



Statement of Issues

20 December 2012

Telstra Corporation Limited - proposed acquisition of Adam Internet Pty Ltd

Introduction

1. Outlined below is the Statement of Issues released by the Australian Competition and Consumer Commission (**ACCC**) on the proposed acquisition of Adam Internet Pty Ltd (**Adam**) by Telstra Corporation Limited (**Telstra**) (**proposed acquisition**).
2. A Statement of Issues published by the ACCC is not a final decision about a proposed acquisition, but provides the ACCC's preliminary views, drawing attention to particular issues of varying degrees of competition concern, as well as identifying the lines of further inquiry that the ACCC wishes to undertake.
3. In line with the ACCC's Merger Review Process Guidelines (available at www.accc.gov.au/processguidelines) the ACCC has established a secondary timeline for further consideration of the issues. The ACCC anticipates completing further market inquiries by **24 January 2013** and anticipates making a final decision on **7 February 2013**. However, the anticipated timeline can change in line with the Merger Review Process Guidelines. To keep abreast of possible changes in relation to timing and to find relevant documents, market participants should visit the Mergers Register on the ACCC's website at www.accc.gov.au/mergersregister.
4. A Statement of Issues provides an opportunity for all interested parties (including customers, competitors, shareholders and other stakeholders) to ascertain and consider the primary issues identified by the ACCC. It is also intended to provide the merger parties and other interested parties with the basis for making further submissions should they consider it necessary.

Background

5. On 24 October 2012 Telstra provided its submission to the ACCC seeking informal clearance of the proposed acquisition. The ACCC commenced a review on 25 October 2012 and issued a market inquiries letter on 26 October 2012.

The parties

Telstra Corporation Limited

6. Telstra is the major wholesale and retail supplier of telecommunications services in Australia and retains a dominant market position in many telecommunications

markets. Telstra also owns the near ubiquitous copper network which its competitors need to access and interconnect with in order to compete against it.

7. Specifically, in relation to the proposed acquisition, Telstra provides the following retail services:
 - a. retail fixed broadband services to residential customers, including through its BigPond brand;
 - b. subscription television services (FOXTEL);
 - c. mobile broadband services;
 - d. fixed and mobile voice services; and
 - e. business and corporate data services.
8. Telstra provides retail fixed line telecommunications services through a combination of its near ubiquitous copper network, its hybrid fibre coaxial cable (HFC) network (located in Adelaide, Melbourne, Sydney, Brisbane, Gold Coast and Perth) and the National Broadband Network (NBN). Telstra also owns 50 per cent of the subscription television provider, FOXTEL.
9. Telstra provides a number of wholesale services to other carriers and carriage service providers (**access seekers**) over its copper network, including services that are regulated by the ACCC under Part XIC of the *Competition and Consumer Act 2010* (Cth) (**the Act**).

Adam Internet Pty Ltd

10. Adam is a privately owned telecommunications services provider. It provides services to residential, government and business customers primarily in South Australia and also in the Northern Territory. Adam provides the following retail services:
 - a. fixed broadband services to residential customers;
 - b. mobile voice and broadband services (using the Optus network);
 - c. voice over internet protocol (**VoIP**) services;
 - d. subscription television services such as Fetch TV; and
 - e. business and corporate data services.
11. Adam owns digital subscriber line access multiplexers (**DSLAMs**) in South Australia that it uses in combination with a number of wholesale services acquired from Telstra and other wholesale service providers to provide retail fixed broadband and VoIP services. Adam also provides retail broadband services over its WiMAX network and has commenced providing services over the NBN.

Other industry participants

iiNet

12. iiNet is a national provider of telecommunications services including fixed and mobile broadband and voice, subscription television and web hosting services. iiNet provides these services through the iiNet, Westnet, Netspace, TransACT and Internode brands.
13. Purchased by iiNet in 2011, the Internode brand provided iiNet with a significantly increased infrastructure and customer presence in South Australia.

Optus

14. Owned by the Singtel Group, Optus is a national provider of telecommunications services including fixed and mobile broadband and voice, subscription television, hosting and wholesale transmission services.

TPG

15. TPG is a national provider of telecommunications services including fixed and mobile broadband and voice, subscription television and web hosting services. Through subsidiaries Pipe Networks and Trusted Cloud, TPG also provides wholesale transmission and corporate hosting services.

Dodo

16. Dodo is a national provider of telecommunications services including fixed and mobile broadband and voice services. Dodo also provides electricity and insurance services.

The transaction

17. Telstra proposes to acquire all of the issued shares in Adam Holdings Internet Pty Ltd, which owns all of the issued shares in Adam. The proposed acquisition was publicly announced on 24 October 2012 and is subject to ACCC approval.
18. Telstra submits that its commercial rationale for the proposed acquisition is to operate an alternative low cost operating model which will be made available to customers nationally and which offers opportunities for growth, particularly among budget conscious consumers.

Market inquiries

19. On 26 October 2012 the ACCC commenced market inquiries regarding the proposed acquisition. A range of interested parties provided responses, including competitors, customers and suppliers.

With/without test

20. Section 50 of the Act prohibits mergers or acquisitions that would have the effect or be likely to have the effect of substantially lessening competition in a market. In assessing a proposed acquisition pursuant to section 50 of the Act, the ACCC considers the effects of the acquisition by comparing the likely future competitive environment post-acquisition if the acquisition proceeds (the “with” position) to the likely future competitive environment if the acquisition does not proceed (the “without” position) to determine whether the proposed acquisition is likely to substantially lessen competition in any relevant market.
21. For the purpose of this Statement of Issues, the ACCC considers that it is most appropriate to proceed on the basis that in the absence of the proposed acquisition, the status quo – that is, Adam continuing to conduct its independent telecommunications business as described in paragraphs 10 and 11 above - would continue. The ACCC has not received any information which would suggest that, absent the proposed acquisition, it is likely that Adam would either leave the market or be acquired by a different entity.

22. The ACCC also notes that the future competitive environment is likely to be influenced by the operation of the measures set out in the Structural Separation Undertaking and the Migration Plan that will apply to Telstra's supply of fixed line access services to its wholesale customers for a designated period. An explanation of these measures and their impact on competition in the future competitive environment 'with' the proposed acquisition, and in the future competitive environment 'without' the proposed acquisition is discussed in paragraphs 28-35 below.

Industry background

Regulatory framework

23. The provision of telecommunications services in Australia is regulated by, among other measures, Parts XIB and XIC of the Act.
24. Part XIB contains industry specific prohibitions against anti-competitive conduct in the telecommunications industry, which are based on the general prohibitions in Part IV of the Act.
25. Part XIC establishes an industry specific regime for regulated access to carriage services and was introduced to make provision for an access regime to promote the long-term interests of end-users of telecommunications services. This framework governs the terms and conditions on which Telstra, as the owner of the network infrastructure, must provide access seekers with services that have been declared under Part XIC of the Act (**declared services**).
26. Under this framework, the ACCC regulates Telstra's provision of declared services to its wholesale customers (i.e. as access seekers), including by setting price and non-price terms relating to the supply of the services.

The National Broadband Network

27. On 7 April 2009 the Government announced that it intended to establish the National Broadband Network Corporation Ltd (**NBN Co**) to build and operate a wholesale only, open access national broadband network. The Government's objective is for NBN Co to connect 93 per cent of Australian premises with fibre to the premises technology with remaining premises being serviced by a combination of fixed wireless and satellite technologies.

Structural reform

28. The Government has implemented broader reform to the structure of the telecommunications industry to assist in the transition to the NBN. As a part of this reform, the *Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Act* (**CACS Act**) was passed in November 2010, which introduced a framework to address Telstra's level of vertical integration.
29. The Government has previously stated that Telstra's high level of integration has hindered the development of effective competition in the sector.¹ The reforms brought about by the CACS Act were intended to address competition concerns caused by Telstra's vertical integration which were not adequately remedied by the existing accounting² and operational separation regimes.
30. Under the framework introduced by the CACS Act, Telstra could elect to either submit a voluntary structural separation undertaking or be subject to mandatory functional and horizontal separation.

¹ Explanatory Memorandum to the *Telecommunications (Competition and Consumer Safeguards) Bill 2010*, p.1

² The accounting separation measures require revenue and cost information for wholesale and retail services to be reported to the ACCC.

31. Telstra elected to submit a structural separation undertaking and draft migration plan, which were subject to the approval of the ACCC. A structural separation undertaking (**SSU**) and final Migration Plan were accepted by the ACCC and came into force on 6 and 7 March 2012, respectively.
32. The SSU essentially provides (with some exceptions) that at all times after the designated date Telstra will no longer provide retail voice and broadband services using a network that it controls, primarily its copper and HFC networks. The designated day is currently 1 July 2018, but may be extended by the Minister³. The Migration Plan provides assurances regarding the way in which Telstra will disconnect services from its copper and HFC networks.
33. Telstra has also entered into commercial agreements with NBN Co (**the Definitive Agreements**) that govern, among other things, the terms on which Telstra will disconnect its fixed line customers from its networks and provide services and access to key infrastructure to NBN Co. Under these arrangements, Telstra will progressively disconnect services from its fixed line networks as the NBN is rolled out.
34. Given this progressive implementation of the structural reform, the SSU also specifies a range of measures that will apply to Telstra's supply of fixed line access services to its wholesale customers during the period up until the designated date (**Interim Equivalence and Transparency Measures**). These measures are intended to promote equivalence and transparency in Telstra's supply of these services to wholesale customers and its retail businesses.
35. The structural arrangements of Telstra and the measures that will apply to the disconnection of services during the transition period to the NBN will be an important determinant of the nature and scope of competition which will exist in Australia's telecommunications markets for at least the next 8 to 10 years while the NBN is rolled out.

Fixed broadband services

36. In Australia, fixed broadband services are provided to residential and business customers using a range of technologies, including ADSL services (provided over Telstra's copper network), cable services (provided predominately over Telstra and Optus' HFC networks) and fibre services (provided over the NBN and other fibre networks). ADSL broadband services are currently the dominant technology for the provision of fixed internet connections in Australia.
37. As an alternative to fixed broadband services, broadband can also be provided using fixed wireless services (including WiMAX), mobile wireless and satellite services.
38. Providers of retail ADSL broadband services can supply these services using two broad methods:
 - Purchasing a wholesale ADSL service from an infrastructure owner (e.g. Telstra) and on-selling this service to its retail customers. Retail broadband providers refer to this approach as 'off-net' supply. Telstra, as the owner of the copper access network, is the largest provider of wholesale ADSL services. In February 2012, the wholesale ADSL service was declared by the ACCC under Part XIC.
 - Installing DSLAM infrastructure in Telstra's exchange buildings and purchasing either an unconditioned local loop service or line sharing service from Telstra. Retail broadband providers refer to this approach as 'on-net' supply.

³ Section 577A (10) Telecommunications Act 1997 (Cth).

Fixed voice services

39. Fixed voice services have traditionally comprised the supply of access (a line) and usage (call services) to provide local, national long distance and international calls generally over the copper network.
40. Increasingly VoIP technologies are allowing the provision of fixed voice services over packet switched data networks (e.g. internet). As a result of the regulatory reforms discussed above, fixed voice services will eventually be predominately supplied using the NBN, rather than the copper network.

Transmission services

41. Transmission capacity broadly refers to links (or 'backhaul') which are used to connect service providers' core networks with points of service delivery (such as exchanges). The domestic transmission capacity service (**DTCS**) is a declared service. Transmission capacity is an important input into the ability of service providers to provide downstream retail and wholesale telecommunications services.
42. Service providers either acquire wholesale transmission services from a third party network owner or utilise their own transmission network.

Data centre services

43. Data centre services encompass the provision of data storage and data management services from a secure physical facility that is specifically designed to contain computing and telecommunications equipment. The services that may be offered using a data centre include:
 - co-location: the customer leases space from the provider and installs and maintains their own IT equipment in the facility either for the self supply of services or the supply of managed ICT services to third parties; and/or
 - managed ICT: the provider offers a package of services to the customer, often including the hosting of data and transportation of the data to the centre, utilising the equipment owned by the provider which is located in the data centre.

Market definition

44. On the basis of market inquiries to date, the ACCC's preliminary view is that the following product markets are likely to be relevant in assessing the proposed acquisition:
 - the supply of retail fixed broadband services;
 - the supply of retail fixed voice services;
 - the supply of data centre services;
 - the supply of wholesale transmission services; and
 - (potentially) the supply of bundled telecommunications services.

Retail fixed broadband services

Product dimension

45. Consistent with previous ACCC decisions, whether broadband services are provided via HFC, copper or fibre technologies is unlikely to be a material factor in the ACCC's assessment of the proposed acquisition.⁴ From a functional or end-use perspective, the services supplied over copper, HFC and optic fibre technologies all support similar downstream applications.⁵
46. Therefore the ACCC considers that, for the purpose of this analysis, the relevant retail product market includes services provided over different fixed broadband technology, including copper as well as HFC and optic fibre based services (including the NBN). In the context of the proposed acquisition, the ACCC considers it unnecessary to reach a conclusive view regarding whether other technologies, such as fixed wireless and WiMAX form part of the same market.

Geographic dimension

47. The ACCC has considered the appropriate geographic dimension of the market for the supply of fixed retail broadband services and, in particular, whether for the purposes of this review it is appropriate to consider the competitive effects in the context of a national or South Australian market.
48. While it is common for providers of retail fixed broadband services with national brands to maintain nationally advertised pricing policies for those brands, information received during market inquiries suggests there is some degree of localised competition in South Australia. Local competition is present both through the advertised pricing and terms offered by brands based in, or focused on, South Australia, such as Adam and the iiNet brand Internode, and through the pricing responses of national suppliers to local competition.
49. Market inquiries indicate that suppliers will target promotions and marketing campaigns in specific geographic areas in response to events such as developments in local competitive dynamics and infrastructure investment. Examples of local competition include Internode's marketing of discounted fixed broadband offers targeted at South Australian residents, in response to the announcement of the proposed acquisition.
50. The extent of local competition also reflects the geographic limitations of the infrastructure put in place by certain suppliers. While Telstra clearly has infrastructure across Australia, the DSLAM infrastructure installed and used by Adam is limited to South Australian local exchanges.
51. In relation to national suppliers of fixed broadband services the ACCC understands these suppliers can respond to the localised nature of the competitive threat presented by local brands by offering discounts, price matches or other advantageous terms to individual customers who notify them that they would otherwise 'churn' (switch) to a competitor.
52. Market definition is a tool to identify and define the boundaries of competitive conduct between the merger parties. Accordingly, the ACCC proposes to consider the proposed acquisition in the context of a South Australian market for retail fixed broadband services.

⁴ ACCC, *Telstra's local carriage service and wholesale line rental exemption applications, Final Decision and Class Exemption*, August 2008, page 48.

⁵ See ACCAN, *NBN: Guide for Consumers – the Basics: The internet and broadband*, April 2011, p4.

53. In relation to the issue of concern discussed below at paragraphs 65-74, the ACCC considers that the likely substantial lessening of competition in the supply of retail fixed broadband services would arise irrespective of whether the proposed acquisition is assessed on the basis of a national market or state based markets.

54. Retail fixed voice services

Product dimension

55. Retail fixed voice services broadly refer to the provision of a call or telephony service that enables the end customer to make local, long distance and international voice calls. Some market participants indicated that VoIP technology is increasingly seen as a substitute for standard telephone services provided over the copper network.
56. The ACCC considers it unnecessary to reach a conclusive view regarding whether fixed voice services supplied using VoIP are substitutable for those provided over the copper network as even if VoIP services are included within the same market, the increase in Telstra's market share as a result of the proposed acquisition would be minimal.

Geographic dimension

57. The market for the supply of retail fixed voice services demonstrates similar characteristics to the market for the supply of retail fixed broadband services and the ACCC considers that a similar approach should be taken to the geographic dimension of this market. The ACCC also notes that in relation to the issue of concern discussed below at paragraphs 65-74, the likely substantial lessening of competition in the supply of retail fixed voice services would also arise irrespective of whether the proposed acquisition is assessed on the basis of a national market or state based markets.

Other markets

58. The ACCC has also considered the impact of the proposed acquisition on the following markets.

Data centre services

59. Market inquiries indicate that there may be a market for the provision of data centre services. The ACCC understands that data centre services broadly encompass the storage of data and/or hosting of IT equipment (e.g. servers) in a secure facility. Access to data centre services is considered by market participants who do not own their own facilities to be a key input in the supply of telecommunications and IT services and products, including managed ICT or hosting services.
60. The ACCC received mixed information from market participants on the appropriate geographic dimension for the supply of data centre services. Some industry participants consider that interstate data centres would be substitutable for a local data centre while others were of the view that local data centres were important in order to compete for certain managed ICT or hosting services contracts.
61. However, market inquiries indicate that post acquisition there would remain a number of alternative data centres available in South Australia, including so-called 'carrier neutral' data centres with excess capacity and, accordingly, the ACCC considers it unnecessary to reach a conclusive view on the geographic market definition regarding the supply of data centre services.

Wholesale transmission services

62. Market inquiries revealed mixed views on the geographic scope of the market for the supply of wholesale transmission services. However, the ACCC did not consider it necessary to reach a view on the appropriate geographic dimension of the relevant market. Market inquiries indicate the size of Adam's purchases of wholesale services are relatively small and even on a narrow market restricted to South Australia, the proposed acquisition is unlikely to result in a substantial lessening of competition in the supply of wholesale transmission services.

Bundled supply of telecommunications services including subscription television services

63. Concerns were raised by industry participants that post acquisition, Telstra would be able to utilise Adam to reduce competition in the supply of bundled telecommunications and subscription television services.

64. The ACCC does not consider it necessary to reach a view on whether there is a separate market for the supply of bundled telecommunications services encompassing subscription television content as the proposed acquisition would not significantly impact Telstra's ability and incentive to offer such bundled services.

The ACCC invites comments from market participants on its proposed definition of the relevant markets. In particular, market participants may wish to comment on the geographic dimension of the market for retail fixed broadband services, including:

- (i) the extent to which national retail fixed broadband service providers offer tailored pricing and plans or special offers in South Australia; and
- (ii) any examples of South Australian based or focused retail fixed broadband service providers, such as Adam, offering products, plans or promotions that are not replicated elsewhere in Australia.

Statement of issues

65. For the purposes of this Statement of Issues, the issues in this matter are divided into three categories, 'issues of concern', 'issues that may raise concerns' and 'issues unlikely to pose concerns'.

Issues of concern

The proposed acquisition would provide Telstra with the ability and incentive to foreclose competition

66. The ACCC has extensively noted the longstanding competition issues that have arisen from Telstra's ownership of the copper network and its participation in downstream retail markets.⁶ Telstra's control over the copper network, combined with its market position, creates an incentive and the ability for it to favour its own retail business in the provision of access to this important infrastructure and thereby lessen competition in the related downstream retail markets, to the detriment of consumers.⁷

67. The structural reform to be implemented by the SSU and Migration Plan is expected to address these concerns. However, the Interim Equivalence and

⁶ ACCC, *Submission to the Department of Broadband, Communications and the Digital Economy "National Broadband Network: Regulatory Reform for 21st Century Broadband"*, June 2009, pp.18 – 39.

⁷ Explanatory Memorandum to the *Telecommunications Legislation Amendment (Competition and Consumer Issues) Bill 2005*, p 13

Transparency Measures in the SSU and elements of the Migration Plan would not apply in an appropriate or effective way to Telstra's operation of Adam post acquisition.

68. The ACCC's preliminary view is that post acquisition, Telstra would have the ability and incentive to utilise its market power to favour Adam over its wholesale customers in the provision of access to its network infrastructure. The ACCC is concerned that this is likely to reduce the ability of alternative retail fixed voice and broadband service providers to constrain Telstra's market power at the retail level, significantly foreclosing competition in the markets for the supply of retail fixed voice services and retail fixed broadband services.
69. The ACCC's concerns with the impact of the proposed acquisition, in the absence of an adequate remedy reflect concerns raised in market inquiries. Market participants submitted that the proposed acquisition would allow Telstra to supply services to Adam on terms and conditions that are not equivalent to the terms and conditions upon which Telstra supplies its wholesale customers and this could provide Adam (and, as a consequence, Telstra) with advantages which would likely result in a substantial lessening of competition in the supply of retail fixed voice services and retail fixed broadband services.
70. The Interim Equivalence and Transparency Measures in the SSU would not effectively constrain Telstra's ability to engage in a foreclosure strategy post acquisition. In particular, the ACCC is concerned that, post acquisition, Telstra may have the ability and incentive to engage in discriminatory behaviour, including but not limited to the following:
 - a. Telstra would be able to charge Adam lower prices for key upstream inputs than it charges its wholesale customers.
 - b. Adam (or its employees) may be able to access important information or be informed by Telstra about Telstra's network issues or operations (including product development) that may not be available to wholesale customers.
 - c. Telstra would be able to supply Adam with services that are not technically or operationally equivalent to those supplied to wholesale customers. For example, Telstra could supply Adam with services of higher quality, with additional functionality or features and not supply an equivalent service to its wholesale customers.
 - d. Adam (or its employees) may be able to access confidential information about Telstra's wholesale customers.
 - e. Telstra would be able to favour Adam when processing orders from Adam and/or utilise different systems to that which it uses for wholesale customers.
 - f. Telstra would be able to offer its employees incentives to favour Adam over its wholesale customers.
71. The ACCC is concerned that, should Telstra engage in such conduct this is likely to have the effect of substantially lessening competition in the markets for retail fixed voice services and retail fixed broadband services.
72. The ACCC's preliminary view is that post acquisition, Telstra's ability to engage in this conduct is unlikely to be effectively addressed through existing regulatory measures that apply to Telstra's supply of fixed line access services.
73. The ACCC is also concerned that post acquisition, the reporting requirements in the SSU (and the Migration Plan) which enable the ACCC to measure Telstra's compliance with its 'equivalence' obligations would no longer provide an appropriate and effective level of transparency regarding Telstra's compliance with its Interim Equivalence and Transparency Measures.

74. The ACCC notes that, as a result of the limited application of the Interim Equivalence and Transparency Measures in the SSU, post acquisition Telstra would have the incentive and the ability to divert customers, and/or assets, from its existing retail business to Adam in order to maximise the impact of any such foreclosure strategy. Telstra may also be able to transfer particular wholesale or network functions to Adam and thereby circumvent the relevant obligations in the Interim Equivalence and Transparency Measures that apply to the performance of those functions.
75. The ACCC notes that the preliminary competition concerns it has identified in paragraph 65 to 73 arise regardless of whether the proposed acquisition is considered on the basis of a national market or state based markets.

The ACCC invites comments from market participants on whether the proposed acquisition is likely to lead to a substantial lessening of competition in the markets for the supply of retail fixed voice and broadband services due to Telstra's enhanced vertical integration. In particular, the ACCC is seeking further information in relation to:

- (i) the potential conduct which Telstra could engage in post acquisition, which may enable Telstra to advantage Adam over its other wholesale customers and/or potentially circumvent the application of the existing Interim Equivalence and Transparency Measures; and
- (ii) the likely effect that such conduct may have on competition in the markets for the supply of retail fixed voice and broadband services.

Issues that may raise concerns

Horizontal aggregation in the provision of retail fixed broadband services in South Australia

76. The ACCC's preliminary view is that the removal of Adam as an independent competitive constraint on Telstra may enable Telstra to increase prices and/or reduce the quality or offering of its retail fixed broadband services in South Australia.
77. Telstra is the largest provider of retail fixed broadband services in South Australia in terms of subscriber numbers, while Adam is the third largest. The proposed acquisition would result in Telstra increasing its market share in South Australia from approximately 40-45 per cent to 55-60 per cent.
78. While the ACCC notes that Telstra has made public statements that post acquisition the Adam brand will be positioned as a low cost alternative to Telstra, market inquiries indicate that Adam is currently positioned at a broadly similar level to Telstra, targeting customers that prioritise reliable broadband performance and high levels of locally based service in their purchasing decisions. These customers are typically not highly price sensitive.
79. The ACCC understands that while Telstra bundles all of its retail fixed broadband services with a retail fixed voice service and Adam sells 'naked' fixed broadband services, market inquiries indicate that the effective prices of the Telstra and Adam ADSL2+ offers are comparable. Adam and Telstra also appear to promote similar levels of customer support with personalised support and Australian based call centres as important aspects of their fixed broadband offers.
80. The ACCC is continuing to explore the degree to which Telstra and Adam are close competitors to each other, in terms of both price and service levels.

81. Market inquiries indicate that lower priced suppliers such as Dodo and TPG would not be likely to provide a strong constraint on Telstra's offerings in South Australia post acquisition. Dodo and TPG appear to offer consistently lower prices than both Telstra and Adam, with some market participants considering that these providers target a different segment of the market to Telstra and Adam with less focus on high levels of personalised customer support.
82. The ACCC understands that other suppliers including iiNet (via its South Australian focused brand Internode) and Optus are positioned in a similar manner to Adam and Telstra in South Australia. The ACCC is considering the extent to which these other suppliers would continue to constrain Telstra post acquisition – although the ACCC notes that such suppliers would provide a limited constraint on Telstra post acquisition unless the vertical concerns identified in paragraphs 65 to 74 above are resolved.
83. The ACCC recognises that Telstra currently maintains an advertised national pricing policy. However, the ACCC is concerned that the proposed acquisition may remove the local competitive constraint provided by Adam in South Australia and Telstra's likely response to this constraint. Post acquisition, customers may be less likely to switch, or to threaten to switch, away from Telstra and Telstra would therefore have less incentive to offer individualised pricing and terms in response to such threats.
84. The ACCC is concerned that the proposed acquisition results in the loss of a local competitive response to Telstra and limits the choices available to customers.
85. Market inquiries indicate that while Adam is a close competitor to Telstra in terms of its market positioning, Adam also offers differentiated product and service offerings specifically targeted to the South Australian market, providing a competitive response to national competitors and additional choice to customers in South Australia.
86. These differentiated offers are often provided through specials or discounts linked to local events or organisations. The ACCC understands that Adam offers a diverse range of discounts and promotions to current and/or potential retail fixed broadband customers in South Australia. Market inquiries have also indicated that Adam's provision of 'naked' ADSL services (which are not offered by Telstra) through its extensive network of DSLAM infrastructure in South Australia are a valued alternative to Telstra's bundled offering.
87. The ACCC considers the likelihood of new entry or significant expansion in the supply of retail fixed broadband services in South Australia to be low in the short to medium term. This market is maturing and the ACCC understands that while access seekers will continue to invest in DSLAMs where it is efficient to do so, DSLAM investment has been decreasing in previous years and the roll out of the NBN is likely to contribute to a continued reduction in investment in DSLAM infrastructure.

The ACCC invites comments from market participants on the likely competition effects of the proposed acquisition on the South Australian market for retail fixed broadband services. In particular, interested parties may wish to comment on:

- (i) the extent to which Adam is currently a close competitor to Telstra, and any competitive harm that is likely to arise from the removal of Adam as a competitor to Telstra in South Australia;
- (ii) the extent to which Adam currently offers unique product, price or service offerings that are not replicated by other retail fixed broadband service providers in South Australia;

- (iii) the level of competitive constraint provided by iiNet/Internode and Optus in retail fixed broadband services in South Australia and the extent to which these operators target similar customers to Telstra and Adam;
- (iv) the level of competitive constraint provided by TPG and Dodo in retail fixed broadband services in South Australia and the extent to which customers of Telstra and Adam would consider these providers to be strong alternatives; and
- (v) the likelihood of entry by retail fixed broadband service providers not present in South Australia and/or the likelihood of expansion from providers already present in South Australia, in particular through additional DSLAM investment.

Issues unlikely to pose concerns

88. The ACCC considers that the proposed acquisition is unlikely to pose competition concerns in respect of the following issues. However, the ACCC will accept submissions from industry participants on these issues and will further consider potential competition issues if it considers that such an assessment is warranted.

Removal of a supplier of data centre services in South Australia

89. Adam currently operates data centres in South Australia and concerns were raised that post acquisition Telstra may limit access by third parties to Adam's data centre, potentially limiting competition in downstream markets for the supply of managed ICT and hosting services. The ACCC understands that access to data centres is considered an important requirement to be able to compete in this downstream market.

90. The ACCC considers that the proposed acquisition is unlikely to substantially lessen competition in the supply of data centre services or related downstream markets, regardless of the market definition adopted, due to the availability of alternative data centres including in South Australia, such as Metronode, Hostworks, Internode and the recent entrant Tier5. Market inquiries indicate that most of these alternative suppliers are likely to have spare capacity.

Removal of a contestable customer for the supply of wholesale transmission services in South Australia

91. The ACCC has considered whether the proposed acquisition would remove a significant amount of contestable demand for the acquisition of wholesale transmission services in South Australia. Adam currently acquires wholesale transmission services from a range of suppliers and concerns have been raised that if Adam were to acquire these services from Telstra post acquisition, this would foreclose rival providers' access to customers, potentially reducing the ability and incentive of suppliers of these services to invest and expand their wholesale transmission networks in the state.

92. The ACCC's preliminary view is that the size of Adam's purchases of wholesale transmission services is relatively small in relation to the total transmission services required nationally and also in South Australia and that were Adam to ultimately obtain these services from Telstra then this would be unlikely to deprive rival wholesale transmission service providers of a sufficient customer base even in the narrow market of South Australia.

93. Accordingly, the ACCC considers that the proposed acquisition is unlikely to result in a substantial lessening of competition in the provision of wholesale transmission services in South Australia.

Bundling of subscription television with retail fixed broadband services in South Australia and nationally

94. Some market participants have expressed concern that the proposed acquisition may have an adverse effect on competition in the market for retail fixed broadband services and any emerging market(s) for the provision of bundled services encompassing subscription television content. It has been submitted that this could occur if the FOXTEL content that Telstra acquires is supplied in conjunction with the Adam brand post acquisition.
95. In particular, it has been claimed that if Telstra bundled FOXTEL with Adam's fixed retail broadband services, it would provide Adam's services with a significant competitive advantage over rival's offerings, potentially jeopardising the commercial viability of competing providers and their ability to constrain Telstra post acquisition, particularly in the provision of retail fixed broadband services.
96. The ACCC's preliminary view is that any competitive advantage that Telstra obtains as a result of its pre-existing relationship with FOXTEL exists with and without the proposed acquisition. For this reason, the ACCC considers it unlikely the acquisition of Adam would enable Telstra to exercise any additional market power in the market for retail fixed broadband services and in any emerging market(s) for the provision of broadband services encompassing subscription television content that it would not have otherwise been able to exercise in the absence of the proposed acquisition. The ACCC also does not consider the proposed acquisition is likely to substantially increase Telstra's incentives to exercise any such market power and engage in a foreclosure strategy.

Horizontal aggregation in retail fixed voice services

97. The overlap in the merger parties' activities in retail fixed voice services is minimal. While Telstra is the leading supplier of retail fixed voice services in South Australia and also nationally, Adam does not currently provide traditional fixed line telephone services. Adam does however provide a relatively small number of VoIP services in South Australia.
98. The ACCC considers that even if VoIP and traditional fixed line telephone services are included in the same market the proposed acquisition is unlikely to have an impact on competition for the provision of retail fixed voice services given the increase in Telstra's market share would be minimal.

The ACCC invites comments from market participants on the likely competitive effects of the proposed acquisition on the markets identified above.

ACCC's future steps

99. The ACCC will finalise its view on this matter after it considers market responses invited by this Statement of Issues.
100. The ACCC now seeks submissions from market participants on each of the issues identified in this Statement of Issues and on any other issue that may be relevant to the ACCC's assessment of this matter.
101. Submissions are to be received by the ACCC no later than **24 January 2013**. The ACCC will consider the submissions received from the market and the merger parties in light of the issues identified above and will, in conjunction with information and submissions already provided by the parties, come to a final view in light of the issues raised above.

102. The ACCC intends to publicly announce its final view by **7 February 2013**. However the anticipated timeline may change in line with the Merger Review Process Guidelines. A Public Competition Assessment for the purpose of explaining the ACCC's final view may be published following the ACCC's public announcement.