



Australian  
Competition &  
Consumer  
Commission

# ACCC submission to the NBN non-commercial services funding options - final consultation paper

November 2015

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# 1. Introduction

The ACCC welcomes the opportunity to make a submission to the Bureau of Communications Research's (BCR) final consultation paper on NBN non-commercial services funding options.

The Australian Government has asked the BCR to consider economically sound ways to fund the rollout of the National Broadband Network (NBN) to regional Australia. The BCR has assessed the non-commercial losses expected from building and operating satellite and fixed wireless services and considered options for funding these losses via industry contributions. The BCR is seeking stakeholder views on initial financial model outcomes and proposed funding options.

## **ACCC's initial submission**

In its previous submission to the BCR's initial consultation paper, the ACCC focused on some of the existing regulatory concepts incorporated within NBN's Special Access Undertaking (SAU) that may assist the BCR's consideration of an appropriate approach to quantifying losses from non-commercial services. The ACCC generally agreed with BCR's conclusions that some elements of the SAU would likely need to be changed to accommodate the introduction of alternative funding arrangements for non-commercial services. However, the ACCC anticipates that NBN Co would need to consider the details of an alternative funding model before it would be able to advise on the extent to which the SAU would need to be varied.

The ACCC also emphasised that the potential impact on infrastructure based competition should be considered when developing a transparent funding arrangement. Rules around funding eligibility and the basis on which the levy is applied should not impose disproportionately higher costs on network operators or increase barriers to entry for network owners.

This submission will not repeat the content of the ACCC's previous submission. It also does not seek to address every issue raised in BCR's further consultation paper. Rather, this submission focuses on two matters raised in the final consultation paper in relation to which, the ACCC has a perspective that may assist BCR's consideration. These matters are:

- ensuring that the proposed funding arrangement provides the right incentives to promote economic efficiency, and
- considering whether the ACCC could have a role in determining the required funding amount.

## 2. Principles based approach to funding options – economic efficiency

The ACCC notes that submissions to the BCR's initial consultation paper were divided on whether an industry funding arrangement should only apply to NBN Co and NBN equivalent industry participants, or whether it should apply to a broader range of participants across the telecommunications industry, including mobile network operators. The BCR is of the view that a funding arrangement limited to NBN Co and NBN equivalent industry participants maintains important existing commercial incentives for NBN Co to control costs, determine

appropriate service standards and innovate.<sup>1</sup> For the reasons outlined below, the ACCC supports the BCR's preferred position.

The BCR has proposed several overarching principles to help guide the development of appropriate funding arrangements. These principles include transparency, contestability, sustainability, economic efficiency and equity.<sup>2</sup> The BCR has also decided to include competitive neutrality as an additional overarching principle. The ACCC agrees that each of these principles should guide consideration of the most appropriate funding arrangement to support the rollout of the NBN to regional areas.<sup>3</sup>

### **Incentives to promote economic efficiency and the NBN special access undertaking**

The ACCC agrees that it is important to assess the incentives associated with any new funding arrangement. The ACCC considers that establishing the right incentives will be particularly important for achieving the principle of economic efficiency. Similar considerations arose during the ACCC's assessment of the special access undertaking (SAU) given by NBN Co. Specifically, the inclusion of incentives to invest, operate and price efficiently which were included in the SAU was a key factor in the ACCC's decision to accept the SAU as discussed below.

The BCR notes that the design of non-commercial funding arrangements should minimise the extent to which it diverts resources away from more highly valued uses. It should also encourage cost-based service provision and provide incentives for investment and innovation. The BCR has argued that an NBN equivalent funding arrangement performs better on the criteria of economic efficiency because it maintains incentives for cost control and market responsiveness for NBN Co.<sup>4</sup>

The ACCC agrees with the BCR's assessment regarding economic efficiency and incentives. The ACCC considers that if the BCR was to move from the NBN equivalent funding arrangement to a broader industry-based arrangement, the incentives for economic efficiency would be diminished.

The ACCC accepted a SAU given by NBN pursuant to section 152CBA of Part XIC of the *Competition and Consumer Act 2010* (the Act) on 13 December 2013. Under the Act, the ACCC can only accept a special access undertaking if it is satisfied that it promotes the long-term interests of end-users, taking into account a range of matters. As part of its consideration of the SAU against this test, the ACCC considered whether the SAU provided incentives to NBN Co to invest and operate in a prudent and efficient manner.

The SAU, as accepted by the ACCC, allows NBN Co to recover its actual expenditure, subject to its expenditure meeting certain prudency conditions specified in the SAU, up to 2023. The ACCC recognised that, in most contexts, allowing a regulated business to recover its actual expenditure does not encourage efficient investment. This is because the business is able to recover additional expenditure from customers if it incurs higher capital expenditure than expected over a regulatory period. Conversely, if the business incurs lower capital expenditure than expected, these savings may be passed through to customers rather than being retained by the business. Together, these do not provide effective

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<sup>1</sup> BCR, NBN non-commercial services funding options, final consultation paper, October 2015, pp.49-55.

<sup>2</sup> BCR, NBN non-commercial services funding options, final consultation paper, October 2015, p.43.

<sup>3</sup> ACCC, ACCC submission to the NBN non-commercial services funding options consultation paper, 5 June 2015, p.2.

<sup>4</sup> BCR, NBN non-commercial services funding options, final consultation paper, October 2015, pp.53-55.

incentives on the business to either limit over-expenditure or seek cost savings because the business is not rewarded for doing so.<sup>5</sup>

However, in the case of the NBN, the ACCC considers that other commitments in the SAU and external factors relevant to the NBN establish good incentives for NBN Co to invest efficiently. For example, the SAU includes initial maximum regulated prices for several NBN offers and price control provisions. These price control provisions limit any individual price increase to CPI minus 1.5 per cent each financial year and apply to all NBN offers and other charges for the full duration of the SAU.<sup>6</sup>

Externally, NBN Co faces a significant capital outlay during the initial rollout period and will face demand risk due to uncertainty regarding the take-up of its services. Combined with the price control mechanisms in the SAU, these factors mean that NBN Co faces uncertainty that it will recover sufficient revenue to recover its costs over time. The ACCC considered that this would provide a strong incentive for NBN Co invest efficiently and control its costs.

In the final decision to accept NBN Co's SAU, the ACCC stated that:

'the ACCC considers that NBN Co will face a high degree of revenue sufficiency risk for most, if not all, of Module 1 [the period to June 2023]. This is due to NBN Co's initial prices and the expected low initial take-up of NBN services. This should provide incentives for NBN Co to invest efficiently. In addition, there are measures in Module 1 to ensure that the individual cost components of the LTRCM will only allow for NBN Co to recover prudent and efficient costs.'<sup>7</sup>

The ACCC considers that these factors, in combination, provide NBN Co with incentives to price services in a way that encourages the take up of services and increase revenue (to address demand and revenue sufficiency risk), and to invest in the network efficiently because it will not be able to increase prices above the price controls to recover higher costs.

Under the proposed NBN equivalent approach, NBN Co would be responsible for making the largest contribution towards fixed wireless and satellite service losses, because it has the largest number of services in operation. NBN Co would continue to face significant revenue sufficiency risk as it would be responsible for bearing most of the costs associated with fixed wireless and satellite services. In practical terms, this is unlikely to result in a significant change to the incentives facing NBN Co to invest, operate and price efficiently.

However, under the broader industry based funding approach, NBN Co would only be responsible for funding about 13 per cent of losses associated with fixed wireless and satellite services. The ACCC considers that this would have a significant impact on the incentives for NBN Co to invest, operate and price efficiently. That is, the ACCC considers that the incentives for NBN Co to control costs would be significantly weakened under the broader industry based funding approach and that an NBN equivalent funding arrangement is preferable to ensure economic efficiency.

### 3. Administration arrangements

The BCR notes that the administration of the non-commercial services funding arrangements would involve two distinct roles. The first would be to determine the required

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<sup>5</sup> ACCC, Draft Decision about the 2012 NBN Co Special Access Undertaking, April 2013, p.141.

<sup>6</sup> NBN Co, SAU, November 2013, Schedule 1C, clause 1C.5.2; Schedule 2B, clause 2B.2.3

<sup>7</sup> ACCC, NBN Co Special Access Undertaking Final Decision, 13 December 2013, p.96.

funding amount in light of revenue and costs for fixed wireless and satellite services. The second role would be to collect the funding contributions from eligible participants.<sup>8</sup>

## **Determining the funding amount**

The BCR has outlined the key responsibilities associated with determining the funding amount as follows:

- determining the total per SIO amount required to fund NBN non-commercial services, based on an assessment of NBN Co costs and revenues for fixed wireless and satellite services
- conducting periodic reviews of the funding arrangement, and
- publishing updated forecasts.

The BCR considers that this role could be undertaken by a number of government agencies, including the ACCC, the Department of Communications and the Arts, or the ACMA. The ACCC agrees that each of these agencies have particular functions that have some alignment with the responsibilities associated with determining the required funding amount.

As the ACCC is the economic regulator of telecommunications services under Part XIC of the Act, the ACCC is particularly well-placed to take on this role for two reasons. First, as acknowledged by the BCR, there would be some alignment with the ACCC's role in the regulation of the NBN through NBN Co's SAU. This includes, among other things, making an annual long term revenue constraint methodology (LTRCM) determination. As outlined in the ACCC's submission to the initial consultation paper, the LTRCM specified in the SAU already provides a framework for defining and quantifying losses incurred by NBN Co.

Secondly, the ACCC has some expertise in demand and expenditure forecasting which may be useful for the periodic re-forecasting of non-commercial losses and recalculation of the funding amount. For example, the ACCC has experience with cost forecasting activities through its price regulation functions.

If the ACCC were to take on the role, it considers that a robust framework should be developed, in consultation with relevant parties that clearly defines the roles and responsibilities of the ACCC. The ACCC expects that it would be consulted further on the development of any such framework.

## **Responsibilities of NBN Co and the regulator**

The ACCC agrees with the BCR's proposal that financial forecasts should be prepared by NBN Co or based on NBN Co input data, with the role of the regulator limited to providing guidance to NBN Co and assessing the financial projections to ensure they meet prudence and efficiency requirements. The ACCC also agrees that industry consultation is important to ensure the regulator makes an informed decision and to promote transparency.

## **Collection of industry contributions**

The ACCC supports the BCR's finding that the ACMA is best placed to collect NBN non-commercial services funding, which aligns with its responsibility for the collection of the Telecommunications Industry Levy.

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<sup>8</sup> BCR, NBN non-commercial services funding options, final consultation paper, October 2015, p.66.

## 4. Other matters

### Potential variation to NBN Co's SAU

The BCR considers that NBN Co's SAU should be updated to recognise NBN non-commercial service funding contributions. The ACCC would like to reiterate the comments made in its submission to the initial consultation paper regarding the process for amending the SAU. As outlined in that submission, and noted in the BCR's final consultation paper, the ACCC does not have powers under Part XIC of the Act to require NBN Co to vary an existing SAU, or to otherwise initiate changes to an existing SAU.

Should NBN Co seek to vary its SAU to accommodate the BCR's proposed funding arrangements and/or the Government's policy that NBN Co transition to price caps, the ACCC will consult with industry and other interested stakeholders as part of its assessment process.

### Regulatory and policy review points

The BCR recommends that regulatory reviews be conducted every five years in order to re-forecast NBN non-commercial service losses and recalculate the funding amount required. The BCR also recommends that the regulator should be authorised to conduct a review outside of the set review points if there is cause to do so, including by the request of the Minister for Communications.<sup>9</sup>

The ACCC considers that this is likely to be an appropriate time period for regulatory reviews, and it is consistent with recent ACCC regulatory decisions for other telecommunications services. The ACCC also considers that the ability to conduct a review outside of these set review points will allow flexibility if circumstances change.

## 5. Concluding remarks

The ACCC appreciates having the opportunity to engage with the BCR as part of its process of developing an appropriate funding model for non-commercial NBN services and advice to Government.

The ACCC would welcome further engagement with the BCR further regarding a possible role for the ACCC in determining the required funding amount, should the BCR recommend that option.

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<sup>9</sup> BCR, NBN non-commercial services funding options, final consultation paper, October 2015, p.69.