



Australian  
Competition &  
Consumer  
Commission

# **Telstra's Structural Separation Undertaking**

**Discussion Paper**

**December 2011**

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## List of acronyms and other terms

ACCC	Australian Competition and Consumer Commission
ADSL	Asymmetric Digital Subscriber Line
AIP	Accelerated Investigation Process
BTS	Basic Telephone Service
BU	Business Unit/s
CCA	<i>Competition and Consumer Act 2010 (Cth)</i>
CRD	Customer Requested Date
CSG	Customer Service Guarantee
DTCS	Domestic Transmission Capacity Service
EOI	Equivalence of input
EOO	Equivalence of outcome
ITA	Independent Telecommunications Adjudicator
LOLO	LinxOnline Ordering
LSS	Line Sharing Service
Ministerial Criteria Instrument	<i>Telecommunications (Acceptance of Undertaking about Structural Separation – Matters) Instrument 2011</i>
PSTN	Public Switched Telephone Network
RMRC	Retail-minus-retail-costs
SLA	Service Level Agreement
Telco Act	<i>Telecommunications Act 1997 (Cth)</i>
TEBA	Telstra Exchange Building Access
TEM	Telstra Economic Model
ULLS	Unconditioned Local Loop Service
WLR	Wholesale Line Rental

## Background

The Australian Competition and Consumer Commission (ACCC) is considering whether to accept a structural separation undertaking and approve a draft migration plan submitted by Telstra.

Telstra lodged a Structural Separation Undertaking (SSU) with the ACCC on 29 July 2011 (the July SSU) under section 577A of the *Telecommunications Act 1997* (the Telco Act).

On 30 August 2011, the ACCC issued a discussion paper (the August discussion paper) which stated that, in the ACCC's preliminary view, the July SSU could not be accepted as it did not comply with the legislative requirement to include a compliance plan for Telstra's primary commitment to be structurally separated from the designated day.

In addition, the August discussion paper set out ACCC concerns in relation to the following:

- the lack of a clear and enforceable commitment to an 'equivalence of outcomes' to ensure that the interim equivalence and transparency measures remain appropriate and effective for the duration of the interim period;
- limitations to a number of the specific interim equivalence and transparency commitments; and
- certain aspects of the proposed arrangements between Telstra and NBN Co in the Definitive Agreements.

Since then, Telstra has engaged in constructive discussions with the ACCC and industry around improving the interim equivalence and transparency measures in the SSU, and Telstra and NBN Co have worked constructively towards resolving the ACCC's concerns around the Definitive Agreements.

On 9 December 2011, Telstra submitted a revised SSU (the December SSU) which includes substantially improved interim equivalence and transparency commitments intended to address ACCC and industry concerns.

## Submissions

Submissions in response to this discussion paper are requested as soon as possible and in any event by no later than **5.00 pm on Friday 13 January 2012**. The ACCC may be limited in its ability to fully consider late submissions, therefore it is important that interested parties make their submissions by the above deadline.

The ACCC prefers to receive electronic copies of submissions in either Adobe PDF or Microsoft Word format that is text searchable.

Please send submissions to the following email address:

[ssu-migration@acc.gov.au](mailto:ssu-migration@acc.gov.au)

The ACCC also accepts hard copies of submissions. Any hard copy should be sent to the following address:

Sean Riordan  
General Manager – Industry Structure and Compliance  
Communications Group  
Australian Competition and Consumer Commission  
GPO Box 520  
Melbourne VIC 3001

### **Confidentiality claims**

To facilitate an informed and open consultation, the ACCC will treat all submissions as public and publish them on the ACCC website. If interested parties wish to submit commercial-in-confidence material to the ACCC, they should submit both a public and a commercial-in-confidence version of their submission. In the confidential version, confidential material should be clearly identified and marked as confidential. In the public version, confidential material should be redacted and replaced with an appropriate symbol or '[c-i-c]'.

It is the ACCC's preference that as much material is disclosed in the public response as possible.

### **Context for the ACCC's assessment**

The ACCC is calling for submissions around Telstra's revised interim equivalence and transparency measures and revised monitoring of compliance measures.

To assist interested parties, this paper highlights the revisions made to the July SSU and draws out particular aspects of the proposed measures.

In light of ongoing concerns around the supply of wholesale ADSL services, the ACCC has announced that it is conducting a public inquiry into declaration of wholesale ADSL under Part XIC of the *Competition and Consumer Act 2010* (the CCA). Provided that the outstanding price equivalence concerns around wholesale ADSL services are resolved, the ACCC is minded to accept Telstra's revised SSU, subject to any new issues of real substance or drafting matters arising from this consultation process.

The ACCC intends to make a final decision on Telstra's SSU in February 2012.

### **Legislative framework**

Subsection 577A(3) of the Telco Act provides that the ACCC must not accept an SSU unless the ACCC is satisfied that it:

- provides for transparency and equivalence in relation to the supply by Telstra of Regulated Services to Telstra's wholesale customers and Telstra's retail business units beginning when the SSU comes into force and ending at the start of the designated day; and
- does so in an appropriate and effective manner.

In deciding whether to accept Telstra's SSU, the ACCC is required to consider whether the interim equivalence and transparency measures in the SSU provide for the matters set out in subparagraphs 4(g)(i)-(vii) of the Ministerial Criteria Instrument.

In addition, the interim equivalence and transparency measures will also be relevant in considering a number of the other mandatory considerations set out in the Ministerial Criteria Instrument.

The ACCC's intended approach to assessing the interim equivalence and transparency measures is outlined at pages 69-73 of the August discussion paper. The ACCC has considered submissions in relation to the ACCC's intended approach and does not consider it necessary to modify its approach from that set out in the August discussion paper.

The overall objective of the interim equivalence and transparency measures is to ensure equivalence in the supply of Regulated Services by Telstra throughout the transition to the NBN. Whether particular measures are appropriate and effective potentially involves questions of degree and judgement. Further, there could be a variety of measures which may be considered as appropriate and effective.

The ACCC considers measures are more likely to achieve this overall objective if they are simple and straightforward, can be implemented quickly, comprise genuine, tangible commitments, and are sufficiently documented and explained.

It is important to note that the ACCC is subject to some overall bounds in considering Telstra's SSU – for example, Telstra is not required to implement functional separation during the interim period.<sup>1</sup> Functional separation would require an 'equivalence of input' (EOI) standard necessitating Telstra's retail business units to use exactly the same access services using the same systems and processes as wholesale customers.

## **Overview of Part D of the SSU**

Part D of the December SSU contains a range of commitments intended to provide for equivalence and transparency during the interim period.

For the purposes of this consultation paper, the ACCC has considered these as follows:

- Telstra's overarching commitment to equivalence of outcomes
- Price equivalence and transparency measures
- Organisational arrangements within Telstra to support equivalence
- Information security
- Operational, systems, and technical equivalence
- Information equivalence
- Equivalence in relation to the Telstra Exchange Building Access Service
- Dispute resolution processes including an internal Telstra complaints-handling process and an Independent Telecommunications Adjudicator (ITA)
- ACCC monitoring of compliance and systems, procedures and processes that promote this, as well as measures ensuring appropriate oversight of compliance by Telstra

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<sup>1</sup> The Hon Stephen Conroy, *Media Release: Structural reform of telecommunications a step closer*, 24 June 2011 ([http://www.minister.dbcde.gov.au/media/media\\_releases/2011/206](http://www.minister.dbcde.gov.au/media/media_releases/2011/206))

## Overarching commitment to Equivalence of Outcomes

The August discussion paper noted that the July SSU did not contain an overarching commitment to equivalence of outcomes (EEO). The ACCC therefore considered there was no assurance that the substantive commitments would remain appropriate and effective until Telstra achieved structural separation so as to ensure the objective of equivalence of outcome for wholesale customers.<sup>2</sup>

Industry supported the ACCC view that Telstra should make a clear and enforceable commitment to provide Regulated Services to an EEO standard and establish a robust compliance framework.

Telstra has responded by incorporating an overarching equivalence commitment in the December SSU which is described at pages 7-11 of Telstra's supporting submission.

### *(i) What is the equivalence commitment?*

Telstra undertakes that the supply of Regulated Services to wholesale customers will be equivalent in respect of: (i) technical and operational quality; (ii) operational systems, procedures and processes; (iii) information about the matters specified in (i) and (ii); and (iv) the price that is charged - to the Comparable Retail Services Telstra itself provides.<sup>3</sup>

The equivalence commitment is subject to a number of qualifications which prevent Telstra from being required to implement measures which Telstra views as being elements of functional separation, including transfer pricing, self consumption of wholesale Regulated Services and EOI.<sup>4</sup> Telstra addresses why it considers these qualifications are appropriate in its supporting submission at pages 7-9.

### *(ii) How will the ACCC be notified of possible breaches of the equivalence commitment?*

Telstra commits to providing a monthly compliance report in which it will report to the ACCC any equivalence issues received from wholesale customers or the ACCC or identified by Telstra in the previous month.<sup>5</sup> The monthly compliance report will also identify any possible breaches of the specific commitments in the SSU (e.g. organisational measures, information security etc).

In addition, any person can notify the ACCC of a possible breach by Telstra of the equivalence commitment.

### *(iii) How will the equivalence commitment be enforced?*

The equivalence commitment has its own compliance and enforcement mechanisms (Schedule 11 of the December SSU). The enforcement threshold for the equivalence commitment mirrors the threshold in respect of Telstra's specific commitments around service quality and operational equivalence<sup>6</sup> and organisational structure<sup>7</sup> (discussed below), such that:

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<sup>2</sup> August discussion paper pp. 74-75

<sup>3</sup> December SSU, clause 9(a).

<sup>4</sup> See December SSU, clause 9(b)(i)

<sup>5</sup> See December SSU, clause 23.3

<sup>6</sup> Clause 11.7(b) & (c) of the December SSU

<sup>7</sup> Clause 8.8 of the December SSU

- Telstra will not be in breach if Telstra’s failure to comply with the overarching equivalence commitment is trivial; and
- the ACCC must not take action in respect of a complaint about an alleged breach of the overarching equivalence commitment which is vexatious or frivolous.

The primary focus of the compliance and enforcement mechanisms is to rectify possible breaches by requiring Telstra to change its conduct/systems or processes. The ACCC may also take action in the Federal Court for orders requiring Telstra to compensate for loss or damage suffered by wholesale customers (or any other person) as a result of a breach of the equivalence commitment.

There is a two track compliance and enforcement process which Telstra submits will incentivise it to self-report possible breaches and offer ‘fixes’ acceptable to the ACCC to avoid court enforcement action.

#### Track 1: Telstra reported breaches

Where Telstra reports a possible breach it *must* submit a Rectification Proposal within 30 days (or such longer period approved by the ACCC) setting out the steps that Telstra proposes to take to remedy the possible breach (a fix).<sup>8</sup> The ACCC may accept that fix, or reject it and specify an alternative fix by giving Telstra a Rectification Direction (the fix process). Telstra must comply with an ACCC Rectification Direction unless it is stayed by the court, or the court determines that it is invalid, unlawful or otherwise of no effect.

The ACCC can seek compensation orders from the Federal Court to redress loss or damage suffered by any person as a result of the breach, but cannot seek penalties in circumstances where Telstra self-reports a possible breach and submits a Rectification Proposal.

#### Track 2: ACCC notified breaches

In circumstances where the ACCC notifies Telstra of a possible breach, Telstra has an opportunity to submit a Rectification Proposal.

##### (a) Where Telstra submits a Rectification Proposal

The fix process (described above) applies and the ACCC may also seek compensation, pecuniary penalties and other orders from the Federal Court.

##### (b) Where Telstra does **not** submit a Rectification Proposal

The ACCC can enforce the equivalence commitment under section 577G of the Telco Act by seeking a declaration from the Federal Court that Telstra has breached the commitment.

Where the court finds Telstra has breached the overarching equivalence commitment, Telstra *must* submit a Rectification Proposal to the ACCC and the fix process (detailed above) applies. The ACCC may also seek compensation, pecuniary penalties and other orders from the Federal Court.

The ACCC must not notify Telstra of a possible breach in circumstances where the possible breach relates to a complaint made by a wholesale customer, unless the ACCC is satisfied that the wholesale customer has raised the complaint with Telstra

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<sup>8</sup> Schedule 11 December SSU, paragraph 2.2(a)



and Telstra has been given a reasonable opportunity to investigate and take action in relation to the complaint.<sup>9</sup>

While this has the potential to undermine Telstra's incentive to seek out and self-report any non-equivalence in the supply of Regulated Services, Telstra submits that wholesale customers need to raise any complaints first with Telstra to ensure that they are dealt with in a speedy and cost-effective manner and that Telstra is made aware of any concerns that wholesale customers have.<sup>10</sup>

*(iv) Requirements for ACCC Directions and court orders*

When making Rectification Directions, the ACCC must be reasonably satisfied that the matters imposed are a proportionate and justified remedy, having regard to whether the benefits outweigh the costs of complying and whether the matters imposed by the Rectification Direction are the least cost solution.<sup>11</sup> In this regard, the ACCC notes that it would typically take these matters into account in many of its regulatory decisions.

That said, these matters would not appear appropriate ACCC considerations when seeking non-injunctive relief from a court for any breach of the equivalence commitment. For example, in circumstances where the ACCC seeks orders for pecuniary penalties and compensation it would seem incongruous that the ACCC be obliged to have regard to whether the matters imposed by the orders are the least cost solution.<sup>12</sup>

Telstra has advised the ACCC that it believes that the ACCC would not be prevented from seeking these orders in any event, because the very nature of these orders is that they are either matters that a court will determine in its own discretion (in the case of penalties) or are to be determined by a court based on matters of fact (in the case of compensation). In addition, the specific matters that the ACCC must have regard to (whether the benefits outweigh the costs of complying and whether the matters imposed by the orders are the least cost solution) would be unlikely to apply in relation to these kinds of orders, so it would be open to the ACCC to decide that they are not relevant to its assessment.

Rectification Directions cannot impose retrospective remedies, compensation or penalties, nor can they require Telstra to implement any of the measures set out in clause 9(b) of the December SSU (e.g. transfer pricing, EOI).

In respect of price issues regarding services which are not declared or where there is no related Part XIC access determination or binding rule of conduct specifying price terms (not including wholesale ADSL), the ACCC cannot obtain retrospective court remedies for conduct occurring before the breach was notified.

**Attachment A** sets out the enforcement tracks diagrammatically.

## **Price equivalence and transparency measures**

The July SSU included a commitment to pass through ACCC pricing decisions made under Part XIC of the CCA, and a public reporting framework regarding unit costs,

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<sup>9</sup> Schedule 11 December SSU, paragraph 3.4(a)(i)

<sup>10</sup> Telstra's supporting submission, p.11

<sup>11</sup> Paragraph 5(a) of Schedule 11 of the December SSU

<sup>12</sup> Paragraph 5(b) of Schedule 11 of the December SSU

prices and Telstra's financial performance on a segmented basis (Telstra's TEM Report).

A price equivalence regime for wholesale ADSL services was also proposed, reflecting that as the service was not declared, it could not be subject to ACCC pricing decisions under Part XIC of the CCA.

In the August discussion paper the ACCC noted that, while further detail appeared necessary before reaching a final view, Telstra's proposed approach appeared capable of improving equivalence – subject to a range of specific limitations being addressed.

The specific limitations related to the degree of detail to be provided in the public reporting framework, and the specification and implementation of the wholesale ADSL price equivalence regime.

Following receipt of industry submissions, the ACCC also notified Telstra of its view that the proposed price methodology for the wholesale ADSL service – of retail minus *avoidable* costs – would not appear to provide assurance that appropriate and effective price equivalence would result for that service.

Telstra has responded to many of these stated concerns by including a raft of improvements to the price equivalence arrangements, and by confirming the form in which the public reports will be provided. Telstra's supporting submission discusses the changes to the price equivalence measures at pages 18-19.

Importantly, Telstra now proposes that, should the ACCC declare the wholesale ADSL service and make a pricing decision for it under Part XIC of the CCA (in a Final Access Determination), Telstra will adopt the price terms specified in that decision as the basis for meeting its price equivalence obligations, in the same way as it proposed for the Declared Services in the July SSU. Telstra also proposes including additional services and prices on its rate card.

Telstra has also strengthened some aspects of the price equivalence regime for wholesale ADSL – which would now apply only in the circumstance where the service is not declared.

For instance, Telstra now proposes to adopt a pricing methodology that deducts *all*, and not just *the avoidable portion*, of Telstra's retail costs in determining the ADSL 'price ceiling'. Telstra discloses that the resulting Wholesale ADSL prices will be \$30 in Zone 1, \$37 in Zone 2 and \$55 for AGVC (Telstra's supporting submission, page 18).

Further, Telstra has clarified the limited circumstances in which BigPond's backhaul requirements would not be considered in applying that pricing methodology.

Notwithstanding these changes, the proposed price equivalence arrangements to apply to wholesale ADSL when it is not a Declared Service still appear comparatively weak. This is because, in that circumstance:

- Telstra would appear to retain considerable latitude in developing and applying the pricing methodology, and hence in deriving the ADSL price table that would constitute the 'price ceiling';
- The proposed measures would not appear to prevent Telstra from engaging in discriminatory behaviour to leverage its market power in the supply of wholesale ADSL services – the nature of this alleged conduct (which has been the subject of competition complaints) was outlined in the August discussion paper;

- The ACCC would appear limited in when it could ‘step in’ and direct Telstra to change its pricing conduct under the equivalence commitment (discussed above), as this commitment cannot require Telstra:
  - to alter the wholesale ADSL price table, unless the pricing methodology by which it was derived was inconsistent with Telstra’s high level ‘fixed principles’; or
  - to discontinue commercial offers that are not offered equivalently, even where the overall level of prices contained in those commercial offers were significantly below the price offers made to other wholesale customers.

That said, the proposed measures to apply where the wholesale ADSL service was a Declared Service appear reasonable – hence there is potential for these concerns to become redundant should the wholesale ADSL service become a Declared Service.

In this regard, the ACCC is considering through a concurrent but discrete inquiry process whether or not it should declare the wholesale ADSL service.

Industry also expressed concerns in their submissions around the limited price equivalence measures that Telstra proposed in its July SSU for ‘exempt exchange service areas’ where Telstra did not owe standard access obligations.

The December SSU does provide some enhanced (albeit comparatively weak) measures to apply to those services. However, this issue has been overtaken by the ACCC’s recent decision to remove the exemption provisions in the Final Access Determinations (FADs) in respect of the WLR, LCS, and PSTN OA services in the course of the ACCC’s inquiry into varying the FADs for declared fixed line services. Consequently, the full price equivalence measures outlined in the December SSU for the relevant services would now be applicable.

## Organisational measures

Organisational measures are intended to address the underlying incentives that vertically integrated access providers have to favour their own retail businesses.<sup>13</sup> In the August discussion paper, the ACCC noted that certain exceptions to the organisational measures proposed in the July SSU would operate to undermine Telstra’s incentives to comply with its price and non-price equivalence commitments.<sup>14</sup>

The December SSU provides some improved commitments, principally to address concerns relating to the “senior management” exception and related information security arrangements. Telstra has also provided further transparency over the operation of the “customer excellence” exception and the strength of separation between the network services and retail business units.<sup>15</sup>

**Senior management exception:** This exception allowed staff with “management responsibilities” to perform both retail and wholesale/network functions on behalf of those business units.<sup>16</sup> Further, certain managers of Wholesale or Network Services Business Units were excluded from localised incentive remuneration arrangements.<sup>17</sup>

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<sup>13</sup> August discussion paper, p.87

<sup>14</sup> August discussion paper, p.89

<sup>15</sup> August discussion paper, p.89 and 91 respectively

<sup>16</sup> August discussion paper, p.92

<sup>17</sup> Clause 8.10(b) of the July SSU

The scope of these carve outs was unclear as “management responsibilities” was not defined.<sup>18</sup>

The December SSU includes an amended clause 8.10 to address these concerns. Now, only the CEO and the Chief Operating Officer are allowed to have “Line Management Responsibilities” for a Retail as well as a Wholesale or a Network Services Business Unit.<sup>19</sup> Any other officer must be approved by the ACCC.<sup>20</sup> An employee will have “Line Management Responsibilities” for a separated business unit when they have accountability for the business unit meeting its objectives and the authority to make decisions about the business unit management and operation.<sup>21</sup> This does not include employees whose functions arise solely as part of group wide responsibilities, such as a Human Resources officer.<sup>22</sup>

**Customer excellence exception:** The ACCC raised concerns over the impact of the “customer excellence” exception which provides that employees who undertake “certain bona fide efforts to resolve a customer issue” would not breach the SSU.<sup>23</sup> While the December SSU does not change these arrangements, Telstra has stated that “there are checks and balances to ensure that the exception cannot be used by Telstra to commit breaches of the SSU.”<sup>24</sup> These include cross organisational commitments on information security, customer agnostic incentive schemes and prohibitions on win-back by network services field technicians.<sup>25</sup>

**Separation of the Network Services business unit:** While the December SSU does not amend Telstra’s commitments regarding the separation of its network services business unit, Telstra has provided further clarity on the nature of the proposed division. Telstra notes that the Network Services Business Unit’s “activities are largely technical and process-oriented tasks that can (and will be) objectively measured in terms of equivalence”. The separation of the functions of this unit is therefore “primarily to ensure that staff in that business unit are not incentivised to give preference to retail customers or orders”.<sup>26</sup> The ACCC considers that Telstra’s commitments in this regard are consistent with the requirements of the Ministerial Criteria Instrument.

**Protected Information:** The December SSU also includes stronger restrictions on the exchange of confidential wholesale customer related information (Protected Information) between separated Business Units. Clause 10.4(a) requires that Telstra’s Wholesale BU and Network Services BU will not disclose Protected Information to any Retail BU unless authorised by a wholesale customer.<sup>27</sup> This extends to disclosure

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<sup>18</sup> August discussion paper, p.92

<sup>19</sup> Clause 8.10(b) of the December SSU

<sup>20</sup> Clause 8.10(b)(iii) of the December SSU

<sup>21</sup> Clause 8.10(c)(i) of the December SSU

<sup>22</sup> Clause 8.10(c)(ii) of the December SSU as identified in Telstra’s submission in support of its Revised SSU, p.6

<sup>23</sup> Clause 8.9(b) of the July SSU

<sup>24</sup> Letter from Telstra regarding organisational arrangements and staff incentives under the SSU; 25<sup>th</sup> August 2011, p.7

<sup>25</sup> Letter from Telstra regarding organisational arrangements and staff incentives under the SSU; 25<sup>th</sup> August 2011, p.7

<sup>26</sup> Letter from Telstra regarding organisational arrangements and staff incentives under the SSU; 25<sup>th</sup> August 2011, p.6

<sup>27</sup> Clause 10.4(a)(i) and (ii) respectively of the December SSU

to any employee outside a Retail Business Unit that has responsibility for the pricing of retail services.<sup>28</sup> Telstra has stated that:

“This will require separation of retail and wholesale information within Telstra Innovation and Product Marketing who have oversight of pricing proposals by the Retail and Wholesale Business Units”<sup>29</sup>

There is an exception to this commitment for Group Managing Directors with responsibility for company-wide pricing and their direct reports who do not work for a Retail Business Unit.<sup>30</sup> The restrictions on Wholesale BU disclosure to employees working for a Network Services BU and those not working for a Retail BU who perform network planning, wholesale product pricing and churn processing and implementation functions are on the less stringent “need to know” basis.<sup>31</sup>

## **Information security**

The information security commitments in the December SSU are broadly similar to those in the July SSU which were discussed at pages 94 - 97 of the August discussion paper.

The scope of Telstra’s July SSU commitments in respect of Protected Information and derived information did not extend to limiting misuse of all information obtained by virtue of Telstra’s vertical integration, in order to gain an advantage in a downstream market.

Specifically, it was not clear what protections would operate in relation to nationally aggregated information which would enable Telstra to identify the wholesale customer.

Telstra has responded to this concern by including nationally aggregated information in clause 10.5(a) of the December SSU, so that where Telstra’s Retail BU requests access to this information, Telstra will not disclose it unless, with the approval of the ACCC, Telstra makes the information available to all wholesale customers at the same time.

## **Non-price equivalence and transparency measures**

Telstra has made a number of improvements to the service quality commitments proposed in its July SSU (which were discussed at length in the August discussion paper at pages 97-105). The ACCC notes that these specific non-price equivalence and transparency measures would now operate in conjunction with the overarching equivalence commitment, which also relates to non-price equivalence.

The changes in the December SSU are discussed below and are further described at pages 12-14 of Telstra’s supporting submission.

### ***Operational quality***

As noted in the August discussion paper, there are various measures which relate to operational quality. These are discussed in turn below.

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<sup>28</sup> Clause 10.5 (c) of the December SSU

<sup>29</sup> Telstra’s supporting submission, p.5

<sup>30</sup> Clause 10.5(d) of the December SSU

<sup>31</sup> Clause 10.4(a)(i)(B) and (C) of the December SSU

*1) Systems and processes to support equivalence in operational quality*

The ACCC drew out a significant concern around limits in the July SSU on court enforceability of Telstra's systems/processes commitment precluding the ACCC from taking action unless it could establish that the failure was material, not an isolated incident, *and* the failure formed part of a demonstrable pattern of non-compliance.<sup>32</sup> Submissions received from industry reflected the ACCC's concern that this threshold was inappropriate.

In response, Telstra has substantially lowered the threshold to one based on triviality, and vexatious or frivolous complaints.<sup>33</sup> This would appear to address the concern.

Submissions from industry raised a concern that the July SSU lacked a commitment providing transparency over the end to end processes/systems used in the provision of Regulated Services to wholesale customers and those used by Telstra Retail. In the December SSU, Telstra has now committed to publishing (and continuously updating) a detailed description about the processes/systems used for service activation, fault rectification and service qualification, for each Regulated Service and Telstra's Comparable Retail Service.<sup>34</sup> This measure is likely to improve transparency over the processes/systems relevant to operational equivalence. Further, in the event that it becomes evident that Telstra's processes/systems are not providing EOO, Telstra would be obliged to rectify the issue in accordance with its overarching commitment to equivalence.

***Operational performance metrics***

The ACCC noted a concern around the metric for ULLS activation (cutover) in that the service level was inferior to those for PSTN and DSL services, which require similar work.<sup>35</sup> The ACCC noted that this could place ULLS wholesale customers at a competitive disadvantage.

In response to this concern, Telstra has changed the ULLS activation metric<sup>36</sup> as follows:

- Telstra has committed to complete ULL individual cutovers on the first date requested by the wholesale customer (Customer Requested Date (CRD)) or, if the date is rescheduled or missed due to an act or omission of the wholesale customer or its end user, the rescheduled CRD, 95% of the time. Importantly, the wholesale customer decides the date, whereas in the July SSU it was extendable by Telstra depending on availability in Telstra's systems.
- For Bands 1 and 2 where there is an intact metallic path at the relevant premises,<sup>37</sup> if the wholesale customer requests, Telstra will offer an appointment 3 clear working days after the request for the ULL individual cutover is received.

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<sup>32</sup> August discussion paper, pages 77 and 102, Clause 10.7 July SSU.

<sup>33</sup> December SSU, Clause 11.7(b) and (c)

<sup>34</sup> December SSU, Clause 11.8

<sup>35</sup> August discussion paper, p 101

<sup>36</sup> December SSU, Schedule 3, Paragraph 5

<sup>37</sup> Intact means a metallic path connected to the network boundary point at a premises where, at the time Telstra receives a ULL Individual Cutover request in respect of that premises, the path is being used to supply a BTS or ULLS or the path has recently been used to supply a BTS or ULLS but is currently vacant.

The CRD in respect of other ULL individual cutovers cannot be earlier than the earliest date applicable in the relevant geographic area specified in the ULLS Industry Code.<sup>38</sup>

Telstra has also made further changes in the December SSU.

First, submissions raised concerns that whilst the performance for some metrics is compared against a Telstra Comparable Retail service (e.g. wholesale line rental is compared against retail line rental), the performance for other metrics is not (e.g. ULLS, LSS and certain DTCS metrics).<sup>39</sup> In response, Telstra undertakes to provide a report comparing the common tasks performed by Telstra's Network Services BU for both ULLS/DTCS/LSS service activation and service activations undertaken for Telstra's Retail BU. To this end, Telstra undertakes to vary the SSU to incorporate any new or amended metrics proposed in the report. This commitment goes to identifying more comparative measures for the metrics.

Second, submissions proposed an alternative approach to the metrics. The service levels measure whether Telstra has met a target time frame (e.g. 97% of instances during the quarter were achieved within 3 days for Telstra Retail, and likewise for wholesale customers). Submissions stated that what should be compared is the actual performance on average (e.g. wholesale customer performance was met in 2.4 days versus that provided to Telstra retail). In this respect, Telstra has committed that for certain metrics it will provide quarterly reporting on the average performance.<sup>40</sup> This additional reporting should provide greater transparency around operational equivalence (or lack thereof) and, in particular, around the appropriateness of existing target timeframes.

#### Exclusions to the metrics

In the August discussion paper, the ACCC also identified concerns around the proposed exclusions in the July SSU which significantly curtailed the application of the metrics and the associated 'fix' and 'pay' arrangements (such that where the exclusion applied, Telstra's performance for that instance would not count).<sup>41</sup>

Telstra has made some significant changes to address these concerns, including the removal of the exclusion in respect of low volume services<sup>42</sup> which would possibly have applied to around 6 metrics (including certain metrics for BTS, ADSL and DTCS).

In addition, Telstra has narrowed the previous exclusion for regions where NBN Co is undertaking installation or connection activities or regions affected by those activities. Where the exclusion applies, it will only apply where a ticket of work is directly affected by NBN-related activities in any Rollout Region, or which is in the course of being migrated to the NBN.

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<sup>38</sup> ULLS – Ordering Provisioning and Customer Transfer Code CS69:2005, as amended from time to time. See December SSU Schedule 3, paragraph 5.

<sup>39</sup> Metrics 1 to 11 and metric 18 are compared to a Comparable Retail Service. The others are compared against an absolute service level.

<sup>40</sup> December SSU, Clause 16.2(d). The measure only applies for metrics compared against Telstra's Comparable Retail Service - metrics 1 to 11 and metric 18.

<sup>41</sup> August discussion paper, pp. 102 and 103.

<sup>42</sup> where there is less than 1,500 orders in a quarter or where there was less than 10% of Telstra Retail's volume.

Further, this exclusion no longer applies to metrics which are compared against Telstra's Comparable Retail Service, meaning that it would only apply to the metrics for LSS, ULLS and DTCS. The ACCC notes that should Telstra develop metrics that compare common tasks for fulfilling tickets of work for LSS, ULLS and DTCS with work done for Telstra's retail business units, the exclusion may become redundant.

#### Issues regarding the rebates

In the August discussion paper, the ACCC identified several concerns regarding the SLA (rebate) Agreement (Schedule 7 of the December SSU). A diagram illustrating the SLA agreement is set out in **Attachment B**.

The first of these concerns was around the exclusion of other remedies. Telstra has responded to this concern by revising the terms of the SLA Agreement so that while wholesale customers waive the right to claim a service level rebate under their wholesale contract, they are not required to waive other contractual remedies for compensation or the right of contribution under the Customer Service Guarantee regime.<sup>43</sup> Further, wholesale customers can also make an equivalence complaint to the ITA or complain to the ACCC regarding a breach of the SSU, the Telco Act or Parts IV/XIB/XIC of the CCA. This appears to resolve concerns.

The ACCC's other concerns related to the level of rebates being too low to incentivise Telstra to meet its obligations, and that the rebates do not scale upwards for severe failures and that therefore Telstra would not be incentivised to remedy ongoing breaches of the metrics. Telstra has amended the LOLO rebate such that the rebate will increase in line with the total number of hours of outage (capped at 100 hours) but has not increased the level of the rebates or made the other rebates scalable. Overall, this appears to be a lesser concern given that other rights are not waived upon entry into the SLA Agreement and referral to the ITA/ACCC is not excluded.

#### ***Quality of systems support***

Submissions raised a concern around the metrics not applying to important pre-ordering processes such as service qualification. Rather than deal with service qualification under the metrics, Telstra has made additional commitments for the systems related to service qualification (discussed at page 13 of Telstra's supporting submission):

- For systems used to process service qualification requests for copper-based services (except for ULLS), Telstra undertakes to provide reliability and response accuracy equivalent to those systems which Telstra uses for Telstra Retail (i.e. over the copper network, Telstra commits to equivalence of outcomes).<sup>44</sup>
- For *new* service qualification systems (except for systems related to ULLS), Telstra will use the same systems for wholesale customers and Telstra retail (i.e. Telstra commits to equivalence of input).<sup>45</sup>

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<sup>43</sup> Pursuant to section 118A of the *Telecommunications (Consumer Protection and Service Standards) Act 1999* (Cth). However, Telstra does not have to pay rebates to a wholesale customer, where the Regulated Service is used by the wholesale customer to supply another service provider which in turn, supplies the end user; and where that other service provider is entitled to make a claim against Telstra (including right of contribution under section 118A of the *Telecommunications (Consumer Protection and Service Standards) Act*).

<sup>44</sup> December SSU, Clause 13.5(a)

<sup>45</sup> December SSU, Clause 13.5(c)



- In relation to ULLS, Telstra commits to permit wholesale customer use of LSS service qualification tools to process ULLS service qualification, until a common service qualification system is developed.<sup>46</sup>

While it is unclear as to what equivalence standard ULLS service qualification will be provided, Telstra has confirmed to the ACCC that it is currently investigating whether its new service qualification systems can in fact be extended to deal with ULLS service qualifications as well.

Furthermore, Telstra has also advised the ACCC that to the extent there is a question about a lack of equivalence in the service qualification functionality for ADSL as between the existing or new service qualification systems and ULLCIS<sup>47</sup> then this is something that could be the subject of an investigation by the ITA.

## Information equivalence

A summary of the information equivalence arrangements provided in the July SSU is provided at page 77 of the August discussion paper (discussed in detail at pages 106-108). The ACCC considered that “taken collectively,” Telstra’s information equivalence arrangements “could promote competition by limiting any informational advantages Telstra may gain through its vertical integration”.<sup>48</sup>

However, the August discussion paper noted that while the proposed notifications “improved on Telstra’s OSP” there remained the “potential for further improvements to provide a higher degree of assurance of equivalence”.<sup>49</sup> In particular, the ACCC considered there to be a lack of clarity as to how the proposed notifications compare to the information and notice period available to Telstra’s retail business units.<sup>50</sup> For example, “major network incident notifications” will be made “in accordance with the terms governing the supply of the relevant regulated service” and Operational Support System (OSS) announcements will be made “in accordance with [Telstra’s] procedures for making OSS announcements that exist from time to time”.<sup>51</sup> As a result it was unclear the extent to which the notifications were *equivalent* to the quality and timeliness of information provided to Telstra’s retail business units.

Clause 14 of the December SSU largely mirrors clause 13 of the July SSU. However, minor amendments have been made to the proposed notifications under Schedule 4. With regard to major network incident notifications, Telstra now commits to providing reasonable information to affected wholesale customers and has specified a more detailed process that requires the crisis management team established by Telstra to deal with any emergency or network incident to:

- include a suitably senior and qualified representative of the wholesale business unit;
  - include appropriate communications to affected wholesale customers in any communications strategy which is developed by the crisis management team;
- and

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<sup>46</sup> December SSU, Clause 1.5(b)

<sup>47</sup> This is the system used by Telstra to process ULLS service qualifications.

<sup>48</sup> August discussion paper, p.107

<sup>49</sup> August discussion paper, p.107

<sup>50</sup> August discussion paper, p.108

<sup>51</sup> August discussion paper, p.108

- ensure that communications to wholesale customers and retail customers in relation to the emergency or network incident are consistent and that the timeliness of those communications is equivalent (except for any differences stemming from technical differences in the methods used to communicate).<sup>52</sup>

The ACCC will be able to ensure that Telstra’s information equivalence commitments remain “fit for purpose” as they are included within the scope of Telstra’s overarching equivalence commitment pursuant to clause 9(a)(iii) of the December SSU.<sup>53</sup>

## **Equivalence in relation to the Telstra Exchange Building Access Service**

The December SSU contains substantially revised and expanded commitments in relation to TEBA. These are contained in clause 12, Schedule 12 and Schedule 13.

**Reservation of capacity by Telstra:** As per the July SSU, Telstra may reserve exchange capacity where it has bona fide documented plans to use the Exchange Capacity within 36 months.<sup>54</sup> The ACCC noted in the August SSU discussion paper that this commitment could provide a degree of assurance that Telstra will not use reservations for the purpose of frustrating access by others, as any such reservations must be bona fide and documented.<sup>55</sup> Telstra has bolstered the transparency arrangements supporting this commitment, by allowing the ACCC to request information on Telstra’s reservations.<sup>56</sup> This supplements the ACCC’s general information request powers in the SSU.<sup>57</sup> These new commitments have the potential to provide greater ACCC oversight over Telstra’s compliance with its substantive obligations regarding reservations.

**Reservation of capacity by access seekers:** The ACCC’s August discussion paper and response submissions raised a specific concern that Telstra’s commitments in relation to TEBA in the July SSU did not appear to provide for any degree of equivalence, as an equivalent right for wholesale customers to place an order to reserve exchange capacity for future use was not available.<sup>58</sup> Telstra’s December SSU commits to allow access seekers to reserve a TEBA allocation for up to 3 years to meet future anticipated requirements.<sup>59</sup>

The process by which Telstra will process access seekers’ requests is set out in Schedule 12 to the December SSU. In short, ordinary TEBA processes and practices will be used for submitting and processing requests to reserve space and to use allocated floor space. The wholesale customer would be required to pay for the allocated floor space at ordinary rates and have up to 36 months to use the reserved space (subject to “roll over” arrangements at the end of that period).

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<sup>52</sup> Subparagraph 7(b) of Schedule 4 of the December SSU

<sup>53</sup> In relation to the technical and operational quality; and operational systems, procedures and processes used in the supply of Regulated Services required under subclauses 9(a)(i) and (ii) respectively.

<sup>54</sup> Clause 12.1(a) of the December SSU

<sup>55</sup> August discussion paper, p.111

<sup>56</sup> Clause 12.1(b), (c), and (d) of the December SSU

<sup>57</sup> Clause 24.4 of the December SSU

<sup>58</sup> SSU Discussion Paper, p.111; see response submissions Macquarie p.4, Optus p.35-36, CCC 26 September p.18, Herbert Geer p.19-20.

<sup>59</sup> Clause 12.6 and Schedule 12

**Exchange capping:** The December SSU, as per the July SSU, contains processes to be followed prior to capping an exchange and supporting compliance arrangements. As previously noted by the ACCC, these processes would appear to promote competition by ensuring Telstra’s wholesale customers are not unreasonably denied access to bottleneck exchange infrastructure. Importantly, the overarching equivalence commitment applies to TEBA. This is subject to a limit that the commitment does not apply if it would prevent Telstra from obtaining a sufficient volume of a Regulated Service to meet its statutory obligations. This narrow carve-out does not extend to Telstra obtaining a sufficient volume to meet its own commercial purposes.

**Exchange queues:** The December SSU contains extensive new commitments in relation to processes to be followed in relation to exchange queues (Schedule 13). This responds to the ACCC’s statement in the August discussion paper that Telstra had not proposed measures to promote competition by ensuring that delays are reasonable.<sup>60</sup> The ACCC understands that these processes largely reflect current practice. Should these arrangements not prove to be fit for purpose over time, then this is something that could be the subject of an investigation by the ITA or addressed under the overarching equivalence of outcomes commitment.

## Dispute Resolution

In the July SSU, Telstra proposed a two part process for the resolution of non-price equivalence complaints from wholesale customers, comprising an internal Accelerated Investigation Process (AIP) and an external process through an Independent Telecommunications Adjudicator (ITA). These processes were discussed in detail at pages 113-120 of the August discussion paper.

In the August discussion paper, the ACCC pointed to the willingness of wholesale customers to participate in the ITA scheme as being fundamental to the effectiveness of the ITA as a dispute resolution mechanism. Response submissions raised concerns about the degree of independence of the ITA and the appropriateness of the ITA process and powers to ensure effective dispute resolution.<sup>61</sup>

**Independence of the ITA:** Telstra has responded to this concern by providing wholesale customers with the ability to elect to have an ITA dispute heard by either the ITA or the ACCC (acting as the adjudicator).<sup>62</sup>

While Telstra will establish the ITA Company, as noted in the August discussion paper, the ACCC has powers over the appointment of the ITA Adjudicator.<sup>63</sup> Telstra must also submit an ITA Constitution and Charter of Independence for approval by the ACCC.<sup>64</sup> These requirements are retained in the December SSU.

**ITA powers:** The August discussion paper highlighted a number of issues with the scope of the ITA powers proposed in the July SSU.<sup>65</sup> In particular, the ACCC considered that limitations on the ITA powers to specify changes or outcomes for process modifications, proposed monetary caps and the apparent lack of a capacity for the ITA to require “reasonable remediation” of processes and systems all weighed

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<sup>60</sup> August SSU Discussion Paper, p.111

<sup>61</sup> August discussion paper, p.68

<sup>62</sup> Paragraph 6.1, Schedule 5 of the December SSU

<sup>63</sup> August discussion paper, p.115; referring to Schedule 5, paragraph 5.1 of the July SSU

<sup>64</sup> August discussion paper, p.115;

<sup>65</sup> August discussion paper, p.118

against a conclusion that the ITA would be an effective dispute resolution mechanism.<sup>66</sup> Noting these concerns, the ACCC stated that “it is incumbent on Telstra to clarify and explain these important aspects of the ITA scheme”.<sup>67</sup>

Telstra has responded to these concerns by empowering the ITA with the ability to direct a party to provide a proposal for the modification of its processes or systems and to make a binding direction on that party if the modification proposal is unsatisfactory.<sup>68</sup> Further, Telstra has provided greater clarity over the application of the monetary caps, with the ACCC not subject to the caps when enforcing the overarching equivalence commitment or operating in its Part IV, XIB or XIC capacity.<sup>69</sup>

A further concern was identified by the ACCC in its August discussion paper in respect of the ITA imposing directly enforceable obligations on wholesale customers. This could significantly deter wholesale customers from participating in the ITA scheme. Telstra has addressed this concern in its December SSU by permitting wholesale customers to opt out of the ITA process at any time up to 10 business days after receiving a final determination from the ITA.<sup>70</sup>

Pages 14 and 15 of Telstra’s supporting submission provide further detail on the revised dispute resolution provisions in the December SSU as well as a description of the interaction of the various dispute resolution processes established under the SSU. The ACCC considers that these amendments are a significant improvement to the dispute resolution arrangements in the July SSU. The July SSU did not provide a mechanism for the resolution of price equivalence disputes.<sup>71</sup> Telstra has addressed this through the inclusion of new provisions in clause 18.7 and Schedule 10 of the December SSU.

## **Monitoring of compliance**

The July SSU did not comply with the legislative requirement to provide for the ACCC to monitor Telstra’s compliance with its primary commitment in Part C of the SSU to be structurally separated from the designated day.

Telstra has addressed this by modifying Part E of the SSU to apply both before and after the designated day. In particular, Telstra commits to the provision of a Separation Compliance Program to the ACCC no later than 6 months prior to the designated day, detailing how Telstra will comply with its obligation to structurally separate.<sup>72</sup> Telstra’s commitment to provide an Annual Compliance Report will now remain after the designated day, and Telstra will report any non-compliance with its commitment to remain structurally separated.<sup>73</sup> These new commitments are likely to facilitate the ACCC’s monitoring of Telstra’s compliance with its structural separation commitments in an appropriate and effective manner.

The arrangements proposed by Telstra in its July SSU to facilitate ACCC monitoring of Telstra’s compliance with the interim equivalence and transparency commitments

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<sup>66</sup> August discussion paper, p.119

<sup>67</sup> August discussion paper, p.8

<sup>68</sup> Paragraph 11.2 of Schedule 5 of the December SSU

<sup>69</sup> Telstra’s submission in support of the Revised SSU, p.13

<sup>70</sup> Paragraph 7.3, Schedule 5 of December SSU

<sup>71</sup> August discussion paper, p.4

<sup>72</sup> Clause 23.8 of the December SSU

<sup>73</sup> Clause 24.2(b)(iii)(A) and (B)

in Part D of the SSU were discussed at pages 120 to 125 of the August discussion paper.

The December SSU includes some improvements to the July SSU compliance reporting arrangements reflecting the expanded scope of Telstra's new substantive commitments. For example, clause 23.3 now requires Telstra to submit monthly reports on its compliance with the overarching equivalence commitment in clause 9(a), detailing:

- any equivalence issues received from Wholesale Customers, or identified by Telstra or the ACCC, during that month;
- Telstra's view of whether a breach of clause 9(a) has occurred, giving reasons; and
- the action that Telstra proposes to take to address or respond to the issue.

Further, the commitments surrounding the Annual Compliance Report have also been enhanced to include details of these matters.<sup>74</sup>

Finally, new clause 24.4 obliges Telstra to provide the ACCC with any information that the ACCC reasonably requires for the purpose of monitoring Telstra's compliance with the SSU or for performing any other function or power under the SSU. The ACCC considers that this clause provides an appropriate and effective mechanism for the ACCC to monitor Telstra's compliance with the SSU.<sup>75</sup>

## **Matters relating to the Definitive Agreements**

Pursuant to the Ministerial Criteria Instrument, in deciding whether to accept an SSU given by Telstra, the ACCC must have regard to the conduct that would be authorised under section 577BA of the Telco Act as a consequence of the ACCC's acceptance of the undertaking or the undertaking coming into force.<sup>76</sup>

The ACCC's August discussion paper set out concerns regarding the following aspect of the proposed arrangements between Telstra and NBN Co that militated against acceptance of the SSU:

- the inclusion of a broad variation mechanism in the commercial agreements between NBN Co and Telstra which could result in either party imposing new or modified restrictions on the competitive behaviour of the other party that could potentially receive the benefit of legislative authorisation pursuant to section 577BA of the Telco Act (the Substantial Adverse Events clause) without regulatory oversight;

In addition, the ACCC's August discussion paper set out the following concerns in relation to the proposed arrangements between Telstra and NBN Co that tended to militate against acceptance of the SSU, including:

- the provisions restraining Telstra from promoting wireless services as substitutable for NBN Co's fibre services (the wireless promotion restriction); and

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<sup>74</sup> Clause 24.2 of the December SSU

<sup>75</sup> As required by subsection 577A(5) of the Telco Act

<sup>76</sup> Paragraph 4(d) of the Ministerial Criteria Instrument

- the limitations on Telstra's ability to provide HFC services to channel providers other than FOXTEL (the Pay TV restriction).

Telstra and NBN Co have engaged constructively with the ACCC in relation to these concerns and have agreed to the following.

The parties will implement a process that would enable ACCC review of any variation to the Definitive Agreements that is entered into pursuant to the Substantial Adverse Events clause (other than a variation that is authorised for the purposes of section 51(1) of the CCA (other than by operation of section 577BA(3) of the Telco Act) or pursuant to Part VII of the CCA). The parties intend to set out this process in a section 87B undertaking that will be submitted to the ACCC for its consideration prior to a decision being made on the SSU as a whole. The ACCC is currently engaging in pre-lodgement discussions with the parties in relation to this undertaking.

The parties will amend the wireless promotion restriction so that it replicates the prohibitions on misleading and deceptive marketing practices in the Australian Consumer Law.

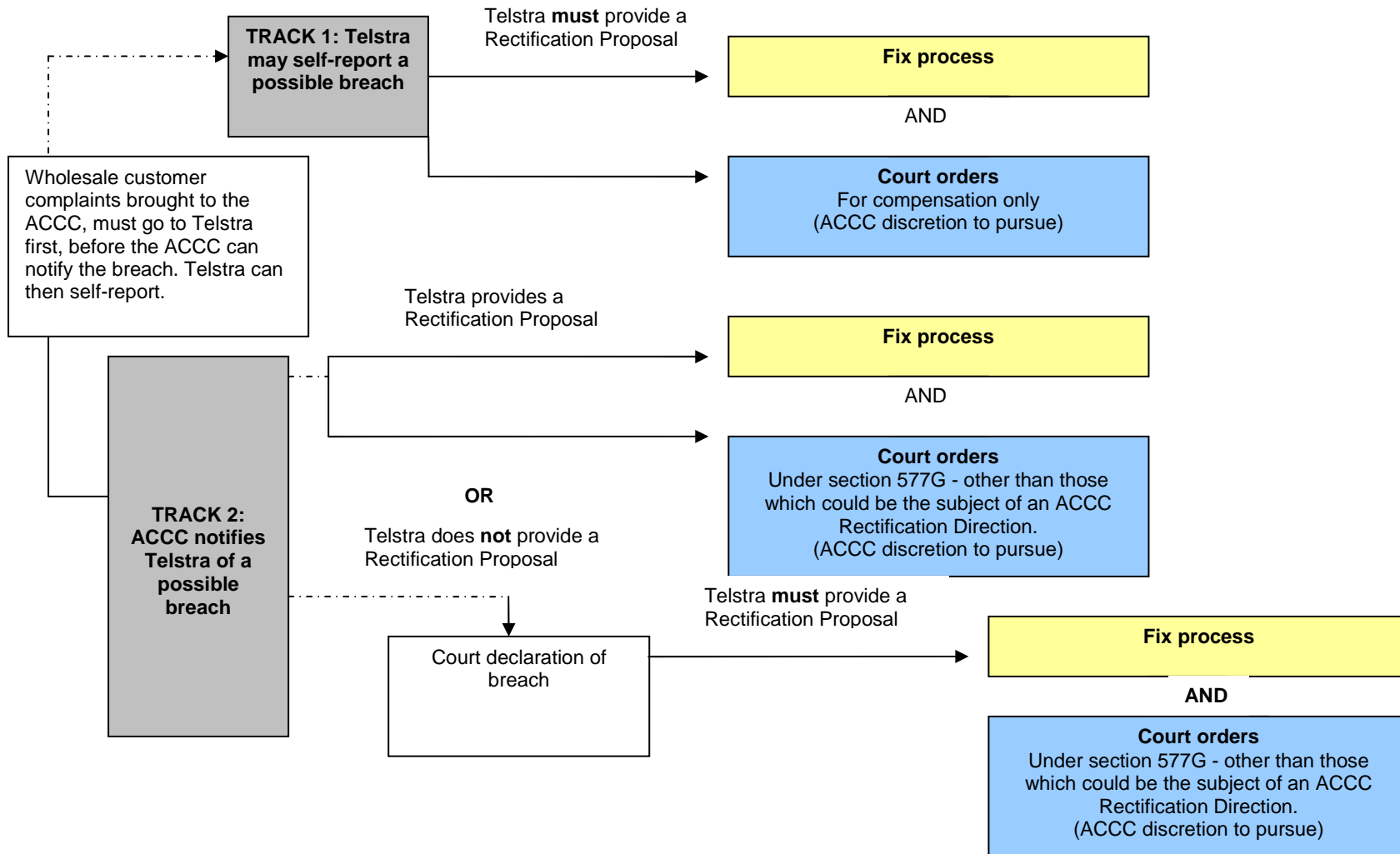
With regard to the Pay TV restriction, the ACCC has sought, and expects to receive, assurance from the parties that existing access seekers who utilise FOXTEL's digital set top unit service will be able to continue to access Telstra's HFC carriage service for that purpose on commercial terms.

The ACCC invites submissions regarding the appropriateness and effectiveness of the interim equivalence and transparency measures, and the monitoring of compliance measures, in Parts D and E of the December SSU.

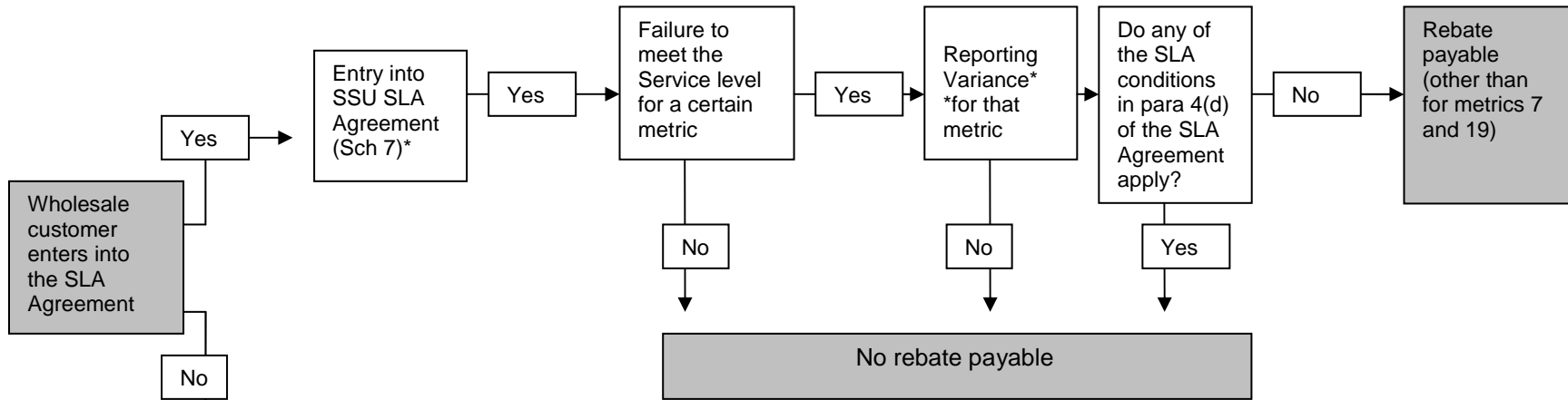
Interested parties may wish to comment on the specific issues discussed in this paper and/or the December SSU more broadly.

Submissions in response to this discussion paper are requested as soon as possible and in any event by no later than **5.00 pm on Friday 13 January 2012**.

**Attachment A: Enforcement mechanisms for equivalence commitment**



**ATTACHMENT B: Rebate scheme**



\*What is waived when the SLA Agreement is entered into? The wholesale customer waives rights to any existing service level rebate under its contract. The wholesale customer waives no other rights including contractual rights to compensation, although the rebate amount may be off-set against monies owing pursuant to those other rights. Wholesale customers can still submit a complaint under Telstra's AIP (and the ITA) and to the ACCC.  
 \*\* A Reporting variance is a variance of 2% or more (in negative terms). See definition under Schedule 1 of the December SSU.