

The logo features a stylized, dashed line graphic that resembles a series of connected arches or a wave, positioned to the left of the company name.

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**TELECOMMUNICATIONS REGULATION: THE  
LATEST IN THE INTERNET/DATA SPACE, AND  
WHAT CAN ISPs AND OTHERS DO ABOUT IT?**

**April 2005**

There's a lot happening under the Telecommunications Act and in the regulatory space that affects Internet and data. In this article, we've summarised and introduced the various things that affect Internet stakeholders, such as ISPs, to the tune of tens of millions of dollars. We go back to basics, and then outline the many things that are happening now.

It's difficult for each ISP to go it alone, but with smart use of resources and solutions, strong outcomes are possible in the regulatory area.

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## 1 Summary

- 1.1 Some things in the Telecommunications Act space self-evidently affect the Internet community. Others, at first sight, seem irrelevant, but in fact they are very material either now or down the track.
- 1.2 There are complex economic, legal, strategic, commercial and technical issues at play. This should not be overlooked, for the correct position is not always what appears at first sight.
- 1.3 Internet stakeholders, including ISPs, are affected by the actual and potential implementation of the legislation in the order of tens of millions of dollars, if not more, yet their voices are hardly heard at all.
- 1.4 The work of the Telecommunications Commissioner is moving rapidly to an increasing Internet/data focus, beyond voice telephony. Of course, Internet Protocol is becoming integral to voice telephony anyway, both in the “*back office*” (eg, within Telecom’s network) and increasingly “*front office*” (eg, VOIP). So Internet and data are major regulatory issues.
- 1.5 The Telecommunications Commissioner is dealing with a wide array of issues. This paper highlights some of the key developments from an Internet/Data perspective. It also deals with the current Ministry of Economic Development review of the Act as well as Commerce Act issues such as the Commission’s claim against Telecom in relation to the way in which data tails have been sold.
- 1.6 Of necessity, this paper only overviews the situation. There are many issues, most of which are very complex.
- 1.7 The work of the Telecommunications Commissioner is heavily dominated by TelstraClear and Telecom. Many decisions are being made that directly affect the Internet community such as ISPs, which have an impact in the order of tens of millions of dollars. It’s unfortunate that the Internet community and ISPs have had only a limited voice so far, but this can change with clever solutions such as use of the technical and commercial resources widely available from ISPs, information that can be pooled from ISPs and others, and combining resources and funding to get better outcomes.
- 1.8 First, we’ll start by explaining how the Telecommunications Act works. Then, we’ll turn to the detail including areas where many in the Internet community might be quite surprised as to how much the regulatory regime affects them in unexpected ways.

## 2 How Does the Telecommunications Act Work?

- 2.1 The Act contains a list of access services in respect of which an “*access seeker*” (usually TelstraClear in practice, but it could easily be an ISP or another telco)

can seek a determination by the Commerce Commission. The request is usually for the supply of a service by an “*access provider*”. Typically this is Telecom. Many of these services are Internet/data-related. Those lists of access services describe the circumstances in which an access provider should be required to provide that service if at all. That generally includes the competitive nature of the market, the terms of the service, and, usually, pricing for the service if it is provided to the access seeker.

- 2.2 When an application is filed, and the Commission decides it will hear the application, the Commission will get submissions from affected parties. It then issues a draft determination, followed by a conference of interested parties. Involvement and comment from interested parties (such as ISPs, other telcos, etc) is welcomed. Note however that, while input is possible, most applications so far have been bilateral (ie: they deal with the position between 2 parties (typically TelstraClear and Telecom) and not a wider group of parties).
- 2.3 Then the Commission issues a final determination (generally only as between the 2 parties to the determination) which will often include an initial assessment of price. The more detailed and complex assessment of final price generally happens later.
- 2.4 The Commission can be persuaded that it should change the preliminary view it expressed in the draft determination. The best example is that this happened on its local loop unbundling decision, when the Commission reversed its draft determination (favouring unbundling), to the opposite in the final determination.
- 2.5 That’s the formal regulated procedure. However, there is a strong focus in the Act on commercial resolution ahead of regulated solutions. Generally, the obligations under the Act do not kick in at the outset. Rather they await a determination by the Commission, and an application to the Commission must be preceded by negotiations. This is a significant point. These access services are not controlled by the Act, even though they are specified in the Act, until someone applies to the Commission. One facet of this is that parties are faced with a choice of either negotiating a commercial deal (typically with Telecom), or applying to the Commission for a determination. The access seekers can’t do both.
- 2.6 A typical example is that TelstraClear has elected to apply for a determination in relation to UBS (the ADSL service added to the regulated list of services following the local loop unbundling enquiry last year). Many other ISPs however have elected to go straight to accepting Telecom’s commercial UBS offering even though many consider that it is inadequate in terms of price, contract terms, the requirement to pay a churn fee etc. Note however that an ISP taking a particular UBS offering (eg: 1 Mb/s downstream) is not precluded from applying to the Commission in relation to a different regulated UBS offering (eg: 2 Mb/s).

- 2.7 Because the Commission has now decided a number of determinations, how the Act applies in each case is becoming increasingly clear. But there are still many issues to resolve.
- 2.8 While parties are able to put in low-cost submissions (and some, including ISPs, have done so), Commission determination applications are expensive affairs, typically involving considerable legal, economic, technical and commercial resource coupled with complex overlaying strategic considerations. It is very difficult for smaller players to be involved in a way which is effective in view of the cost, unless there is highly savvy use of resource (eg, particular technical experts from ISPs) and pooling of effort.
- 2.9 For example, most of the “*low budget*” submissions we have read will probably have had little impact on the Commission, given for example, the complexity of the issues. This skews the process and favours the large telcos which are spending many millions in the process. That’s unfortunate because the Commission won’t necessarily get all the information it needs to help it make fully informed decisions. But a solution to that problem is not easy. It’s a problem in any regulatory and litigation situation. InternetNZ, in its MED submissions, focused on this problem.<sup>1</sup> It’s a pity there’s not wider involvement beyond, typically, Telecom and TelstraClear (with some input from Vodafone and occasional appearances by players such as ihug, BCL etc). The impact on ISPs and others is very considerable, yet they largely do not become involved.

### 3 UBS and Unbundling

- 3.1 Last year, the Minister confirmed the Commission’s recommendations as to unbundling the local loop and dealing with the Telecom data network. Of course, the local loop (that is, in broad terms, Telecom’s copper wire local access network) is not to be unbundled.
- 3.2 Although they overlap, Telecom’s local loop and its data network (the so-called Public Data Network) are treated separately in the Act. As to the data network, the only “*unbundled*” regulated service as a result of the unbundling decision is the ADSL service called UBS (Unbundled Bit Stream). It has a minimum downstream speed of 256 Kb/s and a maximum upstream speed of 128 Kb/s.
- 3.3 The Commission has confirmed that the regulated service includes downstream speeds up to the maximum that are technically available (ie: several Mb/s).
- 3.4 The regulated service is not to be a “*real time*” service (so, subject to technology change, it can’t handle VOIP). This of course is a heavily constrained service compared to what is technically available via ADSL let alone ADSL2.

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<sup>1</sup> <http://www.med.govt.nz/pbt/telecom/implementation-review/submissions/12/index.html>. InternetNZ’s cross-submissions are at <http://www.med.govt.nz/pbt/telecom/implementation-review/cross-submissions/05/index.html>

- 3.5 Oversimplifying what is a complex analysis, the Commission, in making the unbundling and data network decision, had regard to the long-term implications for the economy (dynamic efficiencies) ahead of the short-term gains (static efficiencies) such as short term reduced prices etc. In particular, it decided that it was important to set up an environment which encouraged and enabled Telecom to spend money in the long term on infrastructure (particularly, the roll out of its NGN network). The decision was always going to be controversial, whichever way it went. Its right to emphasise that the issues are not straightforward and that there are complex economic modelling and other issues involved which are hard to take on board without a full reading of the Commission's unbundling decision. This highlights the reality that much of the work of the Commission must be addressed at quite a detailed level, and relatively superficial submissions are not going to carry much weight. The telco industry, and New Zealand generally, are not alone in this. That's not to say, however, that well-made submissions on particular issues at a practical level won't hit the mark; they might do in particular circumstances.
- 3.6 As a result of the unbundling decision, we have the relatively limited UBS offering set out in the Act, the "*Unbundled Partial Circuits*" solution noted below, and we have no local loop unbundling.
- 3.7 A party seeking the regulated UBS service has a choice. It either negotiates a deal with Telecom to get the service commercially (ie, other than under the Act), or it applies for a determination around the detail of that service, to get a regulated service. Because an access seeker can't do both, it faces a stark choice, although it is not stopped from seeking a different level regulated UBS service (eg: if it has a 1 Mb/s commercial service, it can seek a service with unrestricted downstream speeds).
- 3.8 Alongside this regulated service, Telecom introduced its commercial (ie, unregulated) offering which currently goes up to 2 Mb/s downstream. But it is still limited to a heavily constrained 128 Kb/s upstream and it doesn't support real time communications (due to constrained latency etc).
- 3.9 For most, if not all, of the smaller ISPs, there was no choice. There was both:
- 3.9.1 the delay in going to a Commission determination (thereby giving Xtra and other UBS ISPs first mover advantage); and
  - 3.9.2 the cost of the application to the Commission.
- 3.10 This drove most ISPs down the path of accepting the UBS commercial offering made by Telecom. ISPs were concerned (even though Telecom voluntarily offered a faster service) that the commercial terms, pricing (such as the controversial churn fee) etc had Telecom offering only a "*take it or leave it*" choice.

- 3.11 So what should an ISP do? Apply for a determination as to the regulated service or accept the Telecom commercial service? ISPs generally went down the commercial path.
- 3.12 TelstraClear on the other hand decided that it would not take the commercial service. Instead it applied for a determination. Given its size, from a funding point of view, it is better able to do so. But this is still a particularly unsatisfactory step for TelstraClear to take, from its perspective, given the delays in getting the service, the cost involved and so on. They contend that Telecom is pushing the boundaries and making them go through the hoops at each step (that is, prolonged commercial negotiation followed by a prolonged regulatory process).
- 3.13 If TelstraClear succeed with their application, the other ISPs don't necessarily get the benefit of the terms that TelstraClear either negotiates or has regulated. However, Telecom have indicated in their MED submissions that they generally will allow improved terms to trickle down to other players including ISPs.

#### **4 TelstraClear's UBS application: the important detail**

- 4.1 This application is important for other reasons. It is the first time that an application has drilled down to the real detail of a service such as latency, jitter, provisioning times, operational support systems to be provided by Telecom, KPIs, SLAs, value-added services such as static IP addresses, and so on. Much of this detail is particularly important for ISPs. Therefore, this application by TelstraClear in respect of UBS is particularly significant and should be strongly supported by ISPs, whose interests largely align on this application with TelstraClear's. There is a lot that ISPs can do. The application has big and multi-million dollar implications for ISPs and others and ISPs should benefit even if, as the legislation encourages, TelstraClear does a deal on UBS with Telecom.
- 4.2 The TelstraClear application is up to the stage where Telecom and TelstraClear have filed submissions and cross-submissions. The next step is a draft determination by the Commission, followed by a conference, then a final determination. Interested parties such as ISPs and other Internet stakeholders are able to comment and contribute to the process.

#### **5 Unbundled Partial Circuits**

- 5.1 The UBS solution focuses on the residential and small business end of the market. That leaves out local access for large customers (often called data tails). One of the reasons why the Commission did not recommend unbundling of the data network, beyond the limited UBS service, was Telecom's announcement that it would provide to other suppliers a data tail service which is called Unbundled Partial Circuits (typically this would be something like an ATM or other relatively large volume access service).

- 5.2 Not everyone is happy about the process the Commission went through in accepting this Telecom undertaking (that's something of an understatement), nor are they all happy with the final outcome (the overall terms, pricing and so on of the Unbundled Partial Circuits offering).
- 5.3 In short, the outcome of the decision on unbundling of the data side of Telecom's business is a decidedly constrained version of ADSL and the Unbundled Partial Circuits commercial offering. The primary rationale for this outcome is long term economic efficiency.
- 5.4 Data tails are an illustration of the different ways in which the activities of access providers can be controlled. The Commission is taking steps in the High Court under the Commerce Act (instead of the Telecommunications Act) against Telecom in relation to data tails. More about this below.

## 6 VOIP Generally

- 6.1 Skype and other VOIP options are rapidly emerging, and these are already impacting the telcos' often profitable voice telephony business.
- 6.2 On 11 April 2005, Infotech reported someone as saying that Telecom planned to introduce, in its Internet service available to its wholesale customers, additional latency (that is, delay in the time it takes an Internet packet to travel from point A to point B). The article notes Telecom's denial that this is the case, and the Commerce Commission's reassurance on this.
- 6.3 The Commission has, usefully, monitored situations such as this, but only at a relatively high level such as here. The allegation made against Telecom lies within a complex technical and commercial environment, including choices that Telecom makes about shaping the traffic for operational reasons. Without a more detailed review and monitoring, it can be hard to get to the bottom of what is really happening, and to get reassurance that the claims by a carrier such as Telecom are based on genuine technical and commercial considerations rather than being a smokescreen to achieve an inappropriate benefit. Submissions to MED recommend much stronger monitoring and review by the Commission, and that this could be a powerful mechanism for regulatory compliance. The Commission lacks significant technical staff and resourcing, which is a major problem in this and other areas.
- 6.4 Having stronger monitoring can benefit Telecom. For example, Telecom is insistent that the UBS roll-out delays were technical (caused by rapid deployment of UBS) and not deliberate delays. Some in the Internet community are sceptical: strong review and monitoring can help Telecom to confirm the position.
- 6.5 ISPs have a strong role to play in this monitoring process. Not only do they have experts available on tap who can comment on what's happening, but they also often have the information about what's actually happening. That can be



aggregated into powerful information for the Commission and for public release, in a way which does not identify individual IPS.

## 7 Number Portability

- 7.1 This impacts ISPs and the Internet community much more than appears at first sight.
- 7.2 The delays in getting local number portability introduced are legendary. There is every sign that delays will continue even though the industry forum, the Telecommunications Carriers Forum (TCF) is running with this. The TCF has completed Codes for Local and Mobile Number Portability. While the Telecommunications Act anticipates industry agreement to such Codes, there is some question about their enforceability (which might be fixed following the MED Review of the Act noted below). In the meantime, several parties have applied to the Commission for, in effect, validation of the Codes so that questions about enforceability are removed.
- 7.3 This application to the Commission (called the “*Functions application*”) has had very little, if any, input from ISP stakeholders, who are potentially directly affected both in the short and in the long term, for the reasons noted below. While judgment calls need to be made as to the extent to which the Internet community should get involved in applications such as this, lack of involvement early on could be problematic later, particularly as VOIP becomes more widespread. Regulatory action can have a long lead-in time although ihug’s recent experience with its UBS application is that applications can be handled and sorted out quickly. So it’s important to try and think now how regulation might impact in say 3 to 5 years time.
- 7.4 This Functions application is at the stage where submissions can be made prior to release of a draft determination (then, following the usual course, after that draft determination is issued, there is a further chance for submissions to be made, and there may well be a public conference).
- 7.5 Prior to this Functions application, the Commission had issued a draft determination on the allocation of costs of number portability, for both the local number and the mobile services, as between carriers. If a public conference is to be held, that’s the next step, although the prospect of submissions by the Internet community, as to the draft determination, is not entirely ruled out. Submissions on this Cost Allocation Application by Internet players (other than the major telcos) were relatively limited.
- 7.6 The Commission has merged the hearing path for both the Functions and the Cost Allocation applications. The Commission has indicated a relatively short lead-in timeframe up to the final determination.
- 7.7 Vodafone in particular have raised before the Commission, in respect of the latest application (the Functions Application), an issue of significant interest and

concern for the Internet community. There is a legal interpretational issue under the Telecommunications Act about the ability to transfer numbers as between the mobile network and the local number network. This is of particular interest to the Internet community, particularly as VOIP becomes more ubiquitous. Take as an example, a wireless provider such as Woosh (the same issue applies to a landline ISP). The ISP, when it introduces VOIP, will want to be able to migrate someone with a Telecom or TelstraClear number (or possibly even a Vodafone mobile number) across to its own network. To be able to use another carrier's number for Woosh's own VOIP service makes it more likely that someone will migrate to VOIP. This significantly reduces a barrier to churn. There are major technical and practical issues to work through, which can be resolved. But, given the delays with local number portability, unless it's sped up, this could take quite some time, to the detriment of potential VOIP providers including ISPs. If it's taken so many years to deal even with transferring numbers between landline telcos, how long will it take to add number portability between VOIP, landline and mobile? The delays in introducing number portability will create marketing barriers for ISPs.

- 7.8 Vodafone maintain (and Telecom takes the contrary position) that the Act, as drafted, facilitates number portability between local and mobile networks. This is an issue in which ISPs ideally should participate now.
- 7.9 This is likely to become of increasing concern to ISPs over the coming years. The time taken in the Telecommunications Act process are such that, ideally, ISPs and other Internet stakeholders should be looking ahead to sort this sooner than later.
- 7.10 Finally, to complete the picture on number portability, there is potentially a new entrant on the scene, in the form of ENUM, which comprises a new numbering system with plenty of flexibility and in-built portability suitability. Individuals will get the equivalent of a phone number (ie, this will be person-specific not location-specific) and the person can elect which device will receive a call (and that can vary according to time, place, circumstance, etc). It will of course raise a number of issues, and could impact considerably on this number portability concern. Discussions are underway at present around ENUM.

## **8 Telecommunications Services Obligations (TSO)**

- 8.1 The TSO regime is the mechanism by which Telecom gets subsidised for funding the supply of telephone services to customers that aren't commercially viable. Looking at the big picture, whether and how this should be happening is a big issue (a number of players say the TSO should be ditched or replaced by a contestable model). Then there are considerations around the details which affect ISPs (potentially these have considerable impact). Already ISPs are indirectly affected, as TSO liability of upstream telcos gets passed down to their customers (after all, ultimately it's the end user customers which pay for the TSO).

- 8.2 At the end of March 2005, the Commission issued its final TSO determination for the 2002/2003 year. The outcome is highly beneficial to most Internet stakeholders including ISPs, but the MED Review noted below could change things. We now outline the issues relevant to ISPs.
- 8.3 **“Liable person”**: TelstraClear and others have been arguing that the definition of “*liable person*” (which defines which parties have to contribute towards TSO) should be extended much wider than at present. This had the prospect of capturing ISPs within the TSO liability net. However, the Commission has held its ground on this and:
- 8.3.1 limited “*liable person*” to mean those with interconnection agreements with Telecom; and
- 8.3.2 confirmed that “*pure*” ISPs are not caught within the liable person definition. They don’t “*switch*” traffic.
- 8.4 This doesn’t mean that TSO isn’t an issue for ISPs. As they move to VOIP, it becomes an issue, and this will be an increasing trend. For Woosh (a wireless variation on an ISP) this is already an issue for when it rolls out VOIP. We note that ihug is already paying a TSO sum as a liable person.
- 8.5 **“Revenue”**: The next issue is the method of calculating revenue. That’s how a party’s share of the TSO cost is worked out. The method of calculating the contribution is controversial as well. TelstraClear pushed for a “*net revenue*” methodology (which spreads out TSO payments across relevant participants, from the incumbent telco through to the ultimate retailer to the end user). Vodafone called for a “*retail revenue*” methodology which would have payments instead being made only by the retailers to the ultimate end users. An analogy can be drawn between sales tax and GST. The “*net revenue*” approach is like GST. TSO payers would pay a net sum based on inputs and outputs. “*Retail revenue*” is like sales tax, which is only imposed on the retailer to the ultimate customer. In other words, generally, one retailer pays, rather than payment being spread between the incumbent carrier, that retailer, and all parties between.
- 8.6 The net revenue model is best for most ISPs. The retail model would have been highly disadvantageous to most ISPs when and if they are liable to pay. This is illustrated by some figures which indicate that, if UBS fell within the TSO net, 4% of revenues (ie, turnover) from UBS sales would be payable under the TSO tax net. With Telecom selling the UBS service at their retail price less 16%, that 4%, of course, with such tight margins, is a big part of net profit. This might be enough to fatally jeopardise many ISPs’ UBS offerings. Fortunately, from the Internet community’s point of view, the Commission has confirmed the TelstraClear approach (and anyway limited the liable person definition). So, all in all, the current position is a win for most in the Internet community. But the end is not in sight yet. First, there is the prospect of adverse change in the MED Review noted below. Second, Vodafone might try and appeal the decision to

the High Court (they failed on their appeal on the same issue last year on a procedural point).

- 8.7 **Methods for getting around TSO liability:** One of the reasons that “*liable person*” came up on the Commerce Commission agenda is that CallPlus and another operator established their businesses as two separate and unrelated companies, one for the network and one for retail services. They hoped that, by doing this, they would escape the TSO tax net, in view of the unusual definition of liable person. However, in particular by the way it interpreted the definition of “*end user*”, the Commission has found a solution which stops operators from utilising this loophole.

## 9 MED Review of the Telecommunications Act

- 9.1 This is a convenient point to introduce this Review. It commenced late last year and has been through submission and cross-submission by interested parties. Extending the “*liable person*” definition, and altering the method of calculating revenue, remains on the agenda at this policy level. So ISPs are not out of the woods yet. The potential problem for the Internet community has not gone away.
- 9.2 InternetNZ filed comprehensive submissions and cross-submissions in relation to the various issues raised by the MED discussion paper, and this included a push for a restricted approach to TSO, with reduced impact on the Internet community. The submissions are at: <http://www.med.govt.nz/pbt/telecom/implementation-review/submissions/12/index.html>. InternetNZ’s cross-submissions are at <http://www.med.govt.nz/pbt/telecom/implementation-review/cross-submissions/05/index.html>. That website contains the submissions of the other parties as well.
- 9.3 Regrettably, from the perspective of many Internet stakeholders, the MED Review is largely limited to one of process rather than the substance of the Act. There are many that see the Act as having had too light-handed an impact upon the telecommunications market. The review only touches the sides of the Act rather than dealing with its principles. However, it’s expected there will be a more comprehensive review of the Act in a later year.
- 9.4 There are a number of potential changes, including at the process level, which could greatly benefit ISPs and the Internet community. One is to put a stop to the stark choice faced by ISPs when offered a commercial service by an access provider (such as Telecom). If they consider it is less than satisfactory, they often feel they have no choice but to take it, in view of the cost and delay involved in applying to the Commission for a determination. The UBS example (and the choice by ISPs and TelstraClear respectively illustrates this problem).
- 9.5 Other submissions by InternetNZ include:

- 9.5.1 Support for the concept of Reference Offers. The idea here is that, for particular services, the basic terms of that service (such as contract terms, service levels and so on) are either agreed early on, or resolved by some mechanism via the Commerce Commission. Reference Offers are used in similar regimes overseas, and they provide a mechanism by which smaller players get quicker and less costly access to regulated services. For this reason they have the potential to benefit the Internet community.
- 9.5.2 The Commerce Commission can fulfil a very useful role in obtaining information from industry participants and using this, among other things, to monitor compliance requirements, obtain information to enable better decision-making and so on.
- 9.5.3 Given that our regulatory model is based upon commercial negotiation ahead of regulation, add a compulsory mediation step (by which the parties must, if directed by the Commission, meet and endeavour to resolve issues utilising a mediator (that is, a facilitator not a decision-maker). This should help that process and seems a highly desirable addition to the ways in which issues can be resolved. Compulsory mediation is being applied in other areas successfully and there is no reason why it could not be successful here.
- 9.6 MED will now be considering the various submissions. It will come up with a report to the Minister, and that may lead to some amended legislation.

## 10 Internet Peering

- 10.1 The departure of Telecom and TelstraClear from peering is of course highly controversial. That departure requires most other ISPs to pay for access to their networks (by way of Internet transit agreements). If affected ISPs consider that they end up paying beyond what is appropriate as a result, under their Internet transit agreements, one option is to seek a determination by the Commissioner. One of the issues would be whether, as a result of their position in the market, Telecom and TelstraClear are able to extract excessive charges from downstream ISPs (sometimes called monopoly rents). Internet peering and transit agreements do raise complex economic and commercial issues, including respective values and volumes of traffic, respective infrastructure, and so on. So this is not a straightforward area and one which sees some taking a somewhat oversimplified view to what is complex.
- 10.2 Any regulatory action (let alone any other type of action) is unlikely to lead to an outcome by which TelstraClear or Telecom must fully peer in the sense of exchanging all domestic traffic for free. Rather, the issue would probably be more like: *“How much should they be able to charge for exchange of traffic on their network?”*

- 10.3 In view of a recent decision by the Commission it may be arguable that this issue can be reviewed by the Commission under the Act as it stands. If that is not so (and an earlier Commission decision stands), the industry may seek a determination to have those transit services included as a service which can be regulated. Then the issue of whether monopoly rents are being extracted can be considered (a step that is being taken by the competition authority in Australia, the ACCC).
- 10.4 This is part of the array of solutions that the industry could be considering as a result of the Telecom and TelstraClear departure from peering. Practical difficulties are the size and resources of Telecom and TelstraClear (which spend many millions a year in Commission activity), as against the diffused interests of the ISPs. ISPs have the potential ability to make a multi-million dollar difference to their position, but no one ISP can do it alone.

## 11 Wholesale Services

- 11.1 Many wholesale services, supplied to ultimate end-users, are regulated as a result of a TelstraClear application.<sup>2</sup> Where these are utilised by ISPs, they will have details available from Telecom.
- 11.2 In November last year, TelstraClear filed an application for determination in relation to various Telecom Internet-related services such as Private Office Networking, Secure Business Internet and Connect Anywhere. This application has only got as far as the Commission confirming that it can proceed. Apparently, the parties agreed that this application can be put on the back burner while other applications are handled by the Commission. While these are value-added services that ISPs other than TelstraClear's own ISPs might want to rollout, they are probably not as pivotal to ISPs' businesses as, say, UBS.

## 12 Final Price Decisions

- 12.1 Generally, the Commission makes an interim price decision (that is, the price at which the access provider, typically Telecom, must sell to the access seeker). There is provision for determining a final price, based on a much more detailed and complex analysis.
- 12.2 The Internet community including ISPs have the opportunity to become involved in the Commission's decision-making around final pricing principles. As an example, many ISPs are concerned about the price at which they are having to buy UBS from Telecom, saying there is simply not enough margin in

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<sup>2</sup> For further details of the services subject to the wholesale determination see <http://www.comcom.govt.nz//IndustryRegulation/Telecommunications/Wholesale/WholesaleDeterminatons/ContentFiles/Documents/tclwd12may2003.PDF>.



it to make it work from a profitability perspective. Getting involved in final pricing determinations (as well as negotiations leading up to final pricing) can be an effective way of improving profitability. While ISPs and the Internet community often have a lot in common with parties more actively involved before the Commission (and alignments change depending on which particular issue is involved) that is not always the case. Interests are not always on all fours. The most graphic illustration of this is Internet peering. Although not before the Commission yet, this is an issue on which the larger players that are actively involved in the Commission (in particular, Telecom and TelstraClear) have largely opposing views and interests to the ISP community.

- 12.3 The latest development is the release of a principles paper by the Commission on 12 April, dealing with the principles underlying the final discount for resale of business and residential services. This revolves around the costs that are saved by Telecom when resellers perform all or some of the retailing function. The Commission is looking at producing its draft determination in the second half of 2005.

### **13 Commerce Act Runs in Parallel to Telecommunications Act**

- 13.1 The Commerce Act covers the general competition law space in New Zealand. The Telecommunications Act is a specialised form of regulation for this particular industry. In general terms, the Commerce Act continues to affect this space even though there is the Telecommunications Act.
- 13.2 Most notably for the Internet community, the Commerce Commission is currently suing Telecom for alleged breaches under the Commerce Act in relation to the supply of data tails to Telecom's competitors. The Commission seeks an injunction against Telecom as well as a monetary penalty (which could be substantial).
- 13.3 This claim relates to events which started in late 1998/early 1999 so things have moved on since then. However, the Commission's ability to sue under the Commerce Act (and also the Telecommunications Act) will always have a controlling effect on the competitive activities of any party, and Telecom will be no exception to this.
- 13.4 In late 1998 Telecom introduced new pricing for its own retail offerings for high-speed data transmission services. In March 1999 it introduced new wholesale pricing for the two options available to its competitors (resale of those transmission services and access to dedicated data tails in Telecom's network).<sup>3</sup> The Commission is arguing that Telecom has used and taken advantage of its dominant position or market power in the wholesale and retail

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<sup>3</sup> The background is set out in a 21 December 2004 judgment of the High Court: *Commerce Commission v TCNZ and Telecom New Zealand Ltd* CIV 2004-404-1333 Hansen J.

markets for high-speed data transmission services. In particular, the Commission says that Telecom priced access to data tails at prices which:

- “(a) *Exceeds the price Telecom would charge another service provider for resale of the entire “end to end” service;*
- (b) *Exceeds the comparable retail price charged by Telecom for the provision of comparable data services;*
- (c) *Exceeds the price Telecom charges itself for access to the data tails; and*
- (d) *Exceeds the sum of Telecom’s direct incremental cost and opportunity cost of supplying access to the data tails.”<sup>4</sup>*

13.5 This case is in the early procedural stages, and so there is some time before it goes to trial.

## 14 Conclusion

14.1 There’s a lot happening in this space that affects the Internet, but it’s difficult for there to be active involvement when time and cost is high. But there are options and solutions for ISPs and others to make a difference that may be measured in the tens of millions.

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<sup>4</sup> This is extracted from para 7 of the judgment noted above.



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