Appendices:

A. Executive Summary – part of Vodafone's report "Views on Commerce Commission's Mobile Termination Final Reconsideration Report."
22 May 2006 - PUBLIC
Submission to MED on the Commerce Commission Final Reconsideration Report on Mobile Termination

Summary
1. This document presents Vodafone's views on the Commission's Final Reconsideration Report on the Regulation of Mobile Termination.

2. We continue to believe that regulation of Mobile Termination Rates would be a mistake.

Regulation generates tiny gains, even in the best case

Table 1: Comparison of the value of MTR regulation on average each year
Total mobile market ~ $2 billion
Retail FTM market ~$380 million
Mobile termination ~$250 million
Maximum benefits of regulation to consumers $17 million
Maximum benefits of regulation to economy $1 million

3. In total over the five years, the maximum consumer welfare impact of MTR regulation is $63 million on an NPV basis. This $63 million works out (once you adjust for the present value) to just over $4 for each New Zealander per year.

4. The effects on the economy are even smaller. The maximum impact on the economy is just over $1 million a year. For an economy worth around $125 billion a year, it does not seem much for an intervention of this magnitude.

5. Basically what this means is what we have been arguing from the very beginning – MTR regulation is a risky and ultimately pointless exercise in shifting money out of the mobile sector and into the fixed-to-mobile sector.

Even these results are very uncertain
6. We are even more concerned about MTR regulation because the Commission's figures are so fragile. Two examples demonstrate our point.

7. The Commission estimates that mobile subscription prices will rise by 82 cents as a result of this regulation, from $43.68 to $44.50 a month. If in fact prices go up by just 47 cents more, or an additional 1%, then this is enough to remove any benefit from this regulation.

8. The Commission predicts that fixed operators will pass through 100% of the regulated reductions in MTRs into retail fixed-to-mobile calling prices by 2011.
The Commission estimates that pass through of reductions in MTRs into fixed-to-mobile calling prices in the last nine years has averaged only 68%.
If fixed-to-mobile pass through rates grow to 80% there are no benefits at all from this regulation. Even 80% is much higher than anything ever seen in New Zealand, and very high in the absence of enforcement, based on the evidence from overseas. If pass through rates remain at their historic levels, regulation has a negative impact on consumer welfare and the economy.

Regulation has only a small impact on consumers but a massive impact on Vodafone and the mobile market
9. MTR regulation means large gains for fixed-to-mobile customers and operators and large losses for mobile customers and mobile operators.

Table 2: Annual impacts of MTR regulation

Fixed to mobile customers gain	$47 million
Fixed-to-mobile operators gain	$18 million
Efficiency gain	$2 million
Mobile customers lose	-$30 million
Mobile operators lose	-$32 million
Cost of regulating	-$2 million
Total economic effect	$1 million

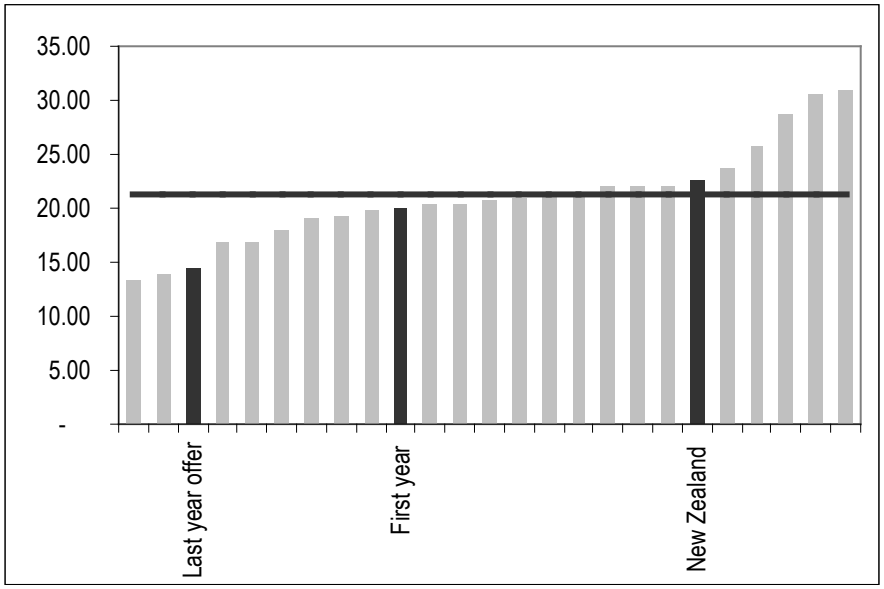
10. The maximum benefit for consumers as a whole from this regulation is $17 million a year.

11. To generate this $17 million benefit involves taking around $62 million a year from mobile operators and customers.

12. This regulation will worsen the business case for Vodafone's 3G mobile broadband rollout, and worsen the business case for new entry into the mobile market.

13. We have made an offer to the Minister to reduce termination rates without regulation. We continue to urge the Minister to accept this offer and avoid further costly, contentious and unproductive argument.

B. Figure 1: MTRs in 23 countries in which Vodafone operates (NZ cpm April 2006)



C. Covec and Ernst & Young Notes

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Analysis of the Revised Vodafone Mobile Termination Commercial Offer

John Small

8 June 2006

On the 10th of May 2006, Vodafone presented an enhanced commercial offer for mobile termination rates to the Minister of Communications. We have analysed the net benefits of setting mobile termination rates at the regulated rates assumed by the Commerce Commission relative to this commercial offer, using the Commission's cost-benefit model. The offer begins on 1 July 2006 and contains the following rates:

Table 1 Mobile termination rates (cents per minute).

	to 31 March 2007	1 April 2007 to 31 March 2008	1 April 2008 to 31 March 2009	1 April 2009 to 31 March 2010	1 April 2010 to 31 March 2011
Termination rate (cpm)	20.0	17.0	16.0	15.0	14.4

The Commission's model estimates the net benefits of regulation (relative to the commercial offer) over a period of five years, from 2007 to 2011. The model is based on June years. The termination rates in the year to June 2006 are also important, as they are the starting point for the analysis. In this year, the termination rates charged by Vodafone and Telecom have differed slightly, as shown in Table 2.

Table 2 Historic termination rates.

	Telecom	Vodafone
Jul-05	0.2600	0.2600
Aug-05	0.2600	0.2600
Sep-05	0.2400	0.2600
Oct-05	0.2400	0.2600
Nov-05	0.2400	0.2600
Dec-05	0.2400	0.2600
Jan-06	0.2400	0.2600
Feb-06	0.2400	0.2600
Mar-06	0.2400	0.2600
Apr-06	0.2250	0.2250
May-06	0.2250	0.2250
Jun-06	0.2250	0.2250
Average	0.2396	0.2513

The Commission's model assumes market shares of 48.9% for Telecom and 51.1% for Vodafone, which gives a weighted average termination rate for the year to June 2006 of 0.2455.

After June 2006, we assumed that Telecom matches Vodafone's commercial offer, so the termination rates in Table 1 applied to all fixed-to-mobile calls. Since the Commission's analysis extends to 30 June 2011 while the commercial offer runs to 31 March 2011, we assumed that the final termination rate of 14.4 cents per minute continued to apply until the end of the period of analysis. We adjusted the offered termination rates to June years as shown in the following table:

Table 3 June year adjustment.

Month	MTR	Month	MTR	Month	MTR	Month	MTR	Month	MTR
Jul-06	0.2000	Jul-07	0.1700	Jul-08	0.1600	Jul-09	0.1500	Jul-10	0.1440
Aug-06	0.2000	Aug-07	0.1700	Aug-08	0.1600	Aug-09	0.1500	Aug-10	0.1440
Sep-06	0.2000	Sep-07	0.1700	Sep-08	0.1600	Sep-09	0.1500	Sep-10	0.1440
Oct-06	0.2000	Oct-07	0.1700	Oct-08	0.1600	Oct-09	0.1500	Oct-10	0.1440
Nov-06	0.2000	Nov-07	0.1700	Nov-08	0.1600	Nov-09	0.1500	Nov-10	0.1440
Dec-06	0.2000	Dec-07	0.1700	Dec-08	0.1600	Dec-09	0.1500	Dec-10	0.1440
Jan-07	0.2000	Jan-08	0.1700	Jan-09	0.1600	Jan-10	0.1500	Jan-11	0.1440
Feb-07	0.2000	Feb-08	0.1700	Feb-09	0.1600	Feb-10	0.1500	Feb-11	0.1440
Mar-07	0.2000	Mar-08	0.1700	Mar-09	0.1600	Mar-10	0.1500	Mar-11	0.1440
Apr-07	0.1700	Apr-08	0.1600	Apr-09	0.1500	Apr-10	0.1440	Apr-11	0.1440
May-07	0.1700	May-08	0.1600	May-09	0.1500	May-10	0.1440	May-11	0.1440
Jun-07	0.1700	Jun-08	0.1600	Jun-09	0.1500	Jun-10	0.1440	Jun-11	0.1440
Average	0.1925		0.1675		0.1575		0.1485		0.1440

The Commission's model generates four different estimates of the net benefits of regulation relative to the commercial offer. These come from two different technical assumptions about the demands in the model, and two different criteria for measuring net benefits. The first criteria, consumer welfare, focuses on the benefits and detriments to consumers only, while the total surplus criterion also takes into account the effects on firms. The net benefits over the five years of analysis are discounted to net present value terms to give a single net benefit figure in each of the four cases.

When June year average termination rates from Table 3 were entered into the Commission's model and all other inputs were unchanged, we obtained the following estimates of net benefits:

Table 4 Net benefits of regulation relative to the commercial offer (NPV, $m).

Demand	Consumer Welfare	Total Surplus
Linear	-2.38	-10.33
Constant Elasticity	-11.33	-14.99

These results indicate that the commercial offer is superior to regulation, both in terms of the impacts on consumers and the effect on total surplus.

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7 June 2006

Mr. Tom Chignell
General Manager, Commercial Development
Vodafone New Zealand Limited
v.nue
20 Viaduct Harbour Avenue
Private Bag 92161
AUCKLAND.

Dear Tom

Agreed upon procedures

As agreed in our engagement letter dated 6 June 2006, we have performed the procedures requested by you, and set out the results below.

As agreed our work has been performed in accordance with the Standard and Guidelines for Agreed Upon Procedure Engagements issued by the New Zealand Institute of Chartered Accountants. The procedures performed do not constitute an audit or a review and, consequently, no assurance on any assertions contained in the financial information or with respect to the integrity of the Microsoft Excel Spreadsheet is expressed. We disclaim any assumption of responsibility for the adequacy or otherwise of the procedures requested by you.

We have undertaken the following procedures:

1. Downloaded the Microsoft Excel spreadsheet titled "CBA Model for Final Reconsideration - Public Version.xls" from the following web site:

   http://www.comcom.govt.nz/IndustryRegulation/Telecommunications/Investigations/MobileTerminationRates/reportsandsubmissions.aspx

2. In the worksheet titled "Commercial offers" input the information provided by Vodafone New Zealand Limited, as shown in Table 1 below, in the following areas:

   * In the area titled "Telecom commercial offer: Mobile Termination Rates" located in cell C10 to cell H9 in the worksheet (the yellow-shaded cells in Table 2 below).

   * In the area titled "Vodafone commercial offer: Mobile Termination Rates" located in cell C30 to cell H29 in the worksheet (the yellow-shaded cells in Table 3 below).

Table 1: Information provided by Vodafone

Period	Mobile Termination Rate (NZ dollars)	Input into Cells on 'Commercial Offers' Worksheet
1 July 2006 to 31 March 2007	0.20	C10:C15, D4:D6, C30:C35, D24:D26
1 April 2007 to 31 March 2008	0.17	D7:D15, E4:E6, D27:D35, E24:E26
1 April 2008 to 31 March 2009	0.16	E7:E15, F4:F6, E27:E35, F24:F26
1 April 2009 to 31 March 2010	0.15	F7:F15, G4:G6, F27:F35, G24:G26
1 April 2010 to 30 June 2011	0.144	G7:G15, H4:H9, G27:G35, H24:H29

Table 2: Input Mobile Termination Rates – Telecom (Yellow-Shaded Cells, Cells C10 to H9)

Telecom commercial offer: Mobile Termination Rates

	2005	2006	2007	2008	2009	2010	2011
Jan		0.240	0.200	0.170	0.160	0.150	0.144
Feb		0.240	0.200	0.170	0.160	0.150	0.144
Mar		0.240	0.200	0.170	0.160	0.150	0.144
Apr		0.225	0.170	0.160	0.150	0.144	0.144
May		0.225	0.170	0.160	0.150	0.144	0.144
Jun		0.225	0.170	0.160	0.150	0.144	0.144
Jul	0.260	0.200	0.170	0.160	0.150	0.144	
Aug	0.260	0.200	0.170	0.160	0.150	0.144	
Sept	0.240	0.200	0.170	0.160	0.150	0.144	
Oct	0.240	0.200	0.170	0.160	0.150	0.144	
Nov	0.240	0.200	0.170	0.160	0.150	0.144	
Dec	0.240	0.200	0.170	0.160	0.150	0.144	

Table 3: Input Mobile Termination Rates – Vodafone (Yellow-Shaded Cells, Cells C30 to H29)

Vodafone commercial offer: Mobile Termination Rates

	2006	2005	2007	2008	2009	2010	2011
Jan		0.260	0.200	0.170	0.160	0.150	0.144
Feb		0.260	0.200	0.170	0.160	0.150	0.144
Mar		0.260	0.200	0.170	0.160	0.150	0.144
Apr		0.225	0.170	0.160	0.150	0.144	0.144
May		0.225	0.170	0.160	0.150	0.144	0.144
Jun		0.225	0.170	0.160	0.150	0.144	0.144
Jul	0.260	0.200	0.170	0.160	0.150	0.144	
Aug	0.260	0.200	0.170	0.160	0.150	0.144	
Sept	0.260	0.200	0.170	0.160	0.150	0.144	
Oct	0.260	0.200	0.170	0.160	0.150	0.144	
Nov	0.260	0.200	0.170	0.160	0.150	0.144	
Dec	0.260	0.200	0.170	0.160	0.150	0.144	

As required, we report in Table 5 the results obtained after inputting the data as described above as displayed in cell D4 to cell E5 in the worksheet titled "Summary results & assumptions".

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Table 4: Results Shown in Cells D4 to E5 on the 'Summary results & assumptions' worksheet

Summary of Results

Sensitivity	CW	TS
Lin	-$2,377,744	-$10,325,743
CED	-$11,333,855	-$14,991,855

For the avoidance of doubt, we describe in Table 5 the cell references on the 'Summary results & assumptions' worksheet corresponding to the figures shown in Table 4.

Table 5: Results of Agreed Procedures & Corresponding Cell References

Cell reference	Amount
D4	-$2,377,744
D5	-$11,333,855
E4	-$10,325,743
E5	-$14,991,855

This letter should be read in conjunction with our engagement letter dated 6 June 2006. This report relates only to the items specified above and does not extend to any financial information of Vodafone New Zealand Limited.

Yours sincerely
Ernst & Young Corporate Finance Limited

Peter Goss
Director

Michael Stanley
Director