



TELSTRA CORPORATION LIMITED

**Response to the ACCC Draft Final Report on review of
the declaration of the domestic transmission
capacity service**

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Executive Summary

Telstra supports the objective of providing greater clarity and certainty around the scope of the domestic transmission capacity service (DTCS) declaration. However, Telstra continues to have serious concerns that the extension of the service description to include Ethernet and other unspecified interface protocols is unnecessary and likely to damage competition and investment.

There is no evidence of market failure in the provision of wholesale Ethernet. For example, Telstra launched a CGE service, which is an Ethernet over SDH service, in 2008, and makes it available in all CGE enabled exchanges where there is capacity. Its competitors similarly provide CGE services, including by acquiring SDH as a regulated input from Telstra or other fibre owners and adding relatively low-cost electronic equipment. Contrary to suggestions by competitors, Telstra has not refused to supply services on our CGE network. There is no evidence of a bottleneck or prospect of a bottleneck arising that would be relieved by the proposed variation.

The ACCC is obliged to conduct a proper analysis of whether the long-term interests of end users (LTIE) are promoted by the proposed variation. However the draft final decision does not refer to the 'with or without' test. A reliance on technology neutrality cannot be a substitute for proper market analysis of whether regulation of Ethernet over SDH is in the LTIE.

Finally, Telstra submits that the ACCC must update the geographic scope of the declaration prior to finalising its inquiry. Competition in transmission now extends well beyond the list of routes and ESAs identified for exemption in 2008. . The ACCC should use the information collected under the infrastructure RKR to ensure that the geographic scope of the updated service description is and remains consistent with the ACCC's exemption threshold. The ACCC cannot make a declaration that does not extend to routes meeting this threshold, because to do so would not be in the LTIE.

A There is no market failure requiring regulation

Regulation, properly applied, is proportionate to and directed at resolving persistent market failure. Telstra submits that there is no market failure in the supply of Ethernet services and the ACCC has not sufficiently taken account of competition in the existing supply of Ethernet.

Ethernet services in this submission refer to Ethernet services that have the characteristics specified in the proposed variation to the service description.

A.1 The current DTCS service description does not include Ethernet services

The DTCS service description does not currently include Ethernet, and it should not do so. It covers the point to point transmission of signals on a permanent basis using only SDH and PDH transportation vehicles. This is clear from the bandwidths specified in the service description which are based on the size of virtual containers used in SDH and PDH transmission and has no bearing on Ethernet. At the time the declaration was made, Ethernet protocols were not widely used in the telecommunications industry and therefore could not have been contemplated as part of the declaration. The declaration itself does not reference an intention to capture all kinds of future transmission technologies.

Should the ACCC decide not to proceed with its proposal to specifically include some Ethernet services, Telstra considers that Ethernet services would remain undeclared.

A.2 There is no bottleneck in the supply of Ethernet services

Telstra submits that there are no barriers to entry relevant to the supply of Ethernet services and therefore no justification for an extension of regulation to cover these services. The ACCC has previously stated that the key barrier to entry affecting competition in transmission markets is the high sunk cost associated with optical fibre deployment.¹ The costs of multiplexing and other electronic equipment have not been considered to create barriers to entry, since unlike the costs of trenching and fibre deployment, the costs of electronic equipment are relatively low and in any event may be recovered

¹ ACCC, *Review of the declaration for the domestic transmission capacity service: Final Report*, April 2004, p30

upon exiting the market and are therefore not sunk.² Indeed, the DTCS exemptions have been granted on the basis of fibre ownership without a requirement for equipment to be installed because the cost of equipment was previously not considered a barrier to entry.

The declaration of SDH and PDH transmission services under the current DTCS service description ensures the supply of data transport services over fibre and copper to access seekers, such that they do not need to incur the sunk costs of cable deployment. Access seekers can and do also use the declared ULLS and SDH transmission services and add equipment to create their own Ethernet over SDH services. Indeed this is exactly how Telstra constructs the CGE service. Telstra converts SDH signals into an Ethernet protocol by placing equipment at both ends having transported the data across the network using Next Generation SDH transmission. Therefore Ethernet services are downstream services of SDH transmission.³

Telstra submits that the cost of conversion of the underlying SDH declared transmission service does not constitute a material barrier to entry for the following reasons:

- 1) the costs are small and in the same order as the costs of electronic equipment used for SDH transmission, which the ACCC did not consider to be a barrier to entry in the context of the DTCS exemptions. Similarly DSLAM costs were not considered to be a barrier to entry for granting of exemptions for resale of fixed line services.
- 2) the equipment costs are similar regardless of whether they are incurred by Telstra or by an access seeker. In many cases the conversion equipment may be cheaper for the access seeker than Telstra, as demonstrated in Telstra's submission to the Discussion Paper.⁴
- 3) in Telstra's experience the equipment costs are declining over time due to increased demand, vendors reducing prices on the older equipment as there is continual innovation in

² The ACCC noted this in its 2004 declaration decision (ACCC, *Review of the declaration for the domestic transmission capacity service: Final Report*, April 2004, p30) and re-stated it in its 2009 decision on Telstra's exemption applications (ACCC, *Telstra's domestic transmission capacity service exemption applications: Final decision*, November 2008 p77)

³ Ethernet over ShDSL is similarly constructed from the declared ULLS plus equipment.

⁴ See also: Telstra, *Response to the ACCC discussion paper reviewing the declaration for the domestic transmission capacity service*, 25 January 2010, section A.2

equipment technology and more favourable exchange rates for importing.

- 4) this equipment is readily available from a number of competing vendors (for example RAD, Ericsson, Alcatel-Lucent and Cisco all offer such equipment).
- 5) Access seekers need to add an equipment box at the customer premise in any case to terminate SDH or Ethernet services. The function of converting signals from SDH to Ethernet can be performed in the equipment at the customer premise with little or no incremental cost to the access seeker by adding a line card, depending on the equipment at the access seekers premises. Some customers prefer to buy the SDH transmission product and do the signal conversion themselves rather than buy CGE.
- 6) Some access seekers use more sophisticated boxes to supply their own Ethernet services in a manner that allows them to manage and control their traffic end to end across their networks, which is necessary for running contended services. In these cases the access seeker will need to add equipment onto the access provider's transmission whether it be SDH or CGE services. The same equipment can also be used to convert SDH to Ethernet services and also allows access seekers to supply into wholesale and retail markets both SDH and Ethernet from a single equipment box. The signal conversion aspect of the equipment, being a line card or a port, is not a driver for the cost of equipment, particularly for high end functionality such as traffic managed using quality of service controls.
- 7) having purchased and installed equipment access seekers can recover the cost of the equipment by leasing out spare capacity by providing ports to other access seekers.
- 8) as the ACCC has previously noted, these costs can be recovered upon exiting the market and are therefore not sunk. Such costs should not be seen as a barrier to market entry.

It is all the more difficult to understand the need to declare Ethernet when the ACCC has previously decided that the cost of the equipment is not a barrier to entry, and the costs of that equipment have not increased, and indeed have fallen, since then.

A.3 There are many competitors offering Ethernet services, demonstrating low barriers to entry

The absence of any significant barriers to entry is evidenced by the competitiveness of supply of Ethernet services. The existence of multiple providers of Ethernet services is evidence that there is no enduring bottleneck and no need for additional regulation of Ethernet.

Competitors may supply Ethernet services through a number of different means, including:

- Deploying their own fibre infrastructure and self-supplying all service elements; or
- Purchasing declared ULLS and declared SDH transmission from Telstra and installing their own Ethernet interface equipment.

One example of a competitor being able to provide such services, largely using their own fibre backhaul network in addition to Telstra's copper is Optus, which offers a number of Ethernet products, including "E-Link". Optus describes E-Link as follows:⁵

"E-Link is Optus' new Ethernet over SDH (EoSDH) leased line networking solution giving carriers and ISPs an easy choice when requiring dedicated and flexible bandwidth options to suit the speed and quality necessary for their networks. E-Link is an ideal highly cost effective scalable access and backbone network solution for carriers building their own IP VPN networks.

E-Link utilises a SDH network more efficiently, minimising expenses for carrier interfaces and the equipment footprint for customers. Speed upgrades are easier and faster for subscribers and there is no need for a field engineer to visit customer sites to increase bandwidth compared with SDH/PDH Access solutions."

Similar Ethernet products are also offered by other competitors, including those listed below. In many instances these competitors would rely on Telstra's declared SDH transmission services supplied over optical fibre and copper including via ULLS as inputs, with the carrier adding the Ethernet conversion equipment:⁶

⁵ Optus E-Link brochure

⁶ For a full review of competitive offerings, refer to Attachment 2 to Telstra's submission to the Discussion Paper (Telstra, *Response to the ACCC discussion paper reviewing the declaration for the domestic transmission capacity service*, 25 January 2010)

- AAPT/Powetel;
- Nextgen Networks;
- TPG-PipeNetworks; and
- AMCOM

In terms of coverage of supply, Ethernet is supplied in different ways in different footprints but is available across the nation. Just as SDH/PDH transmission is available everywhere, so to is the supply of Ethernet by competitors since they can convert SDH and PDH and add their own equipment to create the Ethernet service. Further, Ethernet coverage is available on competitors' fibre networks (where they have deployed fibre and SDH transmission) and Telstra's copper network simply by adding the conversion equipment to their own SDH or ULLS respectively. Lastly Telstra's CGE network is available at Next Generation SDH enabled exchanges.

Telstra's experience in selling CGE is that competition between the above companies and Telstra is vigorous and that there are no existing barriers to such competition. The ability to use the existing declared transmission service and the ULLS as the building block for the Ethernet services ensures this is the case.

Telstra notes that if the DTCS service description was to be varied as proposed by the ACCC, competing wholesale Ethernet offerings would also be subject to regulation.

A.4 Telstra supplies wholesale Ethernet on a commercial basis – there is no refusal to supply

Wholesale Ethernet services are widely supplied today on a commercially competitive and unregulated basis. Parties are able to agree commercially on the terms on which services are supplied and are constrained by competitive market forces in doing so.

For example, wholesale CGE has been supplied by Telstra since October 2008 and take-up has grown strongly since launch.⁷ Similar products are also supplied by Telstra's competitors such as Optus and AAPT.⁸

⁷ Information on Telstra's wholesale CGE product is available on its website:
<http://telstrawholesale.com/products/data/wholesale-carrier-grade-ethernet.htm>

⁸ <http://www.aapt.com.au/services/carriers-service-providers/products/ethernet>

In proposing to intervene, the ACCC is acting on a misconceived apprehension of refusal to supply. Its only reference in the Draft Final Report to market failure in the supply of Ethernet is an indirect one arising from the submissions of Optus and Macquarie Telecom alleging refusal to supply Ethernet services by Telstra.⁹

Telstra is not aware of any instances of refusal to supply Ethernet services in areas enabled for the provision of such services. Moreover, commercial supply of Ethernet is available in the increments that address the concerns raised by the ACCC in the Draft Final Report.

Telstra has, on occasions, been unable to meet requests from access seekers in particular areas because the relevant exchange locations were not enabled for the supply of the Ethernet services being requested. However this is not a refusal to supply - rather the inability to supply particular products in certain circumstances. It is important to note that in these instances Telstra does not supply the service to itself.

Telstra believes there is no basis for such accusations by Optus and Macquarie. No evidence has been provided to support these claims, nor has any dispute been raised and therefore Telstra has not been provided with an opportunity to rebut these allegations. Telstra therefore submits that the ACCC can place no weight on these untested claims in its Final Decision, for to do so would deny Telstra a reasonable opportunity to be heard on these issues.

Declaration would not compel the supply of Ethernet in areas where it is currently unavailable. Telstra strongly supports the position taken by the ACCC in its Draft Final Report that declaration would only require Telstra to provide access where it provides the service to others within a particular ESA.¹⁰ This implies that where Telstra has not enabled exchange locations for Ethernet services, declaration would not impact on the availability of such services.

Given the widespread commercial supply of wholesale Ethernet, no evidence of any refusal to supply, and no impact on supply resulting from declaration, Telstra submits there is no need for regulatory intervention in Ethernet.

⁹ Draft Final Decision, p24

¹⁰ Draft Final Decision, p2

B There has been no proper analysis of the LTIE

B.1 The ACCC has not compared the likely states of competition with and without the declaration of Ethernet

Before making a variation to the DTCS declaration, the ACCC must be satisfied that such a variation is in the LTIE.

In applying the LTIE test, the ACCC has previously considered it useful to examine the current and likely future states of competition on a “with and without” basis:¹¹

“The ACCC considers that in applying the LTIE test, it is useful to consider the likely state of competition in the future both with declaration and without declaration. Reviewing the state of competition as it currently stands will assist in applying the future with and without test.”

The ACCC has also previously stated that declaration under Part XIC should focus on those elements of the fixed-line network which represent “enduring bottlenecks”. The ACCC defines an enduring bottleneck in the following way:¹²

“... an enduring bottleneck is defined to mean a network element or facility that exhibits natural monopoly characteristics and is ‘essential’ to being able to provide services to end-users in downstream markets in a way that promotes the long-term interests of end-users (LTIE). That is, duplication of the network element would result in a loss of technical and allocative efficiency greater than any competitive gains that duplication might achieve.”

In the present case however, the ACCC has not adequately applied the “with and without” test, and as explained above, has not identified any enduring bottlenecks at which to target the variation.

In assessing the impact of the proposed variation on competition, the ACCC refers to the analysis undertaken in its 2009 declaration inquiry and states that the variation would not change this analysis.¹³ While it is true that the ACCC must be satisfied that the

¹¹ ACCC, *Fixed Services Review Declaration Inquiry for the ULLS, LSS, PSTN OA, PSTN TA, LCS and WLR: Final Decision*, July 2009 p11

¹² ACCC, *Fixed Services Review Declaration Inquiry for the ULLS, LSS, PSTN OA, PSTN TA, LCS and WLR: Final Decision*, July 2009 p10

¹³ Draft Final Decision, p23

declaration is in the LTIE, the ACCC must also consider whether the *variation* would promote the LTIE.¹⁴

This requires the ACCC to do more than just re-state its previous market analysis from the 2009 re-declaration. Nor can it reasonably proceed from a re-statement of earlier analysis to an assumption that if the declaration was in the LTIE, then the declaration of even more technologies and services would also promote the LTIE. Rather, the ACCC must consider whether there is any unregulated bottleneck that is not addressed by the existing declaration, and that would be addressed by the proposed declaration, in the LTIE. For the reasons set out in Section A, there is no bottleneck for Ethernet services and the LTIE would not be advanced by declaring Ethernet.

B.2 The ACCC must undertake a proper analysis of the relevant markets

The ACCC has not presented any analysis of the relevant markets in order to test whether competition and the LTIE would be promoted by the proposed variation compared to competition if there was no variation.

As noted above, the ACCC only refers to the competition analysis undertaken in its 2009 declaration inquiry and states that the variation would not change the relevant markets.¹⁵ The 2009 analysis referred to by the ACCC was directed to the question of whether it was in the LTIE to re-declare DTCS as it is presently defined.

However, in this inquiry, the ACCC must test the critical question of whether the proposed variation promotes the LTIE. The “particular thing” being tested for its LTIE impact under s 152AB(2) is the variation, because s 33(3) of the Acts Interpretation Act requires the ACCC to exercise its power in a “like manner” and “subject to like conditions”.

Merely asking whether the declaration (as varied, in its totality) is in the LTIE is not sufficient. If that alone were the test of a variation,

¹⁴ Section 33(3) of the *Acts Interpretation Act* 1901 (Cth) provides that where an Act confers a power to make an instrument, the power shall, unless the contrary intention appears, be construed as including a power exercisable in the like manner and subject to the like conditions (if any) to vary any such instrument. This implies that the power in section 152AL(3) of the TPA to make an instrument declaring a service is to be construed as including a power to make variations. However, the implied power to make variations must be exercised “in a like manner” and “subject to like conditions” under section 33(3) of the *Acts Interpretation Act*. This means that in making a variation to a declaration, the ACCC must be satisfied that doing so will promote the LTIE.

¹⁵ Draft Final Decision, p23

then a varied declaration that is less in the LTIE than the original declaration– yet still more in the LTIE than no declaration at all – would pass such a test, an outcome that would clearly be contrary to the objects of Part XIC.

Whether the variation would promote the LTIE requires consideration of whether proposed further regulation (including the geographic reach of that extended regulation) would promote competition in relevant markets by relieving any upstream bottlenecks. As noted in Telstra’s submission to the Discussion Paper, overseas regulators such as Ofcom have undertaken thorough market inquiries prior to extending regulation to new technologies.¹⁶

Yet the ACCC has not identified any relevant bottlenecks in the supply of Ethernet services, nor considered the state of competition for the supply of such services. Telstra submits that the variation cannot be reasonably made in the absence of this analysis.

B.3 There are no evident “obstacles” to access or threats to continuity of Ethernet supply

The Draft Final Decision states that “obstacles” of access to Ethernet services would be removed by extending the DTCS declaration to include Ethernet.¹⁷

However it is not clear what these obstacles to Ethernet access are, since Telstra makes CGE commercially available wherever the network is enabled and capacity exists. At no point in the Draft Final Decision does the ACCC raise concerns that there is a bottleneck in the conversion of currently declared transmission services into Ethernet services.

The ACCC states that it wants to ensure continued supply of the DTCS, in light of the benefits of declaration set out in its 2009 decision.¹⁸ However there is no present or anticipated threat to continuity of supply of DTCS, and the declaration of Ethernet is not required for the reason of continuity of supply.

Given this, and the widespread commercial supply of Ethernet-services by a range of competitors, it is difficult to see how further

¹⁶ Telstra, *Response to the ACCC discussion paper reviewing the declaration for the domestic transmission capacity service*, 25 January 2010, p26

¹⁷ Draft Final Decision, p23

¹⁸ Draft Final Decision, p23

regulation could promote the LTIE. In particular, the ACCC has not tested how competition would be more robust than it already is in a world with increased regulation.

B.4 The ACCC must have regard to the current state of competition

The ACCC has recently noted the importance of current competition in the relevant markets in determining whether declaration is in the LTIE:¹⁹

“Reviewing the state of competition as it currently stands will assist in applying the future with and without test.”

In this inquiry, where an expansion of the declaration to include Ethernet (and other network interfaces) is being considered, the ACCC must specifically consider the state of competition for the supply of Ethernet services.

It is not sufficient for the ACCC to simply affirm its analysis of barriers to entry in the supply of transmission services generally. Rather the ACCC is required to consider whether the expansion of the declaration to include Ethernet interface protocols (and other protocols) is appropriate, given the state of competition in the supply of Ethernet services.

Compelling evidence before the ACCC points to a conclusion that competition is currently effective and that there is no need for an extension of regulation. This evidence includes, amongst other things:

- Information on the scale and scope of competitive supply and the nature of competitive offerings;²⁰ and
- Information demonstrating that the costs of Ethernet conversion are relatively low for access seekers and do not pose a significant barrier to competition.²¹

In light of this, and in the absence of any substantiated evidence to the contrary, there is no justification to the claim that competition is ineffective and that further regulation is required.

¹⁹ ACCC, *Fixed Services Review Declaration Inquiry for the ULLS, LSS, PSTN OA, PSTN TA, LCS and WLR: Final Decision*, July 2009, p11

²⁰ Refer to section A.3 above and Telstra's submission to the Discussion Paper

²¹ Refer to Telstra's submission to the Discussion Paper, and in particular the analysis of Ethernet conversion costs for Telstra and access seekers: Telstra, *Response to the ACCC discussion paper reviewing the declaration for the domestic transmission capacity service*, 25 January 2010, pp7-9

B.5 “Technology neutrality” is not a justification for expanded regulation

In the Draft Final Report, the ACCC states its view that the DTCS should be varied so that it covers all commonly used interface protocols. The ACCC states that the intention behind the DTCS service description is that it be technology neutral and that in order to achieve technology neutrality, it is necessary to include Ethernet interface protocols in the service description.²²

Telstra is unaware of any evidence to suggest that the DTCS was intended to be technology neutral. In the Draft Final Report the ACCC refers to its decision in 1997 to declare the DTCS and other services, however this decision does not appear to make reference to technological neutrality.²³ In fact in the same decision (and in later decisions) the ACCC has defined a number of services in a technology-specific way, such as ULLS, which is necessarily copper based.²⁴

In any event, technology neutrality is not an end in itself, but a means of limiting regulatory distortions of market outcomes. The policy intent is to ensure that regulation should not “pick winners” but as far as possible let markets decide which technologies should succeed or fail. It does not mean that because one technology is regulated, other technologies should be identically regulated – without analysis of the various markets in which they are offered, or the impacts upon those markets.

Reliance on technology neutrality does not obviate the need to follow basic regulatory principles when determining whether regulation should be applied. The market analysis expected to be undertaken by a regulator prior to deciding to declare a new service involves:

- identifying the market failure which is sought to be addressed including appropriate consideration of the state of competition and any relevant substitute services; and
- ensuring that the regulation applied is proportionate to the extent of the failure by applying regulation only so far as is necessary to address that failure.

²² Draft Final Report, p2

²³ On p2 of the Draft Final Report, the ACCC refers to the 1997 decision to deem certain services (including transmission): ACCC, *Deeming of Telecommunications Services: a statement pursuant to section 39 of the Telecommunications (Transitional Provisions and Consequential Amendments) Act 1997*, June 1997

²⁴ For example, the conditioned local loop service and the unconditioned local loop service are highly technology-specific

The ACCC appears, in its Draft Final Report, to automatically accept the proposition that technology neutrality is in the LTIE, without testing the elements that make up that statutory test.

Technology neutrality may in fact be contrary to the LTIE where technologies are particularly dynamic and there is the potential for ongoing innovation. In this situation, a technologically neutral approach to regulation is likely to stifle innovation since it implies a promise that any new technology will be automatically subject to regulation immediately upon its introduction into the market. The prospect of immediate and certain regulation will asymmetrically truncate expected returns on investment (ie regulation will truncate the upside but not the downside risk of investment) and therefore lead to inefficiently low levels of investment in new technologies.

B.6 The ACCC has not properly considered the risk of harm from unnecessary regulatory intervention

Telstra submits that the ACCC has failed to properly consider the risks of regulatory over-reach. In particular, the ACCC does not appear to address the impact of regulation on investment incentives and the efficient use of transmission infrastructure.

The ACCC considers that its decision will provide incentives for more efficient use of and investment in infrastructure. The ACCC notes the efficiency properties of Ethernet technology and concludes that extending the declaration to include such technologies would therefore promote the LTIE.²⁵ However Telstra submits that regulation of this technology would not necessarily promote the LTIE. As noted above, access seekers are already able to self-supply Ethernet services, often at lower cost than Telstra, and there is widespread commercial supply by a number of carriers. Therefore it is difficult to see how regulation would in any way promote more efficient use of Ethernet interfaces, or transmission infrastructure more generally.

Moreover there is a significant risk that regulation of competitively supplied services like CGE and SDH transmission in competitive locations would damage incentives for efficient use of and investment in infrastructure. Submissions made in the exemption processes elaborate on the risks to investment that can occur when competitive services are regulated. For example, threat of price regulation will limit investment in infrastructure to deliver the

²⁵ Draft Final Decision, p27

regulated services and stimulate investment in infrastructure for substitute services, depending on the relative size of the gap between expected regulated price and costs across the services.

There is a further risk of regulatory error resulting from regulating multiple layers of the supply chain that this variation would do. The risk is that an error in one price will distort prices across downstream and substitute services, and/or sustain arbitrage opportunities. For instance ULLS is used to provide SDH over copper (ShDSL) which is then used to supply Ethernet over ShDSL. An erroneously low regulated ULLS price, would lead to an erroneously low price for ShDSL and EoShDSL. This would encourage over-utilisation and investment in copper relative to an efficient outcome from the correct regulatory price. Similarly in fibre, a low SDH backhaul price would flow through to regulated price of CGE, encouraging over-investment in fibre and conversion equipment compared to alternatives like microwave.

In short, double regulation is likely to result in inefficient pricing signals for builders and buyers of technology resulting in either insufficient investment or inefficient and excessive investment, compared to a competitive outcome.

This risk of harm is particularly significant in light of the ACCC's proposal to regulate unspecified interfaces (in addition to Ethernet), as explained further in the next section.

C Telstra supports those elements of the variation that give greater clarity

C.1 Use of the words Ethernet over SDH

For the reasons set out in sections A and B, Telstra considers that any expansion of the DTCS declaration would not be in the LTIE. However if the ACCC disagrees and considers variation to be in the LTIE, then Telstra submits that the variation should be carefully targeted and unambiguous. This would be consistent with the previous approach to defining the DTCS, which was targeted specifically at SDH and PDH transmission technologies.

The ACCC has indicated in industry discussions that it intends to regulate no more than the Ethernet interface and does not intend to expand the service description to capture a raft of new services. To achieve this objective, Telstra previously recommended identifying the Ethernet technology more directly in the service description rather than simply referring to the characteristics the technology displays. Telstra submits that the ACCC's objectives would be better met if Ethernet over SDH were specifically identified in the service description. Doing so would create the greatest level of certainty about the Ethernet technology that the ACCC intends to regulate. Anything else creates opportunities for misinterpretation and potential disagreement across industry stakeholders about what is declared.

C.2 Telstra supports use of the words “uncontended” and “symmetric”

Telstra agrees with the ACCC that the service description should be as unambiguous as possible. This will promote certainty for both access providers and access seekers.

If the ACCC decides to regulate Ethernet and decides not to name the Ethernet over SDH technology, then the next best approach is to identify the Ethernet over SDH technology by using the words “permanent”, “uncontended” and “symmetric” in the service description. Together with the important concept of permanence, these words improve clarity of what is intended to be regulated under the DTCS.

Omitting the terms “uncontended” and “symmetric” will result in uncertainty over regulation of services that serve quite different markets, are used for different purposes and which are sold under very different contractual arrangements.

It is critical that the ACCC proceeds with the inclusion of these terms in order to provide some certainty as to the scope of declaration. Telstra would strongly object if these words were removed as this would introduce significant ambiguity around the scope of declaration and likely go beyond the ACCCs intention not to declare a range of new services.

C.3 The definition of “network interface” should be exhaustive not inclusive

Telstra submits that the open-ended definition of “network interfaces” in the service description does not promote certainty as it is inclusive, rather than being exhaustive.

The definition states that it “includes” Ethernet, PDH and SDH interface protocols. However this creates uncertainty as to whether other interface protocols may also be included, either now or in future.

There are currently a number of different interface protocols (other than those listed by the ACCC) that are being used by carriers and which could potentially be unintentionally regulated by this inclusive form of the service description. For example, services going into data centres use different interface protocols which are not listed in the service description, but which could be captured by an inclusive definition.

Beyond those currently being used, the inclusive definition could also capture new interface protocols that are yet to be developed. Thus, new interface protocols could potentially be regulated under the inclusive definition, without any analysis of the markets they serve and the state of competition. This would place at risk investment in new technologies which would otherwise deliver significant efficiency gains to the industry in the LTIE.

For the reasons set out earlier in this submission, Telstra believes that the DTCS should not cover Ethernet interface protocols. However, if the ACCC is minded to include Ethernet as well as PDH and SDH interface protocols, it should define “network interfaces” to only include these three. This would offer access providers and access seekers some certainty as to which interfaces are covered by the declaration, and which are not.

An alternative definition could read:

“network interfaces are Ethernet, Plesiochronous Digital Hierarchy (PDH) and Synchronous Digital Hierarchy (SDH) interface protocols used to provide a transmission rate of 2.048 Megabits per second or above which an access provider provides to itself or others”

C.4 Competitors' Ethernet networks will be regulated if the service description is varied as proposed

Telstra notes that the proposed variation to the DTCS service description is a broad regulatory brush that would lead to regulation of competitors' Ethernet services as well as those provided by Telstra.

Access seekers that deliver Ethernet services that are point to point, uncontended, symmetric and permanent transport services will face regulation of those services. It will not be relevant whether access seekers use their own infrastructure or purchase services over Telstra's copper or fibre networks such as ULLS or SDH transmission services. Nor will it be relevant whether their underlying service purchased from Telstra is already regulated under the ULLS or DTCS declarations.

Thus DTCS regulation could apply to both Ethernet services supplied by access seekers and the underlying ULLS and SDH inputs for the Ethernet services that are already supplied by Telstra and others.

D The ACCC has not adequately addressed the geographic scope of exemption

D.1 Roll-back of declaration is required to avoid harming the LTIE

The Draft Final Decision fails to adequately address the geographic aspect of the DTCS declaration and would therefore result in a declaration that is not in the LTIE, if implemented by the ACCC. If the geographic aspect of declaration is not properly addressed, regulation will potentially apply in locations where competition is already effective, thus potentially harming the LTIE.

Although some exemptions from regulation were granted in 2009, these are only a subset of the locations that now meet the ACCC exemption criteria. Following the ACCC's own reasoning in that earlier process, it would promote the LTIE to further reduce the geographic scope of regulation, based on the same competition thresholds. Concluding the current variation process without addressing the deficiencies in the geographic scope of declaration would not be in the LTIE.

The ACCC has previously noted the imperative to closely monitor market developments and update the geographic scope of declaration as appropriate. In its 2009 decision to re-declare the DTCS the ACCC noted:²⁶

"The Commission is aware that the DTCS is a multi-dimensional and dynamic service. During the course of the 5 year declaration changes in market structure and the substitutability of alternative technologies may affect the state of competition in one or more product or geographic markets. To ensure that declaration keeps pace with market developments, and continues to underpin the promotion of the LTIE, the statutory framework provides the necessary flexibility to respond to changes in circumstances including through granting exemptions to the SAOs or varying the scope of a declared service through a further inquiry."

Telstra agrees with this statement and considers that it is critical that the scope of regulation be able to keep pace with market developments. To the extent that regulation does not appropriately reflect the reach of competition, it will not promote the LTIE. Continuing to apply regulation where competition has emerged is likely to distort market outcomes.

²⁶ ACCC, *Final Report on reviewing the declaration of the domestic transmission capacity service*, March 2009, p33

The ACCC has also recognised that regulation in the face of competition can be detrimental to incentives for investment:²⁷

“[DTCS] access must be balanced against providing the correct incentives for efficient investment in the market to ensure the long-term interests of end users are also addressed. To achieve this, the Commission will remain attentive to developments in the market and assess any potentially competitive services with a view of rolling back regulation where it is found to be in the LTIE.”

Elsewhere, the ACCC has recognised that competition develops unevenly across different geographic regions, and future regulatory decisions should be based on robust geographically delineated empirical data.²⁸

The current variation inquiry represents the best opportunity to adjust the geographic scope of declaration to reflect the state of competition. Making this adjustment through the current inquiry process will avoid additional imposts on industry of engaging in a further inquiry around the geographic scope of regulation. A second variation so soon after this variation would unnecessarily consume further industry time and effort

D.2 The geographic scope of the declaration is too broad

The geographic exemptions for the DTCS were granted in 2008, based on information collected in the period prior to lodgement in 2007. The exemptions were granted for routes and ESAs in respect of which Telstra had applied for exemption and on which the ACCC's RKR data showed that there were at least two fibre owners in addition to Telstra.²⁹

However, Telstra believes that:

- The geographic exemptions granted in 2008 covered some but not all of the transmission routes and ESAs in which there are two competitors in addition to Telstra at that time.³⁰ Telstra now knows of many other ESAs in which there were

²⁷ See ACCC, *Final Report on reviewing the declaration of the domestic transmission capacity service*, March 2009, p27

²⁸ See ACCC, *Infrastructure Record-Keeping Rule 2007, Regulation Impact Statement*, December 2007 at pp 6-7

²⁹ ACCC, *Telstra's domestic transmission capacity service exemption applications: Final decision*, November 2008

³⁰ In its submission in support of the December 2007 exemption applications, Telstra noted that the proposed scope of exemption was conservative as it was constrained by the amount of market intelligence that could be gathered at the time (Telstra, *Submission to the Australian Competition and Consumer Commission: Telstra's Domestic Transmission Capacity Service Exemption Applications*, 21 December 2007, p9)

and continue to be two or more fibre owners, particularly in NSW and Victoria.

- New investment has occurred since the time that the exemption was prepared and lodged in 2007, with the result that a significant number of additional routes are now contested by three players (including Telstra).
- To the extent that the service description is varied to include Ethernet, the ACCC must consider the geographic footprint of competition for Ethernet services, which will be different to that for SDH transmission.
- Advances in alternative transmission technologies since 2007 mean that competition is now more intense on many routes still subject to declaration. In particular, microwave technology has evolved to such a point that it would be prudent for the ACCC to reconsider the substitutability of microwave transmission and the number of microwave owners in particular ESAs and on particular routes.
- The introduction of Government-funded competitors (including subsidised deployment of new fibre) on many routes since 2007 has further increased the competitive constraints on Telstra. This includes TasNBNC Co, NBNC Co and NextGen as part of the backhaul blackspots programme.
- Telstra also considers that long-term leases should be considered equivalent to fibre build for exemption purposes.

There are a number of possible competition thresholds that would correct the deficiencies in the current scope of declaration, as set out in the table below. Telstra recommends the competition effects of these alternate thresholds should be investigated by the ACCC.

Competition threshold	Data Sources
Telstra fibre plus 2 optical fibre owners	RKR data
Telstra fibre plus 1 optical fibre owner plus 1 microwave owner	RKR data
Telstra fibre plus 2 Ethernet suppliers	Readily available from Websites
Telstra plus 1 government	Readily available from Websites

subsidised fibre investor	and NBNCo roll-out plans when available
3 suppliers of Ethernet over SDH	Readily available from Websites

Telstra believes there are a significant number of routes still subject to declaration (and which would be subject to declaration if the service description is varied) on which it has two or more fibre infrastructure competitors – this is even before alternative infrastructure such as microwave and routes upon which third parties have long-term leases or rights to use transmission infrastructure are taken into account. However Telstra is constrained to some extent in that it does not have access to the RKR data which would confirm which routes meet the ACCC's exemption threshold. Only the ACCC has access to this data and can make such an assessment.

D.3 The ACCC has actual knowledge of the routes that have two or more competitors to Telstra

The party best informed to assess the number of fibre-based competitors under the ACCC's exemption threshold is the ACCC itself. It has - via the Infrastructure RKR - actual knowledge of fibre infrastructure in core and access networks owned and operated by carriers in Australia.

Telstra submits it is not reasonable for the ACCC to find that the geographic scope of the declaration is adequately dealt with merely by incorporating the 2008 exemption. The ACCC possesses evidence to the contrary; and based on actual knowledge that it holds, is in a position to precisely determine the extent of the routes and ESAs that would meet the exemption threshold. To decide the variation is correct without updating the exemptions would be obfuscation of the ACCC's statutory obligations in relation to declarations and variations.

Before the ACCC can vary or expand the service description, it must use the available evidence to assessment the appropriate geographic scope of the service description variation. The ACCC cannot be satisfied that the variation is in the LTIE without considering the geographic scope to which the varied declaration would apply.

The ACCC has previously used RKR data to grant exemptions for the DTCS and LCS/WLR and PSTN OA. Similarly the Australian Competition Tribunal has used similar RKR data to determine the appropriate conditions in upholding the ACCC decision to grant the LCS and PSTN OA exemptions.³¹

Indeed, the Infrastructure RKR was introduced in order to support the ACCC's ability to make appropriately targeted and timely regulatory decisions focussed on enduring bottlenecks. The objective was to use the data to inform its "ongoing and recurring function" of administering Part XIC – including declaring, not declaring or exempting services from declaration in the LTIE. If the data cannot be used for the purpose of updating the DTCS declaration to reflect the current state of competition, then questions should be asked about what purpose the RKR serves.

Although industry has raised some concerns with the release of granular RKR information, there is general agreement that this information could be used in an aggregated and non-identifying way.³² The ACCC has also previously noted that where there are confidentiality concerns, data may be released at a more aggregated level.³³ In updating the list of competitive routes to be carved out of the service declaration, no other carrier would need to be identified, nor would any particular carrier's information be made public, so there can be no confidentiality concerns.

D.4 Including Ethernet is likely to affect the appropriate geographic scope of declaration

Competitors can purchase SDH transmission over long distances, or for shorter distances bond several ULLS together and add equipment to convert the SDH service to Ethernet. Constructing an Ethernet service using Telstra or another carrier's infrastructure allows for greater Ethernet coverage by our competitors than Telstra has. By installing their own equipment to supply an Ethernet service, access seekers can supply Ethernet wherever they wish.

³¹ *Application by Chime (No 3) [2009] ACompT 4*

³² For example, refer to: Competitive Carriers Coalition, *Comments in Response to Review of Record Keeping Rules*, June 2010, p2; Optus, *Submission to Australian Competition and Consumer Commission on Disclosure of Telecommunications Infrastructure Data*, June 2010, paragraph 3.23; Telstra, *Disclosure of telecommunications infrastructure data: Response to ACCC Discussion Paper on disclosure of Data collected under the Infrastructure Record Keeping Rule 2007*, June 2010, p2

³³ ACCC, *Regulatory Principles for Public Disclosure of Record-Keeping Rule Information*, January 2003, Section 4.4.1

Due to the ease of converting SDH transmission to Ethernet, the number of competitors supplying Ethernet is actually much larger than the number of competitors owning fibre, which was the basis of exemptions for SDH. The exemptions that already apply for SDH and PDH transmission will be insufficient if Ethernet is included in the service description as there are many more locations than listed in the current exemptions where Ethernet is supplied by more than two non-Telstra competitors.

It is therefore incumbent upon the ACCC to consider the impact of variation on the geographic reach of competition and update the scope of declaration accordingly. Failure to properly consider this interaction between the product scope and geographic scope of exemption will result in a declaration that is not in the LTIE.

Telstra believes it is imperative that the ACCC update the geographic scope of the current DTCS service description, prior to finalising this current consultation on the variation of the DTCS service description.

D.5 The service description could incorporate a mechanism which allows for periodic updates of the geographic scope

The ACCC could also issue a service description that refers to a list published periodically by the ACCC. In this way, the ACCC could ensure that the scope of declaration keeps pace with the development of competition, and thus continues to promote the LTIE.

The mechanism adopted by the Australian Competition Tribunal – essentially “standing in the shoes” of the ACCC - in the WLR decision (remitted by the Full Federal Court), illustrates how this may be done.³⁴ In that matter, rollback of regulation was contingent on calculations made and published by the ACCC regarding the extent of competition in a particular exchange area, based on RKR information (among other potential sources). In the DTCS, the calculation would be, if anything, even simpler and more certain, because it could be done on RKR information alone.

³⁴ *Application by Chime (No 3) [2009] ACompT 4*

The ACCC must be satisfied that the LTIE will be promoted if the service description is varied, both in respect of the product dimension and the geographic dimension. Telstra believes that the best means for it to be so satisfied in respect of the geographic dimension would be to vary the terms of the declared service to incorporate such a mechanism.

By this means, once a route was listed on the ACCC's website as a competitive route, it would "automatically" be removed from the scope of the declared service – thus reflecting emerging competition in a timely and effective manner. Periodic updating of the declaration would promote the LTIE, since it would allow regulation to keep pace with market developments. Telstra submits that this is particularly important in a highly dynamic market such as the market for transmission services.

Telstra also believes it is highly desirable for the ACCC to establish a mechanism for periodic updates of the current DTCS service description as soon as possible.

E Conclusion

Telstra considers that there is no reason for the ACCC to extend regulation to Ethernet since there are no barriers to supply and Ethernet is already competitively supplied nationally. Under these circumstances, Telstra submits that regulation of Ethernet would in fact harm the LTIE.

There is no bottleneck or market failure that would be relieved by the proposed variation. Telstra, and others, already supply wholesale Ethernet on a commercial basis, and Telstra does not believe that the unsupported assertions of its competitors implying refusal to supply have any foundation in fact.

Nor has the ACCC properly tested whether the LTIE would be promoted by the proposed variation, such as by analysing the impact of the variation in relevant markets on a 'with or without' basis.

Nevertheless, if the ACCC is minded to extend regulation in this way, Telstra would support a service description which provides certainty for access providers and access seekers. Telstra considers that the greatest level of certainty is achieved by naming in the service description Ethernet over SDH technology. However, if the ACCC has concerns about naming the technology, Telstra supports the use of the words "permanent", "uncontended" and "symmetric" in the proposed service description. Telstra also considers that definition of "network interface" should be amended to remove the word "including", in order to provide certainty as to the future scope of regulation and to preserve incentives to invest in new technologies and interfaces that may well deliver large efficiency gains in future.

Finally, Telstra submits that the ACCC must revisit the geographic scope of declaration prior to finalising its variation inquiry. There is evidence before the ACCC which demonstrates that the current geographic scope of declaration is too broad. Failure to properly consider this evidence and instead adopt an over-reaching service description will result in a declaration that does not promote the LTIE.