

# AAPT Submission

## Implementation of GSM Pricing Principles

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### 1 Overview

- 1 AAPT welcomes the opportunity to comment on the Commission's discussion paper of 15 August 2001 regarding the implementation of GSM pricing principles (**Discussion Paper**).
- 2 Overall, AAPT considers that many of the issues raised in the Discussion Paper are likely to be difficult to resolve satisfactorily because they are the result of a fundamental weakness in the Commission's analysis of pricing the GSM service: that is, the failure to distinguish between the retail and wholesale mobile markets. The use of an historic retail price measure to determine future wholesale charges will suffer from at least the following problems of principle and implementation:
  - (a) it is unlikely to provide useful guidance to commercial negotiations because of the backward-looking nature of the glide path process;
  - (b) it will entrench monopoly rents in wholesale prices, which was identified by the Commission's economic consultants; and
  - (c) it creates opportunities for regulatory gaming by mobile carriers to restructure revenue;
  - (d) it is likely to be distorted because of the difficulty of separating revenues from network facilities and "ancillary revenues" such as content provision over SMS services;
  - (e) it will require onerous and intrusive information collection processes which will result in significant implementation lags.
- 3 In AAPT's view, the basic flaw in the Commission's pricing principles renders the approach so economically unsound that the issues of detail raised in the Discussion Paper will do little, if anything, to preserve the long-term interests of end-users.
- 4 Notwithstanding these reservations about the pricing principles, AAPT makes the following submissions in response to the Discussion Paper.

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### 2 Date of the initial starting point

<b>Is 1 July 2001 considered an appropriate date from which the lowest price should be taken? If not, what would be a preferred date and why?</b>
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- 5 AAPT considers that 1 July 2001 would be an appropriate starting date.
- 6 However, AAPT believes the Commission should first resolve the currently notified disputes, then use the price applying at 1 July 2001 for future disputes.
- 7 The Commission has not addressed the issue of how it will approach backdating in the disputes. The need for a reasonable outcome on backdating is particularly acute in these matters as the public consultation on pricing principles has now

taken over 18 months, during which time no steps have been take to progress the arbitrations. A failure by the Commission to address backdating would result in there being an unregulated price for the declared service during this period, which would clearly contradict the intent of Part XIC. AAPT therefore requests that the Commission indicate in its next discussion of the implementation of pricing principles how it proposes to address backdating.

- 8 If reliable information is available as to the lowest negotiated access price, AAPT submits that the Commission should apply the glide path methodology to that price. If that is not the case, AAPT submits that the only sensible approach would be to apply the July 2001 starting price back to the dates of notification.
- 9 AAPT also notes that the Commission includes a comment in footnote 2 that the lowest access price should be “‘normal’ or representative (ie, without any special conditions attached)”. It is not clear what the Commission intends by this comment and AAPT seeks clarification of what is meant by “special conditions” and how the Commission intends to apply the definition.

**Under a period-on-period approach is it considered appropriate that the starting price for any potential access disputes notified in the future should be the most recent access price agreed between the access seeker and the access provider? If not, what should the starting price be and why?**

- 10 AAPT does not consider it appropriate to reset the starting price for each new access dispute.
- 11 The Commission notes at page 60 of its final report *Pricing Methodology for the GSM Termination Service (Final Report)* that “it would be preferable for the glide path to start from the lowest access price currently *in the market*” [emphasis added]. Under the approach suggested in the Discussion Paper, the Commission appears to be suggesting an approach that would use the current access price between the particular access seeker and provider as the starting point. For the reasons outlined in the Final Report (essentially, that this would reward access providers who refuse to negotiate) AAPT considers that the starting price for new disputes should be the existing access price which has resulted from the application of the glide path from the July 2001 price.

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### 3 Time period for assessing retail price movements

**Is a six monthly basis considered an appropriate timeframe for determining retail price movements and in particular the calendar six month periods 1 January to 30 June and 1 July to 31 December? Will mobile carriers who do not report on the traditional financial year basis of 1 July to 30 June, such as Cable & Wireless Optus and Vodafone, be able to provide information over these timeframes? If not, what would be a preferred basis and why?**

- 12 AAPT has some concerns that a six month period may, in practice, prove too long for determining the glide path.
- 13 It will be necessary to allow a period of some time at the conclusion of each six month period for collection of data and calculation of the glide path ‘deflater’. The result is likely to be a significant lag beyond the end of the six month period.

As a result, that deflator will not be able to be applied until some time after the six month period with the result that backdating payments may be necessary. In AAPT's view, it is likely that the accounting lag created would result in the information being effectively one year behind. Ideally, therefore accounting should be conducted on a quarterly basis and, taking into account the accounting lag, this would be more likely to result in the glide path being six months behind the current price.

- 14 As discussed further below, AAPT suggests that the current record keeping rules (**RKRs**) should be used as the basis for establishing the glide path and, as these require records to be submitted every six months, we consider this to be the appropriate basis on which to collect information.
- 15 AAPT does not consider carriers' reporting obligations in other contexts to be relevant.

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#### 4 How to determine average price per minute and retail price movements

**Is a yield methodology considered to be an appropriate methodology for calculating retail price difference? If not, is a "retail basket" type approach similar to that adopted by the CRU likely to be a more appropriate methodology and if so, why? Is there another, more appropriate, approach detailed by the Commission and, if so, what is that approach?**

- 16 Overall, AAPT considers that the yield approach is the only methodology which could be practically applied.
- 17 In addition to the reasons given by the Commission, AAPT notes that the current RKRs require carriers to provide line items for revenues in respect of "GSM Mobiles" which are described as "provision of services, including access, originating on GSM networks". This is the same information which the Commission suggests is required in the Discussion Paper (with the addition of SMS and value-added services).

**Under the yield methodology, is a revenue per minute approach considered to be an appropriate proxy for average price? If not, is a revenue per subscriber approach considered to be a more appropriate proxy and, if so, why?**

- 18 The appropriate basis for averaging retail costs is per minute, rather than per user.
- 19 The Commission should use as close a proxy to the regulated wholesale services as possible. The service which access seekers acquire from the mobile networks is a per minute usage charge and, therefore, the retail benchmark which should be used for determining the glide path should also be a per minute charge.

#### 4.1 Services for inclusion under a yield approach

**Are the proposed services for inclusion in the revenue calculations and minutes of use considered appropriate? If not, why not, and what would be the preferred approach?**

- 20 AAPT submits that the appropriate services for inclusion under a yield approach are those which are outgoing voice services. As noted above in regard to call minutes, the Commission's task is to arrive at a service which, although retail, most closely reflects the equivalent to the wholesale access service but at the retail level. The services which the ACCC suggests should be included are as follows:
- outgoing calls;
  - access fees;
  - handset charges (if any);
  - connection fees (if any); and
  - voicemail charges.
- 21 AAPT does not consider it appropriate to include SMS services in calculating the yield. These services are not measured on a time basis and, more importantly, are not supplied using the same network elements as voice services. SMS messaging is delivered using the signalling network associated with a GSM mobile network and the traffic can be stored and forwarded rather than requiring a voice circuit to be held. As such, the basis on which these services are efficiently priced is unrelated to efficient pricing of the wholesale services under consideration.
- 22 Additionally, charges for these services increasingly include a content element which results in the charges that do not reflect the cost of providing the underlying carriage service. As an example, Telstra's "Who Wants to be a Millionaire" SMS-based game requires a GSM user to answer a series of questions via SMS at a charge of 30¢ (rather than the usual 20¢) per message. There are similar charges for ancillary services.
- 23 Including SMS messages in the yield methodology also raises the concern that these services are not supplied on a timed basis, and are not included in the retail minutes reported to the Commission under the RKR's. As a result, an increase in SMS traffic will increase revenue without contributing to the retail minutes and will therefore distort the glide path deflator.
- 24 In general, the costing of content-based SMS services is likely to be different to that for user-to-user messages in that the service will effectively be a bundled content and carriage service. As the adoption of WAP and SMS-based services increases,<sup>1</sup> the revenue raised will increase as a proportion of customer spend and result in greater distortion to the glide path deflator.
- 25 Similar considerations apply in regard to value-added services such as voicemail. The Commission's letter does not provide a full explanation of which services would be included. The charges for such services are not proportional to the

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<sup>1</sup> AAPT notes that Telstra's Greg van Mourik suggested that similar products to the Who Wants to be a Millionaire game would be introduced over the next few months (The Australian, 28 August 2000, IT page 3)

traffic created and therefore the methodology suggested would result in an artificial increase in the glide path numbers.

#### 4.2 Allowing for credits under a yield approach

**Is a period-on-period approach considered to be appropriate for determining retail price movements? If not, is a cumulative approach considered to be more appropriate and, if so, why?**

- 26 AAPT is of the view that, due to the increased complexity of implementing a cumulative approach with credits, it would be preferable to rely on the period-on-period approach suggested by the Commission.

#### 4.3 Adjusting for quality

**Should retail price movements, in the context of the retail benchmarking approach, be adjusted to take into account changes in quality and, if so, why?**

- 27 AAPT considers there to be little merit in adjusting prices for quality or attempting to create a “quality index”.
- 28 Cable & Wireless Optus’ submitted on the Commission’s draft report on the pricing principles that the quality difference between services provided on pre-paid pricing plans and post-paid plans should be reflected in the final results. The three existing mobile networks are all mature and, to the extent that there are quality differences between them, AAPT considers these are fully accounted for in the relative prices of retail services available on the three networks. AAPT also agrees with the Commission’s observations as to the quality of handsets being offset through the other elements of packaged services offered in the pre-paid market.
- 29 AAPT also finds it strange that a mobile carrier would argue for quality adjustments. The economically sound approach to including a quality measure would be to treat an increase in quality as a reduction in price. As a result, any increase in aggregate quality of retail services would cause the glide path to trend down more sharply than if aggregate quality stayed at current levels. This suggests that CWO either considers the glide path should be steeper (which is unlikely) or that it intends to reduce average retail quality over time.
- 30 In addition, AAPT has some concerns that the construction and monitoring of any “quality index” would likely result in substantial administrative work and significant further delay to the implementation of the pricing principle.

## 5 Information collection and disclosure

**Should the information required for implementation of the retail benchmarking approach be sought under voluntary provision or required under a record keeping rule? Why? Is there another, more appropriate mechanism for collection of this information?**

- 31 AAPT submits that the most important aspects of any arrangement for the collection of information is that the information provided is timely and reliable. Although it is unlikely that one of the carriers will deliberately provide misleading information, it will be necessary to ensure that the carriers conduct a sufficiently rigorous approach to information collection and auditing such that the information reliable.
- 32 AAPT has previously supported voluntary approaches to information collection. However, the experience in previous access matters suggest that the incentives for taking advantage of information asymmetry are too great for access providers to resist. AAPT considers that the preferable approach is to require information to be provided to the Commission under the current RKR's or a slightly modified version.
- 33 It is worth noting that the information provided by Telstra in the context of the PSTN dispute was the subject of extensive industry consultation processes and independent review by consultants. AAPT's experience in regard to the collection and disclosure of information in the context of Part XIC processes is that the incentives for "padding" are significant and it is therefore necessary that the Commission adopt processes which expose the information collected to independent audit and review.

**Are there any comments regarding the consultation processes outlined above in relation to the treatment of any confidential information, and the disclosure of some, or all, of the collected information?**

- 34 AAPT is concerned that the Commission seems already to have decided that consultation on information collection and disclosure will be limited to access providers. Comments in the Discussion Paper suggest that it has also assumed that much of the information will be commercially sensitive. AAPT disagrees with both these aspects of the Commission's approach.
- 35 With regard to consultation, the approach suggested by the Commission is at odds with that which it has applied in the context of the NERA process, estimation of ULLS-specific costs and estimating retail costs associated with the local carriage service. AAPT can see no reason why the information which the Commission proposes to collect in relation to the GSM pricing principles should be treated differently and submissions only sought from access providers.
- 36 With regard to the confidentiality of that information, AAPT notes that much of it will already be published in the carriers' annual reports.<sup>2</sup> Within the context of

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<sup>2</sup> AAPT is aware of instances where parties have claimed confidentiality for matters that have been included in results. It should be an obligation of parties claiming confidentiality to assure the Commission that material has not already been made publicly available.

arbitrations, there is a set procedure for establishing the confidentiality of any information under section 152DK. AAPT submits that the Commission is required to expose the carriers' claims of confidentiality to the process under section 152DK within the context of the arbitrations.

- 37 AAPT also notes that the Commission proposes only to consult with "relevant access providers" as to the collection and disclosure of information which will be used to implement the pricing principles. As the Discussion Paper illustrates, the Commission's proposed approach is so heavily reliant upon data inputs that limiting consultation in this way will fatally undermine the reliability of the consultation process as a whole. Given the time and resources which have been devoted to this process, a decision to limit consultation on this aspect would be unfortunate.
- 38 AAPT submits that the Commission should reconsider its approach to consultations on collection and disclosure of information. As the Commission notes in relation to a different point in its cover letter to the Draft Report, it is preferable that consultations are "informed, robust and consultative".