

1 April 2008

## Broadband Bilateral

You are meeting with the Minister of Communications on Wednesday 2 April at 9:00 am to discuss the Broadband initiative within Vote: Communications. All other initiatives within Vote: Communications have been addressed through the Theme process.

Ministers met on the 10 March and discussed the following indicative funding amounts:<sup>1</sup>

| <i>Infrastructure Gap</i>     | <i>Funding Amount</i>            |
|-------------------------------|----------------------------------|
| 1. Urban Fibre                | \$200 – 250 million over 5 years |
| 2. Rural Broadband            | \$75 – 100 million over 5 years  |
| 3. International Connectivity | \$15 million in 2008/09          |

Treasury recommends you do not support additional funding in Budget 2008 given fiscal constraints and the level of private investment in Broadband infrastructure. Nonetheless, we have provided advice (below) within the funding amounts discussed by Ministers.

### 1. Urban Fibre **(\$200 – 250 million operating)**

The proposal is to establish a contestable fund to leverage third party investment in open access Broadband infrastructure.

- Open access fibre is likely to deliver better service at lower prices.
- The contestable fund would provide urban fibre loops in the first instance.

Treasury advises that improving Broadband in urban centres is the highest priority and considers there is merit in competing Broadband infrastructure in urban centres. The Ministry of Economic Development (MED) has previously advised that \$75 million would be sufficient to leverage all proposed urban fibre loops of which we are aware.

- This suggests that any contestable funding beyond around \$75 million would be targeted at increasingly marginal projects which are likely to require a higher level of Government subsidy.

The Government's long-term vision is Fibre to the Home. It is unclear how this will be achieved. Options could include provision by the current incumbent, a new monopoly, or a piecemeal approach. Until it is known how this goal will be achieved, there is a risk that large-scale Government subsidies will have unintended consequences.

Should you wish to commit funding at the levels discussed on 10 March, Treasury recommends you support urban fibre funding at a level of \$200 million only to ensure the contestable fund only supports projects with the strongest business cases.

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<sup>1</sup> The MED note from that meeting and the original Bilateral Briefing are attached for your reference.

## **2. Rural Broadband (\$75 – 100 million operating)**

The proposal is to establish a contestable fund to leverage third party investment in both fibre backhaul to rural areas and a range of last mile solutions.

The MED has previously advised that \$75 million would be the minimum feasible Government investment to leverage a noticeable improvement to rural Broadband services.

Should you wish to commit funding at the levels discussed on 10 March, Treasury recommends you support rural broadband funding at a level of \$75 million only given the comparatively low economic benefits of extending Broadband to rural areas, and the desire to focus private sector investment on projects of the highest value.

## **3. International Connectivity (\$15 million capital)**

The proposal is to use a Crown anchor tenant to guarantee a sufficient level of demand to ensure a second international cable is built. A second cable is likely to increase New Zealand's connectivity resilience and have a degree of downward pressure on prices.

Officials are agreed that this proposal is the most cost-effective option to ensure a second international cable is built in the short-term. The most likely Crown anchor tenant is REANNZ, however, the right of use would be transferable should the Crown wish to use the bandwidth for another purpose in the future.

Officials' preliminary view is that the issue of international connection can be separated from an assessment of the overall viability of REANNZ. When officials report back on implementation they will consider the relationship to decisions expected in September on the overall business model of REANNZ. We recommend that funding is dependent on approval of a detailed business case.

Should you wish to commit funding at the levels discussed on 10 March, Treasury recommends you support international connectivity as a contingency at a level of \$15 million only.

### **Next Steps**

- All options require a report back to Cabinet prior to announcements as part of Budget 2008. All reports will be led by the MED with input from Treasury.
- The report back on urban fibre and rural broadband will cover their possible integration into a single, multi-criteria fund; the governance of the fund; implications for Vote: Communications; the desired phasing and any other relevant matters.