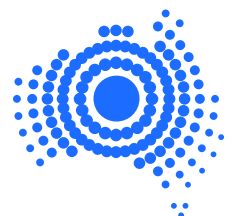


NBN'S SUBMISSION ON WACC METHODOLOGY

**ACCC voice interconnection services access
determination inquiry**

3 September 2025



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1 Summary

nbn welcomes the opportunity to respond to the ACCC's consultation on Weighted Average Cost of Capital (**WACC**) methodologies as part of its access determination inquiry for voice interconnection services.

In particular, this submission sets out nbn's initial response to the draft report by Cambridge Economic Policy Associates (**CEPA**) on WACC methodologies for voice interconnection services as commissioned by the ACCC, where that report also recommends a method that CEPA suggests could be used to estimate the WACC for the purposes of nbn's Replacement Module Application process (**Draft WACC Methodology Report**).

nbn considers that aspects of the Draft WACC Methodology Report prepared by CEPA fall short of undertaking a proper assessment and evaluation of the methods that the ACCC could consider adopting to estimate a WACC, taking into account the specific regulatory frameworks that apply to the relevant entities for which the ACCC will estimate a WACC, the economic literature, new issues and additional information that have emerged in the past decade in the approaches to estimating the WACC, and the merits of practices adopted by other regulators. nbn has set out in this submission its view on CEPA's Draft WACC Methodology Report to assist the ACCC as it evaluates whether the Draft WACC Methodology Report provides the ACCC with a sound basis for estimating nbn's WACC as part of its Replacement Module Determination (**RMD**).

In summary, nbn submits that in the Draft WACC Methodology Report:

- CEPA does not set out to determine a WACC which complies with nbn's regulatory framework under its SAU; and
- CEPA does not purport to critically analyse the majority of positions it recommends – and instead adopts positions on the basis that other regulators have adopted those positions in other contexts for other sectors.

In that context, nbn submits that:

- The ACCC should not take comfort about the robustness of the method recommended by CEPA from the fact that the WACC estimates proposed by both CEPA and nbn are similar.
- The ACCC should exercise caution in relying on aspects of CEPA's Draft WACC Methodology Report to inform the method it uses to set the WACC for nbn when making a Replacement Module Application (**RMA**) under nbn's Special Access Undertaking (**SAU**).
- Any updated CEPA report should describe and apply nbn's regulatory framework correctly and critically examine the merits of positions before recommending them if it is to be used in any way to inform the ACCC's decision in relation to nbn's WACC for the purposes of its RMD.
- CEPA's recommendation to estimate the cost of equity by pairing a current estimate of the risk-free rate and a long-term historical estimate of the Market Risk Premium is internally inconsistent and can produce volatile and implausible outcomes over time. The ACCC should instead adopt the approach developed by IPART, which is internally consistent and more stable.
- The concerns raised by CEPA in relation to using Dividend Growth Models to estimate the Market Risk Premium have already been addressed in the method proposed by nbn in its RMA.

- As indicated by CEPA and Frontier Economics, regulated utilities in other sectors like electricity should not be included in the comparator set used to estimate the equity beta for nbn – this is noting that the SAU regulatory framework requires the WACC used in nbn's RMA process to be commensurate with the efficient financing costs of a benchmark efficient entity with a similar degree of risk as nbn in providing the regulated services. Any suggestion that nbn faces limited competition and has a similar systematic risk profile to regulated utilities in other sectors like electricity networks is outdated and not supported by the available evidence. Furthermore, as indicated by Frontier Economics, exposure to revenue and volume risk is a much greater driver of systematic risk than exposure to competition.

2 Context and structure of this submission

2.1 Context of this submission

Pursuant to nbn's SAU, nbn submitted an RMA to the ACCC on 2 July 2025. nbn's RMA included a Building Block Model Proposal for the proposed Second Regulatory Cycle (FY27-29), which incorporated a proposed WACC for a benchmark efficient entity with a similar degree of risk as nbn in providing the regulated services. nbn's RMA was accompanied by a Supporting Submission and an expert report commissioned by nbn from Frontier Economics regarding nbn's WACC estimates and inflation forecasts (**June Frontier Economics Report**).

Separately, since June 2024, the ACCC has been holding a public inquiry under Part 25 of the *Telecommunications Act 1997* (Cth) about making final access determinations for voice interconnection services, for which the ACCC is developing a TSLRIC+ model to estimate the costs of a hypothetical efficient operator providing voice interconnection services, including the WACC of such an operator.

In that context:

- On 6 August 2025, as part of its voice interconnection inquiry, the ACCC published the Draft WACC Methodology Report prepared by CEPA. The ACCC:
 - noted that it intends to develop a general method that will inform its consideration of WACC issues across different regulatory decision-making processes, including its voice interconnection inquiry and nbn's RMA process; and
 - invited submissions on that report by Wednesday, 3 September 2025, including from stakeholders not directly involved with ACCC's voice interconnection inquiry.
- On 22 August 2025, the ACCC commenced a separate, parallel consultation on nbn's RMA, including on the WACC to apply for nbn in any RMD made by the ACCC for the Second Regulatory Cycle under nbn's SAU (**RMA Consultation**). The ACCC has invited submissions by Friday, 19 September 2025, including from stakeholders not directly involved in the RMA process. As part of this consultation, the ACCC published a separate draft note from CEPA on its WACC estimate for nbn.

nbn provides this response to the ACCC's request for submissions to its voice interconnection inquiry by 3 September 2025 – on the basis that this inquiry will inform the broader WACC method that may

be applied by the ACCC in the RMA process under nbn's SAU. This response is provided with a further report from Frontier Economics which responds to the CEPA's Draft WACC Methodology Report (**September Frontier Economics Report**).

nbn also intends to provide a separate and further response to the ACCC's separate request for submissions as part of its consultation on nbn's RMA by 19 September 2025, including in response to the WACC related questions that the ACCC has asked stakeholders in that consultation.

2.2 Structure of this submission

In this submission:

- Section 3 sets out the regulatory framework for estimating the WACC to apply in nbn's context and nbn's related concerns with the general approach adopted by CEPA in the Draft WACC Methodology Report; and
- Section 4 sets out particular concerns with aspects of the WACC method recommended by CEPA in the Draft WACC Methodology Report.

3 Concerns with CEPA's application of nbn's regulatory framework

3.1 Introduction

The Draft WACC Methodology Report refers to the regulatory framework for estimating a WACC for the purposes of nbn's RMA process, but appears not to describe or apply that framework accurately or consistently. The Draft WACC Methodology Report is dated 1 August 2025 and does not purport to respond to nbn's RMA as lodged on 2 July 2025, the WACC proposed by nbn in that RMA or nbn's explanatory materials in support of its proposal (including the June Frontier Economics Report).

For clarity, nbn describes the relevant framework below, to supplement:

- nbn's submission in support of its RMA, published by the ACCC on 24 July 2025 (in particular, Chapter 11 – *'Rate of return, inflation and gamma'*); and
- Attachment 11.1 of that submission, being the June Frontier Economics Report.

For the reasons set out in this submission, the ACCC should exercise caution in relying on aspects of the draft CEPA report to inform the method it uses to set the WACC for nbn when making its RMD. Any updated CEPA report that is relied upon to inform the ACCC's RMD needs to:

- correctly describe and apply the specific regulatory framework that applies to nbn so as to provide a sound basis for the relevant matters determined by the ACCC in its RMD; and
- examine the merits of positions before recommending them – rather than adopting positions primarily on the basis that other Australian regulators have adopted those positions previously.

3.2 The primary WACC rule applying to nbn's RMA process under the SAU

The SAU sets out rules for estimating the rate of return to be used in an RMA submitted by nbn and an RMD made by the ACCC.

In particular, clause 2G.2.4(d)(i) of the SAU provides that the rate of return will be determined by estimating a nominal vanilla WACC for each Financial Year which is '*commensurate with the efficient financing costs of a benchmark efficient entity with a similar degree of risk as nbn in providing the NBN Access Service, Ancillary Services and Facilities Access Service*'.¹ For the purposes of this submission, we refer to that requirement as the **primary SAU WACC rule**.

Further, clause 2G.2.4(d)(ii) of the SAU provides the rate of return must be calculated in accordance with the formula in that clause – as a weighted average of the expected return on equity for the Regulatory Cycle and the expected return on debt for the relevant Financial Year of the Regulatory Cycle.

The ACCC references these matters on page 43 of the Consultation Paper it released on 22 August 2025 as part of the RMA Consultation (**RMA Consultation Paper**).

3.3 The objectives to be taken into account when estimating the WACC under the SAU

Clause 2G.2.4(d)(i) of the SAU goes on to provide that in estimating the WACC in accordance with the primary SAU WACC rule described above, regard must be had to two objectives, being:

- the objective of producing reliable estimates of the market cost of capital in a wide range of plausible market conditions; and
- the objective of promoting stability in the rate of return over time.

For the purposes of this submission, nbn refers to those objectives as the **SAU WACC objectives**.

nbn included the SAU WACC objectives in the SAU to:

- recognise the relevance of methods for estimating the WACC that are capable of producing reliable estimates in a wide range of market conditions – including periods of financial crises, economic booms and market normality;
- emphasise the relevance of ensuring that rate of return estimates are not unduly influenced by volatility and random statistical noise; and
- promote estimates that are as close as possible to the true cost of capital associated with investing in a benchmark efficient firm with a similar degree of risk as nbn in providing the regulated services.

¹ In this context, the NBN Access Service, Ancillary Services and Facilities Access Service are the services covered by the SAU service descriptions and cover nbn's main services.

The SAU WACC objectives are express mandatory relevant considerations specifically for the task of estimating the WACC when making an RMD under nbn's SAU. The ACCC is required to take those objectives into account and give weight to them as fundamental elements in making its decision.²

3.4 Additional SAU requirement to consider Part XIC criteria

As noted in the Draft WACC Methodology Report, the SAU also requires the ACCC, when making an RMD, to take into account certain statutory criteria in section 152BCA(1) of the *Competition and Consumer Act 2010* (Cth) (**CCA**), which are the same matters that the ACCC must take into account when making an access determination under Part XIC of the CCA.³ nbn addresses these matters in Chapter 2 of its RMA Supporting Submission.

Similar statutory criteria applied to the ACCC's decision to accept nbn's SAU variation of August 2023, which introduced the primary SAU WACC rule for estimating the WACC described above.

The ACCC has stated in its RMA Consultation Paper (pages 43-44) that:

... our preliminary view is that the criteria specified in clause 2G.2.4.(d) of the SAU are consistent with outcomes that could be reasonably expected when having regard to the matters listed in s152BCA(1) of the CCA for the NBN.

In particular, the objective of producing reliable WACC estimates in a wide range of plausible market conditions can enhance confidence in WACC estimates being specified appropriately over time and lead to greater efficiency in long-term investment decisions.

We also consider that stability in the rate of return can promote efficient investment by NBN Co and downstream markets. Given the long-term nature of many investments by NBN Co, this can also facilitate more stable wholesale pricing paths for NBN services in the long run and in turn, the prices paid by end-users.

3.5 Concerns with general approach adopted by CEPA

nbn is concerned that, in preparing the Draft WACC Methodology Report, CEPA:

- has not set out to determine a WACC which meets the primary SAU WACC rule;
- has not given the SAU WACC objectives weight as fundamental elements in developing CEPA's proposed method for setting the WACC for nbn; and
- has not critically analysed the majority of positions it recommends – and instead adopts positions on the basis that other regulators have adopted those positions in other contexts in other sectors.

Relevantly, in the Draft WACC Methodology Report, CEPA states that in providing advice on an approach to estimating the WACC for regulated firms in the telecommunications industry, it has '*not started from first principles*' and instead aims to '*build on the substantial body of existing material*' from regulatory decisions in other regulated sectors which operate under different regulatory regimes.

² See, for example, *R v Hunt; Ex parte Sean Investments Pty Ltd* (1979) 180 CLR 322, 329; *Evans v Marmont* (1997) 42 NSWLR 70, 79–80; *Telstra v ACCC* (2008) 171 FCR 174 at [202]; *Telstra v Australian Competition Tribunal* (2009) 175 FCR 201 at [267]. See also the ACCC's [Draft Decision](#) in its Assessment of FANOC's Special Access Undertaking in relation to the Broadband Access Services dated 17 December 2007, page 30.

³ See clause 5.8 of the SAU, which refers to the statutory criteria in s152BCA(1) of the *Competition and Consumer Act 2010* (Cth).

Further, CEPA states that:

- where it considers there is 'broad consensus' among Australian regulators on an issue, CEPA only presents a 'lighter touch' discussion of that issue; and
- where there are competing approaches among Australian regulators, CEPA considers which approach '*could best meet the ACCC's statutory criteria in the context of the NBN SAU and voice interconnection*' (p. 4).

In that context, when estimating a WACC for nbn's RMA process, it is not clear:

- whether CEPA has considered whether the 'broad consensus' position of Australian regulators on given issues is consistent with the primary SAU WACC rule and the SAU WACC objectives – or whether CEPA has simply assumed that is the case as part of its 'lighter touch' approach (despite those rules and objectives being specific to nbn's regulatory context and only taking effect under nbn's SAU in 2023, and despite CEPA acknowledging in its draft report that '*wide acceptance of a single approach is no guarantee that the method will best meet the ACCC's statutory criteria*' – see p. 11); or
- whether CEPA considers the 'ACCC's statutory criteria' to be only the criteria in s152BCA(1) of the CCA (which the SAU requires the ACCC to take into account when making an RMD, and which CEPA notes are similar to criteria applied by the AER), or also the primary SAU WACC rule and the SAU WACC objectives (which apply specifically when estimating the WACC for nbn).

More broadly, while the Draft WACC Methodology Report makes reference to the primary SAU WACC rule, the report does not expressly set out to determine a WACC which meets the primary SAU WACC rule, and does not appear to structure or guide its analysis by reference to the primary SAU WACC rule. Rather, the report appears to treat the primary SAU WACC rule:

- as simply a factor to take into account rather than a substantive rule which must be satisfied having regard to various factors; and
- as a matter which may ultimately take lower priority or be given less weight than the separate criteria to which the SAU requires the ACCC to take into account when making an RMD (provided that the primary SAU WACC rule and related objectives are considered 'first').

For example, the Draft WACC Methodology Report:

- refers to a need to '*first give appropriate weight to the objectives set out in clause 2G.2.4(d)*' of the SAU – seemingly not drawing a difference between the primary SAU WACC rule and the two objectives in that clause to which the ACCC must have regard (regarding reliable estimates and promoting stability in the WACC);⁴ and
- refers to interpreting the 'reliable estimates' objective '*in the context of wider objectives*' – being the second SAU WACC objective (about 'promoting stability'), the primary SAU WACC rule and the Part XIC criteria for access determinations.⁵

⁴ Draft WACC Methodology Report, pp. 9-10, 24.

⁵ Draft WACC Methodology Report, pp. 70-71.

3.6 Any updated CEPA report used for nbn's WACC must describe and apply nbn's regulatory framework correctly

Any updated CEPA report for use in estimating nbn's WACC under the SAU must describe and apply nbn's regulatory framework.

As the ACCC notes in its RMA Consultation Paper, the ACCC is required to comply with the primary SAU WACC rule when estimating nbn's WACC. In doing so, the ACCC must give weight to the SAU WACC objectives as fundamental elements of its decision. This approach is the same as that required by the SAU for the WACC nbn proposes in an RMA.

It is not sufficient to simply adopt the consensus position of Australian regulators on particular aspects of the WACC method (if there is one), nor is it correct to determine aspects of the WACC only by reference to the criteria in s152BCA(1) of the CCA. Rather, the task is to determine a WACC which meets the primary SAU WACC rule (that the WACC must be commensurate with the efficient financing costs of a benchmark efficient entity with a similar degree of risk as nbn in providing the regulated services) – which is a substantive rule, not simply a factor for consideration.

In doing so, the ACCC must have regard to the SAU WACC objectives (about producing reliable estimates and promoting stability in the WACC) and give those objectives weight as fundamental elements in making its decision – and must also take into account the statutory criteria in s152BCA(1) of the CCA when making an RMD more broadly. The SAU WACC objectives and the s152BCA(1) criteria are factors to consider – they do not override the primary SAU WACC rule.

3.7 Any updated CEPA report should examine the merits of positions before recommending the ACCC adopt them

3.7.1 CEPA should examine the merits of the positions it recommends

nbn considers that the specific requirements for estimating its WACC (which are addressed above) mean that it is not sound for CEPA to recommend aspects of a WACC methodology to the ACCC primarily on the basis that other Australian regulators have adopted those positions previously. nbn's view on this matter is consistent the ACCC's rationale for examining its general WACC method to apply across regulated sectors – i.e., the ACCC seeks to develop a general method which could be taken into account when making regulatory decisions, where that method would be *informed* but not *determined* by previous regulatory decisions. For example, the ACCC's RMA Consultation Paper states:

We also note that economic literature and the practices of other regulators on the WACC and its constituent parameters could be informative to our consideration of appropriate methods. We therefore intend to consider these materials to inform our development of a WACC methodology to apply in this matter...

...new issues and additional information have emerged in the past decade in the approaches to estimating the WACC, which have been considered by other economic regulators. As such, the ACCC is undertaking a review of how it approaches the estimation of an efficient WACC for a regulated firm...⁶

In that context, nbn considers that to provide a sound and robust recommendation to the ACCC on the WACC method it should adopt to estimate nbn's WACC, CEPA should consider and critically evaluate the merits of various positions – where the merits of a position are not determined simply by whether previous regulators have adopted that position.

As noted in the September Frontier Economics Report:

- simply accepting an approach because that is the approach adopted by most regulators is a weak methodology and likely to simply promote 'group think' (where positions never advance and improve);
- it can be informative and useful to focus on positions which are exceptions rather than the norm – where doing so may reveal something that other regulators have missed or failed to address, and where a long-held consensus can be overturned if the merits of an alternative approach are sufficiently persuasive;
- dismissing positions regardless of their merit on the basis they are 'outliers' which are not adopted by other regulators could result in consumers being worse off – which would have been the case if, for example, the AER had not challenged the prevailing wisdom and adopted the 'trailing average' approach to estimating the cost of debt in 2013.

3.7.2 CEPA should not adopt a status-quo bias in favour of a status-quo which does not exist in nbn's context

Further, at other points in the Draft WACC Methodology Report, CEPA state that where there is uncertainty regarding the most appropriate method or a lack of 'overwhelming evidence' for a new method, it is prudent to have a level of 'status-quo bias' – on the basis that changing regulatory positions between regulatory cycles can impact incentives for investment and can produce windfall gains or losses for the regulated company.⁷ It is not clear whether CEPA have considered how this statement is relevant to setting a WACC method to apply in nbn's context – noting that:

- CEPA makes little reference to the method adopted by nbn to calculate the WACC applying under nbn's regulatory framework for the current Regulatory Cycle; and
- a change in the WACC method for nbn between the current and upcoming Regulatory Cycles could not result in any windfall gain or loss for nbn – given that the WACC method proposed by nbn in its RMA is largely consistent with that adopted in its SAU Variation application, and given that nbn is currently under-recovering its annual regulated costs (the 'ABRR', to which the WACC is an input) and that accordingly, nbn's prices are set through a price path determined independently of its regulated costs.

Instead of adopting a status-quo bias in favour of regulatory positions adopted previously in other regulatory sectors but not previously applied in nbn's context, nbn considers that in recommending a

⁶ RMA Consultation Paper, p. 44.

⁷ Draft WACC Methodology Report, pp. 12, 25.

WACC method to apply to nbn, CEPA must examine the merits of that method in the context of nbn's regulatory framework.

In the sections below, nbn addresses particular aspects of the WACC method proposed by CEPA, having regard to the June Frontier Economics Report and the September Frontier Economics Report.

4 Method for estimating the WACC

4.1 Introduction

The WACC proposed in nbn's RMA is calculated using a method recommended to nbn by Frontier Economics, building on and updating the previous reports prepared by Frontier Economics for nbn as part of the 2022-23 SAU variation process. That method is described in Chapter 11 of nbn's RMA Supporting Submission, the June Frontier Economics Report, and addressed further in the September Frontier Economics Report.

In this section 4 :

- **internal consistency in cost of equity parameters:** nbn addresses CEPA's recommendation that the cost of equity be estimated by pairing an estimate of the current or prevailing risk-free rate and an estimate of the long-term Market Risk Premium (**MRP**) derived using historical excess returns – which Frontier Economics notes is internally inconsistent and can produce volatile and implausible estimates of the cost of equity over time;
- **use of DGMs to estimate the MRP:** nbn addresses CEPA's view that a more detailed review of dividend growth models (**DGMs**) is required before recommending those models to produce a current estimate of the MRP – where Frontier Economics notes that all concerns raised by CEPA have already been addressed in nbn's proposed approach, and that the use of DGMs will promote more stable estimates of the cost of equity over time (given that DGM estimates of the MRP tend to move inversely with the risk-free rate);
- **the inclusion of utilities from other sectors in the equity beta comparator set:** nbn addresses the ACCC's suggestion that nbn may have a similar risk profile to regulated utilities / monopolies in other sectors and that consideration could be given to including those firms in the comparator set of firms used to estimate nbn's equity beta – where Frontier Economics and CEPA both acknowledge that nbn is likely to have materially higher exposure to systematic demand risk than those regulated utilities and is exposed to much more significant competition than typical utility network providers;
- **benchmark gearing:** nbn addresses CEPA's recommendation to use net debt (rather than gross debt) to calculate the benchmark gearing ratio – and Frontier Economics' view that there are sound reasons to use gross debt instead; and
- **the cost of debt:** nbn addresses CEPA's recommendation that the cost of debt for nbn be estimated using the 'trailing average' approach – which is consistent with nbn's proposal and recommended by Frontier Economics.

4.2 Internal consistency between cost of equity parameters

4.2.1 nbn's position: internal consistency in estimating the cost of equity

As explained in nbn's RMA Supporting Submission and the June Frontier Economics Report, the cost of equity in nbn's proposed WACC is calculated by giving equal weight to:

- a 'prevailing' or 'current' estimate of the cost of equity – calculated by pairing a current estimate of the risk-free rate with a current estimate of the MRP; and
- a long term historical estimate of the cost of equity – calculated by pairing a long term historical estimate of the risk-free rate with a long term historical estimate of the MRP.

This approach recognises that equity investors in infrastructure assets are likely to have regard to prevailing market conditions and to long-run average returns when making their investment decisions. Further, by ensuring internal consistency in the parameters used to calculate the cost of equity, this approach in turn ensures more stable and reliable estimates of the cost of equity and the overall WACC in a broad range of plausible financial market conditions.

This approach was originally developed by IPART in response to concerns with the position adopted by other regulators of pairing an estimate of the current risk-free rate with an estimate of the long term MRP, which is internally inconsistent and can produce volatile and unreliable estimates of the cost of equity over time.

nbn also adopted and explained the IPART approach in calculating the WACC for its SAU variations of 2022-23.⁸ CEPA has previously commented on this issue in a report to the AER in 2021, concluding that there is 'no good evidence' that the MRP should be assumed to be independent of the risk-free rate as the AER (and the ACCC) currently does.⁹ Yet, CEPA's recommended approach to the ACCC in the Draft WACC Methodology Report adopts precisely that unfounded assumption.

4.2.2 CEPA's position is internally inconsistent and should be rejected

In the Draft WACC Methodology Report, CEPA recommends that the ACCC adopt the approach of pairing an estimate of the current risk-free rate with an estimate of the long-term MRP.

In doing so, CEPA:

- states there is '*near consensus*' among Australian regulators that the risk-free estimate should be estimated using a current / short-term estimate and that CEPA '*see no reason not to align with this consensus view*' (p.14);

⁸ See: nbn's submissions to the ACCC of March 2022 (pp. 151-152) ([here](#)), July 2022 (pp. 44-48) ([here](#)); and November 2022 (Part E, pp.20-21) ([here](#)). See also reports by Frontier Economics for nbn of March 2022 (pp. 19-23) ([here](#)) and December 2022 (pp. 16-20) ([here](#)); and the report by CEG for nbn of June 2022 (pp. 34-46) ([here](#)).

⁹ CEPA, Report to the AER, *Relationship between RFR and MRP*, June 2021, available online here: <https://www.aer.gov.au/system/files/Report%20to%20the%20AER%20-%20Relationship%20between%20RFR%20and%20MRP%20-%2016%20June%202021.pdf>

- recommends a long-term estimate of the MRP (calculated using the 'Historical Excess Returns' or 'HER' method), noting that this is adopted by other Australian regulators, stating that:

...other Australian regulators do not consider that the risk-free rate and MRP must be calculated over the same estimation windows. Instead, they seek to combine what they regard as the most accurate forward-looking estimate of both parameters. For the risk-free rate, most regulators consider that current CGS yields provide the best estimate. Similarly, regulators use HER because they regard these as the best available forward-looking estimate of MRP. Therefore, regulators that rely on HER do not consider that these are inconsistent with a current risk-free rate.¹⁰

In response, the September Frontier Economics Report notes:

- that regardless of whether the MRP is estimated using current / prevailing / short-term data or long-term historical data, the resulting estimates are forward-looking estimates;
- there is still a difference between a forward-looking estimate that is estimated using current / prevailing / short-term data and a forward-looking estimate that is estimated based on long-term historical data;
- that adopting a 'mix and match' approach (i.e., inconsistently pairing an estimate of a current risk-free rate and a long-term MRP) will result in the cost of equity estimates moving one-for-one with changes in prevailing Government bond yields (given the long-term MRP estimate is essentially fixed or stable over time), producing more volatile estimates of the cost of equity over time, which will be counterintuitive and implausible in certain market conditions;
- that such a 'mix and match' approach has been criticised by IPART, CEG, the Supreme Court of Western Australia and CEPA itself; and
- that in the Draft WACC Methodology Report, CEPA focus on the position of other regulators but does not engage with the substance of IPART's criticism of adopting the internally-inconsistent approach to estimating the cost of equity CEPA now recommends to the ACCC. Nor does CEPA express an opinion on whether internal consistency is desirable, or purport to have evaluated how IPART's method has performed over time compared to the position of other regulators.

In that context, nbn submits that the ACCC should not adopt the position in CEPA's Draft WACC Methodology Report, despite that position being adopted historically by other Australian regulators except IPART. Instead, nbn submits the ACCC should engage with and adopt the position developed by IPART and proposed by nbn in its RMA.

4.3 The use of DGMs in estimating the prevailing MRP is established and appropriate

As explained in nbn's RMA Supporting Submission and the June Frontier Economics Report, in estimating the cost of equity for the purposes of its RMA, nbn estimated the current / prevailing MRP using four differently specified dividend growth models (DGMs).

¹⁰ Draft WACC Methodology report, pp. 14, 20.

In the Draft WACC Methodology Report, CEPA states that some Australian regulators place limited weight on DGM evidence and that a more detailed review of the available specifications and performance of these models over time would be needed to form a view on whether to recommend the use of such models.¹¹

In response, the September Frontier Economics Report notes that each of CEPA's concerns regarding the use of DGMs have already been addressed in the method adopted by nbn (which is not considered or addressed in CEPA's Draft WACC Methodology Report).

In summary, the September Frontier Economics Report notes that:

- CEPA raises a concern that there is no consensus on the correct specification of a DGM – which nbn's approach acknowledges and addresses by employing the average estimate from four differently specified DGMs (three that are used by IPART and one developed by the AER). A similar approach is adopted by IPART for the same reasons;
- CEPA raises a concern that there is no consensus on the appropriate inputs to a DGM – which nbn's approach acknowledges and addresses by calibrating each DGM (as suggested by the ACCC in the 2022-23 SAU variation process) – in particular, by selecting the assumed long-term dividend growth rate to ensure that the average MRP estimate produced by the relevant model over a historical period equates with the average observed MRP over that same period;
- CEPA has developed and adopted DGMs for use by UK regulators – without concluding that model selection or uncertainty over input assumptions was so problematic that DGMs should not be used at all;
- CEPA states it has not identified a clear rationale to guide how much weight should be attached to DGM evidence and so gives no weight to that evidence – which nbn's approach addresses by giving equal weight to a current / conditional estimate of the MRP (i.e., from the DGM method) and a long-term historical / unconditional estimate of the MRP (from the HER method), to reflect that investors in infrastructure assets are likely to have regard to both types of estimates when making investment decisions;
- CEPA considers that DGMs may not produce a more reliable estimate of the relevant market cost of capital than the HER approach, if the regulator is setting a fixed WACC allowance for a regulatory period – however, Frontier Economics points out that the HER approach on its own will only produce a reliable estimate of if the true MRP is fixed over time (which CEPA accepts is not the case) or if, through happenstance, prevailing market conditions coincide with long-run market conditions. In all other instances, an unbiased DGM estimate of the MRP will be a more reliable estimate of the MRP that is expected to prevail over a regulatory period because such an estimate will reflect prevailing (rather than long-run historical) market conditions; and
- CEPA appears reluctant to recommend the use of DGMs to estimate the MRP because it is not yet settled whether the risk-free rate and the MRP have an inverse relationship (despite CEPA readily assuming such a relationship in other contexts) – but the use of DGMs does not require or assume a *perfect* inverse relationship between cost of equity parameters, it merely permits and often produces such an inverse relationship, where placing weight on both DGMs and the HER method results in a robust and stable method for estimating the return on equity.

¹¹ Draft WACC Methodology Report, p. 5, 25.

4.4 Estimating beta and gearing using an appropriate comparator set

4.4.1 nbn faces greater demand and revenue risk than monopoly utilities in other sectors

As described in nbn's RMA Supporting Submission and the June Frontier Economics Report, the equity beta and gearing components of nbn's proposed WACC were estimated by reference to the observed equity betas and gearing ratios of a broad sample of listed international telecommunications firms providing broadband services on a monthly subscription basis. CEPA adopts a similar approach in its Draft WACC Methodology Report, which produces a similar asset beta and gearing as proposed by nbn.

In the RMA Consultation Paper, the ACCC seeks views on that approach and suggests that alternative approaches could be considered. This follows the ACCC previously raising concerns about the firms in the beta and gearing comparator set adopted by nbn in the 2022-23 SAU variation process. While the RMA Consultation Paper does not express a concluded view on these matters, it at least suggests the ACCC considers that nbn has similar characteristics and a similar risk profile to monopoly regulated utilities in other sectors (such as energy and water networks). In particular, the ACCC's RMA Consultation Paper states that:

If a 'narrow' approach is adopted, we consider that it would be appropriate that those telecommunication firms that are less comparable to the NBN Co are excluded from the comparator set. If a 'broad' approach is adopted, we consider that to the extent that firms in other sectors (e.g. regulated utilities) may share similar characteristics to NBN Co (e.g. significant monopoly power in providing essential services) it is worth considering whether inclusion of these firms can improve the accuracy and reliability of the equity beta estimate for the NBN.

nbn recognises that this suggestion may be informed by historical ACCC views that nbn is a monopoly or faces very limited competition.

nbn submits that any such views are outdated, not supported by the available evidence and should be re-examined. More information on the competition faced by nbn is set out in its RMA Supporting Submission of July 2025 and the June Frontier Economics Report,¹² and in nbn submissions for previous regulatory processes. CEPA reaches a similar conclusion in its Draft WACC Methodology Report, stating:

While NBN Co may bear some resemblance to regulated network utility providers of energy and water services, we consider that NBN is likely to have materially higher exposure to systematic demand risk than these companies, which is a key driver of beta risk for regulated firms. At the same time, its operating leverage and exposure to systematic asset stranding risk may be slightly higher. On balance, it is likely that regulated utility networks have a materially lower systematic risk exposure than NBN Co, and we do not propose to include these companies in the comparator sample...

...While customers of water or energy utilities are likely to reduce consumption in response to reduced income this is likely to be to a lower extent than for telecommunications services. We would particularly

¹² See: nbn, RMA Supporting Submission, July 2025, Chapter 2, pp. 16-18; Attachment 2.1 (report by Frontier Economics for nbn entitled *NBN Co's competitive environment*); Attachment 11.2, Annexure B (the June Frontier Economics Report).

expect this to be the case where utilities are exposed to economic regulation or can levy standing charges to cover fixed costs...

...We consider that NBN is exposed to much more significant competition than typical utility network providers, and we do not see a distinction in monopoly power relative to the sample comparators.¹³

Further, in its September report, Frontier Economics states that:

- it agrees with CEPA that nbn is likely to face considerably more competition than energy and water utilities, and that there is no material or significant distinction in market power relative to other firms within the comparator set of international broadband service providers;
- even if it was the case that nbn faces less competition than some firms within that comparator set, it is far from clear that would reduce nbn's systematic risk (and therefore be relevant to estimating equity beta, which only seeks to capture systematic risk that cannot be diversified away by investors) – and it would be unfortunate if the ACCC jumped straight to the conclusion that the competition faced by nbn is a key driver of systematic risk;
- the empirical evidence indicates that competition is not a strong driver of systematic risk – noting there are examples of industries with firms which face a high degree of competition with relatively low betas (e.g., supermarkets) and industries with firms which face limited competition with relatively high betas (e.g., water utilities and airports); and
- the more material driver of systematic risk for a firm is its exposure to revenue and volume risk, – such that the comparator sample should focus on firms drawn from the same industry (because these firms will tend to have similar exposure to revenue and volume risk).¹⁴

In that context, nbn continues to submit it is appropriate to draw the beta comparator set from firms in the telecommunications industry which provide broadband services on a monthly subscription basis – without including regulated utilities from other sectors which clearly have less demand and volume risk than nbn. nbn faces significant demand and revenue risk. It does not face inelastic demand and its regulatory framework does not allow nbn to increase prices to compensate for any decrease in volumes. Among other matters, the demand and revenue risk faced by nbn is evident in the very significant historical under-recovery of its revenue requirement, reflected in the Initial Cost Recovery Account (ICRA).¹⁵

nbn also agrees with the statements in the September Frontier Economics Report that:

- the market conditions that would result in a retail service provider losing customers or volumes would likely have the same effect on nbn – such that there is no substantive difference between the systematic demand and revenue risk faced by wholesale and retail providers of broadband services;
- CEPA's claim that nbn is likely to face lower bad debt risk than retail service providers is not supported by evidence – and while retailers would be expected to face a greater frequency of bad debts (because they have more customers), the bad debts faced by wholesalers are likely to be larger than those faced by retailers; and

¹³ Draft WACC Methodology Report, pp. 39, 51.

¹⁴ See June Frontier Economics Report, pp. 58-61

¹⁵ For completeness, the ICRA is a regulatory concept under nbn's SAU – it is not a standard accounting measure and does not appear in nbn's statutory accounts.

- there is no recent evidence that the beta associated with the supply of mobile broadband services is higher than that associated with the supply of fixed broadband services – and while mobile broadband service providers may face more competition, much of that competition is likely to be non-systematic.

4.4.2 CEPA should adopt a more objective approach to estimating equity beta

The September Frontier Economics Report also states that CEPA relies too much on subjective judgement to position nbn within the range of estimated betas of the comparator set and exercises that judgement based on weak evidence. For example, CEPA finds that nbn's systematic risk profile should more closely resemble that of its wholesale comparators and therefore positions nbn at the lower end of the range of betas of the comparison set, despite:

- those wholesale comparators having a near identical range as the overall comparator set (0.35-0.39 relative to 0.35-0.40);
- those wholesale comparators including wholesale tower companies, which typically enjoy the certainty of long-term contracted revenues, in comparison to the monthly subscription-based business models of nbn and other broadband providers; and
- the two wholesale companies which provide fibre broadband services (Chorus in New Zealand and Netlink Trust in Singapore) having materially different beta estimates.

Frontier Economics recommends the more objective approach of taking the median beta estimate of the full comparator set (to minimise the impact of outliers) and states that a more objective assessment of just the empirical evidence presented by CEPA would support, at the least, an estimate of nbn's beta of 0.37 (based on that being the mean of its four estimation periods and sample windows).¹⁶ Frontier Economics also suggest that further consideration should be given to the sample medians.

4.5 Use of gross or net debt in calculating gearing

The benchmark gearing ratio used to calculate nbn's proposed WACC was calculated using the 'gross' or 'total' debt of the comparator set firms (as reported by Bloomberg) to de-lever the observed equity betas of those firms into asset betas.

In comparison, in the Draft WACC Methodology Report, CEPA recommends the ACCC calculate gearing using net debt, on the basis that holding cash offsets financial risk which should lower a firm's beta and that '*a cleaner interpretation of the impact of the liquidity buffer on beta is desirable*'.¹⁷

In response, the September Frontier Economics Report states that:

- while there are arguments for either approach, there are sound grounds for the use of gross debt;

¹⁶ Although nbn's proposed method involves adopting the median beta estimate for the comparator sample, CEPA recommends using the mean estimate. That approach, applied to the individual beta estimates presented by CEPA, would support a point estimate for the asset beta of at least 0.37.

¹⁷ Draft WACC Methodology Report, August 2025, pp. 61-62.

- the main reason in favour of using gross debt is that it is more consistent with the overarching assumption regarding beta estimation – that the task is to estimate the WACC of a benchmark firm – and while firms may hold cash for a number of reasons, it is difficult to ‘second guess’ those reasons by assuming that all firms (or the benchmark firm) would use all cash holdings to retire debt; and
- the overall effect of this issue is relatively minor, given that using gross debt will result in higher gearing estimates and in turn produce lower asset betas, which is offset in the WACC through a higher proportion of relatively cheaper debt financing (and conversely, the use of net debt will result in lower gearing estimates and in turn produce relatively higher asset betas, which is offset by a lower proportion of debt financing).

4.6 Use of the 'trailing average' approach to the cost of debt

In the Draft WACC Methodology Report, CEPA recommends a 'trailing average' approach to estimating the cost of debt for nbn and an 'on the day' approach to estimating the cost of debt for voice interconnection services.

nbn supports the use of a trailing average approach for the purpose of determining the WACC to apply in any RMD made by the ACCC. That is the approach:

- proposed by nbn in its RMA of July 2025 (see Chapter 11 of nbn's supporting submission); and
- adopted by nbn to calculate the cost of debt values for the First Regulatory Cycle, which are stated in Attachment J of the SAU.

nbn notes CEPA's commentary in the Draft WACC Methodology Report which appears to question whether the trailing average approach is an available option for the purposes of the nbn RMA process under the SAU, stating that:

- the term 'market cost of capital' in the first SAU WACC objective could mean '*today's market cost of capital*', which in turn suggests the 'on the day' approach should be adopted;
- it is '*plausible that the phrase is ambiguous and that the wording should be interpreted in the context of the wider objectives*', which CEPA list as the second SAU WACC objective (about 'promoting stability'), the primary SAU WACC rule and the s152BCA(1) criteria; and
- therefore, '*a case could be mounted that a trailing average approach best aligns with the ACCC's statutory objectives for the NBN SAU*'.¹⁸

nbn rejects any suggestion that there is ambiguity in this respect. The SAU itself acknowledges that the trailing average approach is available for the purposes of the RMA and RMD process – that is inherent in the 'return on debt true-up' provision in clause 2G.2.6 of the SAU, which allows an adjustment to the forecast ABBRR '*if the expected return on debt for each Financial Year of the immediately preceding Regulatory Cycle was determined using a trailing average approach*'.¹⁹

More generally, nbn considers that adopting the trailing average approach is consistent with the primary SAU WACC rule – on the basis that a reasonable simplifying assumption is that a benchmark

¹⁸ Draft WACC Methodology Report, pp. 70-71.

¹⁹ See clause 2G.2.6 of the SAU and chapter 12 of nbn's RMA supporting submission of July 2025. The Draft WACC Methodology Report itself also separately acknowledges that provision is 'embedded' in the SAU – see p. 70.

efficient firm would stagger the issuance of debt so that only a small proportion of debt falls due and has to be refinanced each year. As CEPA and Frontier Economics note, this approach was first applied in Australia by the AER in its 2013 rate of return guideline (under a regulatory framework which also required that the WACC be commensurate with the efficient financing costs of a benchmark efficient entity with a similar degree of risk as the regulated firm) and a version of that approach has since been adopted by most Australian regulators.²⁰

Finally, even absent the context of nbn's regulatory framework, there is no reason to consider that the term 'market cost of capital' should be interpreted as meaning 'the cost of capital of refinancing the entirety of a firm's debt if that were done today'. Rather, the 'market cost of capital' faced by a firm is more realistically represented as a blend of the market rates at which the firm raised debt historically (where it must continue to service that debt and pay those rates until that debt matures) and debt raised at the prevailing market price when refinancing a portion of the firm's debt portfolio. That is the theory underlying the 'trailing average' approach, which has now been accepted almost universally by regulators in Australia.

We note that, in its RMA Consultation Paper, the ACCC states that '*there appears to be a sound argument for adopting the 'trailing average' approach for the RMD*' (p 52).

²⁰ Draft WACC Methodology Report, p. 69. nbn notes that that consideration of the trailing average approach by the Australian Competition Tribunal and Full Federal Court over 2016-17 related to the AER's method of *transitioning* from its previous application of the 'on the day' approach to its new application of the 'trailing average' approach – where the validity and rationale for the trailing average approach itself was not in dispute.