

# **WOOSH SUBMISSIONS**

**To the Ministry of Economic  
Development**

## **TELECOMMUNICATIONS SERVICE OBLIGATIONS REGULATORY FRAMEWORK**

**Discussion Document**

**15 October 2007**

## **TSO REVIEW - DELIVERING A BETTER FUTURE FOR NEW ZEALANDERS**

### **Background**

1. Woosh welcomes the TSO review being undertaken by the Ministry for Economic Development. For the reasons set out below we believe that changes to the TSO regime could bring about better services for New Zealanders.

### **The Current TSO Arrangements and the Impact on Consumers**

2. We have reviewed the breakdowns of the TSO loss as provided by the Ministry for Economic Development. In particular we have focussed on the figures for Southland, a region in which Woosh has a widespread network.
3. We understand that the TSO loss for Southland is calculated as follows:
  - 3.1. there are 5,464 commercially non-viable households
  - 3.2. the annual operating TSO loss associated with serving those households is approximately \$9.4m (calculated as 12% of \$78.3m (05/06 draft TSO loss)).
4. Given Woosh's experience in Southland and the relative quality and price of services that it provides, Woosh believes that there are ways in which to structure TSO obligations and funding to better serve these customers.
5. The current arrangements have two key areas of weakness:
  - 5.1. the TSO provider has no incentive to provide anything other than the minimum services;
  - 5.2. operators other than the TSO provider have no incentive to offer service in an area where the TSO provider is receiving a subsidy.
6. Operators, such as Woosh, are able to offer services significantly superior to those required by the TSO. Compare, for example, Telecom's standard household offering with that offered by Woosh:

<b>TSO CUSTOMERS</b>	<b>WOOSH CUSTOMERS</b>
\$40 for POTS only - no voicemail - no caller ID	\$34.95 for POTS and broadband services - free voicemail - free caller ID
Poor data speeds – many rural users struggle to hold a dial-up internet connection	All customers are offered broadband services.
Legacy toll calling boundaries, resulting in common and expensive toll calls (Southland alone is divided into 9 local calling regions)	Offer customers much larger on-net calling areas (the entire South Island on-net is a single free local calling area). Legacy interconnect structures prohibit Woosh from offering similar service for off-net calls.

7. The current TSO arrangements add to the already significant barriers to extending competitive services to rural areas.

### **Woosh's Experience in Southland**

8. Woosh has built a wireless broadband network in Southland offering phone and broadband services.
9. We now offer services to around [ ]% of the households in the Southland region. We estimate this to be [ ] of the 36,000 households in the Southland area (made up of Invercargill, Gore and Southland districts). Therefore there are around [ ] homes to which we do not offer service in Southland currently.
10. As a consequence, Woosh offers service to around more than [ ] of the households considered "commercially non-viable" by the Commerce Commission – we do not consider those customers to be commercially unviable.
11. The capital cost of this network was \$[ ]. This compares with the Commerce Commission's calculations (as we understand them) that Telecom loses \$9.4m each and every year serving the TSO customers in Southland. Rather than receiving a TSO subsidy to operate this network, Woosh is paying a TSO levy to Telecom which increases each time Woosh wins a new customer.
12. While stimulated by an initial capital subsidy, Woosh has proven a successful model with its Southland network. We understand that we now have around 30-40% of the broadband customers in Southland.

### **Goals of the TSO**

13. The current TSO structure grants one party a monopoly over TSO funding. In the ordinary course, the TSO areas are ones in which competition will be late to arrive. Requiring a new entrant to provide an ongoing subsidy to its monopoly competitor means that competition is less likely to occur. As a result the TSO compounds the already shaky economics for new entrants in rural areas.
14. The best way in which to address this is to allow market forces to determine who, in a particular area, is to be the TSO provider and put in place a mechanism which ensures that all providers (including the TSO operators) have incentives to improve their offerings in the TSO areas.
15. The focus of the TSO review should be on delivering a TSO structure which:
  - 15.1. continues to guarantee a minimum level of service for all customers;
  - 15.2. provides mechanisms and incentives for efficient operators to offer those customers improved services over time.

### **Achieving Those Goals**

16. The best way in which to achieve these goals is to have a TSO regime under which:
  - 16.1. there is a competitive process to select the providers of last resort i.e. those who will guarantee a minimum level of service to the relevant households;
  - 16.2. other providers are given incentives to compete in TSO areas by being offered a subsidy proportional to each commercially unviable household which purchases their service.
17. In preparing this proposal we have drawn on the methods of allocating USO funding in the USA and would be happy to discuss this further with you.

### **Appointment of Providers of last resort**

18. Telecom is currently New Zealand's provider of last resort i.e. while other operators may choose to offer service to those customers, Telecom has a legal requirement to do so.
19. Telecom has a monopoly over the TSO subsidy associated with being the operator of last resort. Services to customers could be improved and/or the TSO subsidy reduced if a competitive process were introduced where other operators could offer to be the provider of last resort for customers in an area.
20. Woosh proposes a process where:
  - 20.1. an independent network operator states that it wishes to have "provider of last resort" status in a particular region.
  - 20.2. that operator would need to meet independent criteria during the application process demonstrating that its services meet minimum requirements (as discussed in more detail below).
  - 20.3. a competitive process could then be undertaken to determine which operator is to be the provider of last resort for the region (e.g. tender, auction).
  - 20.4. the successful participant would receive the relevant funding for a specified period at which time another competitive process might be undertaken.
21. Some relevant considerations for this process are:
  - 21.1. It would not be necessary, or appropriate, to have a tender process for all regions from the start of an amended TSO regime. The reality of coverage today is that there are very few areas where any operators would reasonably expect to tender to be a provider of last resort to an entire region. In areas where there is no competition, the current arrangements could continue with Telecom as the provider of last resort. Then as an operator was at a stage where they could offer sufficient service they could trigger a competitive process to select the provider of last resort.
  - 21.2. To avoid excessive tender processes, there would be a minimum period between tenders. If, for example, Vodafone sought to tender for the Wellington region and was successful then no other operator could seek another tender process for a minimum period of, say, 5 years. This would ensure the operator had a sufficient period to allow them to carry out business plan and get a return on investment etc.
  - 21.3. Given this process it would not be necessary to predefine all TSO areas. As all areas need not be put through the tender process from the start it is not necessary to define all areas. The size of area will be a determinant as to how competitive the process is likely to be. If, for example, the South Island were declared a region then Telecom are unlikely to be challenged for many years. On the converse, regions should not be so small as to create administrative burdens with excessive tenders. We would recommend a region size no bigger than the PROBE regions and perhaps no smaller than a single territorial local authority. Within these boundaries, competitive operators may elect what region they wish to bid for.
  - 21.4. This process could be made more competitive by providing bidders technology options to serve the TSO customers. These options might include:

- 21.4.1. the network operated by that operator (in Telecom's case the fixed line and for others likely to be by terrestrial wireless means);
- 21.4.2. provide some time for a new entrant to complete their network by serving customers on the existing copper network for a period;
- 21.4.3. permitting operators to serve customers using satellite technology in remote areas.

### **Eligible TSO providers**

- 22. This process, while it provides a level of competition for the TSO subsidy, does not necessarily in itself create more competition for consumers. As it is a relatively costly process, it will not happen frequently and so operators will not, with this process alone, have the ability to provide constant competitive pressure on each other in uneconomic areas.
- 23. It is therefore desirable to have an additional mechanism by which operators are to compete for TSO funding and ensure that TSO providers have some competition, not just for provider of last resort status, but also to win customers on a day-to-day basis in the relevant TSO region.
- 24. Woosh supports a process under which operators, although they may not be the provider of last resort, are able to apply for "Eligible TSO carrier" status. We envisage it working like this:
  - 24.1. To achieve "eligible" status the operator would need to demonstrate that the services they were offering customers met certain minimum requirements (discussed in more detail below);
  - 24.2. That operator could then be active in the retail market knowing they would receive a portion of the TSO subsidy for each commercially non-viable customer that they won;
  - 24.3. the new TSO operator would be eligible to receive a portion of the TSO subsidy for every "commercially non-viable household" to which they provided services;
  - 24.4. The provider of last resort would also maintain a share of the subsidy for that household as they would be required to maintain network in the area in case the customer wished to revert to their services i.e. a subsidy to recognise their status as provider of last resort.
- 25. The benefits of this are:
  - 25.1. The ability to compete for TSO funding on a "per customer" basis provides operators with the incentives to compete for otherwise commercially non-viable customers in order to win the customer's revenue as well as the TSO subsidy. This should bring about additional competition between operators to offer better services, ensuring improving services (and reducing prices) for these customers over time.
  - 25.2. This avoids needs for operators to cover entire regions in order to be eligible for TSO funding – funding would be proportional to the TSO customers they hosted on their network. For the provider of last resort the TSO funding would be a function of their agreeing to be the provider of last resort with additional funding from having the relevant households as customers.

### **Setting the TSO Subsidy**

26. Operators will compete for TSO subsidies in two ways:

#### *Funding for the Provider of last resort*

- 26.1. This amount will be independent of the number of commercially unviable customers to which the provider of last resort actually provides service
- 26.2. Where the region has been tendered, this value will be determined by the tender process. Where the region has not been tendered this amount could be calculated from time to time by the Commerce Commission.

#### *Funding for TSO Households Served*

- 26.3. This amount will be based on the number of commercially unviable households to which the operator provides service.
- 26.4. This amount could be calculated from time to time by the Commerce Commission on an infrequent basis (say every 5 years).

### **Funding The TSO Services**

27. Funding of the TSO can be dealt with separately from the subsidy mechanism. Telecommunications services are a public good and the Government has been vocal in its demand for better services, and in particular better broadband services. Broadband networks are expensive to deliver with uncertain return. If the Government wishes to accelerate development it should be prepared to invest in that development, in addition to the significant investment and TSO subsidy provided by the industry.

### **Details Of TSO Obligations**

28. As part of the Woosh proposal an operator seeking status to provide TSO services, and so be eligible for TSO subsidies, should be expected to meet certain criteria. Those criteria will relate to the services to be provided to TSO households. Examples may include:
- 28.1. capped retail price
- 28.2. free local calling
- 28.3. access to emergency services.
- 28.4. availability of battery back-up for use during power cuts.

29. In addition, the provider of last resort would have to meet certain coverage requirements, as Telecom does currently in respect of historical services.

### **Incentives for Rural Broadband Services**

30. At this stage it is not practical to mandate that all TSO households be offered a broadband service. However, in order to stimulate such services the Government could establish two levels of subsidy:
- 30.1. a base subsidy for operators who meet the basic phone service requirements (with perhaps minimum dial-up speeds);
- 30.2. a higher subsidy for any operator which provides a TSO household with a broadband service.
31. This will assist to drive innovation and increasing broadband networks in rural areas, a key goal of the Government.