ACCOUNTING SEPARATION OF TELSTRA:

IMPUTATION TESTING AND NON-PRICE TERMS AND CONDITIONS REPORT FOR THE DECEMBER QUARTER 2013

March 2014

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GLOSSARY AND ACRONYMS

ADSL	Asymmetric digital subscriber line is a digital technology that supports high speed services over conventional copper telephone lines. It is a high bandwidth downstream service (toward the customer) with a lower bandwidth upstream service.
FTM	Fixed to mobile
ISDN	The integrated services digital network is a network that has evolved from the PSTN. ISDN services enable end users to send and receive information at faster speeds and with greater reliability than is possible using the standard PSTN service.
KPI	Key performance indicator
LCS	The local carriage service is a service for local call resale. That is, the carriage of telephone calls from customer equipment at an end-user's premises to separately located customer equipment of an end-user in the same standard zone.
PSTN	The public switched telephone network is the standard fixed-line telephone network, used primarily for the supply of long-distance, fixed-to-mobile and mobile-to-fixed calls to end-users in Australia.
PSTN-O	PSTN originating access service
PSTN-T	PSTN terminating access service
RAF	Telecommunications industry regulatory accounting framework
RKR	Record-keeping rules are rules issued by the ACCC under s. 151BU of the *Competition and Consumer Act 2010* (formerly the *Trade Practices Act 1974*) that require carriers or carriage service providers to keep and retain records and to give any or all of the reports to the ACCC as required.
SIO	Services in operation
ULLS	The unconditioned local loop service involves the use of unconditioned lines (typically copper) between end-users and a telephone exchange, where the line terminates. This service enables the supply of advanced, high-speed data services to customers as well as local and long-distance voice services.
WACC	Weighted average cost of capital
WLR	Wholesale line rental

SUMMARY

The imputation and non-price terms and conditions reports are produced in accordance with a Direction issued by the Minister for Communications, Information Technology and the Arts on 19 June 2003, and Record Keeping Rules (RKR) issued by the ACCC.

The reports are intended to provide greater transparency of Telstra's operations and to assist the ACCC to monitor whether Telstra is unfairly discriminating between access seekers using its network and its own retail operations.

It is a requirement for the ACCC to publish this imputation and non-price terms and condition report pursuant to the Ministerial Direction (*Australian Competition and Consumer Commission (Accounting Separation – Telstra Corporation Limited) Direction (No. 1) 2003*).

On 28 February 2012, the ACCC accepted Telstra's Structural Separation Undertaking (SSU).

Under clause 16.2 of the SSU, it is a requirement for Telstra to report upon a number of Equivalency and Transparency (E&T) metrics related to the operational quality and standard of delivery of Regulated Services and the comparable retail services. Under clause 18.4 of the SSU, Telstra provides a report to the ACCC which sets out, for each quarter, the fully allocated costs, revenues and economic return associated with Reportable Wholesale Products and Reportable Retail Products. This report is derived from Telstra's internal financial reporting management system called the Telstra Economic Model (TEM). The TEM is used to calculate an External Wholesale Price (EWP) and Internal Wholesale Price (IWP) for each of the Reportable Wholesale Products and Reportable Product Bundles.

Telstra's reporting under the SSU (through the TEM and E&T metrics) is broadly comparable to the Accounting Separation regime. Accordingly, since the commencement of reporting under the SSU, the Accounting Separation regime has become less important.

In February 2014, the Department of Communications conducted a public consultation on the proposed repeal of the Accounting Separation Direction, and a decision concerning the future of the enhanced accounting separation regime is pending. If the Minister repeals the Direction, then it is open to the ACCC to consider revoking the RKRs made under the Direction. The ACCC's decision to consider revocation of the Accounting Separation RKRs is based on the view that the Accounting Separation Regime has been largely superseded by Telstra's SSU. The ACCC intends to make a decision to revoke the RKRs shortly after the Minister announces whether to revoke the Direction.

IMPUTATION TESTING

Telstra is required under the *Imputation Testing Record Keeping Rule* (Imputation RKR) to undertake quarterly imputation testing. Imputation testing adds up the costs of buying a wholesale service and transforming it into a retail service, and compares that figure with the retail price charged by Telstra. Telstra is determined to have passed the imputation test if the retail price is sufficiently high so as to provide a margin between it and the combined wholesale and transformation costs.

The primary objective of imputation testing is to examine whether an equally efficient access seeker can compete with Telstra in retail telecommunications markets. This provides preliminary indications of whether Telstra is engaging in systematic price-squeeze behaviour in relation to its core telecommunications services.

A negative imputation margin could indicate Telstra is engaging in anti-competitive behaviour (e.g. a price squeeze) against its retail competitors. However, a negative margin, on its own, is not sufficient to determine whether anti-competitive behaviour is occurring. There may be other reasons why Telstra fails an imputation test that are not related to anti-competitive behaviour. For example, an increase in competition that drives down retail prices could cause a negative result for an imputation margin. There may also be reasonable explanations for increases in costs that could contribute to a negative result.

Imputation testing has been undertaken for the following retail services: local calls and line rental, domestic and international long-distance calls, fixed-to-mobile calls and ADSL services (both stand-alone and bundled). Imputation testing concerns the retail services supplied using certain regulated access services: unconditioned local loop services (ULLS), public switched telephone network originating and terminating access services (PSTN OTA) and local carriage services (LCS).

Key findings for the December 2013 quarter are:

- The results were broadly consistent with the previous September 2013 quarter results.
- Telstra passed 11 out of 15 imputation tests.
- Margins for local calls and line rental services for both residential and business customers remain negative.
- Margins for both standalone ADSL services and bundle of ADSL and fixed voice service for residential customers continue to remain negative.

NON-PRICE TERMS AND CONDITIONS KEY PERFORMANCE INDICATORS

The non-price terms and conditions section of this report measures Telstra's relative performance in provisioning services, fixing faults, and keeping appointments for retail and wholesale basic access and ADSL customers. Performance is assessed against the Customer Service Guarantee standards or similar measures.

The overall results do not provide any evidence of systemic discrimination by Telstra against access seekers in respect of performance.

That said, Telstra continues to report a negative variance for the rectification of residential basic access faults. In the December 2013 quarter, Telstra reported a variance of -3.09 per cent for this metric, a slight deterioration from the negative variance reported for the September 2013 quarter.

1. INTRODUCTION

On 19 June 2003, the Minister for Communications, Information Technology and the Arts directed the ACCC to use its record keeping rule (RKR) making powers under the *Trade Practices Act 1974*, (now the *Competition and Consumer Act 2010* (the Act)) to introduce enhanced accounting separation of Telstra.

In accordance with this direction, the ACCC issued RKRs requiring Telstra to provide the ACCC with reports on:

- regulatory accounting statements that have been prepared on a current cost basis, in addition to reports prepared on a historical cost basis, under the Telecommunications Industry Regulatory Accounting Framework (RAF) for core services (CCA reports)
- imputation analysis comparing Telstra's retail prices and the costs faced by access seekers in purchasing core services from Telstra to supply competing retail services (imputation reports)
- key performance indicators on non-price terms and conditions that compare Telstra's customer service performance between specified retail and wholesale supplied services (NPTC reports).

The direction also requires that the ACCC publish the reports and a commentary which discusses the accuracy of the reports and the extent to which the reports comply with:

- the regulatory accounting framework (for the imputation report only)
- any other relevant record-keeping rules made by the ACCC
- any direction given by the ACCC for Telstra to make public information contained in the reports.

The comments are to include any qualifications that the ACCC considers necessary. The ACCC must also summarise the results of the imputation analysis.

1.1 PURPOSE OF THE REPORTS

The purpose in establishing the enhanced accounting separation framework for Telstra is to provide the ACCC, access seekers and the public with greater transparency with respect to Telstra's wholesale and retail costs.[1]

This is intended to assist the ACCC in investigating conduct that may breach Part IV (restrictive trade practices) or Part XIB (the telecommunications industry: anti-competitive conduct and record-keeping rules) of the Act. This would include conduct such as predatory pricing, margin squeezing, cross-subsidisation and vertical cost shifting.[2] In such investigations, it is important to be able to carefully distinguish between wholesale costs and retail costs.

1.2 LIMITATIONS OF THE REPORTS

It should be noted that there are limitations associated with the information published in this report. In particular, the information captured under these arrangements is highly aggregated and can hide specific instances of anti-competitive behaviour. Further, accounting separation requires only a notional allocation of costs across wholesale and retail operations, and therefore does not contribute greatly to detecting and remedying specific occurrences of anti-competitive conduct. As a result, it does not completely remove incentives for Telstra to favour its retail operations. It does not compel Telstra to ensure that it consistently applies equivalent treatment of its wholesale and retail customers in the normal course of business.

[1]Department of Communications, Information Technology and the Arts, *Draft Direction on Telstra's accounting separation issued for public comment*, media release, 19 March 2003.

[2]See ACCC*, Current cost methodology for Telstra's subsequent reports under the accounting separation regime*, *framework document*, January 2004, pp. 8–9.

2. IMPUTATION REPORT

2.1 INTRODUCTION TO THE IMPUTATION RKR

This section presents the analysis of the imputation results of Telstra for the following residential and business services: local call and line rental; domestic and international long distance; fixed-to-mobile; the total bundle of fixed voice services; ADSL; and the total bundle of fixed voice and ADSL services. The imputation tests are conducted in accordance with an ACCC record keeping rule issued in September 2004.[3]

Imputation results based upon both historical and current cost are presented in the report. However, the analysis in the report focuses on the historical cost results. There is generally little difference between the imputation results based on historical cost and current cost measures.

The primary objective of the reports provided under the imputation RKR is to indicate whether Telstra is engaging in systematic price squeeze behaviour in relation to core telecommunications services.[4]

2.2 BACKGROUND

2.2.1 VERTICAL PRICE SQUEEZING

Telstra is a vertically integrated carrier that owns the delivery platform from which its services are supplied. Telstra supplies retail telecommunications services to end-users and wholesale access services to competing retail suppliers. For many telephony services, Telstra's retail competitors rely on wholesale supply from Telstra, such as access to the 'local loop' (such as origination and termination on the PSTN). The competitors then add network services (e.g. long-distance transmission for long-distance calls) and additional services to transform the core input into the retail service (e.g. billing or call centre support).

A vertical price squeeze may occur if Telstra reduces the margin between its price for a retail service, and the wholesale access price it charges for an essential input to that retail service. Telstra could reduce the margin by lowering the retail price for the service, raising the wholesale access price for the essential input, or doing both.

If the difference between the retail price and the wholesale access price is not sufficient to cover Telstra's network transformation and retail costs of supply, competitors who are equally efficient as Telstra in the supply of the retail services may not be able to remain in the market, because their profit margins would be negative. Imputation testing can therefore be used as a first step in detecting possible price squeezes in the retail market.

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[3] An earlier made RKR was revoked at this time as the data that was available to Telstra did not allow it to be fully implemented.

[4] Senator Richard Alston, *Government boost to telecommunications competition*, media release, 24 September 2002.

2.2.2 WHAT ARE THE ELEMENTS OF AN IMPUTATION TEST?

An imputation test compares:

- the price charged by Telstra for a particular retail service it supplies, and by other retail service providers who wish to supply the same retail service using Telstra's network.
- the wholesale price charged by Telstra for access to its network, plus the additional costs incurred by Telstra, in transforming the essential input into the retail service.

Where the retail price is less than the sum of the wholesale access price and additional costs, the imputed margin is negative, which may indicate potential anti-competitive behaviour by Telstra.

2.2.3 LIMITATIONS OF IMPUTATION TEST RESULTS

The objective of imputation testing is to indicate whether Telstra is engaging in systemic price squeeze behaviour in relation to core telecommunications services.[5] However, a 'fail' result for an imputation test does not exclusively determine that Telstra has engaged in such behaviour.

There are a number of limitations of the imputation testing including:

- the imputation tests require allocations of common costs across wholesale and retail operations and across services. These can be arbitrary in nature.
- the costs of transformation reported under imputation testing are those of Telstra and are on an average basis. Access seekers targeting niche segments of the market may have lower costs of transformation.
- In addition to the level of access price charged by Telstra, the likelihood of an access seeker successfully competing with Telstra is influenced by its own efficiency as well as service quality and differentiation.
- the data is highly aggregated on a national basis and may not identify particular examples of price squeeze behaviour. The aggregated data may also hide that some access seekers may only target certain high value customers or may operate in lower cost areas.
- the imputation RKR uses average total cost in calculating the retail price as well as the cost of transforming Telstra's core service into a retail service. A retailer targeting niche services or customers may be able to make a profit in providing a service even where the imputation margin is negative.
- the bundles of fixed voice and fixed voice and ADSL services are notional bundles which are derived from the fixed-voice and ADSL data. These bundles may not accurately represent the bundles bought by consumers.

In addition there are certain data limitations. For example, imputation testing is conducted using cost data from the last available half-year Regulatory Accounting Framework report. This means that in the results for this December quarter 2013 imputation report, the unit cost data was obtained from the RAF data for the period January to June 2013. Further limitations of the data are examined in sections 2.6 and 2.7. Accepting these limitations, the ACCC considers that the principles on which these imputation tests are based are sound, and whilst imputation testing may provide an indicator of possible price squeezing behaviour, they cannot be solely relied upon.

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[5] Senator Richard Alston, *Government boost to telecommunications competition*, media release, 24 September 2002.

2.3 THE IMPUTATION TESTS IN THIS REPORT

In this report, imputation testing is conducted on the following retail services that use Telstra's core telecommunications services as inputs:

- local calls and line rental, which use the local carriage service (LCS)
- domestic long-distance calls, which use the public switched telephone network originating/terminating access (PSTN-O/T) services
- outgoing international calls, which use the public switched telephone network originating access (PSTN-O) services
- fixed-to-mobile calls, which use the PSTN-O services
- ADSL services, which use the unbundled local loop service (ULLS).

There are three main variables in an imputation test:

- the 'retail price' - the average retail price of each retail service, calculated by using the total revenue and volume data provided by Telstra
- the 'access price' - the volume-weighted average of the prices Telstra charges its access seekers for the underlying core service in relation to the retail service, and
- the 'unit cost' - the average total cost of transforming the core service into the relevant retail service.

The imputation RKR details how each variable is calculated. The results are presented in Tables 2.1 to 2.6 of this report.

Costs are derived from Telstra's reports under the RAF, which requires the allocation of direct and common costs across Telstra's services.

The costs attributed to 'retail services' in the RAF are the 'retail costs' used for the imputation tests. However, there are further costs incurred in transforming a core service to a retail service, such as the transmission costs. These are included under 'other costs' in the imputation results. The tests also separate out the cost of capital (i.e. the cost of holding the capital assets necessary to transform the core services) and ancillary charges (e.g. charges for access to Telstra's exchange).

The sum of the 'retail costs', 'other costs', 'ancillary charges' and 'cost of capital' per unit of retail service is the 'unit cost'.

The imputation RKR requires Telstra to provide data calculated on both a historical cost accounting basis and a current cost accounting basis.[6]

[6] Under current cost accounting reporting, assets and liabilities are valued based on replacement costs, which are the present-day costs of acquiring an identical or substantially similar asset that could provide equivalent services and capacity as the existing asset. Replacement costs are based on current market values and current technology.

The ACCC and Telstra have agreed to certain procedures for addressing methodological issues about costs, as outlined in section 2.7.

The imputed margin for each retail service can then be calculated as follows:

- The 'imputed margin' is calculated by subtracting the 'access price' and 'unit cost' from the 'retail price' for each retail service. This 'imputed margin' (in dollar terms) represents the profit margin that could be available to Telstra's competitors in the retail markets, who are equally efficient as Telstra, if they supply the retail service to their customers using Telstra's core service.[7]
- The 'imputed margin' is further expressed as a percentage of the retail price.

2.4 RESULTS SUBMITTED BY TELSTRA

2.4.1 CURRENT QUARTER RESULTS

In accordance with the ACCC's imputation testing RKRs, Telstra has submitted imputation reports in relation to the December 2013 quarter for both fixed-line voice telephony services and ADSL services. These reports are shown in the following Tables 2.1 to 2.6. Separate reports are presented based on historical accounting costs and current accounting costs.

[7] As noted above, this margin is calculated after a contribution is made to 'common costs', that is, costs that are shared among multiple services.

TABLE 2.1 FIXED TELEPHONY REPORT FOR DECEMBER 2013 QUARTER ON HISTORIC COST BASIS

	Local carriage service		Domestic PSTN originating and terminating access services		Domestic PSTN originating access service				Total Bundle of Fixed Voice Products		
	Local calls and Line rental		Domestic long distance		International long distance		Fixed to mobile		Bundle		
	Business	Residential	Business	Residential	Business	Residential	Business	Residential	Business	Residential	Total
Revenues											
Retail	191,795,192	381,080,864	18,111,169	63,984,100	2,251,047	14,788,701	50,735,394	88,797,637	262,892,802	548,651,302	811,544,104
Other	0	0	0	0	0	0	0	0	0	0	0
Total	191,795,192	381,080,864	18,111,169	63,984,100	2,251,047	14,788,701	50,735,394	88,797,637	262,892,802	548,651,302	811,544,104
Retail Costs											
organisation	14,125,909	33,037,257	972,710	3,679,450	40,548	687,100	2,071,500	3,509,981	17,210,666	40,913,788	58,124,454
product and consumer	22,311,633	51,974,059	1,854,409	7,014,636	607,312	10,291,122	13,019,388	22,060,254	37,792,742	91,340,070	129,132,812
Total	36,437,541	85,011,315	2,827,118	10,694,086	647,860	10,978,222	15,090,888	25,570,235	55,003,408	132,253,858	187,257,266
Other Costs											
organisation	0	0	482,128	1,823,738	9,064	153,601	-35,045	-59,381	456,148	1,917,958	2,374,106
product and consumer	0	0	50,220	189,965	1,470	24,905	-8,773	-14,865	42,917	200,006	242,922
network expenses	0	0	974,772	3,687,250	21,040	356,522	-92,512	-156,754	903,299	3,887,018	4,790,317
Total	0	0	1,507,120	5,700,953	31,574	535,028	-136,330	-230,999	1,402,364	6,004,982	7,407,346
Ancillary*	N/A	N/A	199,972	756,430	4,624	78,364	123,663	209,536	328,259	1,044,330	1,372,589
Cost of Capital	6,612,187	15,518,826	721,340	2,728,599	63,354	1,073,551	1,378,948	2,336,510	8,775,828	21,657,486	30,433,314
Retail Volume*	1,907,606	4,563,982	161,554,444	611,108,912	7,472,132	126,617,956	199,811,196	338,563,186			
Retail price	$100.542	$83.497	$0.112	$0.105	$0.3013	$0.1168	$0.2539	$0.2623	$137.8129	$120.2133	$125.4011
Access price	$83.124	$71.385	$0.019	$0.019	$0.0094	$0.0094	$0.0097	$0.0095	$85.7788	$74.8652	$78.0822
Unit cost	$22.567	$22.027	$0.033	$0.033	$0.1000	$0.1000	$0.0824	$0.0824	$34.3414	$35.2676	$34.9946
Imputed margin	-$5.149	-$9.914	$0.061	$0.053	$0.1918	$0.0074	$0.1619	$0.1704	$17.6927	$10.0805	$12.3243
Imputed margin %	-5.12%	-11.87%	54.08%	50.99%	63.68%	6.35%	63.75%	64.97%	12.84%	8.39%	9.83%

TABLE 2.2: FIXED TELEPHONY REPORT FOR DECEMBER 2013 QUARTER ON CURRENT COST BASIS

	Local carriage service		Domestic PSTN originating and terminating access services		Domestic PSTN originating access service				Total Bundle of Fixed Voice Products		
	Local calls and Line rental		Domestic long distance		International long distance		Fixed to mobile		Bundle		
	Business	Residential	Business	Residential	Business	Residential	Business	Residential	Business	Residential	Total
Revenues											
retail	191,795,192	381,080,864	18,111,169	63,984,100	2,251,047	14,788,701	50,735,394	88,797,637	262,892,802	548,651,302	811,544,104
other	0	0	0	0	0	0	0	0	0	0	0
total	191,795,192	381,080,864	18,111,169	63,984,100	2,251,047	14,788,701	50,735,394	88,797,637	262,892,802	548,651,302	811,544,104
Retail Costs											
organisation	13,776,517	32,219,198	948,620	3,588,326	39,006	660,970	2,021,073	3,424,537	16,785,216	39,893,030	56,678,246
product and consumer	22,303,408	51,954,803	1,853,841	7,012,491	607,276	10,290,507	13,018,201	22,058,242	37,782,727	91,316,043	129,098,770
total	36,079,926	84,174,001	2,802,461	10,600,816	646,282	10,951,477	15,039,274	25,482,779	54,567,943	131,209,073	185,777,016
Other Costs											
organisation	0	0	453,233	1,714,437	8,446	143,114	-33,571	-56,883	428,108	1,800,667	2,228,775
product and consumer	0	0	49,539	187,392	1,455	24,658	-8,738	-14,806	42,256	197,244	239,501
network expenses	0	0	974,770	3,687,245	21,040	356,522	-92,512	-156,753	903,298	3,887,014	4,790,313
total	0	0	1,477,543	5,589,074	30,940	524,294	-134,821	-228,442	1,373,663	5,884,926	7,258,588
Ancillary*	N/A	N/A	199,972	756,430	4,624	78,364	123,663	209,536	328,259	1,044,330	1,372,589
Cost of Capital	6,521,913	15,307,460	687,841	2,601,884	62,326	1,056,133	1,394,532	2,362,916	8,666,612	21,328,393	29,995,004
Retail Volume*	1,907,606	4,563,982	161,554,444	611,108,912	7,472,132	126,617,956	199,811,196	338,563,186			
Retail price	$100.542	$83.497	$0.112	$0.105	$0.3013	$0.1168	$0.2539	$0.2623	$137.8129	$120.2133	$125.4011
Access price	$83.124	$71.385	$0.019	$0.019	$0.0094	$0.0094	$0.0097	$0.0095	$85.7788	$74.8652	$78.0822
Unit cost	$22.333	$21.797	$0.032	$0.032	$0.0996	$0.0996	$0.0822	$0.0822	$34.0408	$34.9403	$34.6751
Imputed margin	-$4.914	-$9.684	$0.061	$0.054	$0.1923	$0.0079	$0.1621	$0.1706	$17.9933	$10.4078	$12.6438
Imputed margin %	-4.89%	-11.60%	54.57%	51.51%	63.82%	6.72%	63.82%	65.03%	13.06%	8.66%	10.08%

Notes to Tables 2.1 and 2.2

* All retail volumes are reported in minutes with the exception of the local carriage service where volumes are in SIOs.

TABLE 2.3 ULLS REPORT FOR DECEMBER 2013 QUARTER ON HISTORIC COST BASIS

	Unconditioned Local Loop Service		Unconditioned Local Loop Service	
	ADSL Service		ADSL, local calls, line rental, domestic long distance, international and fixed to mobile	
	Business	Residential	Business - 1 x ADSL Service + 4 x Voice Lines	Residential - 1 x ADSL Service + 1 x Voice Lines
Revenues				
retail	63,390,487	279,363,077	193,709,508	498,251,247
other	0	0	0	0
total	63,390,487	279,363,077	193,709,508	498,251,247
Retail Costs				
organisation	2,849,142	21,944,515	11,380,669	38,267,349
product and consumer	5,549,741	42,744,936	24,284,043	79,185,678
total	8,398,883	64,689,451	35,664,713	117,453,027
Other Costs				
organisation	9,050,950	69,711,767	11,870,900	77,479,737
product and consumer	1,119,538	8,622,846	6,999,822	19,413,314
network expenses	15,538,259	119,677,988	39,852,243	167,922,280
total	25,708,747	198,012,600	58,722,965	264,815,331
Ancillary Charges (TEBA)	1,148,349	8,844,757	1,189,030	9,261,399
Cost of Capital	8,083,766	62,262,370	32,101,301	109,260,463
Retail Volume	236,406	1,820,832	236,406	1,820,832
Retail price	$268.1428	$153.4261	$819.3945	$273.6394
Access price	$51.9984	$51.9984	$66.2484	$56.4319
Unit cost	$183.3279	$183.3279	$540.0802	$275.0338
Imputed margin	$32.8166	-$81.9002	$213.0659	-$57.8263
Imputed margin %	12.24%	-53.38%	26.00%	-21.13%

TABLE 2.4 ULLS REPORT FOR DECEMBER 2013 QUARTER ON CURRENT COST BASIS

	Unconditioned Local Loop Service		Unconditioned Local Loop Service	
	ADSL Service		ADSL, local calls, line rental, domestic long distance, international and fixed to mobile	
	Business	Residential	Business - 1 x ADSL Service + 4 x Voice Lines	Residential - 1 x ADSL Service + 1 x Voice Lines
Revenues				
retail	63,390,487	279,363,077	193,709,508	498,251,247
other	0	0	0	0
total	63,390,487	279,363,077	193,709,508	498,251,247
Retail Costs				
organisation	2,780,384	21,414,934	11,101,011	37,330,530
product and consumer	5,548,192	42,733,004	24,277,530	79,164,161
total	8,328,577	64,147,937	35,378,541	116,494,690
Other Costs				
organisation	8,992,450	69,261,188	13,591,792	80,129,584
product and consumer	1,118,158	8,612,218	7,040,332	19,475,669
network expenses	15,538,222	119,677,701	39,852,262	167,922,100
total	25,648,830	197,551,108	60,484,386	267,527,353
Ancillary Charges (TEBA)	1,148,349	8,844,757	1,189,030	9,261,399
Cost of Capital	4,866,349	37,481,345	46,223,469	118,583,131
Retail Volume	236,406	1,820,832	236,406	1,820,832
Retail price	$268.1428	$153.4261	$819.3945	$273.6394
Access price	$51.9984	$51.9984	$66.2484	$56.4319
Unit cost	$169.1673	$169.1673	$606.0575	$281.1169
Imputed margin	$46.9771	-$67.7396	$147.0886	-$63.9095
Imputed margin %	17.52%	-44.15%	17.95%	-23.36%

Notes to Tables 2.3 and 2.4

* As per instructions from the ACCC, ancillary charges are calculated as TEBA revenues per ULL service that are reasonably expected in a mature market. This is calculated as the TEBA revenue for the December quarter divided by the adjusted number of installed tie cable pairs. The adjustment factor set by the ACCC is 66%.

**Retail volumes are reported in terms of SIOs.

TABLE 2.5 ADJUSTED ULLS REPORT FOR DECEMBER 2013 QUARTER ON HISTORIC COST BASIS

	Unconditioned Local Loop Service		Unconditioned Local Loop Service	
	ADSL Service		ADSL, local calls, line rental, domestic long distance, international and fixed to mobile	
	Business	Residential	Business - 1 x ADSL Service + 4 x Voice Lines	Residential - 1 x ADSL Service + 1 x Voice Lines
Revenues				
retail	63,390,487	279,363,077	193,709,508	498,251,247
other	0	0	0	0
total	63,390,487	279,363,077	193,709,508	498,251,247
Retail Costs				
organisation	2,849,142	21,944,515	11,380,669	38,267,349
product and consumer	5,549,741	42,744,936	24,284,043	79,185,678
total	8,398,883	64,689,451	35,664,713	117,453,027
Other Costs				
organisation	9,050,950	69,711,767	11,870,900	77,479,737
product and consumer	1,119,538	8,622,846	6,999,822	19,413,314
network expenses	15,538,259	119,677,988	39,852,243	167,922,280
total	25,708,747	198,012,600	58,722,965	264,815,331
Ancillary Charges (TEBA)	1,148,349	8,844,757	1,189,030	9,261,399
Cost of Capital	8,083,766	62,262,370	32,101,301	109,260,463
Retail Volume	236,406	1,820,832	236,406	1,820,832
Retail price	$268.1428	$153.4261	$819.3945	$273.6394
Access price	$51.9984	$51.9984	$63.7507	$55.5647
Unit cost	$183.3279	$183.3279	$540.0802	$275.0338
Imputed margin	$32.8166	-$81.9002	$215.5637	-$56.9591
Imputed margin %	12.24%	-53.38%	26.31%	-20.82%

TABLE 2.6: ADJUSTED ULLS REPORT FOR DECEMBER 2013 QUARTER ON CURRENT COST BASIS

	Unconditioned Local Loop Service		Unconditioned Local Loop Service	
	ADSL Service		ADSL, local calls, line rental, domestic long distance, international and fixed to mobile	
	Business	Residential	Business - 1 x ADSL Service + 4 x Voice Lines	Residential - 1 x ADSL Service + 1 x Voice Lines
Revenues				
retail	63,390,487	279,363,077	193,709,508	498,251,247
other	0	0	0	0
total	63,390,487	279,363,077	193,709,508	498,251,247
Retail Costs				
organisation	2,780,384	21,414,934	11,101,011	37,330,530
product and consumer	5,548,192	42,733,004	24,277,530	79,164,161
total	8,328,577	64,147,937	35,378,541	116,494,690
Other Costs				
organisation	8,992,450	69,261,188	13,591,792	80,129,584
product and consumer	1,118,158	8,612,218	7,040,332	19,475,669
network expenses	15,538,222	119,677,701	39,852,262	167,922,100
total	25,648,830	197,551,108	60,484,386	267,527,353
Ancillary Charges (TEBA)	1,148,349	8,844,757	1,189,030	9,261,399
Cost of Capital	4,866,349	37,481,345	46,223,469	118,583,131
Retail Volume	236,406	1,820,832	236,406	1,820,832
Retail price	$268.1428	$153.4261	$819.3945	$273.6394
Access price	$51.9984	$51.9984	$63.7507	$55.5647
Unit cost	$169.1673	$169.1673	$606.0575	$281.1169
Imputed margin	$46.9771	-$67.7396	$149.5863	-$63.0422
Imputed margin %	17.52%	-44.15%	18.26%	-23.04%

Notes to Tables 2.5 and 2.6
* As per instructions from the ACCC, ancillary charges are calculated as TEBA revenues per ULL service that are reasonably expected in a mature market. This is calculated as the TEBA revenue for the December quarter divided by the adjusted number of installed tie cable pairs. The adjustment factor set by the ACCC is 66%.
**Retail volumes are reported in terms of SIOs

2.5 SUMMARY OF RESULTS

2.5.1 OVERVIEW

RESULTS FOR THE QUARTER

Table 2.7 provides a summary of the imputation test results (on a historic cost basis) for Telstra for the December 2013 quarter. A discussion of results in relation to the specific retail services is provided in sections 2.5.2 to 2.5.6.

TABLE 2.7: TELSTRA IMPUTATION TESTING RESULTS (ON A HISTORICAL COST BASIS)

			Dec-12	Mar-13	Jun - 13	Sep-13	Dec-13	
Retail service	**Core service(s)**							
Local calls and line rental	**LCS**	Business	-5%	-3%	-6%	-4%	-5%	Fail
		Residential	-15%	-10%	-12%	-13%	-12%	Fail
Domestic long-distance	**PSTN–O/T**	Business	52%	56%	57%	53%	54%	Pass
		Residential	49%	55%	54%	51%	51%	Pass
International long-distance	**PSTN–O**	Business	44%	37%	41%	72%	64%	Pass
		Residential	17%	-2%	-13%	13%	6%	Pass
Fixed-to-mobile	**PSTN–O**	Business	56%	58%	60%	63%	64%	Pass
		Residential	60%	62%	62%	64%	65%	Pass
Bundle of fixed voice services #	**LCS and PSTN–O/T**	Business	12%	14%	12%	14%	13%	Pass
		Residential	8%	11%	8%	8%	8%	Pass
		Total	9%	12%	9%	10%	10%	Pass
ADSL	**ULLS**	Business	20%	8%	8%	10%	12%	Pass
		Residential	-32%	-53%	-51%	-53%	-53%	Fail
Bundle of ADSL and fixed voice services *	**ULLS and PSTN–T**	Business	26%	25%	25%	25%	26%	Pass
		Residential	-11%	-19%	-20%	-22%	-21%	Fail

\# The bundle of fixed voice services comprises local calls and line rental, domestic and international long-distance and fixed-to-mobile calls.

* The bundle for business customers is assumed to contain one ADSL service and four fixed-voice services, while the bundle for residential customers is assumed to consist of one ADSL service and one fixed-voice service.

Key findings for the December 2013 quarter are:

- The results are broadly consistent with the last quarter's results.
- Telstra passed 11 out of 15 imputation tests.
- Margins for local calls and line rental services for both residential and business customers remain negative.
- Margins for both standalone ADSL services and bundle of ADSL and fixed voice service for residential customers continue to remain negative.

ACCESS PRICES OVER FOUR QUARTERS

Retail prices, access prices, and the costs of transformation (unit costs) are reported in the imputation tests on an average per unit basis. As such, changes in these prices can be due to changes in underlying revenues and/or volumes (e.g. the number of local calls per service in operation), the access price or the costs of transformation.

Telstra's estimates of the average access prices for the core services in relation to imputation testing are represented in Figures 2.1 and 2.2 below.

Figure 2.1 shows that the access price for local calls and line rentals has increased slightly in the December 2013 quarter. The overall negative trend in the period followed the access price cuts for wholesale line rental (WLR) and the local carriage service (LCS) announced by the ACCC in its interim access determination in March 2011. The ACCC then issued its final access determination for these services in July 2011.

FIGURE 2.1: AVERAGE ACCESS PRICES FOR CORE SERVICES USED IN LOCAL CALLS/LINE RENTAL AND FIXED VOICE BUNDLED SERVICES

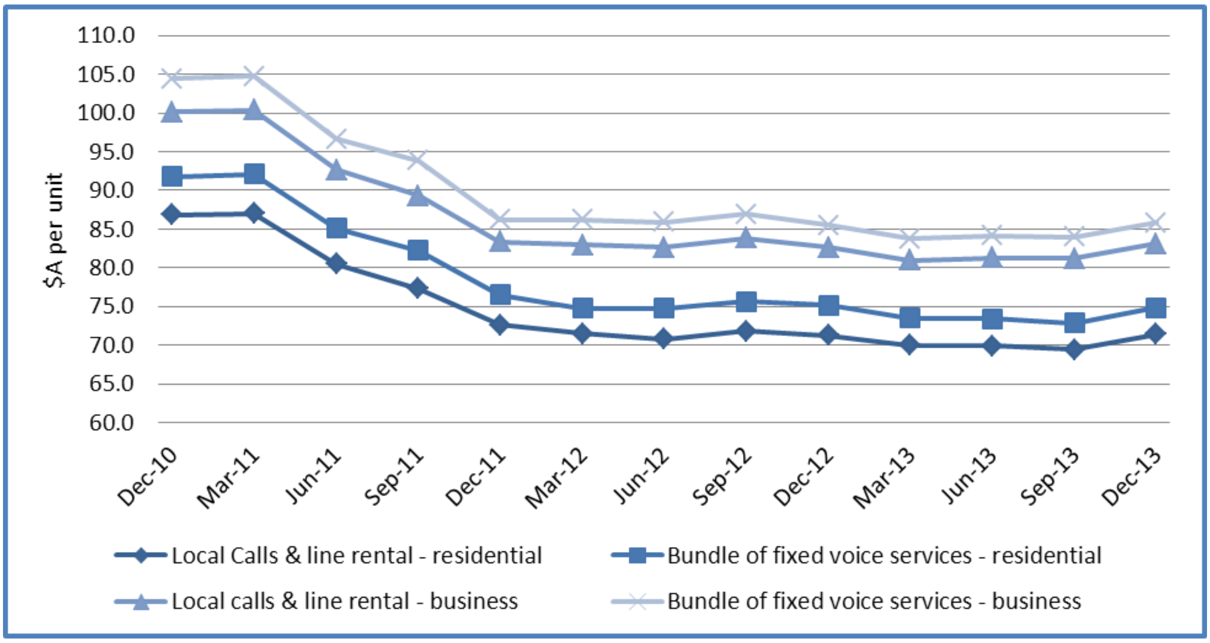
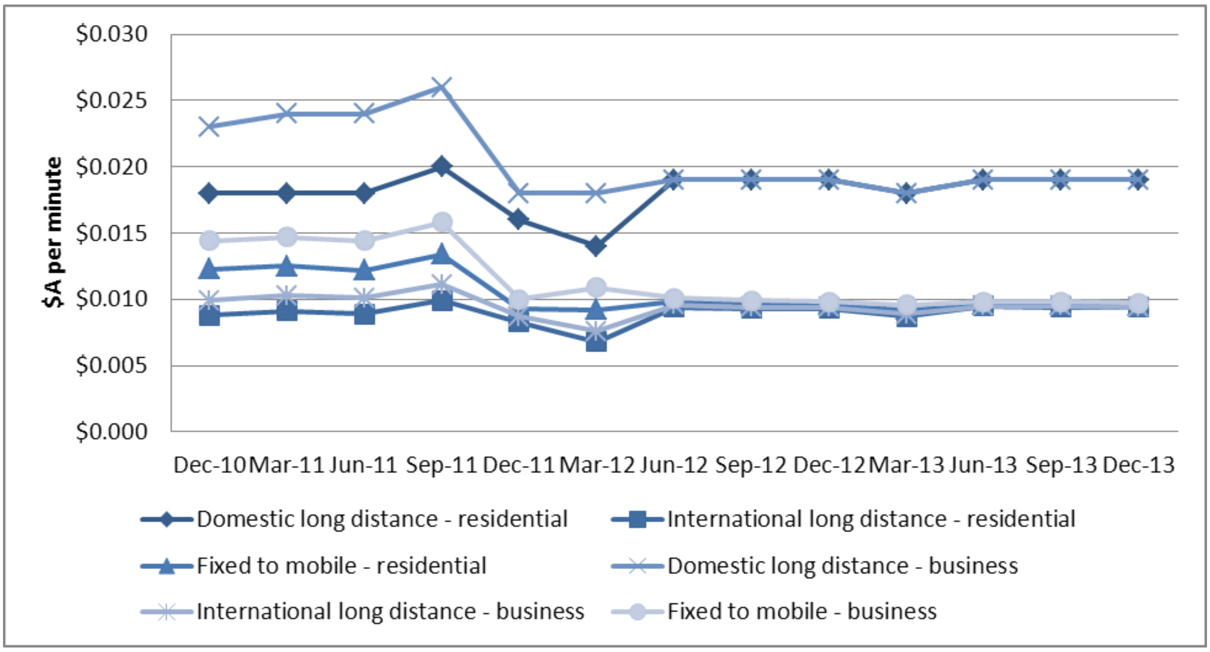


Figure 2.2 shows movements in average access prices for long distance call and fixed-to-mobile call services. Average access prices remained stable in the December 2013 quarter.

FIGURE 2.2: AVERAGE ACCESS PRICES FOR CORE SERVICES USED IN SUPPLYING DOMESTIC & INTERNATIONAL LONG-DISTANCE AND FTM CALL SERVICES



The PSTN originating/terminating services are the underlying core services for the services shown in Figure 2.2. Average PSTN originating and terminating prices are dependent upon call hold times and the geographic area in which calls are supplied. Changes in reported PSTN-O/T prices can therefore be caused by changes in traffic characteristics as well as changes in the underlying rates/prices for PSTN-O/T services.

2.5.2 LINE RENTAL AND LOCAL CALLS

Telstra has reported negative imputed margins for the supply of local calls and line rental for both residential and business customer groups since reporting commenced.

In the December 2013 quarter, the imputed margin remained negative. The margin decreased for business by one per cent, while the margin for residential customers has increased by one per cent.

2.5.3 DOMESTIC AND INTERNATIONAL LONG-DISTANCE AND FIXED-TO-MOBILE CALLS

For domestic long-distance calls, international long-distance calls and fixed-to-mobile calls, Telstra again passed the imputation test for the December 2013 quarter with large positive margins.

In relation to margins for fixed-to-mobile services, it is assumed that Telstra's fixed-to-mobile calls are terminated off-net, that is, on a mobile network other than Telstra's own mobile network. The ACCC estimates that the cost Telstra incurs to terminate a fixed-to-mobile call on its own network is less than that currently charged by other mobile network operators for the mobile terminating access service. To the extent that access seekers can terminate calls on their own networks, the margins available to access seekers may be understated. This qualification is also relevant to the bundles that include fixed-to-mobile calls.

Telstra has recorded a positive imputation margin for residential international long-distance calls for the second successive quarter. Telstra previously advised that the negative margins for residential international long distance was due to the introductory promotion for an International Calling Pack of $10 per month to eligible HomeLine services, which allowed unlimited calls to fixed and mobile phones in a number of countries. This promotion ended on 26 May 2013, and the price of the pack is now $15. It is possible that the expiry of this offer has led to Telstra recording a positive margin for two successive quarters.

The imputation test for business services also passed with large positive margins.

2.5.4 BUNDLE OF FIXED VOICE SERVICES

Imputation testing has also been undertaken for a notional bundle of fixed-line voice services, consisting of line rental and local, domestic and international long-distance and fixed-to-mobile calls. Telstra passed the imputation test for both business and residential customers in the December 2013 quarter. The margin for business customers and residential customers remained unchanged since the September 2013 quarter. The margin for business customers was 13 per cent, while the margin for residential customers was 8 per cent.

2.5.5 ADSL

The margin for residential ADSL customers had a significant decline to a value of -53 per cent in the March 2013 quarter, since then it has improved slightly by 2 percentage points last quarter before declining 2 points again to be at -53 per cent where it has remained unchanged.

Previously, Telstra has advised that the decrease in the imputation margins (e.g. observed during the March 2013 quarter) is due to a rebalancing of cost allocations by Telstra using the half-year RAF reports. Telstra has stated that due to revisions that it has made in how it allocates shared network costs between different services, there is an increased value allocated to the cost in converting ULLS access into ADSL. This has impacted the notional imputation margins for different services by producing a greater negative imputed margin percentage.

The negative imputed margins indicate that there is no business case to support a national competitive network built on ULLS. This is consistent with what has been observed in practice, where ULLS based networks have been deployed in lower cost areas and service providers have offered a bundle of ADSL and voice over internet protocol services.

The imputation margin for business customers is 12 per cent, up two percentage points from the previous quarter.

In considering whether the reported imputation results for the ULLS provide an accurate indication of market conditions faced by ULLS access seekers, the factors outlined in 2.2.3 should be considered as well as:

- that the test focuses on the use of ULLS to supply ADSL, but other retail services can be supplied in conjunction with ULLS (e.g. local and long-distance calls) that may yield significantly higher retail revenues.
- on the other hand, the reported imputation tests exclude connection costs and revenues—should access seekers subsidise connections to acquire customers, their actual margins would be less (i.e. more negative) than those reported.

In assessing the reported cost, it should be noted that the test excludes costs associated with the installation, removal or connection of equipment to/from customer premises.

In considering the difference in results between customer groups, the following factors should also be considered:

- the customer groups are now being determined based on the basic-access product code for the line on which the ADSL service is supplied.[8]
- the revenues for BigPond services are averaged across customer groups. Consequently costs and revenues are not allocated to each group. For example, if one class of customers generally subscribes to higher-priced BigPond plans, the reported results would understate the revenues earned from that customer group and overstate the revenues received from other customer groups.
- as the RAF does not disaggregate costs between customer groups, the costs are averaged over each customer group's demand for the service.

Telstra claims that the results of the Limb 2 imputation tests do not reflect the margins available to access seekers because of fundamental issues with the methodology. Telstra also claims that the TEM reporting under the SSU is a more accurate reflection of the costs underlying Telstra's business, because the cost allocation is derived directly from Telstra's internal financial management reporting system.

2.5.6 BUNDLE OF ADSL AND FIXED VOICE SERVICES

Imputation tests have been undertaken on two types of notional bundles of ADSL and fixed voice services (comprising local calls, line rental, domestic and international long-distance calls and fixed-to-mobile calls).

The first bundle is the bundle of ADSL and fixed voice services for residential customers, which comprises one ADSL service and one voice service. In the December 2013 quarter, Telstra reported a negative margin of 21 per cent, an increase of one per cent from the September 2013 quarter.

The second bundle is the bundle of ADSL and fixed voice services for business customers, which comprises one ADSL service and four voice services. In the December 2013 quarter, Telstra reported a positive margin of 26 per cent, also an increase of one per cent.

Given the bundle of ADSL and fixed voice services is made up of the ADSL service and voice services, the reasons outlined for failing the stand-alone ADSL imputation test (as discussed in 2.2.3, 2.5.1 and 2.5.5) are also relevant for Telstra failing the bundle of ADSL and fixed voice service for residential customers. Likewise the assumption that in the calculation of imputation margins, all fixed-to-mobile calls are terminated off-net, as outlined in section 2.5.3, is not necessarily the case. This means that the profit available to access seekers for this service is likely to be understated.

Also, the imputation test assumes that the costs of supply of the voice services in this bundle would be in line with costs of supply of voice services over the PSTN. Service providers wishing to supply voice services and

[8] Initially, these groups were populated on the basis of unaudited survey data collected by Telstra when the customer first connects the ADSL service. The ACCC considers the current method to be more robust than that previously used. For the June quarter 2006 report and future reports, Telstra made further corrections to its procedure in allocating retail revenues to its business and residential customers to fully align the procedure with Telstra's Regulatory Procedure Manual for imputation testing.

broadband services over the PSTN could choose to do so by using voice over broadband, data or Internet protocol (IP) alternatives. This may result in significantly lower costs than those reported in the current tests.

The ACCC again notes that these tests focus on the use of ULLS to supply ADSL and voice services on a national basis, but that other wholesale inputs may be used. Additionally, use of the ULLS core service enables a wide range of retail services, not limited to just ADSL and the aforementioned voice services, to be supplied.

The results of these imputation tests indicate that it is not simply the access price of the ULLS that is likely to be driving the imputation test results. This is because the costs incurred in transforming the ULLS into ADSL are much higher than the access price.

Telstra has provided additional imputation results for the ULLS/ADSL and voice services bundle that are prepared on the basis that certain geographically averaged transformation costs are replaced by costs specific to the geographic areas where ULLS is currently being supplied. [9]

The transformation costs that have been substituted concern the costs of termination of local calls that originate on an access seeker's ULLS. Table 2.8 sets out the unadjusted and adjusted results.

TABLE 2.8: SUMMARY OF IMPUTED MARGINS WHEN LOCAL CALL TERMINATION CHARGES ARE ESTIMATED ON A GEOGRAPHIC-SPECIFIC BASIS, DECEMBER QUARTER 2013

	ULLS Test	Business: 1 ADSL + 4 voice lines	Residential: 1 ADSL + 1 voice line
Historic Cost Basis	Unadjusted	26.00%	-21.13%
	Adjusted	26.31%	-20.82%
Current Cost Basis	Unadjusted	17.95%	-23.36%
	Adjusted	18.26%	-23.04%

While some of the assumptions on which these additional results have been derived could bear closer scrutiny, it is likely that the reported results are broadly indicative of the effect of using geographically specific local call termination costs instead of fully distributed average termination costs in these imputation tests.

2.6 RECONCILING IMPUTATION RKR DATA WITH THE RAF

Telstra prepares its imputation reports each quarter. In doing so, for each of the retail services subject to imputation testing, Telstra uses revenue and volume data for the quarter to obtain the average retail price and average access price, and uses RAF data to obtain average unit costs.

Ideally, the imputation test results would be based on retail price, access price and unit cost figures appropriate to the quarter. Telstra is able to obtain retail price and access price data from its management systems on a quarterly basis. However, the RAF report is published twice a year only (i.e. for the January–June and July–December reporting periods) and is not available until after the imputation testing results must be

[9] The ULLS is predominantly supplied in urban areas (bands 1 and 2) with few services supplied outside those areas (bands 3 and 4). Telstra advised that around four per cent of ULLS were supplied in band 1, and 94 per cent in band 2. Source: Telstra CAN RKR Data December 2013.

submitted to the ACCC. Imputation testing is therefore conducted using cost data from the last available half-year RAF report. For example, for this December 2013 quarter imputation report, the unit cost data was obtained from the RAF data for the period January to June 2013.

Reconciliation reports are prepared every six months to check whether the accuracy of the imputed margins disclosed in the quarterly reports is affected by the use of lagged RAF cost data and current-quarter revenue and volume data. These reconciliation reports compare the results shown in the quarterly reports (which use management system and lagged RAF data) to results obtained using revenue, volume and cost data from the RAF appropriate to the test period.

In relation to the December quarter 2013 report, RAF data for the period July to December will be available when the next imputation report (for the March quarter 2014) is prepared. A reconciliation report will be provided at the time of the March quarter 2014 report, depending upon the outcome of the Department of Communications consultation on the proposed revocation of the Accounting Separation Direction.

2.7 EXTENT TO WHICH THE REPORTS COMPLY WITH THE RAF AND OTHER RKRS

The Ministerial Direction requires the ACCC to comment on the extent to which the reports comply with:

- the RAF;
- any other relevant record-keeping rules made by the ACCC (whether for the purposes of the Minister's Direction or otherwise); and
- any Direction given by the ACCC for Telstra to make public information contained in the reports.

This section discusses the extent to which the reports comply with the RAF.

2.7.1 RELATIONSHIP BETWEEN THE RAF AND THE IMPUTATION RKR

Telstra provides financial information to the ACCC in the RAF. Under the RAF, Telstra must provide capital-adjusted profit and loss statements for its retail services, internal wholesale services and external wholesale services. Telstra must also provide statements in relation to capital employed and fixed assets for those three service classifications.

The Ministerial Direction requires that Telstra provide the imputation RKR information to the ACCC each quarter. Telstra currently provides RAF information to the ACCC every six months. To address this time disparity, the ACCC requires Telstra to:

- obtain revenue information for core and retail services for the relevant quarter from Telstra's general ledger accounts
- obtain volume information for core and retail services for the relevant quarter from Telstra's management information systems
- obtain cost information for retail services each quarter by multiplying the volume data for the relevant quarter with the unit costs of the service derived from the RAF accounts for the six-month reporting period preceding that quarter.

The RAF records volume information for retail and core services. The imputation RKR requires Telstra to use volume data for retail services from the RAF for the previous six months to unitise cost information. It also requires that volume data for the relevant quarter be used, which can later be compared to the volume data that appears in the RAF.

The RAF does not disaggregate data between business and residential customer groups.

2.7.2 REVENUE DIFFERENCES BETWEEN THE IMPUTATION RKR AND THE RAF

The RAF allocates revenues across various retail services. The imputation RKR requires Telstra to allocate its retail revenues in a manner consistent with the RAF. This allows for the reports provided by Telstra to be reconciled with the RAF data in future periods.

That said, there are two material differences in the service descriptions that are used in the RAF and in the imputation test:

- The domestic long-distance service in the imputation RKR excludes revenues from operator-assisted calls, which are included in the corresponding RAF category. Therefore, the domestic long-distance revenues in the RKR will be lower than the RAF revenue for the national long-distance retail service.
- The RAF fixed-to-mobile service includes ISDN-originated calls.

As noted in section 2.6, differences between the imputation RKR and the RAF revenues also occur due to the effect of different accounting treatments. Differences also occur due to the inclusion of ADSL installation discounts and ULLS connection charges.

The revenues in the imputation RKR are otherwise consistent with the revenue items for these services in the RAF.

2.7.3 COST DIFFERENCES BETWEEN THE IMPUTATION RKR AND THE RAF

The RAF allocates common costs as well as direct costs to wholesale and retail services. The costs attributed to retail services in the RAF are appropriate for calculating 'retail costs' for the imputation test, but do not include all costs in the transformation of a core service to a retail service (such as transmission costs). Therefore, additional costs (listed separately as 'other costs') are included in Telstra's imputation testing results.

Telstra uses unitised cost information from the RAF reports from the preceding six-monthly reporting period, which is multiplied by the volume for the relevant quarter. This cost information is later reconciled with the RAF. In constructing the imputation test, Telstra raised implementation issues relating to the calculation of appropriate retail and other costs using the RAF data. Telstra and the ACCC agreed on ways to resolve these issues. This has resulted in some adjustments to the RAF figures in the imputation test. The adjustments relate to:

- the removal of installation costs from the cost of line rental and ADSL – as required by the imputation RKR
- the removal of modem costs from the cost of ADSL – implied from the definition of ADSL in the imputation RKR
- the use of a mobile termination methodology for costing fixed-to-mobile services
- avoiding the double-counting of ULLS and PSTN originating and terminating access service costs
- adjustment to call costs used in the bundle of ADSL and fixed-line voice products when services are provided over the ULLS
- ancillary costs.

The last four dot points are described in more detail below.

MOBILE TERMINATION METHODOLOGY FOR FIXED-TO-MOBILE SERVICES

As the imputation tests have been designed to show whether an efficient access seeker is able to compete with Telstra, the imputation test needed adjustment to account for Telstra's on-net fixed-to-mobile calls (i.e. voice calls that originate from Telstra fixed lines and terminate on Telstra's mobile network). The ACCC and Telstra agreed that Telstra impute the weighted average mobile termination charge that would apply to an access seeker that terminates fixed-to-mobile traffic on Telstra's mobile network.

DOUBLE-COUNTING ULLS AND PSTN ORIGINATING AND TERMINATING COSTS

To calculate the costs of transforming the PSTN and ULLS core services into the retail services specified in the imputation RKR, Telstra uses its Retail and Internal Wholesale accounts in the RAF. However, the Internal Wholesale accounts include costs of network elements and functions that are already captured in the access prices for the PSTN O/T and ULLS. For example, the Internal Wholesale costs recorded in the RAF allocate local switching and transmission costs to the domestic long-distance service, which are already factored into the PSTN access price.

To overcome this issue, Telstra deducts the common elements located in the External Wholesale accounts (which are used to calculate the access price) from the costs located in the Internal Wholesale accounts in the RAF. This adjustment is done at a relatively high level.

NON-ULLS CALL COSTS

For the bundled tests involving ADSL and fixed voice products, the costs for origination and termination for fixed telephony calls change when the underlying service is ULLS.

The ACCC and Telstra have agreed to a methodology that involves several steps. For local and domestic long-distance calls, the PSTN terminating access (TA) network costs are removed from the RAF and PSTN TA charges are added, using a similar method to that used to remove double-counted costs. For international long-distance calls, the international settlement payments are used for termination of such calls. For fixed-to-mobile calls, the methodology explained above for mobile termination is used.

ANCILLARY CHARGES

The imputation RKR requires Telstra to calculate ancillary charges for the PSTN (consisting of switchport charges) and ULLS (Telstra Exchange Building Access or TEBA charges). The imputation reports may double count some of the ancillary charges.

2.7.4 CONCLUSION ON THE EXTENT TO WHICH THE REPORTS COMPLY WITH THE RAF

Subject to the exceptions noted in sections 2.7.2 and 2.7.3 above, the revenue data for retail services and the cost data for retail services are likely to comply with the RAF. Other data involved in the imputation testing is not required to comply with the RAF.

2.8 ACCURACY OF THE IMPUTATION RKR REPORTS

The Ministerial Direction requires the ACCC to comment on the accuracy of the reports lodged by Telstra.

2.8.1 AUDIT PROCESS

Clause 13 of the imputation RKR addresses the audit requirements for the reports. The clause requires that a single audit be undertaken each year in respect of the reports that are prepared under the imputation RKR and an audit report be provided to the ACCC.

In July 2013, the ACCC granted Telstra an exemption from the auditing requirement of imputation report for 2012-13. This is because the ACCC considered the cost of auditing the reports would outweigh any potential benefits given the introduction of interim equivalence and transparency measures under Telstra's structural separation undertaking. The ACCC further considered that Telstra would have been operating on the basis that its reports would need to be audited and would have prepared as such.

2.8.2 ACCURACY OF REPORT

Given that the Telstra December 2013 quarter reports have not been audited, the ACCC cannot conclusively state whether these reports comply in all respects with the Imputation RKR.

3. NON-PRICE TERMS AND CONDITIONS REPORT

3.1 OVERVIEW

3.1.1 WHAT DOES THIS REPORT DO?

This report presents various key performance indicators (KPIs) for the services that Telstra supplies to retail customers and wholesale customers. The data for these reports is compiled by Telstra and submitted to the ACCC.

The KPIs are on the ordering and provisioning (i.e. the connection of new services) and handling of faults for the basic access service and the ADSL service (see Table 3.1). The KPIs measure Telstra's basic access service levels against the standard specified in the customer service guarantee (CSG)[10] and Telstra's ADSL service levels against similar standards. Separate KPIs are presented for residential and business services.

TABLE 3.1: METRICS FOR WHICH PERFORMANCE IS ASSESSED

Metric 1	Basic access - Ordering and Provisioning - The percentage of basic access customer installation orders provisioned in the quarter on or by the performance standard – previous service available for automatic connection
Metric 2	Basic access - Ordering and Provisioning - The percentage of basic access customer installation orders provisioned in the quarter, on or by the performance standard – new service with available cabling and capacity
Metric 3	Basic access - Ordering and Provisioning - The percentage of basic access orders provisioned in the quarter, on or by the performance standard – new service which requires additional cable or network capacity
Metric 4	Basic access - Ordering and Provisioning - The percentage of basic access order appointments that are met in the quarter
Metric 5	Basic access - Faults and Maintenance - The percentage of basic access faults that are rectified in the quarter, on or by the performance standard (Includes dial-up faults)
Metric 6	Basic access - Faults and Maintenance - The percentage of basic access fault appointments that are met in the quarter (includes dial-up faults)
Metric 7	Basic access - Faults and Maintenance - The percentage difference in recurring fault ratio
Metric 8	ADSL service activation - The percentage of services provisioned within performance standards – where the customer or end-user has an existing and functioning basis access service capable of supporting ADSL services
Metric 9	ADSL service activation - The percentage of services provisioned within performance standard – held orders
Metric 10	ADSL - Faults and Maintenance - The percentage of faults rectified within performance standards

[10]The KPIs are not, however, directly comparable to those reported by the Australian Communications and Media Authority (ACMA) in the context of CSG reporting. This is because CSG reporting concerns only those customers with five lines or less.

Metric 11	ADSL - Faults and Maintenance - The percentage of appointments kept

The reporting of KPIs is intended to provide an initial indicator of whether or not Telstra is providing equivalent service levels, on average, to Telstra wholesale and Telstra retail customers.

The report is not intended to identify whether particular instances of anti-competitive behaviour by Telstra may have occurred. Rather, the results in this report serve as possible indicators. The ACCC will, therefore, continue to monitor any trends in Telstra's performance and respond to complaints of discrimination on their merits.

3.2 SUMMARY OF KPIS FOR THE FOUR QUARTERS ENDING 31 DECEMBER 2013

Table 3.2 presents Telstra's non-price KPI report for the four quarters up to 31 December 2013 as well as calculating an average for that period. By examining Telstra's performance over four quarters, the possibility of drawing conclusions regarding Telstra's performance based on a quarter affected by transient or seasonal factors is minimised.

For any performance metric, if the difference between the percentage of wholesale customers and retail customers for which Telstra has met the performance standard is positive, then Telstra has performed better in meeting the performance standard for its wholesale customers than its retail customers. Therefore, a positive performance metric indicates that Telstra is unlikely to be systematically discriminating in its own interests and against the interests of competitors in that area.

Conversely, for any performance metric, if the difference between the percentage of wholesale customers and retail customers for which Telstra has met the performance standard is negative, then Telstra has performed worse in meeting the performance standard for its wholesale customers than its retail customers. Where a performance metric is highly negative, it may provide an initial indicator that Telstra is favouring its own retail unit over its wholesale business unit.

TABLE 3.2: AVERAGE VARIANCES IN KPI METRICS - 12 MONTHS ENDING 31 DECEMBER 2013[11]

	Business services					Residential services				
Metric	Difference in performance between wholesale and retail business customers (%)					Difference in performance between wholesale and retail business customers (%)				
	Mar-13	Jun-13	Sep-13	Dec-13	Ave.	Mar-13	Jun-13	Sep-13	Dec-13	Ave.
1	1.11	-0.22	-2.89	0.13	-0.47	4.23	3.65	0.7	-0.22	2.09
2	7.05	-0.67	-3.07	3.68	1.75	6.16	5.17	-0.57	2.32	3.27
3	17.69	10.74	-0.86	8.61	9.05	17.22	19.53	19.15	22.06	19.49
4	0.95	0.94	1.19	0.48	0.89	2.07	2.23	2.08	1.93	2.08
5	1.71	2.70	1.26	-1.00	1.17	-0.42	-0.66	-2.66	-3.09	-1.71
6	-0.38	0.21	0.27	-0.54	-0.11	0.24	0.15	-0.04	-0.09	0.07
7	0.39	0.00	1.09	0.74	0.56	0.26	0.58	0.99	1.56	0.85
8	0.91	0.76	0.82	0.52	0.75	0.97	2.05	0.22	0.26	0.88
9	3.45	3.64	0.17	-0.14	1.78	3.22	1.15	0.2	1.34	1.48

[11] The performance standard used for all metrics is the same as that used for the Customer Service Guarantee, unless otherwise stated.

10	5.7	11.14	21.21	23.60	15.41	4.00	4.12	4.97	6.21	4.83
11	-0.19	1.22	1.70	0.61	0.84	-0.43	-0.07	0.38	-0.01	-0.03

Notes: A positive difference means that Telstra Wholesale has met the performance standard in a greater percentage of cases than Telstra Retail.

3.3 DISCUSSION OF PERFORMANCE

The overall results do not provide any evidence of systemic discrimination by Telstra against access seekers in respect of performance.

Several results are negative (indicating Telstra favoured its retail service) but these results are not outside the 2 per cent tolerance limit.

For Metric 5, which relates to the percentage of basic access (standard telephone service) faults that were rectified in the quarter on or by the performance standard:

- there continued to be a notable deterioration for Wholesale residential services over the last 12 months, from -0.42 per cent in the March 2013 quarter to -3.09 per cent in the December 2013 quarter
- Telstra's performance in relation to Wholesale business services also declined from 1.26 per cent in the September 2013 quarter to -1.00 per cent in the December 2013 quarter.

Telstra has not identified any specific causal issues for the residential result. Telstra contends that Metric 5 does not give an accurate view of its performance and has stated that the residential variance is due to the methodology under the Accounting Separation rules used to count tickets that do not meet the restoration target. In this regard, Telstra notes that a variance of this magnitude for the corresponding SSU metric does not occur in relation to its operational equivalence reporting, which shows a closer alignment in operational performance for Telstra Retail and Telstra Wholesale for the same quarter.

When calculating its performance in relation to the equivalence and transparency metrics under the SSU, Telstra is permitted to extend the target restoration timeframe to take account of the effect of any mass service disruptions (MSDs) caused by natural disasters or extreme weather conditions. The results reported under the Accounting Separation metrics do not take into account MSDs.

In previous Accounting Separation reports, Telstra has explained that negative variances for residential basic access services resulted from high fault workloads in MSD areas, which affected wholesale services more than retail services.

3.4 EXTENT TO WHICH TELSTRA'S REPORTS CONFORM WITH THE RKR REQUIREMENTS

The ACCC considers that the December quarter 2013 report conforms to the requirements of the RKR.

3.5 ACCURACY

Given that the underlying Telstra data used in the December 2013 quarter results has not been audited, the ACCC cannot conclusively state whether the reports provided by Telstra for the period comply in all respects with the *Non-price terms and conditions KPI RKR*.

In July 2013, the ACCC granted Telstra an exemption from the auditing requirement of non-price terms and conditions report for 2012-13. This is because the ACCC considered the cost of auditing the reports would outweigh any potential benefits given the introduction of interim equivalence and transparency measures under Telstra's structural separation undertaking. The ACCC further considered that Telstra would have been operating on the basis that its reports would need to be audited and would have been prepared as such.