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Submission by Herbert Geer Lawyers on behalf of:

Adam Internet Pty Ltd,

iiNet Limited,

Internode Pty Ltd, and

TransACT Communications Pty Ltd

in response to the ACCC discussion paper of December 2011 relating to Telstra's structural separation undertaking

1. INTRODUCTION

This submission is made on behalf of Adam Internet Pty Ltd, iiNet Limited, Internode Pty Ltd, and TransACT Communications Pty Ltd (collectively, **our Clients**) in response to the ACCC's December 2011 discussion paper on Telstra's structural separation undertaking (**the December Discussion Paper**). The December Discussion Paper is in response to the submission by Telstra of a revised structural separation undertaking submitted on 9 December 2011 (referred to below as **the SSU**).

Telstra had originally submitted its structural separation undertaking on 29 July 2011 (**the July SSU**). However, in a discussion paper released in August 2011 (**the August Discussion Paper**), the ACCC raised a number of concerns with the July SSU, and indicated that it was inclined to reject the July SSU. We provided a submission on behalf of Adam Internet Pty Ltd, iiNet Limited, and Internode Pty Ltd in response to the August Discussion Paper (**the Previous Submission**)[1].

As stated in the Previous Submission, our Clients believe that the ACCC's decision relating to the SSU has the potential to be the single most important decision that the ACCC has made in respect of telecommunications since competition in telecommunications markets was opened up. Our Clients note the following comment by the ACCC in the December Discussion Paper:[2]

> *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.*

Taken at face value, this comment suggests that the ACCC believes that all concerns raised in respect of the July SSU, except those relating to Wholesale ADSL (**WDSL**) pricing, have been satisfactorily resolved. Although our Clients acknowledge that the SSU is an improvement on the July SSU, our Clients believe that it still falls well short of what is required. In light of this, the ACCC's comment quoted above gives rise to significant concern.

2. STRUCTURE OF THIS SUBMISSION

Following the executive summary in section 3 below, this submission provides comments on the test that the ACCC must apply when considering the SSU. The issues that our Clients believe prevent the ACCC from accepting the SSU are then set out. These issues relate to the following:

- The overarching commitment to equivalence[3]
- Price equivalence and transparency measures[4]
- Operational, systems, and technical equivalence[5]

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[1] The Previous Submission is dated 27 September 2011 and is available on the ACCC's website at: http://www.accc.gov.au/content/index.phtml/itemId/1005504.
[2] December Discussion Paper, p.5.
[3] This heading encompasses clause 9 of the SSU and related Schedules.
[4] This heading encompasses clause 18 of the SSU and related Schedules.
[5] This heading encompasses clauses 11, 13, 15, 16 and 17 of the SSU and related Schedules.

- Information equivalence[6]
- Access to Telstra Exchange Buildings and External Interconnect Facilities[7]
- Organisational arrangements within Telstra to support equivalence[8]
- Information security[9]
- Enforcement and dispute resolution[10]
- Implementation[11]

We note that unlike the August Discussion Paper, the December Discussion Paper does not request any submissions in respect of Telstra's migration plan. We trust that the points that were made in section 6 of the Previous Submission will be considered by the ACCC when it makes a decision on Telstra's migration plan.

Note that a reference in this submission to a clause or Schedule is a reference to a clause or Schedule of the SSU unless specified otherwise.

3. EXECUTIVE SUMMARY

Our Clients submit that the ACCC cannot accept the SSU without amendments that address the following problems:

(a) The SSU excludes *all* aspects of functional separation, which contradicts Telstra's requirement to give a commitment to the Equivalence Obligation.

(b) The overarching commitment to equivalence does not satisfy the requirement for Telstra to provide for transparency and equivalence under s 577A(3) of the *Telecommunications Act 1997* (**TA**) because:

(i) the scope of the obligations in clause 9(a) of the SSU are not broad enough;

(ii) many of the carve outs in clause 9(b) of the SSU are inconsistent with the equivalence obligations; and

(iii) the overarching commitment to equivalence needs to be given precedence in the event of any inconsistency between it and any other provision of Part D of the SSU.

(c) The price equivalence and transparency measures are inadequate because:

(i) the combined effect of clauses 9(b)(viii) and 18.3(e) is contrary to the Equivalence Obligation because (except in the case of the Wholesale ADSL Layer 2 Service) a wholesale customer may not

[6] This heading encompasses clause 14 of the SSU and related Schedules.
[7] This heading encompasses clause 12 of the SSU and related Schedules.
[8] This heading encompasses clause 8 of the SSU and related Schedules.
[9] This heading encompasses clause 10 of the SSU and related Schedules.
[10] This heading encompasses Schedule 11 and clauses 19 and 20 of the SSU and related Schedules.
[11] This heading encompasses clause 21 of the SSU and related Schedules..

be able to obtain the benefit of Rate Card pricing until a pre-existing contract has expired;

(ii) clause 1.2(c) of Schedule 8 relating to exemptions or exclusions contained in final access determinations or binding rules of conduct is inconsistent with the Equivalence Obligation and should be deleted;

(iii) no provision is made for future regulated services that are not declared services;

(iv) clause 2(a) of Schedule 8 has the potential effect of placing Telstra in a position to argue that any future price determination made by the ACCC with respect to TEBA charges is invalid, especially with respect to the access disputes regarding the Internal Interconnection Cable charge currently before the ACCC;

(v) Telstra's failure to ensure that TEBA terms are equivalent and transparent does not comply with s.577A(3)(a) and (b) of the TA; and

(vi) Telstra's WDSL terms fail to address issues raised in the consultation process, clearly indicating the need for WDSL to be declared.

(d) The operational, systems and technical equivalence measures are inadequate because:

(i) the Metrics relating to ULLS, LSS and DTCS are not fit for purpose, and the commitment given by Telstra in clause 16.5 is insufficient to remedy the problem; and

(ii) compliance with the Metrics could become an end in itself rather than the means to the end of achieving and demonstrating equivalence.

(e) The information equivalence provisions are not fit for purpose.

(f) Regarding the organisational arrangements within Telstra to support equivalence under clause 8 of the SSU:

(i) two concerns that were noted by the ACCC in the August Discussion Paper have not been satisfactorily addressed; and

(ii) many of the ring fencing provisions may end up being only of cosmetic effect.

(g) Regarding information security, the undertaking given in clause 10.5(a) should prevent Telstra Retail from being provided with the relevant information unless, with the approval of the ACCC, the relevant information is made available to Wholesale Customers at the same time.

(h) The enforcement and dispute resolution measures are inadequate because:

(i) Wholesale customers are prohibited from enforcing the SSU;

(ii) the threshold to trigger enforcement of the EOO Enforcement Mechanism or ITA Process is deceptively higher than it seems;

(iii) the relationship between the EOO Enforcement Mechanism and the Accelerated Investigation Process in clause 19 of the SSU is unclear;

(iv) the limitations on the ACCC's ability to issue a Rectification Direction make the EOO Enforcement Mechanism inappropriately weak; and

(v) the carve out to the EOO Enforcement Mechanism relating to Non-Regulated Price Equivalence is inappropriate.

(i) Section 577A(3)(a) of the TA clearly requires the Transparency and Equivalence Obligation to apply from when the SSU comes into force, however, clause 21 has the effect of delaying many of the commitments to equivalence and transparency.

4. THE TEST TO BE APPLIED WHEN CONSIDERING THE SSU

In the December Discussion Paper, the ACCC indicates that it intends to adopt the approach set out on pages 69-73 of the August Discussion Paper[12]. On pages 69 and 70 of the August Discussion Paper, the ACCC identifies the requirements of section 577A(3) of the TA as follows:

> *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* [**referred to below as the first limb of section 577A**]*; and*
> - *does so in an appropriate and effective manner* [**referred to below as the second limb of section 577A**].

It is submitted that the first limb of section 577A provides a threshold test so that regardless of the appropriateness or effectiveness of the measures contained in the SSU, the SSU cannot be accepted unless the scope of those measures correspond with the scope of the obligations referred to in the first limb of section 577A. This point is of crucial significance when considering the overarching commitment to equivalence[13] (see section 5 below).

As regards the second limb of section 577A, the ACCC states the following:[14]

> *The term "appropriate and effective" has not been defined in the legislation or supporting legislative materials. The meaning of a term such as this is however reasonably well understood as being informed by the subject matter, purpose, and scope of the statute in which it appears. In this case, the relevant statutory provisions were introduced as part of a policy to significantly promote competition*

[12] December Discussion Paper, p.6.
[13] Note that a reference in this submission to the 'overarching commitment to equivalence' is a reference to clause 9(a) of the SSU.
[14] August Discussion Paper, p.72.

> *and economic efficiency until structural separation is completed in markets that are dependent upon the Regulated Services as key inputs.*
>
> *Put in this context, appropriate and effective measures would result in significant improvements in access to Regulated Services that better allow Telstra's wholesale customers to compete on their respective merits against Telstra's retail business units in converting network access into downstream services throughout the interim period.*

Note that for ease of expression the obligation for Telstra to provide transparency and equivalence will be referred to as **the Transparency and Equivalence Obligation**. Also for ease of expression the transparency component will be referred to as **the Transparency Obligation** and the equivalence component will be referred to as **the Equivalence Obligation**.

We note that in the December Discussion Paper the ACCC states the following (footnotes omitted):[15]

> *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. 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.*

The Equivalence Obligation has a close relationship with functional separation. However, this relationship needs to be treated with care. The closeness of this relationship is demonstrated by the following passage in the Explanatory Memorandum to the *Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Bill 2010*[16] (emphasis added):

> *The proposed functional separation framework will be implemented through legislative amendment to the Telecommunications Act 1997 with more detailed requirements to be addressed by Telstra to be set out in a determination to be made by the Minister.*
>
> *Broadly, Telstra will be required to submit undertakings to the Minister concerning the implementation of functional separation, and ongoing commitments to functional separation. These undertakings will be contained in a draft Functional Separation Undertaking (FSU). Those undertakings must be directed at achieving key principles and objectives of functional separation and must include specific matters set out by the Minister in a requirements determination.* ***The key principles*** *of the new functional separation regime include:*
>
> - *Telstra to operate its network and wholesale functions at arm's-length from the rest of Telstra;*
> - ***non-Telstra wholesale customers to access regulated services on equivalent price and non-price terms and conditions as is provided to Telstra's retail unit****;*
> - *Telstra's retail unit to only be consulted on future products and future demand requirements at the same time and in the same way a non-Telstra access seeker is consulted; and*
> - *strong internal governance structures with transparency so that Telstra's competitors and the regulator can be confident that Telstra's retail unit is being treated the same as competitors.*

[15] December Discussion Paper, p.6.
[16] Explanatory Memorandum to the *Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Bill 2010*, p.26.

The fact that the Equivalence Obligation can be seen as being a key principle of functional separation is testament to the fact that there are different ways of implementing the Equivalence Obligation. The most direct way to implement the Equivalence Obligation would be by means of structural separation. The next most direct way would be by means of functional separation. However, it is crucial to appreciate that structural separation and functional separation go beyond the concept of 'equivalence' and into the concept of 'identicalness'. In other words 'identicalness' will always satisfy a requirement of 'equivalence' but a requirement of 'equivalence' can be satisfied without 'identicalness'. This fact is acknowledged in the Explanatory Statement to the *Telecommunications (Acceptance of Undertaking about Structural Separation—Matters) Instrument 2011* as follows[17]:

> *The transparency and equivalence measures are not intended to require Telstra to implement functional separation. Functional separation would, at a minimum, require Telstra's retail business units to use exactly the same access services on exactly the same terms and conditions and using the same systems and processes as its wholesale customers. It would also require a much stricter form of organisational separation than is intended under the interim transparency and equivalence measures.*

The distinction between 'equivalence' and 'identicalness' is best illustrated by way of a practical example as follows[18]. Telstra uses LOLO to process orders from wholesale customers. Telstra uses a different system to process orders from Telstra Retail (**the Telstra Retail System**). It takes two days to process an order through LOLO. It takes half a day to process an order through the Telstra Retail System. A standard of identicalness would not allow Telstra to use different systems as between wholesale customers and Telstra Retail. A standard of equivalence does allow Telstra to use different systems as between wholesale customers and Telstra Retail. However, the Equivalence Obligation would require LOLO to be upgraded so that it would be able to process orders in half a day[19].

This example illustrates that equivalence without identicalness is possible if the focus is on the outcome.

While we accept there is justification for the view that it is not intended that the Equivalence Obligation require functional separation, there is no support for the view that all individual aspects of functional separation are off limits. Indeed, if the passage in the explanatory memorandum to the *Telecommunications (Competition and Consumer Safeguards) Act 2010* quoted above is correct, the Equivalence Obligation itself is one of the key principles of functional separation. Therefore, it is contradictory to say that you can do both of the following:

- give a commitment to the Equivalence Obligation; and
- exclude all aspects of functional separation.

[17] Explanatory Statement to the *Telecommunications (Acceptance of Undertaking about Structural Separation—Matters) Instrument 2011*, p.2.

[18] Note this example is purely for illustrative purposes and is not intended to reflect the actual performance of LOLO as compared to the system used by Telstra Retail.

[19] Of course, if Telstra felt it would be cheaper and more effective to use one system rather than upgrade LOLO, it would be free to do so.

In light of this, we strongly agree with the following comment in the August Discussion Paper (footnotes omitted):[20]

> *In this regard, the Minister has stated that the requirement for interim transparency and equivalence measures was not intended to require Telstra to implement functional separation during this period. Functional separation would, at a minimum, require an "equivalence of input" standard and require a much stricter form of organisational separation than is intended under the interim transparency and equivalence measures. Functional separation involves more substantial investment by the incumbent in redesigning legacy systems. This is not to say that the interim measures cannot include other initiatives that might be a feature of a functional separation model which would be appropriate to apply during the interim period. That is, although functional separation is a different separation model to the model of structural separation, there should be no implication that any model proposed for the interim measures cannot include similar matters to those envisaged for functional separation.*

The relationship between functional separation and the Equivalence Obligation is relevant to the scope of Telstra's overarching Commitment to Equivalence (discussed in section 5 below).

5. TELSTRA'S OVERARCHING COMMITMENT TO EQUIVALENCE

While we acknowledge that clause 9(a) of the SSU does attempt to provide an overarching commitment to equivalence, its scope is not broad enough to satisfy the requirements of section 577A(3)(a) of the TA. We submit that the overarching commitment to equivalence does not satisfy the first limb of section 577A(3) because:

- even without the carve outs in clause 9(b) of the SSU, the scope of the obligations in clause 9(a) of the SSU are not broad enough to satisfy the first limb of section 577A(3);
- the carve outs in clause 9(b) (i), (iii), (v), (vi), (vii) and (viii) of the SSU are inconsistent with the obligations required by the first limb of section 577A(3); and
- the overarching commitment to equivalence needs to be given precedence in the event of any inconsistency between the overarching commitment to equivalence and any other provision of Part D of the SSU.

Accordingly, unless these defects are rectified, the ACCC cannot accept the SSU.

Further detail on each of these points is provided below.

[20] August Discussion Paper, pp.72-73.

5.1 Comparison of the requirements of the first limb of section 577A(3) and what is provided for in clause 9(a) of the SSU

This comparison is best done by means of the following table:

Issue	What the first limb of section 577A(3) requires	What clause 9(a) of the SSU provides
1.	transparency and equivalence in relation to the supply by Telstra of regulated services	the supply of Regulated Services to Wholesale Customers will be equivalent
2.	equivalence in relation to terms and conditions relating to price or a method of ascertaining price; and equivalence in relation to other terms and conditions[21]	equivalence only in relation to the matters specified in clause 9(a)(i) to (iv) which are dependent on there being a 'Comparable Retail Service'

As regards issue 1, although at first sight there does not appear to be a great deal of difference, the difference is in fact significant. It is submitted that the obligation '*in relation to the supply by Telstra of regulated services*' is wider because it applies not just to regulated services but also to ancillary services that are provided with the regulated services or are necessary for the supply of a regulated service. The ACCC applied a similar interpretation in determining that call diversion is a matter 'relating to' access to the ULLS. This approach was subsequently confirmed by the Federal Court.[22] This has recently been an issue for at least one of our Clients in recent contractual negotiations with Telstra, where Telstra refused to accept a requested amendment that acknowledged that a service which is necessary for the supply of a regulated declared service is 'related to' the supply of the regulated declared service. In order to avoid any inconsistency, the following clauses of the SSU (both of which carve out any obligations in respect of non regulated services) should be deleted:

- clause 7.3(e); and
- clause 9(b)(iii) (discussed in section 5.2 below).

As regards issue 2, the fact that the obligation in clause 9(a) is tied to 'Comparable Retail Services' means that the obligation in clause 9(a) is clearly much narrower in scope than the obligation contemplated in the first limb of section 577A(3). This has the potential to make the overarching commitment to equivalence one step removed from its true objective. For example, tying the overarching commitment to equivalence to specific 'Comparable Retail Services' could allow Telstra to avoid the overarching commitment to equivalence by introducing new retail services which are more favourable to Telstra Retail than the 'Comparable Retail Services'. In this situation Telstra would not be in breach of the overarching commitment to equivalence because it would still be providing wholesale services that are equivalent to the Comparable Retail Services. At the very least, the ACCC should be given an express power to vary or add to the list of Comparable Retail Services in order to deal with any such problems that could arise and to ensure that the overarching commitment to equivalence remains fit for purpose. This issue is also relevant to the service Metrics discussed in section 7.2 below.

[21] By virtue of the definition of equivalence in clause 69 of Division 1 of Part 9 of Schedule 1 to the TA.
[22] *Telstra Corporation Limited v Australian Competition and Consumer Commission* [2009] FCA 757

5.2 The carve outs

(a) Clause 9(b)(i)

Clause 9(b)(i) attempts to carve out all aspects of functional separation. As stated in section 4 above, the relationship between equivalence and functional separation needs to be treated with care. A desire to avoid functional separation should not be used as a justification for extensive carve outs being made to the overarching commitment to equivalence. Therefore, if a carve out preventing functional separation is felt to be necessary (note this is not an express requirement of the legislation), it should be in conjunctive terms and not disjunctive terms (i.e. it should prevent functional separation in its totality rather than individual aspects of functional separation).

(b) Clause 9(b)(iii)

Clause 9(b)(iii) provides that the overarching commitment to equivalence does not require Telstra to:

> *supply any service which is not a Regulated Service, or to supply a Regulated Service with any feature, functionality, application or content that is not included in the declared service description for that Regulated Service, or if the Wholesale ADSL Layer 2 Service is not a declared service, Telstra would not otherwise be required to supply by virtue of the undertakings given in clause 15;*

Clause 9(b)(iii) should be deleted for two reasons. Firstly, it prevents the overarching commitment to equivalence applying to ancillary services. In order to be acceptable, the SSU must contain an overarching commitment to equivalence that is applicable in respect of the full scope of the first limb of section 577A(3) (see section 4 above). Secondly, the reference to *'the declared service description for that Regulated Service or if the Wholesale ADSL Layer 2 Service is not a declared service*' wrongly assumes that the only possible regulated services are:

- those services that are declared under Part XIC of the Competition and Consumer Act 2010 (**CCA**); and
- the Wholesale ADSL Layer 2 Service.

This is clearly not correct. TEBA is also a regulated service to which the overarching commitment to equivalence should apply[23]. It is also possible for other regulated services that are not declared services to exist in the future - i.e. the Minister could exercise his power under section 71(4) of Schedule 1 of the TA again and determine that other services which have not been declared under Part XIC of the CCA are regulated services. The SSU should not contain provisions which prevent the overarching commitment to equivalence from applying to any such regulated services.

[23] See the *Telecommunications (Regulated Services) Determination (No. 1) 2011*.

(c) Clause 9(b)(v)

Clause 9(b)(v) provides that the overarching commitment to equivalence does not require:

> *in the case of a Non-Regulated Price Equivalence Issue, Telstra to do more than change the relevant price of the Regulated Service with effect from the date that Telstra notified the ACCC or the ACCC notified Telstra (as the case may be) of the possible breach in accordance with Schedule 11;*

Telstra should have an incentive to apply equivalent pricing in respect of all services to which the overarching commitment to equivalence applies from when that obligation first applies. If Telstra fails to fulfil this obligation, it should face appropriate consequences (including having to apply back dated charging). In light of this, the carve out in clause 9(b)(v) is inappropriate. This issue is also relevant to Schedule 11 (see section 11.5 below).

(d) Clause 9(b)(vi)

Clause 9(b)(vi) provides that the overarching commitment to equivalence does not require:

> *if the ACCC has not specified a price for the Wholesale ADSL Layer 2 Service in an access determination or binding rule of conduct, Telstra to change the price-related terms for that service other than to the extent that the RMRC methodology used by Telstra to set those price related terms does not comply with the Fixed RMRC Principles;*

Clause 9(b)(vi) should be deleted. The SSU must provide a commitment to the Equivalence Obligation in respect of all regulated services. The effect of clause 9(b)(vi) is to provide a commitment to something far weaker (i.e. ensuring that the RMRC methodology complies with the Fixed RMRC Principles).

(e) Clause 9(b)(vii)

Clause 9(b)(vii) provides that the overarching commitment to equivalence does not require Telstra:

> *to modify the TEM or any TEM Report other than as permitted by Schedule 9;*

As regards assessing whether Telstra is complying with the Equivalence Obligation, this cannot be done unless the 'terms and conditions' on which Telstra provides services to itself have been identified, disclosed and properly scrutinised. This is where the Transparency Obligation has work to do. The same reasoning that requires an overarching commitment to equivalence also requires an overarching commitment to transparency. In the August Discussion Paper, one of the reasons given for requiring an overarching commitment to equivalence was to ensure that Telstra's structural separation undertaking remained fit for purpose[24]. In light of this, a clause such as clause 9(b)(vii), which seeks to limit the ACCC's ability to

[24] August Discussion Paper, pp. 74 and 75.

ensure that the SSU remains fit for purpose in terms of providing for the Transparency Obligation, should be rejected.

(f) Clause 9(b)(viii)

Clause 9(b)(viii) provides that the overarching commitment to equivalence does not have the following effect:

> *requiring Telstra to supply a Wholesale Customer with a Regulated Service on price related terms which are inconsistent with any wholesale contract between Telstra and that Wholesale Customer in force as at the Commencement Date, provided that this does not limit the requirement for Telstra to comply with clause 18.3(c) if a Wholesale Customer supplied with the Wholesale ADSL Layer 2 Service under a contract in force at the Commencement Date has elected to acquire the Wholesale ADSL Layer 2 service at the Reference Price;*

Section 577A(3)(a) of the TA clearly requires the Transparency and Equivalence Obligation to apply from when the SSU comes into force[25]. In order to be consistent with this requirement, a wholesale customer should not be prevented from obtaining the benefit of equivalent pricing in respect of a regulated service simply because that regulated service is being provided under a pre-existing contract that provides for non equivalent pricing. Our Clients, and we expect the bulk of Telstra's wholesale customers, have existing agreements with Telstra for the supply of regulated services. Though the individual service schedules for each regulated service contain validity periods for price terms, the overarching agreement between Telstra and its wholesale customers[26] provides Telstra with the ability to rollover price terms and their validity periods, seemingly for as long as Telstra chooses. An SSU containing this carve-out therefore may potentially result in Telstra effectively having no price equivalence obligation because price terms in existing agreements are simply rolled over and remain in force. In light of this, it is submitted that section 577A(3)(a) of the TA prevents the ACCC from accepting a structural separation undertaking that contains clause 9(b)(viii). This issue is also relevant to clause 18.3 discussed in section 6.1 below and clause 21 discussed in section 12 below.

5.3 The overarching commitment needs to be given precedence

Given the potential for significant overlap between the overarching commitment to equivalence and other provisions in Part D of the SSU, in order to avoid any unnecessary disputation regarding the scope of the overarching commitment to equivalence, the SSU should contain a term which provides that in the event of any inconsistency between the overarching commitment to equivalence and another provision in Part D of the SSU, the overarching commitment to equivalence prevails.

6. PRICE EQUIVALENCE AND TRANSPARENCY MEASURES

Our clients have the following concerns relating to the price equivalence and transparency measures contained in the SSU:

[25] i.e. section 577A(3) refers to the period beginning 'when the undertaking comes into force'.
[26] Telstra's Customer Relationship Agreement Standard Terms.

- The combined effect of clause 9(b)(viii) and clause 18.3(e) is that, except in the case of the Wholesale ADSL Layer 2 Sevice, a wholesale customer may not be able to obtain the benefit of Rate Card pricing until a pre-existing contract has expired. This is contrary to the Equivalence Obligation.

- The carve out contained in clause 1.2(c) of Schedule 8 relating to exemptions or exclusions contained in final access determinations or binding rules of conduct is inconsistent with the Equivalence Obligation and should be deleted.

- No provision is made for future regulated services that are not declared services.

- Clause 2(a) of Schedule 8 has the potential effect of placing Telstra in a position to argue that any future price determination made by the ACCC with respect to TEBA charges is invalid, especially with respect to the access disputes regarding the Internal Interconnection Cable charge currently before the ACCC.

- The carve out in clause 2(c) of Schedule 8 that excludes TEBA pricing from the TEM Reports is inappropriate. Our Clients remain concerned that the SSU fails to ensure equivalent pricing for TEBA, unless the service is declared and the subject of regulated pricing. Telstra's failure to ensure that TEBA terms are equivalent and transparent does not comply with s.577A(3)(a) and (b) of the TA.

- Telstra's WDSL terms fail to address issues raised in the consultation process, clearly indicating the need for WDSL to be declared.

Each of these concerns are considered below.

6.1 The relationship between the Equivalence Obligation and pre-existing contracts

As stated in section 5.2 above (when considering clause 9(b)(viii)), section 577A(3)(a) of the TA clearly requires the Transparency and Equivalence Obligation to apply from when the SSU comes into force. In order to be consistent with this requirement, a wholesale customer should not be prevented from obtaining the benefit of equivalent pricing in respect of a regulated service simply because that regulated service is being provided under a pre-existing contract that provides for non equivalent pricing. The combined effect of clauses 9(b)(viii) and 18.3(e) is that, except in the case of the Wholesale ADSL Layer 2 Sevice, a wholesale customer may not be able to obtain the benefit of Rate Card pricing until a pre-existing contract has expired. This is clearly contrary to the Equivalence Obligation. In light of this, it is submitted that section 577A(3)(a) of the TA prevents the ACCC from accepting a structural separation undertaking that contains clauses 9(b)(viii) and 18.3(e). Accordingly, clauses 9(b)(viii) and 18.3(e) should be deleted and clause 18.3 should contain a clause that expressly allows a wholesale customer to obtain equivalent pricing notwithstanding the existence of a pre-existing contract. We note that clause 18.3(d) allows a wholesale customer to obtain equivalent pricing in respect of the Wholesale ADSL Layer 2 Service notwithstanding the existence of a pre-existing contract. However, clause 18.3(d) also expressly precludes the application of any equivalent non price terms and conditions. In light of this, we submit that clause 18.3(d) should also be deleted and replaced with the following:

> *If a Wholesale Customer acquires from Telstra a Regulated Service under a wholesale contract which exists as at the Commencement Date, that Wholesale Customer may elect to acquire the Regulate Service under that contract at the Reference Price by giving Telstra written notice within 3 months of the date of Telstra first publishing the Reference Price for the Regulated Service following the Commencement Date.*

6.2 The carve out in clause 1.2(c) of Schedule 8

Clause 1.2(c) of Schedule 8 provides:

> *Where pricing in an access determination or binding rule of conduct exists but does not apply in respect of any of the services listed in paragraph 1.1 supplied by Telstra by virtue of any exemption or exclusion provided for by the access determination or binding rule of conduct, the Reference Price for the relevant service will be equal to the charge as specified in the Wholesale Section of the Our Customer Terms or other price list published by Telstra on its website from time to time which Telstra makes available to Wholesale Customers as the commercial "list price" for that service.*

The Equivalence Obligation applies to all declared services and not just declared services which are subject to pricing in an access determination or binding rule of conduct. Therefore, even if the ACCC decided that the terms of an access determination or binding rule of conduct should not apply to a certain subset of a declared service (**Exempt Services**), this would not prevent the Equivalence Obligation from applying to all of the regulated services. It is nonsensical to say that an ACCC final access determination price and Telstra's rack price can both be the equivalent price for the same declared service. However, this is what clause 1.2(c) of Schedule 8 is attempting to do.

It is important to note that notwithstanding that the standard access obligations (**SAOs**) may be inapplicable to Exempt Services, Exempt Services still have the status of declared services under Part XIC of the CCA[27]. Therefore, Exempt Services come within the definition of 'regulated service' for the purposes of the Equivalence Obligation. Given that the legislature has deliberately chosen to define 'equivalence' and 'regulated service' in the way that it has, there is no scope for the ACCC to 'read down' the scope of the Equivalence Obligation by accepting an SSU that clearly and expressly attempts to carve out price equivalence from applying to regulated services simply because the SAOs do not apply.

Furthermore, even if such 'reading down' of the Equivalence Obligation were permissible, it is not appropriate to do so. The only possible justification for not including the Exempt Services within the scope of the Equivalence Obligation is the fact that the SAOs are inapplicable to the Exempt Services. It is submitted that this fact is of no relevance to the Equivalence Obligation. The fact that the statutory definition of 'regulated service' includes two services to which the SAOs do not apply[28], clearly shows that it was not intended that the reach of the Equivalence Obligation should be determined by the extent to which the SAOs apply. In light of this, there is no justification for not applying the Equivalence Obligation to a regulated service, or a subset of that regulated service, simply on the basis that the

[27] Clause 5 of the Final Access Determinations Nos.1 to 6 of 2011 for Fixed Line Services provides the current basis for the exemptions in respect of Wholesale Line Rental, Local Call Service and PSTN OA.

[28] i.e. Wholesale ADSL Layer 2 and Telstra Exchange Building Access - see *Telecommunications (Regulated Services) Determination (No.1) 2011*.

SAOs are inapplicable. The Equivalence Obligation is a specific legislative measure that is part of a wider reform of the industry. Therefore, the Equivalence Obligation is an entirely separate obligation from the obligation to comply with the SAOs, and it should be treated as such.

6.3 Future regulated services that are not declared services

The Transparency and Equivalence Obligation applies to regulated services. Regulated services comprise:

- those services that have been declared under Part XIC of the CCA; and
- those services that have been included in a determination made by the Minister under section 71(4) of Schedule 1 of the TA (currently WDSL and TEBA) (for ease of reference referred to as **Non Declared Regulated Services**).

Although clause 1.1 of Schedule 8 to the SSU contains a commitment to provide a Rate Card price for any future declared service, there is no similar commitment for future non declared regulated services. As the Equivalence Obligation applies to all regulated services and not just declared services, the SSU should contain such a commitment.

The importance of services becoming regulated is demonstrated by considering scenarios involving two important services supplied by Telstra. Firstly, external interconnection cabling ('EIC') into Telstra's exchange buildings and secondly, duct access.

Though the description of TEBA in clause 5 of the *Telecommunications (Regulated Services) Determination (No. 1) 2011* is broad enough to encompass an access seeker's EIC that connects to Telstra's facilities, it is not broad enough to require Telstra to provide access to NBN facilities installed in TEBA space. Telstra's SSU does not undertake to provide EIC access for NBN interconnection, and of course Telstra is not required to give this undertaking. Clearly, however, the need for this access will be vital and there is potential for it to become a regulated service.

Underground ducts are defined as 'eligible facilities' in Schedule 1 to the TA. Accordingly, Telstra is required to provide competitive access to its ducts on agreed terms. As raised by several parties in submissions on Telstra's first SSU, access seekers are concerned that Telstra will exercise its contractual right to evict competitors from Telstra's ducts at the end of licence periods in order to make room for NBN Co's cables. This is to Telstra's competitive advantage and further, the published summary of the agreement between NBN Co and Telstra strongly implies that Telstra in fact has an obligation to undertake this action to assist in facilitating the rollout of the NBN.

In both examples, there is reasonable potential for future regulation. Our Clients consider that Telstra's SSU needs to address this potential.

Furthermore, it is submitted that the price equivalence obligation has the most work to do in respect of Non Declared Regulated Services. This is because a declared regulated service is likely to have pricing determined by the ACCC. In order to avoid issues of the type that have arisen in relation to WDSL pricing (discussed below), it would make a great deal of sense for the SSU to give the ACCC an express power to determine terms for Non Declared Regulated Services.

6.4 Determination of Reference Price for TEBA

Clause 2(a) of Schedule 8 provides that the Reference Price for TEBA will be separate prices for the five activities or services listed under that clause, "*being Telstra's standard charges from time to time*". Our Clients submit that this clause has the potential effect of placing Telstra in a position to argue that any future price determination made by the ACCC with respect to TEBA charges is invalid.

This issue is best illustrated with the following example regarding the Internal Interconnection Cable (**IIC**) charge. Clause 2(a)(iv) of Schedule 8 provides that Telstra will publish a Reference Price for the IIC, which will be Telstra's standard charge for the IIC "*from time to time*". Clause 18.3(c) of the SSU provides:

> *Telstra undertakes that it will supply each of the Reference Services on the price terms:*
>
> *(i) set out in a Reference Price; or*
>
> *(ii) as otherwise agreed with a Wholesale Customer.*

The IIC, being captured within the definition of "TEBA services" under clause 2(a)(iv) of Schedule 8, may also therefore be considered a "Reference Service" by virtue of clause 18.2(a)(ii) of the SSU.

Along with a number of other access seekers, three of our four Clients have lodged access disputes that are currently being considered by the ACCC under the transitional provisions of the *Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Act 2010* (Cth), seeking a final determination to be made with respect to the IIC charge (**IIC Access Disputes**)[29]. The ACCC is yet to make a determination on these disputes. If the ACCC accepts Telstra's SSU in its current form and the SSU comes into force, it is likely that Telstra would argue that any subsequent determinations made by the ACCC in the IIC Access Disputes will be invalid by virtue of s 152ER of the CCA.

Section 152ER provides as follows:

> *(1) This section applies if an undertaking given by Telstra is in force under section 577A, 577C or 577E of the* Telecommunications Act 1997*.*
>
> *…*
>
> *(3) The Commission must not perform a function, or exercise a power, under this Part so as to prevent Telstra from complying with the undertaking.*

It is likely that Telstra would argue that it cannot comply with clause 18.3(c) of the SSU if the ACCC exercises its power to make final determinations in the IIC Access Disputes that are inconsistent with the Reference Price set by Telstra for the IIC.

Therefore, our Clients submit that clause 2 of Schedule 8 of the SSU should be amended so that the TEBA Reference Price must match any subsequent price determination made by the ACCC regarding that specific TEBA Reference Price. This could be amended by inserting into clause 2 a provision similar to clause 1.2(d) of Schedule 8, however making sure that Telstra must match *any* relevant price

[29] See the list of access disputes relating to the LSS and ULLS currently before the ACCC at: http://www.accc.gov.au/content/index.phtml/itemId/635059.

determination made by the ACCC, not just those made in an "access determination" or a "binding rule of conduct".[30]

6.5 The carve out in clause 2(c) of Schedule 8

Clause 2(c) of Schedule 8 provides:

> *For clarification, while TEBA Reference Prices will be included in the Rate Card, IWPs and EWPs are not required to be established or reported in the TEM Reports unless and until TEBA price-related terms are specified in a binding rule of conduct or access determination in accordance with paragraph 1.2(d).*

As stated above in section 5.2 when discussing clause 9(b)(vii), the same reasoning that requires an overarching commitment to equivalence also requires an overarching commitment to transparency[31]. It is submitted that there is little point in including TEBA Reference Prices if there is no way of being able to ascertain whether those reference prices are equivalent to the prices Telstra charges itself. It is submitted that given that TEBA is a regulated service to which the Equivalence and Transparency Obligation applies, the SSU must provide for a way in which to ascertain whether the reference prices that Telstra offers are equivalent to the prices Telstra is charging itself[32]. Therefore Telstra should be required to establish IWPs and EWPs in respect of TEBA.

6.6 WDSL

Our Clients agree very strongly that it is imperative for WDSL to be declared and subject to regulated terms, particularly in regards to price terms. Telstra's willingness to accept WDSL declaration is positive, however, our Clients agree with the ACCC's view that the SSU's proposed price equivalence arrangements that would apply when WDSL is not declared remain inadequate and weak. This supports the need for declaration but also emphasises Telstra's failure to ensure equivalence in its SSU.

Our Clients' concerns regarding the SSU's WDSL fixed RMRC principles include the following:

- The ACCC has previously stated that RMRC is an appropriate methodology.
- The Retail Price should not exclude enterprise and government services, which other carriage service providers will also wish to compete for.

Our Clients' concerns regarding the structure of the WDSL Reference Price include the following:

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[30] This is because any determination made by the ACCC in the IIC Access Disputes would not fall within the definition of "access determination" or "binding rule of conduct" as those terms are defined in the CCA.

[31] See August Discussion Paper, pp. 74 and 75 where the reason why an overarching commitment to equivalence was said to be required was to ensure that Telstra's structural separation undertaking remained fit for purpose.

[32] One of the things that the ACCC must consider is whether the SSU provides for measurable standards - see clause 4(g)(iii) of the *Telecommunications (Acceptance of Undertaking about Structural Separation - Matters) Instrument 2011*.

- The Rate Card should include a Reference Price for the Reportable Bundles listed in clause 4.1(a) of Schedule 9. In particular there should be a Reference Price for a bundle of WLR and WDSL. Bundling is a common and cost effective option that consumers prefer due to lower pricing and the convenience of a single bill. If the regulated WDSL price is only for a standalone ADSL product, it will remain unviable to compete with Telstra, as Telstra's retail prices for bundled Voice/ADSL2+ products are discounted significantly compared to its retail prices for the standalone ADSL2+ product. Our Clients do not consider that Telstra's proposal to include a proportion of bundling charges in the calculation of the Retail Price in the Fixed RMRC Principles[33] will address this issue to an appropriate degree. In these circumstances, where competitors only have access to a wholesale charge that is largely based upon the far more expensive standalone ADSL2+ plans, the current situation, where they simply cannot compete with Telstra, will remain unchanged. A clear indication of this is gained by simply comparing Telstra's retail ADSL2+ standalone plans with its retail Voice/ADSL2+ bundled plans. Telstra's standalone ADSL2+ retail plans are far more expensive than its bundled plans. As a result, if Telstra's SSU proposal is accepted and WDSL prices are largely based on Telstra's retail ADSL2+ standalone plans, WDSL prices will remain unreasonably high and competition will suffer. To provide equivalence, there must also be a reasonable and regulated price for a WLR/WDSL bundle in order for Telstra's undertaking to have a beneficial effect on competition.

  The importance of this is further emphasised when the NBN is taken into consideration, where basically the mantra will be 'whoever bundles, wins'. Firstly, bundled consumers will most likely simply be transposed to the NBN by the same service provider. However, if the consumer uses different service providers for broadband and phone, the consumer will choose between the service providers when their services are transposed to the NBN. Secondly, the NBN pricing structure is such that all services will be a broadband/voice bundle. It will be prohibitively expensive for a consumer to have a different service provider for each product. In the lead up to the NBN, it is vitally important that service providers can compete for the voice and broadband bundle on reasonable terms.

  Telstra does currently offer a WDSL/WLR bundle, though, to the knowledge of our Clients, only in limited geographic areas where there is or there is likely to be DSLAM based competition, i.e. Zone 1. The SSU does not include this bundling offer, meaning that acceptance of the SSU could result in an even worse environment for competition than already exists unless the parties enter into an agreement.

- Though Telstra has dropped the AGVC price from $65 to $55, it remains uncompetitively high and will inhibit competition for high bandwidth services such as IPTV. It is our Clients' firm view that it is economically unviable to attempt to compete with Telstra BigPond and provide IPTV over Telstra WDSL if such high AGVC costs are incurred.

- Telstra's Zone 1 and Zone 2 categories are based upon the existence or potential installation of DSLAMs in an exchange service area (**ESA**) rather than geographic designations. The two-tiered pricing structure, with higher

[33] Clause 3.1(b) of Schedule 8 to the SSU.

WDSL pricing in Zone 2 where there are no competitive DSLAMs inhibits competition in those ESAs. Telstra's ability to allocate any proportion of its Total Retail Costs to either Zone 1 or Zone 2 is arbitrary and appears designed to inhibit competition rather than actually reflect the cost of providing services in different geographic areas.[34]

- Telstra's forced bundling of the AGVC with WDSL is unreasonable, inhibits competition, and increases the price that end-users must pay for a broadband service. Allowing Telstra's WDSL customers to purchase backhaul services from other carriers would promote competition and drive down costs.

- There is no explanation regarding how the connection charge will be calculated, for instance, whether it will reflect contractor labour costs in a manner similar to the ACCC's determination of LSS and ULLS connection charges.

- The WDSL Reference Price will not be subject to any change where a Telstra retail ADSL price change results in a change of 5% or less of the headline monthly charge. There is no indication in the SSU as to whether the 5% is a cumulative or once off alteration. If this allows cumulative changes, then Telstra has the ability to reduce its retail charge several times but still not have to alter the Wholesale Reference Price. Even in the event that Telstra's intention is not to allow cumulative variations to its retail price to avoid corresponding variations in the wholesale price, a 5% variation gives Telstra an unreasonable and significant market advantage that should not be ignored if price equivalence is mandated.

- The Wholesale ADSL Reference Price will not be subject to change where a retail ADSL change only relates to products or plans targeting government and enterprise customers.[35] Wholesale customers should be able to compete with Telstra in this valuable market on reasonable terms. By avoiding this, the SSU is not providing equivalence.

- The Wholesale ADSL Reference Price will not be subject to change where it relates to customised or other specialised pricing that is not mass marketed.[36] Wholesale customers should be able to compete with and test new products on an equivalent basis to Telstra. Further the scope of this exception is very vague and has potential to allow Telstra to act anti-competitively but still be operating within the terms of its undertaking. For instance, the time period of a 'trial' and the size of a 'small group of customers' is not defined, unreasonably leaving both terms open to Telstra's interpretation.

- The Wholesale ADSL Reference Price will not be subject to change where it relates to 'bona fide short term discounts or promotional offers' that do not continue for over six months and are not the same as a promotional offer in the last six months.[37] Again, wholesale customers should be able to compete with and test new products in the same manner as Telstra. This option should not be solely in Telstra's camp, as it will result in competitors

[34] Section 3.4(c) of Schedule 8 to the SSU.
[35] Section 4.2(e) of Schedule 8 to the SSU.
[36] Section clause 4.2(d) of Schedule 8 to the SSU.
[37] Section 4.2(d) of Schedule 8 to the SSU.

appearing to lack innovation, which is not a good position in the communications industry. The six month time lag between promotional offers also provides Telstra the opportunity to ramp up its marketing in bursts prior to and during 'promotional offers', which is a practice that is quite common in various industries. Where a pattern of regular promotional offers or sales exists, consumers can simply wait for the next 'promotional' offer to come along before purchasing a new service or product, even if the next offer is not 'substantially' similar to the last.

- The ACCC's ability to commence a review of the WDSL reference price calculation is unreasonably limited. There should not be a 3 year period before a review can commence and it should not be limited to consideration of the SSU Guidance and economic principles.[38]

- The process in clause 5 of Schedule 8 to the SSU that provides for review of the Wholesale ADSL Reference Price should allow for the ACCC to make a final decision that is backdated to the date of notification referred to in sub clause 5.1 of Schedule 8 to the SSU. Clause 5.1 does not provide for a review to be finalised with any binding result unless it is by agreement between Telstra and the ACCC.

7. OPERATIONAL, SYSTEMS AND TECHNICAL EQUIVALENCE

Our Clients have the following concerns relating to operational, systems and technical equivalence:

- The Metrics relating to ULLS, LSS and DTCS are not fit for purpose, and the commitment given by Telstra in clause 16.5 is insufficient to remedy the problem.

- Compliance with the Metrics could become an end in itself rather than the means to the end of achieving and demonstrating equivalence.

7.1 Metrics relating to ULLS, LSS and DTCS

It appears that the Metrics are intended to satisfy two purposes as follows:

- to provide a reference point for the applicability of the service level rebates; and

- to provide a reference point which can act as the basis for a comparison between the treatment of wholesale customers and Telstra Retail.

The Metrics and reporting for ULLS, LSS and DTCS are not fit for purpose because they do not allow a comparison to be made between the treatment of wholesale customers and Telstra Retail. Although Telstra has provided a commitment in clause 16.5 to identify 'Common Retail/Wholesale Job Tasks', this commitment does not go far enough and is one step removed from what is required. Our Clients note the following statement in the December Discussion Paper:[39]

> *The ACCC considers measures are more likely to achieve this overall objective* [i.e. equivalence] *if they are simple and straightforward, can be implemented quickly,*

[38] Section 5 of Schedule 8 to the SSU.
[39] December Discussion Paper, p.6.

> *comprise genuine, tangible commitments, and are sufficiently documented and explained.*

In light of this our Clients believe that the commitment in clause 16.5 should clearly state that Telstra is committing itself to developing appropriate Metrics for ULLS, LSS and DTCS that will provide a measurable standard to determine whether ULLS, LSS and DTCS are being provided to wholesale customers in an equivalent manner as compared to Telstra Retail. Furthermore, given the requirement that these Metrics must be fit for purpose, the potential carve out in clause 16.5(a)(i) regarding the weighing of anticipated costs and benefits is not appropriate - i.e. measurable standards are mandatory, they are not negotiable[40].

7.2 Metrics could become an end in themselves rather than the means to the end of achieving and demonstrating equivalence

As many of the Metrics are tied to 'Comparable Retail Services' it could become possible for Telstra to satisfy the Metrics but still provide better treatment to Telstra Retail (for example if Telstra provides a better standard of service in respect of a service that is not a 'Comparable Retail Service'). In order to deal with this swiftly and appropriately, the ACCC should be given an express power to vary or add to the list of Comparable Retail Services and/or the Metrics.

8. INFORMATION EQUIVALENCE

Our Clients note the following comments in the August Discussion Paper as regards the July SSU:

> *One means of assessing the appropriateness of the measures is to consider whether they would provide information relevant to wholesale customers' ability to compete with Telstra on a fair and equal basis. The scope of Telstra's information equivalence measures appears to encompass matters relevant to delivery or operational quality of Regulated Services. The proposed notifications improve on Telstra's OSP, but there is potential for further improvements to provide a higher degree of assurance of equivalence. For example, where a change is initiated by the network services business unit (rather than at the request of a Telstra retail unit), Telstra could commit to providing equivalent notifications to wholesale customers and Telstra's retail business units.*
>
> *In this regard, the SSU and Telstra's supporting material do not make clear how the proposed network notifications in Schedule 4 compare to the information and notice period available to Telstra's retail business units.*

These comments remain applicable to the SSU. Given that information equivalence is identified in the legislative instruments as a particular subset of equivalence[41], unless the above quoted comments are addressed, it is difficult to see how it can be concluded that the information equivalence provisions are fit for purpose.

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[40] See clause 4(g)(iii) of the *Telecommunications (Acceptance of Undertaking about Structural Separation - Matters) Instrument 2011.*

[41] See clause 4(g)(v) of the *Telecommunications (Acceptance of Undertaking about Structural Separation - Matters) Instrument 2011.*

9. ORGANISATIONAL ARRANGEMENTS WITHIN TELSTRA TO SUPPORT EQUIVALENCE

Our clients have the following concerns relating to clause 8 of the SSU:

- two concerns that were noted by the ACCC in the August Discussion Paper have not been satisfactorily addressed; and
- many of the ring fencing provisions may end up being only of cosmetic effect.

Each of these concerns will be considered in turn.

9.1 Concerns expressed in the August Discussion Paper

In the August Discussion Paper, the ACCC expressed the following concerns:

- That the carve out relating to 'customer excellence' could have the potential to undermine Telstra's commitment to comply with the Transparency and Equivalence Obligation.[42]
- That the threshold for enforcement by the ACCC was too high[43].

Each of these issues will be considered in turn.

(a) <u>The carve out relating to customer excellence</u>

The carve out is contained in clause 8.9(b) which provides as follows:

> *Telstra will not be regarded as having breached this Undertaking if the bona fide efforts of an Employee to resolve a customer issue raised by a particular Retail Customer or Wholesale Customer (whether or not the issue was raised directly with that Employee) or which came to the attention of the Employee in the course of providing services to an end-user would otherwise be in breach of this Part D, provided that:*
>
> *(i) no breach of the rules about use of and access to Protected Information was involved; and*
>
> *(ii) any reward provided to the Employee for his or her conduct is provided as part of a Telstra policy of rewarding Employees who show similar initiative and excellence in customer service, whether for Retail Customers or Wholesale Customers.*

Clause 8.9(c) provides as follows:

> *For clarity, if an Employee who works for a Network Services Business Unit attends the premises of an end-user that is a customer of a Wholesale Customer or another CSP:*
>
> *(i) if the end-user is not also a Retail Customer, the Employee must not undertake any Marketing Activity to the end-user; and*
>
> *(ii) if the end-user is also a Retail Customer, the Employee must not undertake any "win back" or other Marketing Activity related to*

[42] August Discussion Paper, p.92.
[43] Ibid, p.93.

> *alternative Telstra products to the product or products supplied by that Wholesale Customer or other CSP to the end-user.*

It should be noted that clause 8.9(b) is not stated to be subject to clause 8.9(c). Therefore, it is possible for clause 8.9(b) to apply where a breach of clause 8.9(c) has occurred. This is unsatisfactory.

In the December Discussion Paper, the ACCC refers to Telstra's justification for the carve out for customer excellence, and to Telstra's claim that there are appropriate checks and balances that apply to this carve out[44]. These checks and balances are set out in a letter dated 25 August from Telstra to the ACCC. The checks and balances are stated to be as follows:[45]

> *[1] the conduct must not involve a breach of the information security commitments;*
>
> *[2] any incentive provided to the relevant employee for demonstrating customer excellence must be equally available regardless of whether the customer who is assisted is a retail or wholesale customer;*
>
> *[3] for field staff attending the premises of an end user that is not a retail customer of Telstra, the conduct must not involve marketing or selling Telstra products and services; and*
>
> *[4] for field staff attending the premises of an end user that is both a retail customer of Telstra and of a retail competitor, the conduct must not involve attempting to 'win-back' the customer.*

It is unclear why only 1 and 2 have been included as qualifiers to clause 8.9(b) but 3 and 4 have not but have instead been included in a separate clause. Given the issue identified above regarding the potential breach of clause 8.9(c) being excused by clause 8.9(b), either of the following is required:

- clause 8.9(b) should be made expressly subject to clause 8.9(c); or
- 3 and 4 above should be included in clause 8.9(b).

(b) <u>The threshold for enforcement</u>

The July SSU provided that a failure to comply with the requirements of clause 8 would not be a breach of the undertaking unless it was material, not an isolated incident and formed part of a demonstrable pattern of repeated non compliance[46]. Our client's acknowledge that this threshold has been substantially reduced. The threshold is now that the breach must not be 'trivial'[47]. For the following two reasons, it is submitted that there should not be any threshold. <u>Firstly</u>, what is or is not 'trivial' is by no means clear cut and is open to significant disputation. <u>Secondly</u>, a breach is a breach. While the extent of the breach may be relevant to whether the ACCC seeks to take any enforcement action, it should not be relevant to

[44] December Discussion Paper, p.12.
[45] Letter from Telstra to the ACCC dated 25 August 2011 at p.7 - available at: http://www.accc.gov.au/content/index.phtml/itemId/1003999.
[46] July SSU, clause 8.8.
[47] Clause 8.8(a) of the SSU.

whether or not a breach has occurred. It is submitted that the prohibition against frivolous or vexatious complaints in clause 8.8(b) gives sufficient protection to Telstra against any possible disproportionate consequences arising from 'trivial' breaches.

(c) The cosmetic effect of the ring fencing provisions

It is hard to escape the conclusion that the ring fencing provisions in the SSU amount to no more than tinkering with the existing operational separation provisions. Our Clients submit that an appropriate and effective measure that would promote equivalence, and that is related to the ring fencing provisions, would be for Telstra to allow access seekers to directly avail themselves of the services of Telstra's Network Business Unit for work that has a nexus to the supply or use of a regulated service[48], on a fee for service basis, with such fees being equivalent to the amount Telstra charges itself.

10. INFORMATION SECURITY

There is a drafting issue in clause 10.5. The undertaking given in clause 10.5(a) should not only apply in circumstances where Telstra Retail requests the relevant information (i.e. it is possible for Telstra Wholesale to initiate the giving of the relevant information). Therefore the undertaking given in clause 10.5(a) should prevent Telstra Retail from being provided with the relevant information unless, with the approval of the ACCC, the relevant information is made available to Wholesale Customers at the same time.

11. ENFORCEMENT AND DISPUTE RESOLUTION

As regards enforcement and dispute resolution, Telstra's past conduct shows that Telstra cannot be trusted to regulate itself, and that Telstra is not afraid of bringing unmeritorious legal proceedings to frustrate or intimidate its competitors and the regulator. This past conduct includes:

- engaging in anticompetitive conduct[49];
- a refusal to provide access seekers with ACCC indicative pricing voluntarily[50];
- unmeritorious legal challenges to ACCC arbitration decisions[51]; and
- an unmeritorious legal challenge to the constitutionality of the telecommunications access regime[52].

[48] For example, work related to the installation of a regulated service.
[49] This has resulted in the ACCC issuing eight competition notices to Telstra, and has also resulted in the ACCC taking Federal Court action against Telstra - see for example - *Australian Competition and Consumer Commission v Telstra Corporation Ltd* [2010] FCA 790.
[50] This contributed to the disproportionately high number of access disputes under the telecommunications access regime as compared to access regimes for other industries.
[51] See: *Telstra Corporation Limited v Australian Competition and Consumer Commission* (2008) 171 FCR 174; and *Telstra Corporation Limited v Australian Competition and Consumer Commission* (2009) 179 FCR 437.
[52] See *Telstra Corporation Limited v the Commonwealth* [2008] HCA 7.

In light of this, Telstra's commitment to equivalence should be subject to strong and swift enforcement and dispute resolution mechanisms. Note that for ease of expression the enforcement mechanism contained in Schedule 11 of the SSU will be referred to as the **EOO Enforcement Mechanism**.

Our Clients have the following concerns regarding enforcement and dispute resolution.

- Wholesale customers are prohibited from enforcing the SSU.
- The threshold to trigger enforcement of the EOO Enforcement Mechanism or ITA Process is deceptively higher than it seems.
- The relationship between the EOO Enforcement Mechanism and the Accelerated Investigation Process in clause 19 of the SSU (**AIP**) is unclear.
- The limitations on the ACCC's ability to issue a Rectification Direction make the EOO Enforcement Mechanism inappropriately weak.
- The carve out to the EOO Enforcement Mechanism relating to Non-Regulated Price Equivalence is inappropriate.

Each of these concerns will be considered below.

11.1 The prohibition on wholesale customers enforcing the SSU

Clause 7.4 of the SSU prevents wholesale customers from directly enforcing the SSU. Given that:

- the SSU is supposed to lead to a significant improvement on current arrangements[53]; and
- the SAOs can be directly enforced by an access seeker,[54]

this prohibition is inappropriate (i.e. enforcement of the Transparency and Equivalence Obligation should be more effective not less effective than enforcement of the SAOs).

11.2 The threshold to trigger enforcement of the EOO Enforcement Mechanism or ITA Process

Clause 1(b) of Schedule 11 to the SSU provides that Telstra will not be in breach of clause 9(a) in circumstances where the breach is 'trivial'. Clause 7.2(b)(i) provides that the ITA must not accept an equivalence complaint that relates to a 'trivial matter'. Clause 11.7(b) of the SSU provides that Telstra will not be in breach of clause 11 if the breach is 'trivial'. If the word 'trivial' is given its ordinary meaning, these provisions seem fairly innocuous. However, the word 'trivial' in the SSU has a defined meaning, and this meaning is capable of significantly reducing the effect of the Equivalence Obligation.

[53] See the comments in section 4 above regarding the second limb of section 577A.
[54] By virtue of section 152BB of the CCA.

In order to identify the defined meaning of the word 'trivial' and thereby appreciate the potential effect of the carve outs referred to in the previous paragraph, it is necessary to have regard to:

- clause 1(b) of Schedule 3; and
- the definition of 'Reporting Variance'.

Clause 1(b) of Schedule 3 provides:

> *Telstra's reported performance in respect of the Equivalence and Transparency Metrics set out in this Schedule 3 is not, and is not intended to be, determinative of any failure by Telstra to comply with the provisions of this Undertaking or the CCA. However, for the purposes of clause 11.7, paragraph 7.2(b) of Schedule 5 and paragraph 1(b) of Schedule 11, a Variance in Telstra's reported performance against an Equivalence and Transparency Metric which is not a Reporting Variance will be treated as trivial.*

The definition of Reporting Variance in the dictionary in Schedule 1 to the SSU is as follows:

> *Reporting Variance means, in respect of a relevant Metric, when the E&T Performance Result that is reported in the relevant Operational Equivalence Report shows a Variance of 2% or more (in negative terms):*
>
> *(a) in the case of Metrics 1–11 (inclusive), 17, 18 and 19 between performance levels for Wholesale Customers and for a Retail Business Unit; and*
>
> *(b) in the case of Metrics 12, 13, 14, 15, 16, 20 and 21, against the minimum percentage performance thresholds of the target Service Level which is specified in Schedule 3 for that Metric or if no minimum percentage performance threshold is specified for a Metric, it will be 90%.*

These provisions leave open the following potential argument for Telstra:

> *Where a breach of the Equivalence Obligation amounts to a failure to meet a Metric, that breach will be trivial unless it is of a magnitude that results in Telstra having to notify a Reporting Variance.*

Clearly, if this argument were to be accepted, it would drive a coach and horses through the enforcement and dispute resolution mechanisms. In order to avoid the potential of Telstra utilising this argument, the threshold requirements relating to 'trivial' breaches or matters should be deleted from the SSU.

11.3 The relationship between the EOO Enforcement Mechanism and the AIP

Clause 3.4(a)(i) of Schedule 11 provides as follows:

> *The ACCC must not: exercise the power to give notice under paragraph 3.1 of this Schedule 11 in circumstances where the possible breach relates to a complaint of a Wholesale Customer, unless the ACCC is satisfied that the Wholesale Customer has raised the complaint with Telstra and Telstra has been given a reasonable opportunity to investigate and take action in relation to the matters that are the subject of the complaint.*

This requires Telstra to be given an opportunity of investigating and taking action in respect of a wholesale customer complaint before the ACCC is able to invoke the EOO Enforcement Mechanism.

Under the AIP, a wholesale customer can be deemed to have accepted a Telstra rectification plan if the wholesale customer has not objected to that rectification plan within five Business Days of receiving it[55]. What is currently unclear is what effect, if any, such deemed acceptance would have on the wholesale customer's ability to request the ACCC to exercise its powers under Schedule 11 in respect of the same complaint. It is submitted that in order to avoid any unnecessary disputation, the SSU should contain an express clause that states that nothing in the AIP prevents the ACCC from exercising its powers under Schedule 11.

11.4 The limitations on the ACCC's ability to issue a Rectification Direction

There are four significant limitations on the ACCC's ability to issue a Rectification Direction under Schedule 11 that make the enforcement mechanism under clause 11 inappropriately weak:

- The ACCC is unable to issue a Rectification Direction unless Telstra has first submitted a Rectification Proposal. Where the ACCC notifies the possible breach, there is nothing to stop Telstra from simply refusing to submit a Rectification Proposal, thereby preventing the ACCC from issuing a Rectification Direction[56]. Putting Telstra in the position of controlling whether or not a Rectification Direction can be issued is clearly inappropriate.

- The inclusion of an award of compensation as part of a Rectification Direction is not permitted[57]. Any award of compensation must be enforced through the Courts. This is unwieldy and does not meet the requirement for swift enforcement.

- A Rectification Direction cannot have retrospective consequences[58]. This could arguably prevent any backdating in respect of non equivalent charges. The ACCC having a power to backdate is necessary in order to provide Telstra with an incentive to provide equivalent pricing.

- The requirement that a Rectification Direction impose the least cost solution[59]is too restrictive, as this will likely always favour Telstra and not necessarily result in the most appropriate solution. Considerations of this nature are best dealt with as part of the ACCC's 'proportionality' enquiry[60], which our Clients accept is an appropriate consideration.

11.5 The carve out in Schedule 11 relating to Non-Regulated Price Equivalence

Telstra should have an incentive to apply equivalent pricing in respect of all services to which the Equivalence Obligation applies. If Telstra fails to fulfil this obligation it should face appropriate consequences (including having to apply back dated

[55] See clause 19.3(e) of the SSU.
[56] i.e. clause 3.2(a) provides that Telstra *may* submit a Rectification Proposal. There is no obligation to do so. Unless Telstra submits a Rectification Proposal, the ACCC's power to issue a Rectification Direction under clause 3.2 of Schedule 11 will not be enlivened.
[57] See clause 6(a)(ii) of Schedule 11.
[58] See clause 6(a)(i) of Schedule 11.
[59] See clauses 5(a)(i) and (ii) and 5(b)(i) and (ii) of Schedule 11.
[60] See clause 5(a) of Schedule 11.

charging). In light of this, the carve out that relates to Non-Regulated Price Equivalence[61] is inappropriate.

12. IMPLEMENTATION

As discussed in sections 5.2 and 6.1 above, section 577A(3)(a) of the TA clearly requires the Transparency and Equivalence Obligation to apply from when the SSU comes into force[62]. This means that the ACCC cannot accept the SSU due to the fact that clause 21 has the effect of delaying many of the commitments to equivalence and transparency.

Herbert Geer Lawyers on behalf of:

Adam Internet Pty Ltd,
iiNet Limited,
Internode Pty Ltd, and
TransACT Communications Pty Ltd

13 January 2012

[61] See clauses 2.4(b), 3.4(b) and 4.1(c) of Schedule 11.
[62] i.e. section 577A(3) refers to the period beginning 'when the undertaking comes into force'.