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Inquiry to make a final access determination for the wholesale ADSL service

Introduction

Macquarie Telecom Pty Limited (“**Macquarie**”) welcomes the opportunity to make this submission to the Australian Competition and Consumer Commission (“**ACCC**”) in relation to its discussion paper concerning the above.¹ The conduct of the ACCC’s inquiry follows its decision to declare the wholesale ADSL service and its making of an interim access determination for this service (“**ADSL IAD**”).

Macquarie considers that the making of a final access determination for the wholesale ADSL service (“**ADSL FAD**”) is fundamentally important for Australia’s telecommunication sector. In particular, an ADSL FAD is expected to:

- close-off opportunities for Telstra to harm retail competition in the provision of ADSL services;
- bring the pricing methodology of ADSL services into line with that of other declared fixed access services;
- deal with the fact that Telstra’s current wholesale ADSL prices are not constrained by competition and are widely acknowledged as being significantly above cost;
- reduce the price of wholesale ADSL services and thereby stimulate competition particularly in regional Australia; and
- provide access seekers with greater certainty that the wholesale ADSL service will be supplied on competitive terms.

Responses to Consultation Questions

In this section, Macquarie has addressed each of the questions raised in the Discussion Paper. For ease of reference, each consultation question has been reproduced in a shaded text box which is then followed by Macquarie’s response.

¹ ACCC, Public inquiry to make a final access determination for the wholesale ADSL service, Discussion Paper, February 2012 (“**Discussion Paper**”)



1. How do you consider that the mandatory criteria should be interpreted for the purpose of making this FAD?

Macquarie notes that the ACCC must have regard to seven criteria specified in subsection 152BCA(1) of the *Competition and Consumer Act 2010* when making an FAD. The Discussion Paper sets out the ACCC's approach to these criteria. Macquarie's views on the application of each criterion to the ACCC's current inquiry is discussed below.

1. Promotion of the LTIE

Macquarie notes that the ACCC interprets this criterion on the basis of three factors, i.e., the promotion of competition, achieving any-to-any connectivity and efficient use of infrastructure. In relation to these factors, Macquarie comments as follows:

- Promotion of Competition

Macquarie is strongly of the view that the making of an ADSL FAD will promote competition. This is because an ADSL FAD will ensure that the wholesale ADSL service is supplied on the basis of:

- cost-reflective prices; and
- regulated non-price terms and conditions.

This should in turn close-off opportunities for Telstra to harm competition through engaging in price discrimination and refusal to supply. In addition, it should also reduce the price of wholesale services principally through a reduction in the AGVC component price.

- Any to Any Connectivity

Macquarie considers that the making of an ADSL FAD will promote any-to-any connectivity. This is because an ADSL FAD will promote the use of ADSL services in retail markets which in turn enables end-users to connect with each other. That is, through applications made possible on the Internet such as, IP telephony, email, social media, web logs, podcasts, etc. wider use of ADSL services in retail markets promoted by an ADSL FAD in turn promotes communication between end-users.

Macquarie does, however, note that the ADSL service does not provide a user-to-user service *per se*. As such, Macquarie accepts that this criterion has less relative importance.

- Efficient use of Infrastructure

Macquarie considers that the making of an ADSL FAD will promote the efficient use of infrastructure. This is because an ADSL FAD will enable access seekers to gain access to Telstra's copper network thereby opening up the opportunity to migrate end-users from voice-only services to broadband services. That is, an ADSL FAD will promote the utilisation of the existing copper network to supply additional services. As was noted in the ACCC's declaration inquiry process, the addressable market for end-users in outer metropolitan and regional areas does not usually support more than one DSLAM operator. Therefore open access arrangements to Telstra's ubiquitous DSLAM infrastructure will lead to more efficient use of existing infrastructure and bring greater retail choice to end-users.



2. Legitimate Business Interests of Supplier

Macquarie considers that the legitimate business interests of Telstra as a wholesale supplier will be served by the making of an ADSL FAD. In particular, a cost-based price as determined by the ACCC will ensure that Telstra does not price the wholesale ADSL service below cost. As such, this will ensure that Telstra does not incur any losses when it supplies the wholesale ADSL service to access seekers and that it will recover its reasonably incurred costs.

3. Interests of All Persons who Have a Right to Use

Macquarie considers that the interests of access seekers will be promoted by the making of an ADSL FAD. In particular, an ADSL FAD will open up opportunities for access seekers to supply services to end-users. That is, an ADSL FAD will remove obstacles which currently constrain access seekers, such as a refusal to supply and excessive pricing.

4. Direct Costs

Macquarie considers that this criterion should be met by ensuring that Telstra's direct costs incurred in supplying a wholesale ADSL service are fully recovered through the prices determined by the ACCC. This outcome would be achieved through the application of a cost-based pricing methodology to the wholesale ADSL service.

5. Extensions or Enhancements of Capability

Macquarie considers that this criterion should be met by ensuring that the costs that Telstra recovers through the prices determined by the ACCC for supplying the wholesale ADSL service should only include costs which are necessarily incurred by Telstra in order to provide the service.

6. Safe and Reliable Operation

Macquarie considers that this criterion should be met by ensuring that the non-price terms and conditions of the FAD do not compromise the safe and reliable operation of the wholesale ADSL service.

7. Efficient Use of Services and Infrastructure

Macquarie considers that the making of an ADSL FAD will promote the efficient use of services and infrastructure. This is because an ADSL FAD will enable access seekers to gain access to Telstra's copper network thereby opening up the opportunity to migrate end-users from voice-only services to broadband services. That is, an ADSL FAD will promote the utilisation of the existing copper network to supply additional services.



2. What markets should be considered in applying the mandatory criteria to this FAD?

Macquarie considers that the relevant market that should be considered in applying the mandatory criteria to this FAD is characterised as:

- a market for downstream (retail) fixed network broadband services;
- the inclusion of both ADSL and substitutable services, i.e., broadband services provided over HFC and optic fibre networks; and
- a national market.

3. What “other matters” should be considered when making this FAD?

Macquarie considers that there are several “other matters” which the ACCC should consider when making the ADSL FAD. These include:

- the need to protect and promote competition during the period in which the national broadband network is being rolled-out;
- the importance of having wholesale ADSL services regulated in line with other fixed network access services;
- the importance of having wholesale ADSL services regulated to ensure the effective operation of price equivalence arrangements under Telstra’s structural separation undertaking (“SSU”);
- consideration of a “pathway” toward effective regulation of fibre to the node deployments by Telstra; and
- consideration of the effective use that can be put to determining regulated rates by reference to data derived from Telstra’s TEM produced pursuant to its SSU.

4. What charges do you consider should be addressed in this FAD? Please consider the type of charges outlined above as well as any other material charges?

Macquarie is broadly satisfied with the existing structure of charges for the wholesale ADSL service which the ACCC has adopted in the ADSL IAD. Such charges comprise:

- access charge;
- transmission charge;
- installation charges; and
- early termination charges.

5. What methodology or methodologies should be used to develop price terms for this FAD?

Macquarie is strongly of the view that a cost-based methodology should be used to develop price terms for the ADSL FAD. This is because the use of a cost-based methodology is widely considered to be industry best practice and is consistent with the methodology used by the ACCC for the setting of price terms for other fixed network access services.



Macquarie does, however, recognise that the application of a cost-based methodology to develop price terms for the ADSL FAD would be a complex and a potentially time consuming and costly exercise. While the ACCC should not lose sight of adopting a pure cost-based pricing approach using a cost model, Macquarie believes that the ACCC could determine price terms by reference to a combination of benchmark prices and data derived from Telstra's TEM produced pursuant to its SSU.

6. What overall charge structure should be considered, eg. between access fees and usage fees?

As noted above in its response to question 4, Macquarie is broadly satisfied with the structure of charges for the wholesale ADSL service as set out in the ADSL IAD. However, Macquarie is concerned that the pricing of the AGVC as set out in the ADSL IAD is excessive. The ADSL IAD price is \$45.50 per megabit per month for the period up to 30 June 2012 and is then priced at \$33.65 from 1 July 2012. Macquarie considers such prices to be excessive in comparison to NBN Co's pricing of its connectivity virtual circuit which is currently \$20 per megabit per month.

7. Should any of the charges be levied on a zone basis, or should they be levied on a nationally consistent basis? On what basis should areas be grouped into zones, if this construct is to be used?

Macquarie notes the relative merits of de-averaged versus nationally averaged pricing of wholesale access services. In determining price terms for the ADSL FAD, there is a need to weigh up the efficiency of de-averaged wholesale prices against the national uniformity of retail prices and the consequences of access seekers being potentially unable to afford wholesale services in high-cost locations. Macquarie also notes that the ACCC has already established a two-tiered pricing structure for the ULLS. Macquarie considers that the two-tiered pricing structure which the ACCC has adopted in the ADSL IAD is an appropriate balance between the competing pressures and should be adopted in the ADSL FAD.

Macquarie considers that a two-tiered pricing structure for the ADSL FAD should be based on costs. In a two-tiered structure this essentially means "lower cost" areas versus "higher cost" areas. In the absence of a cost study of Telstra's exchanges, this may, for example, be estimated on the basis of CBD and metropolitan exchanges versus regional and remote exchanges.

8. On what basis (if any) should price discrimination between access seekers be encouraged or discouraged?

Macquarie considers that *prima facie* there may be some merit in adopting a discriminatory pricing model to the extent that it may provide incentives to access seekers to adopt more efficient and effective operational practices which in turn may reduce costs for the access provider. However, Macquarie cautions against this on the following grounds:

- the practical difficulty in quantifying the monetary value of an efficient practice and translating it into a pricing model;
- the pricing discretion that this would likely provide to the access provider;



- the additional complexity that it would impose on the ACCC to provide effective oversight of a discriminatory pricing model; and
- the potential for the access provider to manipulate competition outcomes via use of its market power in other related markets.

Macquarie considers that the above factors outweigh the potential benefit of a discriminatory pricing model. As such, Macquarie does not support the use of a discriminatory pricing model in the ADSL FAD.

9. What other price-related terms should be addressed in this FAD? In general terms, what do you consider an appropriate outcome for these terms and conditions?

Macquarie is of the view that the price-related terms adopted in the ADSL IAD provide an appropriate structure to be followed in the ADSL FAD. Macquarie considers that an appropriate outcome for the price-related terms and conditions for the ADSL FAD would be characterised as follows:

- a pricing structure which comprises an access charge, a transmission charge, installation charges and early termination charges;
- the cost-based pricing of each component and, in particular, a lower price for the AGVC component than is currently set out in the ADSL IAD;
- the potential use of benchmark prices to estimate cost-based prices;
- a two-tiered pricing structure for the access component; and
- non-discriminatory prices, i.e., all access seekers face the same prices.

10. What do you consider are the key commercial terms needed for commercial supply of the Service to occur? Do you consider the 2008 Model Terms should be applied (where relevant) in developing an FAD that addresses those terms? If not, on what basis should these terms and conditions be developed?

Macquarie considers that the key commercial terms that are needed for the commercial supply of the wholesale ADSL service can be based on the 2008 Model Terms. Such an approach is consistent with the position adopted by the ACCC in setting FADs for other fixed network access services.

In particular, Macquarie considers that terms from the 2008 Model Terms concerning the following areas are appropriate for the ADSL FAD.

- billing and notification;
- creditworthiness and security;
- general dispute resolution procedures;
- confidentiality provisions;
- communication with end-users; and
- suspension and termination.

Macquarie notes that this approach is consistent with the ADSL IAD.



11. What other non-price terms and conditions of access do you consider should be included in this FAD? Please consider those access terms outlined above as well as any other access terms that you consider to be of material significance.

Macquarie does not believe that it is necessary to include non-price terms and conditions in the ADSL FAD other than those which are specified in Macquarie's response to question 10.

In addition, Macquarie considers that the non-price terms and conditions should not contain restrictive "fair use" conditions which have the effect of limiting the use of the ADSL service for emerging bandwidth hungry end-user application and thereby constraining the capacity of retail service providers to innovate.

12. What general approach do you consider would be appropriate in developing an FAD that addresses those terms?

As per its response to question 11, Macquarie does not believe that the non-price terms and conditions should extend beyond those specified in Macquarie's response to question 10.

13. In general terms, what do you consider to be an appropriate outcome for each of these terms and conditions?

Macquarie believes that an appropriate outcome regarding non-price terms and conditions is for the ADSL FAD to adopt the terms from the 2008 Model Terms in respect of the areas specified in Macquarie's response to question 10.

14. Should SAOs apply to operators of non-dominant networks?

No. Macquarie is strongly of the view that the SAOs should not apply to operators of non-dominant networks. This is essentially because Telstra is the dominant supplier of ADSL services.² Macquarie considers that it is appropriate for the focus of the ACCC's regulatory intervention on this matter through the ADSL FAD should be on the dominant network operator. Moreover, it is evident that competition concerns raised with the ACCC in respect of wholesale ADSL services are exclusively in regard to services supplied by Telstra.³

Macquarie believes that if the SAOs were to extend to operators of non-dominant networks it would impose obligations and requirements which would be unlikely to be exercised. That is, seekers of ADSL services require these services from Telstra because Telstra is the dominant supplier of ADSL services.

² ACCC, Declaration of the wholesale ADSL service under Part XIC of the Competition and Consumer Act 2010, Final Decision, February 2012, page 1

³ ACCC, Interim access determination for wholesale ADSL service, Statement of Reasons, February 2012, page 17



15. Should the ACCC consider exempting particular geographic areas from the SAOs and/or terms and conditions included in the access determination? Why/why not?

No. Macquarie is very strongly of the view that the ACCC should not consider exempting particular geographic areas from the SAOs and/or terms and conditions included in the access determination. Granting an exemption would mean that Telstra would not be obliged to provide the wholesale ADSL service to access seekers in specified areas. Such exemptions are not appropriate for the simple reason that Telstra is the dominant supplier of wholesale ADSL services. Macquarie is particularly concerned that exemptions would result in detriment to competition through Telstra's capacity and motivation to:

- increase the price of wholesale ADSL services in the exempt areas; and
- deny the supply of wholesale ADSL services to access seekers in the exempt areas.

Macquarie notes the recent decision of the ACCC to remove geographic exemption provisions in FADs for a range of fixed line services. In particular, Macquarie considers that the detrimental impact of the exemption provisions indicates that exemption provisions are not appropriate in respect of the wholesale ADSL service.

Finally, to the extent that the regulated supplier is regulated in areas where there is choice of wholesale supply, e.g., some inner metro exchange areas, no detriment is incurred by the dominant provider as it is the case that it will need to price in these areas by reference to competitive supply markets.

16. What is an appropriate time period for the FAD?

Macquarie notes that ACCC's declaration of the wholesale ADSL has five year time period, expiring 13 February 2017. *Prima facie* this provides a convenient basis for setting the time period for the ADSL FAD. However, given the significant reforms which are occurring in Australia's communications sector, Macquarie considers that five years is too long a time period for the ADSL FAD.

Macquarie suggests that a two year time period would provide an appropriate balance between providing access seekers with regulatory certainty against the need to ensure that regulatory settings are relevant to contemporary market conditions. It is also the case that information about Telstra's costs and revenues incurred in relation to the supply of this service will likely arise from the SSU and related processes. This information would then inform further consideration of appropriate pricing over that two year period.

17. Are there any circumstances that warrant a difference in the expiry dates of the access determination and the wADSL declaration?

Macquarie is of the view that there are circumstances that warrant a difference in the expiry dates of the ADSL FAD and the wADSL declaration. Of particular concern to Macquarie is the setting of price terms. Macquarie believes that price terms must be reasonably contemporary. As such, Macquarie is of the view that the price terms of the ADSL FAD should be reviewed no later than two years after they have been set.

Closing

Macquarie welcomes the opportunity to make this submission. Macquarie is strongly of the view that the making of an ADSL FAD is fundamentally important for Australia's telecommunication sector.

Macquarie would welcome an opportunity to discussion this submission with you. In the meantime, please do not hesitate to contact me.

Yours sincerely



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