TELSTRA'S BAND 2 MONTHLY CHARGE ACCESS UNDERTAKING FOR THE UNCONDITIONED LOCAL LOOP SERVICE

RESPONSE TO ACCC DRAFT DECISION DATED NOVEMBER 2008

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1. INTRODUCTION

Adam Internet, iiNet/Chime and Agile/Internode (***the Access Seekers***) agree with the Commission's draft decision to reject Telstra's Band 2 monthly charge access undertaking for the ULLS (***2008 Undertaking***). The Access Seekers note that the Commission proposes to reject the 2008 Undertaking on the basis that the price term of the Proposed Monthly Charge of $30 falls outside what would be considered to be a reasonable price range. The Access Seekers note that the Commission has reached this conclusion that the undertaking fails to meet the reasonableness criteria for the following reasons:

(a) The underlying assumptions of the TEA model are not reasonable;

(b) The Proposed Monthly Charge is excessive when compared to international benchmarks;

(c) The 2008 Undertaking is unlikely to promote the LTIE;

(d) The 2008 Undertaking will result in Telstra recovering more than is necessary to promote its legitimate business interests;

(e) The 2008 Undertaking will harm the interests of access seekers who have rights to use the ULLS;

(f) The price terms exceed the direct costs of providing access; and

(g) The 2008 Undertaking is not likely to facilitate the economically efficient operation of the ULLS.

Each of these will be considered in turn below.

2. THE UNDERLYING ASSUMPTIONS OF THE TEA MODEL ARE NOT REASONABLE

The Access Seekers agree with the Commission's view that Telstra's confidentiality undertakings have affected interested parties' ability to provide full, timely analysis and comment on the TEA model. Nonetheless, MJA, Optus and Ovum all commented on the inefficiencies present in the TEA model. The Access Seekers agree with the Commission's conclusion that the TEA model does not reflect an efficient network of a hypothetical operator.

The Access Seekers agree with the Commission's view that lead-in costs and entrance facility costs are not legitimate costs incurred in providing the ULLS.

The ULLS is provided via Telstra's CAN, with the vast number of services being originally connected in order to provide a standard telephone service (***STS***). New customers who request a telephone connection to a property with no existing in-place connection are responsible for the cost of pre-provisioning work on their property, this includes trenching. The cable that connects a residence to Telstra's network is called a 'lead-in' cable. This is the section of cable on a customer's own property. Telstra's responsibility is to provide a service to the property, but this does not include trenching of the lead-in cable after the property boundary. As a result, Telstra's lead-in costs are not particularly high and are most likely recovered or possibly over-recovered in the $299 connection charge that Telstra imposes on each new customer. Please see the advice that Telstra provides to people building a new home for further details about trenching and connection costs, attached at **Annexure A**.

As the Universal Service Provider, it is Telstra's responsibility to ensure that standard telephone services are reasonably accessible to all people in Australia on an equitable basis. The costs that Telstra incurs in performing this obligation are recoverable under the Universal Service Fund.

In a review of the Universal Service Obligation (***USO***), the Department of Broadband, Communications and the Digital Economy, explained the application of trenching costs in reference to the USO as follows:

> *11.1.1 Telstra's current arrangements and the Universal Service Obligation*
>
> *The USO places an obligation on Telstra as the primary universal service provider (PUSP) to provide all Australians with reasonable access on an equitable basis to an STS. However, the Telecommunications (Consumer Protection and Service Standards) Act 1999 (TCPSS Act) does not prescribe these terms and conditions. These are determined by Telstra, subject to the general price control arrangements applying to it, as set out in its standard marketing plan (SMP), and approved by the Australian Communications Authority (ACA). The SMP refers to the schedules contained in the 'Basic telephone service' section of our customer terms and covers the responsibilities of Telstra and its customers and the fees that are charged for a telephone connection.*[1]

Page 5 of Telstra's *Universal Service Obligation Standard Marketing Plan*, which is publicly available on Telstra's website[2] and attached at **Annexure C**, includes the following details of Telstra's obligations:

> ***2. The Standard Telephone Service In Australia***
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> ***2.1 The Service***
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> *The standard telephone service provides for voice telephony or an equivalent service to meet the requirements of the Telecommunications (Consumer Protection and Service Standards) Act 1999 and the Disability Discrimination Act 1992.*

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1 http://www.dbcde.gov.au/communications_for_consumers/telephone_services/fixed_telephone_services/industry_issues_policies_and_legislation/the_universal_service_obligation_uso/review_of_the_operation_of_the_universal_service_obligation_2004/universal_service_obligation_and_customer_service_guarantee_review/contents/11_network_extension_and_trenching_costs
Please refer to Annexure B

2 http://www.telstra.com.au/abouttelstra/commitments/docs/uso_smp.pdf
Please refer to Annexure C

- *The provision of a standard telephone service from Telstra includes a connection from Telstra's local telephone exchange to the network boundary in a building on the customer's premises. This includes the lead in cable and any associated equipment such as the conduit between Telstra's network in the street and the network boundary at the customer's premises. Where a service connection requires a new lead in cable to be provided, any trenching necessary between the point that the lead in cable enters the customer's property and the point that the lead in cable enters the building, will be the responsibility of the customer. The customer may chose to dig the trench themselves, use a contractor of their choice or use a contractor recommended by Telstra.*

In light if this, the Access Seekers agree that lead-in costs should not be included in a network costs model as they are likely to be completely recovered via customer connection charges or the Universal Service Fund.

3. THE PROPOSED MONTHLY CHARGE IS EXCESSIVE WHEN COMPARED TO INTERNATIONAL BENCHMARKS

The Access Seekers agree with the Commission's view that the Proposed Monthly Charge of $30 cannot be justified when international benchmarks indicate otherwise. Network costs will of course differ between different countries, however, without cogent substantiation from Telstra explaining why its costs should be so much higher than network charges in other countries, it is appropriate to use data from other countries as a benchmark to measure the reasonableness of proposed network charges in Australia. Telstra's proposed charges are considerably higher than ULLS charges in each of the 15 nations that the Commission used as comparisons in Figure 6.1 of the Commission's draft decision. This is extraordinary given that Australia's Band 2 population density is significantly higher than the population density in any of the listed countries. In such circumstances, where the Australian Band 2 network is able to reach a far larger number of residences using less cable and less trenching, the cost per service in Australia should be lower that the international benchmarks rather than higher.

4. THE 2008 UNDERTAKING IS UNLIKELY TO PROMOTE THE LTIE

Consideration of the LTIE is of fundamental importance in evaluating the 2008 Undertaking by virtue of section 152AB of the *Trade Practices Act 1974* (***TPA***). The Access Seekers note that the Commission has concluded that the 2008 Undertaking is unlikely to promote the LTIE as it fails to satisfy the following objectives under section 152AB(2) of the TPA:

(a) Promoting competition in markets for carriage services and services supplied by means of carriage services (section 152AB(2)(c)); and

(b) Encouraging the economically efficient use of and economically efficient investment in infrastructure (section 152AB(2)(e)).

There is also a third objective under section 152AB(2)(d), i.e. the objective of achieving any-to-any connectivity in relation to carriage services that involve communications between end-users. In regards to the Commission's views that the 2008 Undertaking does not directly affect this objective, the Access Seekers are of the view that it neither supports nor detracts from the current situation in regards to this objective. Given that a large number of premises cannot be serviced via the ULLS because of technology blockers such as RIMs and pair gains, the Access Seekers consider that in order to promote the LTIE, the 2008 Undertaking should improve any-to-any connectivity. Telstra does not undertake to remove technology blockers or transport services to copper lines in order to allow greater uptake of the ULLS. As such, the Access Seekers also consider that this objective has not been achieved.

The Commission has correctly noted the matters under section 152AB(6) that it must have regard to in determining whether the 2008 Undertaking encourages the economically efficient use of and economically efficient investment in infrastructure. Although the Commission is not limited to these matters in assessing the extent to which the 2008 Undertaking satisfies the objective under section 152AB(2)(e) by virtue of section 152AB(7), it is required to take the three matters listed into account.

The Commission notes on pp 50-51 of its draft decision that:

> *… an access price that reflects efficient, forward-looking costs best meet* [sic] *the objective of encouraging the economically efficient use of and investment in infrastructure. This is because such prices:*
>
> - *are consistent with the access provider's legitimate commercial interests;*
> - *enable access providers to exploit economies of scale and scope; and*
> - *provide correct incentives for the access provider and access seekers to make efficient investment in infrastructure used to supply the ULLS and downstream services.*
>
> *The ACCC's view is that where access prices are based on costs that are not the costs of a fully optimised and efficient network, the resulting access prices may not reflect the efficient costs of providing the service and will not encourage appropriate build/buy decisions. On this basis the ACCC considers that the objective of promoting efficient investment is not achieved when costs of providing the ULLS are based on a network which has not been fully optimised and does not use forward looking and efficient cost values.*

The Access Seekers seek clarification from the Commission in addressing the matters listed under section 152AB(6). In particular, the Access Seekers ask the Commission to detail its consideration of:

> *(a) whether it is, or likely to become, technically feasible for the services to be supplied and charged for, having regard to:*
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> > *(i) the technology that is in use, available or likely to become available; and*
> >
> > *(ii) whether the costs that would be involved in supplying and charging for, the services are reasonable or likely to become reasonable; and*

(iii) *the effects, or likely effects, that supplying, and charging for, the services would have on the operation or performance of telecommunications networks*

(b) *the legitimate commercial interests of the supplier or suppliers of the services, including the ability of the supplier or suppliers to exploit economies of scale and scope;*

(c) *the incentives for investment in:*

(i) *the infrastructure by which the services are supplied; and*
(ii) *any other infrastructure by which the services are, or are likely to become, capable of being supplied.*

If the Commission is of the view that it has adequately considered the matters listed above, the Access Seekers request that the Commission clarifies where these matters have been in considered in its draft decision.

5. THE 2008 UNDERTAKING WILL RESULT IN TELSTRA RECOVERING MORE THAN IS NECESSARY TO PROMOTE ITS LEGITIMATE BUSINESS INTERESTS

The Access Seekers agree that Telstra's proposed cost of capital is overestimated and would result in Telstra recovering more than its legitimate business interests. Further, the Access Seekers reiterate that Telstra should not be able to recover costs that exceed its actual historically incurred costs.

6. THE 2008 UNDERTAKING WILL HARM THE INTERESTS OF ACCESS SEEKERS WHO HAVE RIGHTS TO USE THE ULLS

The Access Seekers agree with the Commission's view that access seekers are served by an access price that enables them to compete on their merits in downstream markets. On page 39 of the draft decision, the Commission notes:

> *Chime submits that a competitive ULL environment is relied upon in other telecommunications areas. For example Telstra's current LCS and WLR exemption relies on reasonable levels of competition between ULL providers. As well as being an important contributor to whether a service is exempt from declaration, Chime notes that competition is essential to ensure that innovative products – such as Naked DSL – continue to be offered to end users.*

Though now overruled by the Australian Competition Tribunal, the Commission's decisions and reasons for its decisions in initially granting LCS and WLR exemptions to Telstra indicate that the Commission wishes to roll-back regulation of declared services and that to implement this step, a significant degree of competition between ULLS providers is required.

The Access Seekers further submit that in addition to the LCS and WLR exemption previously mentioned, the PSTN OA exemption provided to Telstra also relies on a significant degree of competition between ULLS providers.

Telstra's Proposed Monthly Charge being significantly above the current prevailing ULLS price is not only likely to distort the competitive process and harm the access seekers' interests, but more importantly, would also not promote the LTIE.

7. THE PRICE TERMS EXCEED THE DIRECT COSTS OF PROVIDING ACCESS

The Access Seekers agree that the Proposed Monthly Charge exceeds the direct costs of providing access.

The Access Seekers note that the second last paragraph on page 55 of the draft decision appears to be incomplete:

> *The average monthly charge necessary to recover the direct costs of the customer access network across all areas is significantly lower than the Proposed Monthly Charge. This indicates that the Proposed Monthly Charge of $30 will allow Telstra to over recover the direct costs of providing the ULLS, and that it could recover these costs under a lower monthly charge. Operational and technical requirements necessary for the safe and reliable operation of a carriage service, a telecommunications network or facility.*

The Access Seekers request that the Commission clarify this paragraph.

8. THE 2008 UNDERTAKING IS NOT LIKELY TO FACILITATE THE ECONOMICALLY EFFICIENT OPERATION OF THE ULLS

The Access Seekers agree with the Commission's decision that the 2008 Undertaking is not likely to facilitate the economically efficient operation of the ULLS.

9. ADDITIONAL DOCUMENTS

The Access Seekers wish to provide the Commission with copies of the following documents that were referred to in the Access Seekers' submission of 13 August 2008:

- iiNet Ltd, *Submissions on Draft ULLS Pricing Principles and Indicative Prices*, May 2008 (**Annexure D**);
- Internode Pty Ltd, *Submissions on Draft ULLS Pricing Principles and Indicative Prices*, May 2008 (**Annexure E**);
- Adam Internet Pty Ltd, *Submissions on Draft ULLS Pricing Principles and Indicative Prices*, May 2008 (**Annexure F**);
- Singtel Optus Pty Limited, *Optus Submission to Australian Competition and Consumer Commission on ULLS Pricing Principles & Indicative Prices*, May 2008 (**Annexure G**).

10. ANALYSYS COST MODEL

The Access Seekers note that Telstra's proposed ULLS monthly charge of $30 is more than twice the Band 2 charge estimated in the Analysys cost model for Australian fixed network services.[3] As the Analysys cost model is a truly independent model and not designed to further the interests of any party, the Access Seekers consider that the results it presents are likely to be unaffected by bias and therefore of satisfactory accuracy. Though the Analysys cost model is still

[3] ACCC, *Analysys cost model for Australian fixed network services*, Discussion Paper, December 2008, p. 48. **Attached at Annexure H**

in its early stages of public discussion and scrutiny, the disparity between the 2008 ULLS Band 2 cost of $14.74 estimated by Analysys and Telstra's $30 proposal is so vast that the unreasonableness of Telstra's undertaking is abundantly clear. Further, the Analysys cost model estimate is reasonably proximate to the Commission's 2007-08 ULLS Band 2 indicative price of $14.30 and in fair proportion to the Commission's comparison of international ULLS charges in Figure 6.1 of the Commission's draft decision. This lends substantive weight to the Analysys cost model's accuracy.

The Access Seekers consider that the Analysys cost model provides firm support to the Commission's view that the TEA model costs assumptions would lead to an over-estimation of the costs of providing the ULLS and that Telstra's undertaking is unreasonable and should be rejected.

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23 December 2008