contracts with Spark.
- 1.6.2 As previously explained, the cost of fast-tracking migrating customers from Spark's resale voice services onto an alternative wholesale service, such as Chorus' Baseband services, is high. We would also need to negotiate contracts with other providers of these wholesale inputs. Contract negotiation can take a considerable amount of time, and we would need to be confident that changing providers would be in the best interests of our customers.
- 1.6.3 Like Vodafone and Vocus, we believe that a transition period of 2-3 years would be more appropriate. One year is too short a time period to undertake such a transition.
- 1.6.4 For any questions relating to the material in this submission, please contact Peter Gregory, Business Manager – Telecommunications on 07 572 9888.

Regards,



**JESSICA BEVIN**  
**REGULATORY ADVISOR**

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<sup>8</sup> Commerce Commission, Draft report on whether Spark's Resale Voice Services should be omitted from Schedule 1 of the Telecommunications Act 2001, [149].