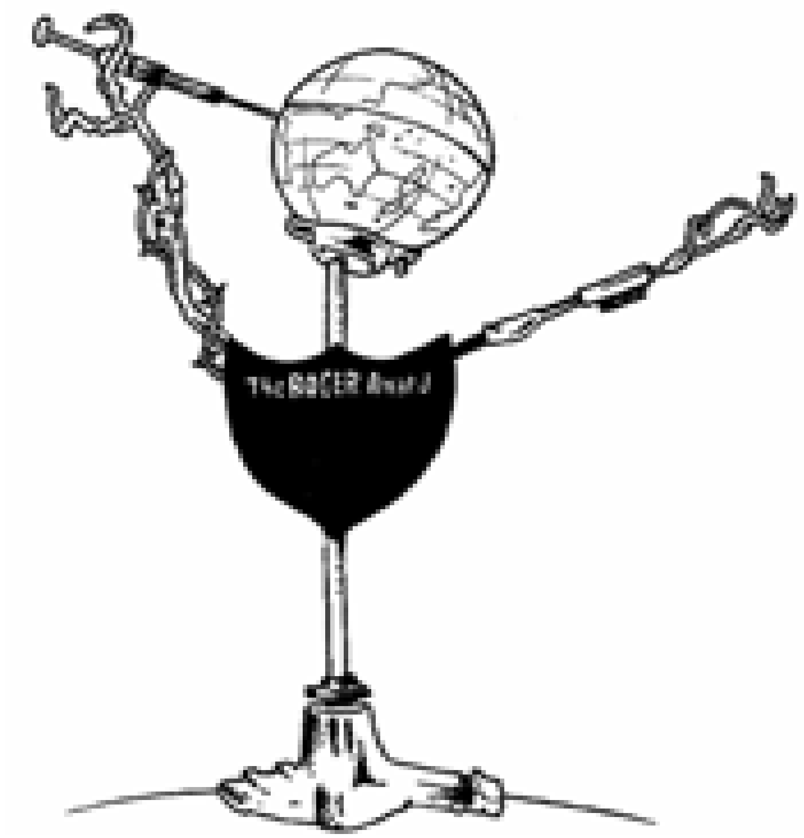
Roger Award 2007

For the worst
Transnational
Corporation
operating in Aotearoa in 2007



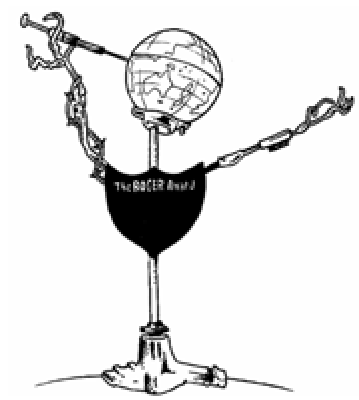
Winner

Telecom

Organised by
Campaign Against Foreign Control of Aotearoa (CAFCA)
GATT Watchdog

STATEMENT FROM THE JUDGES

February 2008



Geoff Bertram
Paul Corliss
Cee Payne-Harker
Laila Harre
Anton Oliver
Brian Turner

"Ribena contains 7 mg of Vitamin C per 100ml", "Faster cheaper broadband", "family pledges to 'look after' Independent Liquor workers", "Spotless defends lockout on health and safety grounds", "our marketing is aimed at adults who are aware of the risks of smoking", "no threat to news quality from sacking of sub-editors", "Pike River mine project will have low environmental impact", "ANZ CEO says 9% profit 'probably a little low".

As Sir Walter Scott wrote: "Oh what a tangled web we weave when first we practise to deceive!" The eight 2007 Roger Award nominees offended in all or some of the official categories – economic dominance, people, environment and political interference. But it was the guile of their public relations claims, unsupported or contradicted by the evidence in line with that old public relations principle that you can fool some of the people all of the time and all of the people some of the time, that unified the 2007 stable of contenders for the title "Worst Transnational Corporation in New Zealand in 2007."

The judges want to start by thanking all nominators for their contribution to exposing corporate hypocrisy.

Our Winner this year, Telecom, crossed the finish line with room to spare, but in declining form as the regulators finally (please, finally) took control and imposed the telecommunications equivalent of a tough anti-doping regime. Unfortunately all others not only had strong finishes but were looking no less villainous at the start of 2008!

Here's how we viewed the activities of the also-rans in NZ in 2007.

Glaxo Smith Kline

Most of us didn't know that the Ribena brand was owned by drug czars until two Kiwi school girls exposed it as a mere placebo. Not only did the juice fall short of the Vitamin C claims made to generations of mums who have unwittingly been mainlining their toddlers refined sugar, but the popular boxed drink contained no detectable Vitamin C at all! GSK was fined $217,500 in the Auckland District Court for the 15 breaches of the Fair Trading Act it admitted. Pakuranga College students Jenny Suo and Anna Devathasan had sprung the second largest food and drug company in the world. What GSK got away with for so many years is staggering and their inability to, when finally caught, fess up showed true corporation arrogance. Profiteering and cultural imperialism? Yes, in spades. But the Roger Award will not be going to the white sugar barons this year – our judges were satisfied that the punishment of creating the best scandal of 2007 would suffice. We do hope though that Pharmac has tested the NZ's favourite GSK antibiotic, Augmentin.

Pike River Coal

Had former Minister of Conservation, Chris Carter, been in the running for an Accomplice Award for his role as Pike River Coal's mouthpiece, spinning down the environmental impacts of this coal project, he would have been in with a chance. The company has something more to thank Government for – rescuing them from the Roger. It was Government involvement in a project which most judges are agreed is not in the interests of the West Coast, NZ or Planet Earth that most offended us this year. There might be nothing extraordinary about a mining company wreaking environmental havoc. But the complicity of Carter and the Department of Conservation is lamentable as is the fact that it was the lobbying by a Government-owned company, Solid Energy, which created the regulatory soft spot through which Pike River has been able to push its own project. For the record, the evidence presented to us indicated that far from the "low environmental impact" and "very small footprint" claimed, the mining operation will produce 6.8 million tones of CO_2 equivalent in the form of methane through fugitive emissions during mining and processing on top of the greenhouse gasses that the use of the coal will emit, and impact on landscape, scenic values and an important catchment that is home to many endangered species. What's more the transportation of the coal has been a lose-lose for the West Coast. While the original proposal to ship from the Coast would have resulted in a steady column of trucks down the Grey Valley (a truck every five minutes on the Coast is a traffic jam in Auckland), it would also have been positive for port development. But the deal with Pike River Coal intended to re-launch the port of Greymouth was wrecked when in November 2007 Solid Energy announced it would now rail Pike River Coal to Christchurch. Grey District Mayor Tony Kokshoorn said the deal "had been ruined by the might of Solid Energy and rail operator Toll Holdings" (*Press*, 28/11/07) and he was very gloomy about any future at all for the port of Greymouth.

ANZ

Two very different nominations were received for one of New Zealand's Australian-owned and its largest bank. One highlighted the complicity of the Bank in rainforest destruction in Papua New Guinea. Yes, it's a global village, and the Bank's connections to illegal logging operations deserve to be condemned, but the Roger has borders. The scandal implicating the ANZ, Credit Suisse First Boston Asian Merchant Partners (CSFBAMP), Feltex directors, and finally another Australian corporate, Godfrey Hirst, and which ended with the 2006 collapse of a significant New Zealand company and a series of questionable sales of its assets, made this company a very worthy nominee. At the very least (and in the absence of hard evidence [yet] to locate clear responsibility in the Bank's vaults) the ANZ played the role of the big lender in the wings with its eyes ostensibly tight shut, while the Feltex directors and CSFBAMP took their profits at the expense of ordinary New Zealand investors. Likewise, its complicity, at Feltex sale time, in Godfrey Hirst's tactics to dodge Overseas Investment Office scrutiny and make profits for Godfrey Hirst and its Chief Executive Officer (CEO). In 2007 ANZ's refusal until the 12th hour to cooperate with the Feltex liquidator was one reason it earned the Shareholders' Association's 2007 Golden Glob Award. Jointly accused with other banks of a tax rort worth $1.7 billion and a profiteer from its one-way bet in laundering hot money through pushing higher household debt, the ANZ continues to suck New Zealand dry.

APN News And Media

It's a bit surprising that media organisations do not get nominated for the Roger more often, and even this nomination was somewhat narrower in its scope than the owner of 42.8% of our daily newspaper market, including the *New Zealand Herald* with a 28.1% share of its own, and a huge stake in radio (Radio Network) deserves. The case zeroed in on the contracting out of sub-editing by the country's biggest paper, the *Herald*. The 20% loss in salary for those transferred and the threat to news quality made this action culpable. Reading between the lines the material contained plenty of evidence of profiteering and cultural imperialism, as well as growing monopolisation of the New Zealand news media. We would have added the *Herald's* 2007 "Democracy under attack" campaign against controls on third party election spending and anonymous party funding (the Electoral Finance Act) to the charges. It's one thing to take an editorial line and another to so blatantly use news stories and page space to promote it. Can't wait to see how they write up the Awards this year – how about "Democracy under attack part 2- How the transnationals are getting it all their own way".

Independent Liquor

This outfit has been a nightmare for unions for years. The company's purchase by Pacific Equity Partners after the death of founder Michael Erceg makes it foreign-owned and exposes its ongoing activities to Roger scrutiny. Time and time again a committed core of workers has built support on their job for improvements in pay and fair treatment and been thwarted by anti-union tactics including the dismissal of union activists. In late March 2007 one worker, Steve Tipene, took his own life after being sacked. The Unite Union's unjustified dismissal case was settled in mediation, a settlement that we hope gave some comfort to his family. The last photo of Steve holding up a sign on Unite's picket line reading "Stop bullying and harassment at Independent" said it all. Then there is the impact on consumers and society of Independent Liquor's RTDs (ready to drinks - pre mixed spirits and alcopops) especially aimed at the youth market. These present far more serious health risks than you would ever guess from the advertising. The association of RTDs with teenage binge-drinking puts the company up there. A relatively small player in an industry with some really big operators, IL should clean up its act.

Joint Runners-Up:

Spotless And British American Tobacco

It was a photo-finish in second for our two runners up. The fact that one of them didn't do anything more heinous than usual in 2007 did not disqualify it for a place. The other took its profiteering from public health dollars and poor employment practices to a higher level.

Spotless

Perhaps it was jealousy at fellow Aussie giant Progressive Enterprises' Roger Award for locking workers out in 2006 that drove Spotless into a big ditch which they only stopped digging on Employment Court orders. If there was an award for the stupidest TNC in NZ in 2007 it would have been no contest.

Once again union solidarity – led by low paid long-serving and longer-suffering Service and Food Workers Union members – and public humiliation did the job. Actually, the SFWU should be given a bosses' award for the "Cheekiest Union in 2007". Their tactic of issuing strike notices for all but a few minutes every hour led this greedy parasite on the public purse into an elegant industrial trap.

There they were exposed as a company prepared to de-stabilise the public health system, to illegally lock out and further impoverish minimum wage workers and their families, to create insecurity and fear among NZ patients, and to co-opt a few elected District Health Board members to boot. And all this to block a wage settlement for 800 public hospital workers that was to be funded by the public purse. "Shameless" cry the judges, not "Spotless".

Spotless and its biggest competitor in the contract catering industry, Eurest, act as a cartel against workers, bidding down wages and working conditions both in their own operations and among the minnows who swim in their wake. While we are on the subject of awards, a National Award for workers in service sector jobs devalued through competitive tendering and profiteering would be a great election promise, Helen et al.

Spotless might have missed out on the Roger this time but can take heart from the news that their political lackeys in the Whanganui DHB have earned an Accomplice Award for their services to transnational greed.

British American Tobacco

The scale of harm caused by BAT's product might not have increased in 2007, but is so large every year that the judges decided that being as bad as ever is sufficient in this case. Bad, in this case, is very, very bad.

The 2006 *Judges' Statement* indicated that BAT "may well have a chance in 2007 as the Government moves to bring in explicit labelling and BAT does what it can to minimise the damage to its sales", but neither Government action nor company resistance was apparent from the evidence we saw.

The biggest development in 2007 appears to be the reporting of further evidence that cigarette shop displays make it harder for people to quit – more grist to the mill of the campaigners and regulators. Signs in BAT colours setting out the ban on cigarette sales to under-18s appear a clever device to do the opposite. Stealth marketing on You Tube and social networking sites has been exposed. And it seems that the duty free industry has assisted in blocking a ban on duty free cigarette sales promised in the international Framework Convention on Tobacco.

Yes, it's legal. Yes, we have been warned. And judges also recognised the difficulty of drawing a clear line between tobacco and other dangerous legal products (fast food, alcohol, anti-social media products). However that is a problem for regulators and does not forgive BAT the harm it causes. Smoking is responsible for more preventable deaths than anything else, and BAT is the worst culprit in New Zealand. The difficulties for regulators do not absolve BAT from accountability at the Roger Awards for profiteering at the expense of individual and public health.

The Winner:

Telecom

Much to the judges dismay, the prediction of the 2006 Roger Award judging panel that "Telecom's charmed life as the monopoly with the longest record of resisting and undermining regulation seems to be coming to an end", has not come to pass. Murray Horton's August 2007 piece in *Foreign Control Watchdog* was, alas, right on. "A year that started out seeming to promise so much ... has actually delivered so little because of Telecom's familiar trick of dragging the chain in order to (very profitably) suit itself."

The most frequent finalist in this contest picks up its second Roger Award, in 2007.

After looking as though the company would finally come to terms with regulation in the public interest, the year 2007 saw yet another round of delaying tactics, the Xtra debacle that stranded customers in cyberspace, the cabinetisation project which undermines the potential for local loop unbundling to deliver competition, an obscene $5.4 million final year payment to outgoing CEO Theresa Gattung, the scrapping of concessions for non-government organisations and the School Connection scheme. These sins and more ensured Telecom was in top form in this race for the worst transnational in NZ in 2007. Far from taking heart from the appointment of a new soft-sell CEO, the judging panel has heard too many Telecom promises of co-operation to feel anything but dismayed at the confidence the Government is placing in UK import Paul Reynolds.

As the new charm offensive got underway the company continued to defer investment and introduce carefully selected bits of new technology (cabinets) purpose designed to shut competitors out of the Internet market once the local loop is unbundled. Most of 2007 was frittered away on the detail of the three-way split and the Telecom threat of an investment strike. Pledging to go beyond the Government's requirements for accounting separation, and to do so in a transparent way and alongside competitors, Telecom used its well-practiced fear tactics to try and keep the regulators off its back. It seems likely to us that it was Telecom's scaremongering rather than good regulatory practice that resulted in the new legislation leaving the Minister, rather than the Commerce Commission, managing the operational split.

March saw 025 cellphone customers' access shutdown and the dumping of not-for-profit concessions. In August the School Connection scheme was scrapped, ending a lucrative funding source that had allowed customers to transfer some of Telecom's monopoly profits to schools of their choice. The company announced that phones powered off the network will no longer work and customers will have to have separately powered devices in their homes, making phone service vulnerable to power-system outages. Telecom's proposed battery backup will be limited to eight hours in roadside cabinets, leaving emergency services out on a limb.

Prices remained high – a Commerce Commission report in April 2007 placed NZ among the five most expensive in the Organisation for Economic Cooperation and Development (OECD) - and were raised outside Wellington and Christchurch from March 2007. Investment stayed low and inadequate. The OECD's communications outlook for 2007 found we spent 5.39% of our Gross Domestic Product (GDP) on telecommunications in 2005, the highest in the OECD, but only reinvested 8.7% of that revenue, almost half the OECD rate of 15.3%. The Yellow Pages sale in March (into 100% overseas ownership) raised $2.2 billion. $1.1 billion of that was simply handed out to shareholders.

In September 2007 it became public that the NEAX switches in the Telecom exchanges are now so old (often 40 years) that spare parts are no longer produced by NEC, the manufacturer, and that tape drives are "on their last legs" (*Press* 5 September 2007).

Throughout the year the shockingly poor quality of broadband service continued, getting worse rather than better. Ernie Newman, head of the Telecommunications Users Association of New Zealand (TUANZ), summed up frustrations with Xtra: "If a phone company in 2007 can't run a reliable ISP (Internet service provider) that doesn't go off the air with extreme regularity, then there is something fundamentally wrong". The migration of Xtra customers to the new Yahoo!Xtra service was so poorly managed that for some services were lost for more than ten days. Telecom's public relations response was typically arrogant. The *Listener (*17 November) called the project "calamitous", concluding that "the stated rationale for the unwieldy joint venture now appears to be in tatters".

With Telecom in the driving seat "faster, cheaper broadband" remained nothing more than a slogan in 2007. Even millionairess Jenny Gibbs had to go public to get broadband installed in her Paratai Drive home (one of the most prestigious streets in Auckland), bringing Telecom's rivals knocking on her door. A huge advertising campaign featuring the vacuous "Xtraordinaries" and the false "Go Large" broadband promises collapsed when Telecom was forced to refund Go Large customers and shut it down because its own system could not cope with unlimited high speed broadband.

Reynolds' appointment as CEO took effect in October, with Theresa Gattung richly rewarded for her services to monopolism. Meanwhile 700 staff redundancies (10%) were expected by the end of 2007, with an ongoing risk to call centre jobs through further outsourcing overseas.

By November it became apparent that Telecom's new roadside cabinets will strand competitors' equipment in local exchanges while raising Telecom's broadband speeds to meet the competition as and when Telecom chooses. Why make it easy for voice over Internet services to deprive oneself of the profits still to be made from a monopoly on fixed line rentals? This is coming into place on Paul Reynolds' watch, with no sign that Telecom is planning anything other than an anti-competitive outcome.

No other finalist could have competed with the action upon inaction described by nominators and evidenced in accompanying material. Even the Library and Information Association felt compelled to condemn ads denigrating libraries in favour of internet tools for homework. This was one of Telecom's finest years!

Accomplice Award

Whanganui District Health Board

Like so many Roger finalists this year, Spotless shared its guilt with accomplices within the Government apparatus, in this case the Whanganui District Health Board (WDHB).

Around the country Mayors, Councillors and MPs joined locked out workers on their picket lines. Many DHBs put pressure on Spotless in support of the union claims. But not in Whanganui where Spotless has a monopoly on all cleaning, kitchen and orderly services.

WDHB knew that the Government was willing to fund the pay demand through changes to the WDHB/Spotless contracts. WDHB had obligations under the Employment Relations Act and Health and Disabilities Act to take into account the needs of its workforce including those employed by contractors. Despite this WDHB (formerly known as Good Health Wanganui and embroiled in controversy over hospital safety issues throughout 2007) worked with Spotless on its lockout tactic.

The DHB breached its statutory obligation to allow union representatives (including Spotless employees) to enter the premises and all elected representatives refused to meet with the union and its members. Locked out workers were refused entry to on-site toilets. And when two orderlies refused to leave the site (as they were legally entitled to do) the DHB called the Police and had the pair arrested.

In awarding the WDHB the Accomplice Award we recognise not only their 2007 services to overseas profiteering on poor health and public money in NZ, but also the leading role they have played in the creation of Public Private Partnerships through the extensive contracting out of core hospital services with a consequent reduction in quality, loyalty and dignity for patients and workers alike.

ROGER AWARD REPORT 2007

This year is an important year for the Roger Award. Now, with over a decade of exposing the exploitative, profiteering and monopolising nature of foreign owned companies operating within New Zealand, Roger is slowly becoming a feature on the cultural landscape, especially those landscapes sloping to the left. If success is measured, as it often is, by way of media attention then the Roger Award has far exceeded expectation. This was no more clearly proven than this year when a request was made by a major Sunday newspaper for exclusive rights to the results prior to their being announced. Of course this request was denied.

Destined For The Hall Of Shame?

Telecom has featured as a finalist in every Roger Award since its inception in 1997 and achieved the auspicious honour of winner in 2004. If, as looks quite likely, Telecom were to win the Award again next year or indeed anytime in the future it could be made a permanent occupant of the Hall of Shame. In doing so, Telecom would be following closely the footsteps of Tranz Rail (the current sole occupant of the Hall of Shame) which after three winning titles was rendered ineligible for nomination to allow other such worthy companies the opportunity to obtain the winning gong.

Telecom came very close to winning this Award in 2006. Were it not for the Progressive Enterprises' lockout of their distribution centre workers in 2006 that pushed them just a nose in front, Telecom would have been on the winning podium.

Telecom – A Sordid Past

For many the mere mention of Telecom evokes images of asset selling and market deregulation. As a profiteering monopoly it symbolises all of the privatising ventures of the early 1990's. In 1987 Telecom bought the telecommunications branch of New Zealand post for NZ$3.2 billion[1]. It was at this stage a State-Owned Enterprise (SOE). Progressively over the next three years the telecommunications market was deregulated. After just three years as an SOE Telecom was sold to wholly owned subsidiaries of Bell Atlantic Corporation and Ameritech Corporation for NZ$4.25 billion. From here a downward (or upward depending on your perspective) profit driven spiral ensued. In 1991 the company appeared on the stock market in the United States, Australia and New Zealand. Since then Telecom has expanded to meet growing Internet and mobile needs. In 2007 Telecom's net earnings were $3.27 billion and assets were valued at $8.27 billion[2].

Many New Zealanders struggle to pay their phone bills because the uncompetitive nature of the telecommunications industry is causing prices to be constantly bumped up. That the Government once had ownership of this provider of telecommunications and knowingly encouraged, and strove towards deregulation is a sad display of the disturbing element of greed that capitalism is so successful at bringing out in people - the sort of greed that leaves the majority of people struggling so that a few fat cats at the top can enjoy their champagne and caviar.

The revolting Rogernomics driven reforms of the 1980's and early 90's are certainly not fading in the memory of those who lived through them. The

[1] http://www.telecom.co.nz/content/0,2502,200633-1548,00.html
[2] http://annualreport07.telecom.co.nz/download/telecom-annual-report-2007.pdf

generations who have grown up with these reforms know nothing of a world where the competitive market wasn't the driver behind nearly all aspects of the economy. This is a strong reason why the continuance of events such as the Roger Award is so crucial. As soon as we stop acknowledging what is wrong with the everyday we legitimise it.

April 2007 – Yellow Pages Did The Walking

In April 2007 Telecom sold the Yellow Pages Group Limited to YPG Finance, owned by various overseas interests, for a mere $2.24 billion. The Yellow Pages Group Limited publishes the Yellow Pages, White Pages, Local Directories, on-line directories and the 018 service[3]. These services are in daily use by New Zealanders yet at ownership level they are completely isolated from those to whom they are providing the services. As we know, the more removed the providers are, the more likely they are to hike prices with little regard of the impact on consumers. This distance from the consumers also impacts on accountability. Without these companies having an on-shore presence it is difficult to target them in shame campaigns. It also limits the Government's ability to have any semblance of influence. This type of on-selling conjures up a picture of large bits of New Zealand being sold to the highest bidder. Then the successful bidder takes his big chunk of the economy and on-sells some smaller bits – creating a spreadsheet of foreign ownership or, in layman's terms, a sub-dividing of the New Zealand economy. Like any sub-division it is a scar on the landscape and reeks of dodgy infrastructure.

What Gives? Telecom Are All Take Take Take

As seen in their selling off of the Yellow Pages Group Limited, Telecom will stop at nothing to make a buck. What they increasingly shy away from, however, is returning any of those bucks to New Zealand – even if just in the form of maintaining their assets. For a very detailed explanation of how Telecom fails to significantly reinvest profits into its infrastructure, and how it massages the figures in its annual accounts to make its reinvestment look better than it is, see Sue Newberry's *Financial Analysis* which follows this. It is clear that Telecom is simply providing a service at the lowest cost to itself. The predictable result, as seen in the examples throughout this report, is that the services begin to crumble.

[3] Bill Rosenberg "Telecom Sells Yellow Pages To Canadian-Led Consortium", *Foreign Control Watchdog* 115, August 2007.

Schools And Not-For-Profit Organisations Left High And Dry – Even The Nats Are Crying About It

In a true display of decency and generosity, in 2007 Telecom gave both the education sector and the not-for-profit sector hefty blows. Funding and fundraising programmes were removed from schools. The programme had allowed residential customers to sponsor a school with the company providing credits to the school based on how much the sponsor spent with Telecom[4]. Even National Party List MP Kate Wilkinson was outraged at this: "I am baffled by the decision by Telecom that threatens to jeopardise a really positive and worthwhile relationship with our local school community"[5]. If the Nats are getting outraged at large companies, you know they must be pretty bad. The only saving grace is the fact that, although at present 96% of schools have accounts with Telecom that amount to about $8 million, the New Zealand School Principals' Federation reports that a large number of these schools are now considering alternative telecommunication providers[6]. This significant loss in profit for Telecom far exceeds the costs of allowing the sponsorship scheme to continue.

Furthering their theme of community kindness, in 2007 Telecom announced it would no longer support not-for-profit organisations through discounted line rentals and free local calls. Again, in this David and Goliath struggle, David wins again. The community trusts have gone elsewhere to find discounted deals. Telecom's competitor TelstraClear has offered a deal that will see a collection of community groups save upwards of $18,000[7]. A thin silver lining on an otherwise volatile cloud. But what happens if and when TelstraClear makes the same decision that it isn't making enough profit from the goodwill to justify the cost? Where will those groups go to then? Surely the answer is Government policy such as regulated lower prices for these consumers?

Jobs? The Cheaper The Labour The Better

As well as its community exploits, Telecom is following the popular trend of outsourcing its services. The clearest and most recent examples are its call centres. By January 2007, 230 staff had been made redundant and it was suggested that up to 700 people could meet a similar fate. Two help desks – pre-paid mobile phones and dial-up Internet

[4] Jon Hoyle, "Sponsorship axe could be costly", *Press*, 27/8/07.
[5] Robyn Bistrow, "Schools lament Telecom move", *Press*, 17/10/07.
[6] Hoyle, *Press*, 27/8/07.
[7] Phil Hamilton, "23 groups bargain with Telecom", *Press*, 18/8/07.

- were moved to Manila[8]. A move obviously inspired by the cheaper labour costs involved.

As Murray Horton pointed out in his article in the August 2007 *Watchdog* there are two sides to this story. We must not forget that the call centres move to Manila means much needed jobs for Filipino workers. This is a valid and important point, however what also must not be forgotten is the motive behind Telecom's actions. The wages must be minuscule for the move to be economically viable.

Telecom – Bans Gays

Throughout 2007 Telecom experienced several embarrassments but an incident in April excelled in its offence. Telecom's limited generic service was illustrated in the most politically incorrect of ways when its systems bounced back an email from a woman trying to access the email helpdesk. It was revealed that the woman's name, Gay, was a trigger word for a spam detector. Therefore this woman was unable to access any help as her name was deemed offensive. In their defence Telecom claimed that there were filters placed on the word heterosexual as well[9]. At least we can be thankful that it is not discriminating solely against one particular sexuality.

Emergency Services Reduced To Pen And Paper

The examples of Telecom's incompetence over the last year are ample and far exceed what can be covered in this *Report*. One of the categories under which a winning company must offend is "people". In November 2007 Telecom suffered a breakdown at a data centre in Central Auckland that caused major disruptions to broadband computer links, email and pagers and other computerised communications around the country for most of the day. The most concerning of those affected was the emergency services. Emergency services call centre staff were reduced to having to record information by pen and paper and pass this on to police, ambulance and fire dispatchers[10]. This is completely outrageous. It is only luck that played a part in ensuring that injury or death was not sustained through the incompetence or reluctance of Telecom to ensure its facilities are up to scratch. What's next? Will all customers upon employing Telecom's services be issued with a feather, a bottle of ink and a carrier pigeon for those times when the services may spontaneously cease to work?

Animal Exploitation – A Mockery

Animal exploitation is another of the required categories for nomination. Though this is not obvious within the exploits of Telecom it too played a role in animal exploitation in 2007. Telecom's "animals" are, of course, the mock ones used in its TV commercials (following in the tradition of Spot the Telecom dog of the 1990s). These ads are more than a little annoying and insulting to our intelligence.

Paul Reynolds – A Modest Earner

Struggling along with other low paid New Zealanders is new immigrant Paul Reynolds. Reynolds filled the Chief Executive Officer's chair left empty by Theresa Gattung. With an annual salary of $5.25 million Reynolds is more than comfortable. Having moved to New Zealand for the position, Reynolds' family will not get the opportunity to miss their homeland with ten trips home each year on top of Reynolds' salary[11]. This is one household that won't be struggling to pay its phone bill.

So Then …….

The examples given in this *Report* that support awarding Telecom with the 2007 Roger Award are only a small collection of the multitude of examples that could have been included. Many other points were made in Murray Horton's August 2007 *Watchdog* article on Telecom and also in the *Judges' Statement*. There are always examples surfacing about Telecom and its transnational exploits. Again Roger's name is a reminder of why we find ourselves in this situation today. The sale of State Owned Assets in the late 80's and early 90's has really paved a way for businesses to hold New Zealanders at ransom. Even the economically naïve can clearly see that selling an asset that generates such a high annual revenue is a silly concept. Bell Atlantic Corporation and Ameritech Corporation were given a gift when they purchased Telecom for $4.25 billion in 1990, and this is a gift that keeps on giving.

So - think twice about who your telecommunications provider is. Think twice about whether you want to be a customer of such a monopolising company. And think twice next time you're watching telly and one of their clever toys advertisements comes on - switch the telly off!

---

[8] Murray Horton "Telecom drags the chain", *Foreign Control Watchdog* 115, August 2007.

[9] Jonathan Marshall, "Gay filtered in Telecom emails" *NZ Herald*, 29/4/07.

[10] "Blackout at Telecom centre", *Press*, 5/11/07.

[11] Marta Steeman "No Plans to sell network", *Press*, 5/10/07.

FINANCIAL ANALYSIS

Telecom Corporation of New Zealand Limited

Sue Newberry

Telecom's reported high profits and very high dividend payouts have allowed it to trumpet its share market ranking in "the top tier of [telecommunications] players" internationally.[i] Sadly, this seems to have been achieved largely through profiteering in New Zealand and running down the telecommunications infrastructure. In 2007, following adverse public comment about its high prices, low level of reinvestment, and the generally poor state of telecommunications infrastructure in New Zealand, Telecom changed the way it reports its capital expenditure. As will be shown, this change exemplifies how Telecom's use of "confusion as its chief marketing tool" extends to Telecom's financial reporting practices.[ii]

In 2007, Organisation for Economic Cooperation and Development (OECD) data revealed that telecommunications prices in New Zealand are in the top five in OECD countries, but reinvestment of telecommunications revenues in equipment is among the lowest.[iii] Telecom is not the only provider of telecommunications services in New Zealand but it is the major one. When the OECD report was issued, Telecom did not comment on the prices but did argue that its level of investment in equipment was higher than the level suggested by the OECD report.[iv] This analysis of the last five years of Telecom's annual reports (2003-2007) focuses first on Telecom's prices and then on its capital expenditure.

Prices

Telecom's annual reports contain a note (segment note) which provides summarised information about Telecom's revenues, earnings and assets according to geographical area. Those geographical areas are New Zealand, Australia and Other. Tables 1 and 2 bring together in reorganised form information from the geographical segment notes over the five years from 2003-2007, showing for each geographical area the revenue, the earnings before interest and tax (EBIT), the amount reported for property, plant and equipment (PPE), and total assets. To that information, I've added two percentage calculations, both of which are similar to usual business calculations to assess profitability. These are EBIT as a percentage of revenue, and EBIT as a percentage return on total assets.

Table 1 gives the totals for Telecom as a whole (Telecom Totals). In most years, EBIT as a percentage of revenues is in the mid – to high 20% range, although it falls in 2006, mainly because of large write downs in Australia. For the five years 2003-2007, the EBIT as a percentage of revenues averages 22%. Over that time, EBIT as a percentage return on total assets is around the 15 – 20% range. These are healthy looking returns.

Table 1: Telecom Total Revenue And Assets

	2003	**2004**	**2005**	**2006**	**2007**	**Totals**
Telecom totals	**$m**	**$m**	**$m**	**$m**	**$m**	**$m**
Revenue	5191	5380	5759	5755	5582	27667
EBIT	1496	1428	1600	217	1282	6023
PPE	4635	4312	4283	3301	3681	
Total Assets	7755	7500	7421	6203	8276	
EBIT as % of revenue	29%	27%	28%	4%	23%	22%
EBIT as % of total assets	19%	19%	22%	3%	15%	

Table 2 shows the Telecom total figures from Table 1 analysed over each of the geographic segments (the eliminations at the bottom of this table consist of the amounts required to reconcile the segments with the totals). Again, the dollar information is drawn directly from Telecom's audited financial reports. I have added the percentage calculations.

The first geographical segment information presented is about New Zealand. This analysis shows that Telecom earns approximately 75% of its revenues in New Zealand. With the exception of 2007 where it is 30%, the EBIT as a percentage of revenues is in the mid 30s to low 40s. For the five years 2003-2007, EBIT as a percentage of revenues averages 37%. EBIT as a percentage of total assets is around the mid-20% range. Note that all of the percentages shown for New Zealand are higher than the percentages shown for the overall Telecom totals in Table 1. In contrast, the percentages for both of other two geographical segments are much lower. Telecom's Australian operations have incurred overall losses for the five years.

Table 2 Telecom Geographical Segment Revenue And Assets

NZ	**2003**	**2004**	**2005**	**2006**	**2007**	**Totals**
	$m	**$m**	**$m**	**$m**	**$m**	**$m**
Revenue	3652	3808	4190	4403	4277	20330
EBIT	1499	1538	1539	1598	1288	7462
PPE	3674	3484	3586	3079	3157	
Total Assets	6363	6002	5549	5811	5195	
EBIT as % of revenue	41%	40%	37%	36%	30%	37%
EBIT as % of total assets	24%	26%	28%	27%	25%	
Australia						
Revenue	1466	1490	1358	1291	1327	6932
EBIT	24	35	0	-1398	-51	-1390
PPE	900	768	643	182	495	
Total Assets	1377	1215	1055	625	845	
EBIT as % of revenue	2%	2%	0	-108%	-4%	-20%
EBIT as % of total assets	2%	3%	0	-224%	-6%	
Other						
Revenue	73	54	57	75	87	346
EBIT	24	6	28	17	45	120
PPE	61	60	54	40	29	
Total Assets	868	1062	1045	1023	2236	
EBIT as % of revenue	33%	11%	49%	23%	52%	35%
EBIT as % of total assets	3%	1%	3%	2%	2%	
Eliminations						
Revenue		28	154	-14	-109	59
EBIT	-51	-151	33			-169
Total Assets	-853	-779	-228	-1256		

These figures confirm what NZ consumers already know: as captive consumers in a telecommunications market monopolised by Telecom, the prices they pay for telecommunications services subsidise Telecom's marginal and/or unprofitable elsewhere. For as long as Telecom dominates the market in New Zealand, it can continue to keep prices high. How much longer that can continue depends on technology developments

and the willingness of politicians to regulate the industry. Even in 2005, Telecom foresaw eventual change. The Management Discussion and Analysis in Telecom's 2005 *Annual Report* commented that: "Telecom has experienced a change in revenue mix, with decreasing revenues from higher margin traditional fixed line telephony services, offset by increasing revenues from other products and services, particularly mobile, broadband and solutions. These newer revenues generally yield lower margins than traditional fixed line services. Traditional fixed line revenues are being eroded as a result of pressure on both prices and volumes owing to increased competition and regulatory activity coupled with product substitution as mobile, email and Internet are increasingly being used by customers as substitutes for fixed line calling."[v] Perhaps it is unsurprising that Telecom should be perceived as doing its utmost to resist efforts to introduce competition and even to try to thwart the efforts to facilitate competitor access to the fixed line network. Telecom seems to be dependent on keeping its captive New Zealand users.

Capital Expenditure/ Level Of Reinvestment Of Revenues

The *Judges' Statement* criticises the poor state of telecommunications equipment in New Zealand. Clearly, that reduces the chances of consumers receiving an effective telecommunications service. The judges also cite the OECD report that showed very low levels of reinvestment of telecommunications revenue in New Zealand, 8.7% of those revenues as opposed to an OECD average of 15.3%. Telecom's response when the report was first publicised was that it did not know how the OECD figures had been prepared, and to say that Telecom's reinvestment rate for the "year to June 2005 was 13.5% of New Zealand operating revenues of $4.3 billion. To the year to June 2006, the rate was 13.7% of $4.5 billion". Telecom estimated reinvestment of $683 million for the year to 30 June 2007, and said it had "spent more than $1.7 billion in capital expenditure in New Zealand between the year to June 2004 and the year to June 2005".[vi]

Information from Telecom's annual reports for the five years allows closer scrutiny of Telecom's capital expenditure. Telecom gives detailed information about capital expenditure in the Management Discussion and Analysis section of its annual reports. The total of capital expenditure reported between 2003 and 2007 compared with total revenue reported shows an average of 12% reinvested until 2007 when the amount reinvested jumped to 15%. The 2007 jump lifted the average for the five years to 13% (see Table 3).

Table 3: Total Capital Expenditure Reported Compared With Total Revenues

	2003	2004	2005	2006	2007	Total
	$m	$m	$m	$m	$m	$m
Total capital expenditure	600	608	703	751	844	3506
Total revenue	5191	5380	5759	5755	5582	27667
Capital expenditure as % of total revenue	12%	11%	12%	13%	15%	13%

While these totals provide a useful starting point for assessment, the issue in New Zealand does not relate to the total revenues and total amounts reinvested as capital expenditure. Rather, it relates to Telecom's revenues in New Zealand and the amount reinvested that relates to New Zealand. Over the four years 2003-2006 Telecom used roughly comparable categorisations to report its capital expenditure. Table 4 shows the total capital expenditure for those four years, analysed to identify the total New Zealand investment, before then adding to it the international, Australian operations, and Corporate and Other Capital expenditure. It should be noted that the New Zealand government paid for some of this New Zealand investment: $11 million in 2004, and $20 million in 2005 to support the regional extension of broadband.

Table 4: Analysis Of Total Capital Expenditure 2003 - 2006

	2003	2004	2005	2006
NZ Investment	**$m**	**$m**	**$m**	**$m**
Wired: Growth	165	161	202	203
Wired: Upgrades and replacements	81	76	122	140
New Investment				
Product development	17	16	No analysis provided	No analysis provided
New network capability	5	31		
New IS capability	46	64		
Total New investment	**68**	**111**	102	136
Total NZ Wired	**314**	**348**	**426**	**479**
NZ Wireless	69	68	89	93
Total NZ investment	**383**	**416**	**515**	**572**
International	108	68	35	14
Australian Ops	83	101	118	131
Corporate & Other	26	23	35	34
Total	**600**	**608**	**703**	**751**

The "more than $1.7 billion"[vii] Telecom claimed to have spent on capital expenditure in New Zealand during the two years of 2004 and 2005 is almost double the $931 million reported as Total NZ Investment in Telecom's annual reports ($416 million in 2004 and $515 million in 2005).

Table 5 shows the total New Zealand investment Telecom reported for the four years 2003-2006 compared with the New Zealand revenue reported for the same four years as previously shown in the segment information, and calculates percentages. These percentages are higher than the 8.7% reported by the OECD for New Zealand as a whole. They are also a little lower than the percentages Telecom claimed when the OECD report was publicised (13.5% in 2005 and 13.7% in 2006).

Table 5: Total NZ Investment Reported Compared With Total NZ Revenues

	2003	2004	2005	2006	Total
	$m	**$m**	**$m**	**$m**	**$m**
Total NZ investment	383	416	515	572	1886
Total NZ revenue	3652	3808	4190	4403	16063
NZ Capital expenditure as % of total NZ revenue	10%	11%	12%	13%	12%

The judges' comments reveal concern about the poor state of the fixed line network. Financial reports provide no information about the physical state of assets such as the telecommunications infrastructure, and reliance on numbers is a very poor substitute for such information. Even so, closer analysis of this matter may be assisted by focusing on the categories of capital expenditure shown in Telecom's NZ Wired section of Table 4. In its 2004 *Annual Report*, Telecom described its NZ Wired categories as follows[viii]:

The NZ Wired: growth category "covers those capital costs directly associated with meeting demand for, and extending coverage of, existing products and services. This includes cabling new subdivisions and increasing capacity in exchanges for both voice and data products and increasing capacity on links between exchanges". NZ Wired upgrades and replacements "include capital expenditure not directly associated with meeting growth or development of new capabilities. Upgrades and replacements includes meeting interconnect and regulatory requirements, upgrading street cables, providing seismic security and fire protection systems, upgrading power plant and air-conditioning systems, provision of business infrastructure such as office equipment, motor vehicles, mobile phones for staff use and Telecom's own internal voice and data networks. Capital costs incurred by Telecom Advanced Solutions in acquiring and refreshing client networks included in managed information and communications technology (ICT) solutions are also included in this category". The NZ Wired New Investment category is described as "the development of new products and the deployment of new capabilities into the network (such as Voice over Internet Protocol – VOIP - capability) or information systems (IS - such as a new billing capability)".

As indicated by the explanation of the categories, the "wired: upgrades and replacements" category seems to be the one related to the replacement and renewal of the fixed line network but it also includes various other items that seem unrelated to the fixed line network. Even so, at $419 million, this amount represents 27% of the total New Zealand wired investment ($419m expressed as a percentage of $1567m), and 22% of Total New Zealand investment ($419m expressed as a percentage of $1886m).

In its 2007 *Annual Report*, Telecom changed the presentation of its capital expenditure, adopted vague names to describe the categories presented, and shifted amounts to new categories. Telecom also provided comparative figures for 2006, restating what had been published previously. The new presentation for 2007, with 2006 comparative figures is in Table 6.

Table 6: Analysis Of Capital Expenditure 2006-2007

$millions	**2006**	**2007**
Keep NZ connected	196	187
Build NGT capability	47	62
Network provider of choice	199	213
Service provider of choice	62	87
Invest for returns	91	89
International	14	48
Yellow pages	11	15
Total NZ operations	**620**	**701**
Australian operations	131	143
Total	**751**	**844**
Total NZ Revenue	4403	4277
NZ Capital expenditure as % of total NZ revenue	14%	16%

The 2006 *Annual Report* figures in Tables 4 and 5 showed the Total NZ investment as $572 million, but Telecom's new presentation in Table 6 shows the Total NZ investment for 2006 as $620 million. The jump from $572 million to $620 million was brought about by including within the New Zealand total, the "international" and "corporate and other" categories that previously had been excluded from it. The "international" category is still visible, but the "corporate and other" category has disappeared and the amount involved absorbed into the new categories. This has the effect of inflating the capital expenditure reported for New Zealand and thus inflating the percentage calculation when expressing that capital expenditure as a percentage of New Zealand revenue. In Table 5 the percentage for 2006 was 13% whereas this changed presentation increases it to 14%. The effect of the change in presentation helps to illustrate how accounting numbers can be massaged. It should be noted, however, that massaging numbers does not change the reality that failure to reinvest will lead to deterioration of the network. The judges' concern is not about the numbers, it is about the poor state of the network.

Closer scrutiny of these new categories is warranted, and Telecom explains five of them on p. 24 of its 2007 annual report. These explanations are reproduced in full:

Keep New Zealand Connected – comprises investment needed to meet statutory, regulatory and contractual obligations and to sustain existing service performance. This includes meeting customer demand for legacy services while maintaining current service levels, mitigating risks to continuity of these services, rehabilitating and renewing the access network, maintaining existing capability of Telecom's business infrastructure (including information technology - IT) and developing capabilities to meet current regulatory and statutory requirements.

Build NGT Capability – comprises the investment in the technology and services required to deliver Next Generation Telecom. This includes VOIP capability, creating infrastructure for new channel capability (particularly online), developing new customer management systems and establishing new technology management capability.

Network Provider of Choice – comprises investment required to extend network coverage, augment capacity in line with strategic business growth (e.g. growth in broadband and mobile), develop and deploy new technology capabilities needed to deliver retail and wholesale services cost-effectively, and implement the requirements of the Telecommunications Amendment Act 2006 and Telecom's Undertakings.

Service Provider of Choice – comprises investment in service-specific and customer service systems needed to deliver, grow and sustain retail services. This includes ICT outsourcing and customer premises equipment investment, developing contact centre and customer service systems and capability and other retail channel investment.

Invest for Returns – comprises investment outside core strategic programmes and justified based on the projected rate of return of the investment."

What was previously reported as "wired: upgrades and replacements" seems now to be categorised as "keep New Zealand connected", but the 2006 amount reported under the earlier presentation ($140m) has jumped to $196 million in the new presentation. Telecom has not explained the changes. Certainly, the timing of this change in presentation coincides with the requirements imposed on Telecom following the 2006 legislation. Another possibility is that this is Telecom's response to the public attention drawn to the perceived low level of reinvestment of telecommunications revenue in New Zealand and concern about the poor state of the fixed line network. The changed presentation increases the amounts reported for both, as well as increasing the percentage reported as reinvested.

The *Press* article commenting on the OECD report said the Telecommunications Users Association of NZ (TUANZ) had used the OECD report "to argue that Telecom, one of the world's most profitable phone companies, is failing adequately to invest in its fixed line services. TUANZ Chief Executive, Ernie Newman, said it was little wonder New Zealand's infrastructure was 'creaking' and the country was being denied the basic service needed to participate in the modern economy". Telecom's response was denial: "We are puzzled by any claim New Zealanders are being denied basic services and things are creaking".[ix] The changed presentation of its capital expenditure prompts questions whether Telecom really is puzzled, or whether it is trying to hide something.

Although the figures Telecom provided in response to the publicity about the OECD report give a more flattering representation than is supportable from Telecom's annual reports, it must be noted that the level of investment shown in Telecom's annual reports is higher than the 8.7% identified in the OECD report for New Zealand overall. Especially given the concerns expressed at the time by TUANZ, and by the judges, about the state of the telecom infrastructure in New Zealand, there does seem to be an issue. Questions must be asked about how Telecom could report a reinvestment level of even 12-13% of its New Zealand revenues and yet still be facing such public dissatisfaction over the poor state of that equipment. My further analysis of Telecom's capital expenditure considers three factors that may help to illuminate this issue: the purpose of telecommunications investments; the choice of investment; and Telecom's accounting practices.

Purpose Of Investment

TUANZ thinks Telecom has under-invested in the fixed line network. Similarly, the judges argue that Telecom has tended to defer investment, and further that when it does invest in plant and equipment, it is to introduce selected pieces of new technology that will shut out competitors from its fixed line network. Exemplifying such a selective investment is what seems to be Telecom's response to the intended loop unbundling which will force Telecom to allow competitors access to Telecom's exchanges. As reported by the *National Business Review* (*NBR*), Telecom installed "fibre cabling from some exchanges to road-side cabinets, breaking the continuous copper connection from the subscribers to the exchange. Some competitors have raised concerns that exchange-to-cabinet fibre plans will render their equipment in exchanges unusable, leaving them unable to piggy back on the copper network",[x] In other words, as the judges suggest, perhaps Telecom has invested in capital expenditure, not to improve the fixed line services for users, but rather, to protect its monopoly over fixed line users and therefore over its ability to charge them high prices. This would give the appearance of a higher percentage of reinvestment even as the fixed lines deteriorate. It is difficult to know under which of the new capital expenditure categories expenditure such as this might be reported. Perhaps Telecom's "Network provider of choice" category should be re-titled, "Network provider of no choice".

Choice Of Investment

The OECD report noted that rapidly changing technology in the telecommunications industry means that telecommunications companies cannot simply maintain and replace older assets. Instead, they must strike a balance between keeping older technology running and deciding which new technology to invest in.

With Telecom's revenues from the existing technology falling, it seems likely that the choice of investment will be new technology rather than old technology. Thus it seems possible that the condition of fixed lines is deteriorating because Telecom is concentrating its investment on new technology and in new areas where it can see returns (the "invest for returns" category). A problem facing Telecom, however, is that its customers seem unhappy with the new technology as well.

In this rapidly changing environment, it would be unreasonable to expect success from every one of Telecom's investments in new technology. But Telecom has had some significant failures, the most recent being the fiasco from the forced migration of its email customers to Telecom's new Yahoo!Xtra service.

Closer analysis of the extent and significance of Telecom's new technology bungles would require a telecommunications analyst to assess Telecom's investments and to identify the successes and failures. Telecom's new Chief Executive Officer, Paul Reynolds, however, does seem aware that Telecom's new technology record is poor, the *NBR* quoting him as saying: "We are working hard with our teams to figure out how to introduce products and services with a much better right-first-time approach than is typical in this industry".[xi] Telecom's capital expenditure totals include both successful and unsuccessful investments. How much of Telecom's new investment has been lost because the technology has not delivered on the promises is overlooked. This too will inflate the percentages reported when capital expenditure is compared with revenues.

Telecom's Accounting Practices

Telecom's capital expenditure figures all rely on Telecom's accounting practices, but some of its accounting practices prompt questions about the validity of the figures reported. This point is exemplified by Telecom's 2007 revised presentation of its capital expenditure in New Zealand, as explained above.

How the amounts recorded for capital expenditure are determined, and whether the prices paid are reasonable are matters generally not brought into question. And yet earlier concerns about dubious accounting practices adopted by telecommunications companies generally, including Telecom, prompt further questions about Telecom's reported capital expenditure over recent years. Just one example may help to illustrate this point about the potential for the particular accounting practices adopted to inflate the amount of capital expenditure reported.

In 1998, Telecom joined the global rush to construct high capacity fibre optic cable and engaged in a project to build a $1.1 billion sub-marine cable loop linking New Zealand, Australia, mainland USA, Hawaii, and Fiji. This project was conducted through an associate company, Southern Cross Cables, in which Telecom held 50% of the shares. Like most of Telecom's associate companies, this one very quickly incurred losses greater than Telecom's share investment in it. Once this happened (in 2001), the accounting requirements meant the company became the New Zealand equivalent of an off-balance sheet entity. This means that only selected parts of the activities conducted through Southern Cross make it into Telecom's financial reports, and provides scope for misleading financial reporting.

It soon became apparent that ocean regions had far more cable capacity than could reasonably be used, and prices for using the cable plummeted by about 90%, as did the value of making such an investment. This presented problems for other telecommunications companies besides Telecom, and some tried to improve their financial reports by engaging in capacity swap deals at inflated prices. In 2002, during the fall out in the United States from the collapse of Enron, Telecom was named as the counter party to dubious transactions engaged in by Global Crossing and Qwest, two other telecommunications operators then under investigation for accounting fraud, among other things. The transactions investigated included capacity sale and purchase transactions at inflated prices. Questions included why the companies engaging in these deals would want to purchase capacity at inflated prices, or agree to longer term commitments to purchase capacity, given the glut of capacity that existed and the price slump. At the time, inflated price transactions such as these were condemned as shams.[xii] The focus of attention at the time was on the way these deals inflated the companies' reported profits. What received less comment was the way these deals also inflated the amounts reported for capital expenditure and, consequently, inflated the amounts reported as assets in company balance sheets. Telecom was reported as a counter party to capacity sale and purchase arrangements investigated.

In its 2002 *Annual Report*, Telecom reported having purchased cable capacity from Southern Cross that was included in its assets with a book value (cost minus depreciation) of $260 million. Telecom also disclosed its contractual commitments to purchase additional capacity from Southern Cross at fixed prices totalling approximately $180 million over the next three years (2003-2005).[xiii] With the price for cable access having collapsed, these fixed price commitments may have exceeded the value of the access to be obtained. By 2007, Telecom reported having purchased capacity totalling $456 million, the most recent purchase being from Southern Cross during 2007 for $30 million. All of this $456 million will have been included in capital expenditure. Given the extent of the price slump (about 90%), if the fixed prices were excessive, then this would inflate the amount reported for capital expenditure and help to project a misleading impression that Telecom's capital expenditure is more extensive than it really is.

An additional question arises about the $30 million capacity purchase from Southern Cross in 2007. I've commented previously on Telecom's questionable accounting in the years up to 2004, including circular "money out and money back in" transactions through Southern Cross.[xiv] The cumulative losses of Telecom's off balance sheet entities, most of which relate to Southern Cross, are $292 million, and their shareholders' funds are minus $539 million.[xv] In Telecom's 2007 financial report, its $30 million purchase of capacity from Southern Cross (money out?) coincides with an $18 million dividend Southern Cross paid to Telecom (money back in?) that boosted Telecom's reported profit for 2007. How Southern Cross could be in such a parlous financial state and pay a genuine dividend to Telecom is not clear. What is important to note here is that circular "money out and money back in" transactions do more than just inflate reported profits; they can also inflate reported capital expenditure and the amount reported as assets.

Conclusion

For some years, Telecom has focused on reporting high profits and paying out high dividends to shareholders, and trumpeted its very high international share market ranking on this score.[xvi] Telecom has achieved this by exploiting its New Zealand customer base: to bear the cost of its failed investments and marginal or loss-making adventures elsewhere; to pay its management high salaries and bonuses; and to still report high profits so it can continue to pay high dividends to shareholders. All of this may be seen in Telecom's financial reports. So too is it apparent that some of Telecom's reported profits have involved the use of questionable accounting techniques that have long lasting effects, those effects including inflating the amounts reported as capital expenditure and assets.

Financial reports give no information about the physical state of the telecommunications infrastructure. While accounting numbers, such as the percentage of revenues reinvested as capital expenditure, might provide a rough guide, reliance on numbers is a poor substitute for information about the physical state of the infrastructure. Reliance on numbers is an even poorer substitute when the numbers themselves are dubious. I have outlined examples from Telecom's financial reports showing how the numbers reported for capital expenditure (and assets) may be increased even as the physical state of the telecommunications infrastructure deteriorates.

A problem for Mr Reynolds, and for the Telecom board and management, is that they need valid and reliable financial information to do their job properly. When the use of confusion as a marketing tool extends into financial reporting practices, the directors and management can be as easily confused as those external to the company. In suggesting that some of the public anger directed at

Telecom arises from the public setting unrealistic standards,[xvii] perhaps Mr Reynolds has been confused by Telecom's reporting. As a new recruit to Telecom, Mr Reynolds has the ideal opportunity to review thoroughly the state of Telecom's telecommunications infrastructure and its financial reporting, and to check what is reported against the reality. It is to be hoped he will shun any dubious practices he finds, and make the changes needed, which may require large write downs, to remove the confusion and restore credibility.

Sue Newberry is Associate Professor of Accounting at the University of Sydney.

[i] Telecom Corporation of New Zealand Limited, Annual report 2005, p. 9.
[ii] Press, 15/5/06, "Telecom's cynical manipulation a tragedy for us all"
[iii] Press, 20/7/07, "Telecom criticised for low investment"
[iv] Press, 20/7/07, "Telecom criticised for low investment"
[v] Telecom Corporation of New Zealand Limited, Annual report 2005, p. 45.
[vi] Press, 20/7/07, "Telecom criticised for low investment"
[vii]Press, 20/7/07, "Telecom criticised for low investment"
[viii] Telecom Corporation of New Zealand Limited, Annual report 2004, p. 40.
[ix]Press, 20/7/07, "Telecom criticised for low investment"
[x] National Business Review, 14/12/07, "Telecom's crunch-time looms large"
[xi] National Business Review, 14/12/07, "Telecom's crunch-time looms large"
[xii] www.pbs.org/newshour/bb/business/jan-june02/global_crossing_2-13.html
[xiii] Telecom Corporation of New Zealand Limited, Annual report 2002, p. 42.
[xiv] Watchdog, August 2004, "Financial reports: weapons of mass deception" http://www.converge.org.nz/watchdog/06/03.htm., see "exemplifying the alternative view: Telecom"
[xv] Telecom Corporation of New Zealand Limited, Annual report 2007, p. 44.
[xvi] Telecom Corporation of New Zealand Limited, Annual report 2005, p. 9.
[xvii] National Business Review, 14/12/07, "Telecom's crunch-time looms large"

The Roger Award
P O Box 2258
Christchurch