

**Optus Supplementary Submission to  
Australian Competition and Consumer Commission**

**on**

**Telstra's Access Undertaking for the Unconditioned Local Loop  
Service: Response to Draft Decision**

**March 2009**

## Impact on Investment

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- 1.1 In its ULLS undertaking, Telstra has proposed a substantial increase in the regulated price of the ULLS in Band 2 metropolitan areas, from \$14.30 (the regulated price at March 2008) to \$30.00 (the proposed undertaking price).
- 1.2 In its draft decision the ACCC recognised that “*a significant, unanticipated rate increase may also reduce the incentive for access seekers and potential new entrants to make infrastructure-based investment such as in DSLAMs*”.<sup>1</sup>
- 1.3 Optus submits that the proposed substantial, rapid increase in the ULLS charge would indeed significantly discourage investment.
- 1.4 An argument frequently made by Telstra and other incumbents is that regulated access leads to lessened investment in the telecommunications industry. However, this claim has been refuted in empirical research. On the contrary, there have been a number of studies which demonstrate the positive effects of unbundling on investment. For example:
  - i) Willig et al. (2002) confirmed the alternative ‘competitive stimulus hypothesis’: they found that low unbundling rates induce competition and stimulate investment by incumbents, such that “a one percent decrease in the UNE-P rate<sup>2</sup> generated between a 2,1 and 2.9 percent increase in ILEC investment.”<sup>3</sup>
  - ii) Willig (2003) noted that “the Competitive Stimulus Hypothesis follows naturally from basic economic theory and its understanding of competitive markets. Increased competition enabled by UNEs can be expected to result in lower retail prices both because of efficiency improvements induced by competition and because of the pressure competition places on above-cost pricing. .. Additionally, in a competitive environment, both the incumbent and the entrant will face enhanced incentives to improve quality and innovate with respect to services, leading to further investment.”<sup>4</sup>
  - iii) Hassett and Kotlikoff (2002) raise a number of interesting results in their study of market dynamics under a variety of potential industry structures. “First, telecom investment and output generally increase significantly and telecom prices decrease significantly when new firms enter a market. This is

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<sup>1</sup> ACCC, *Assessment of Telstra’s Unconditioned Local Loop Service Band 2 monthly charge undertaking*, Draft Decision, November 2008, p.51

<sup>2</sup> UNE: unbundled network elements (US). UNE-P: a combination of UNEs including the local loop and switching that allow end-to-end service delivery by an access seeker in the US.

<sup>3</sup> Based on Makova (2006) in Heinacher and Preissl, *Fibre-optic networks: On investment, regulation and competition*, CESifo DICE Report 3/2006, p.24.

<sup>4</sup> Willig, *Investment is appropriately stimulated by TELRIC*, unpublished manuscript, October 2003. Available from URL: [http://psc.ky.gov/pscecf/2003-00379/5200700\\_efs/04132004/MCI\\_ST\\_MTB\\_EX\\_14\\_04%2013%2004.pdf](http://psc.ky.gov/pscecf/2003-00379/5200700_efs/04132004/MCI_ST_MTB_EX_14_04%2013%2004.pdf)

true whether or not the entry occurs because of normal economic forces or as a result of wholesaling arrangements under which competitors rent access to customers from incumbents. ... Second, *unbundling* (forcing the ILECs to rent to the CLECs all or part of their network elements) can dramatically increase CLEC entry by lowering their costs of doing so. Third, competition raises consumer welfare relative to having a regulated monopoly in local voice and unregulated duopoly in broadband.”<sup>5</sup>

- iv) Ford and Spiwak (2004) conducted an econometric analysis to test the ‘unbundling deters investment’ hypothesis, in terms of the relationship between broadband deployment and local loop prices. The study found the opposite to be true, that “unbundled loop prices based on Total Element Long Run Incremental Cost (“TELRIC”) actually lead to *increased availability* of broadband services and increased availability of *competitive* broadband services defined as area with at least four broadband providers.”<sup>6</sup> The authors conclude that “this study adds to the mounting work showing that wholesale network access requirements (like unbundling) do not dampen broadband availability or investment incentives more generally.”<sup>7</sup>

1.5 Further, the Ford and Spiwak (2004) study also cites a number of studies in support of their empirical findings:<sup>8</sup>

- v) Research has already conclusively proved that the competition produced by the market opening provisions of the 1996 Act increased the incumbent Bell companies’ average net CapEx investment by \$759 per year, or about 6.4% per year in the aggregate, for each UNE-P access line. PHOENIX CENTER POLICY BULLETIN NO. 5, *Competition and Bell Company Investment in Telecommunications Plant: The Effects of UNE-P* (17 September 2003) (<http://www.phoenixcenter.org/PolicyBulletin/PolicyBulletin5.pdf>). *See also:*
- vi) PHOENIX CENTER POLICY BULLETIN NO. 6: *UNE-P Drives Bell Investment - A Synthesis Model* (17 September 2003) (available at: <http://www.phoenix-center.org/PolicyBulletin/PolicyBulletin6Final.pdf>);
- vii) G. S. Ford and M. D. Pelcovits, *Unbundling and Facilities-Based Entry by CLECs: Two Empirical Tests* (July 2002): [www.telepolicy.com](http://www.telepolicy.com);

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<sup>5</sup> Hassett and Kotlikoff, *The role of competition in stimulating telecom investment*, October 2002, p.3

<sup>6</sup> Ford and Spiwak, *The positive effects of unbundling on broadband deployment*, Phoenix Center Policy Paper No. 19, September 2004, p.4

<sup>7</sup> Ford and Spiwak, *The positive effects of unbundling on broadband deployment*, Phoenix Center Policy Paper No. 19, September 2004, p.12

<sup>8</sup> Ford and Spiwak, *The positive effects of unbundling on broadband deployment*, Phoenix Center Policy Paper No. 19, September 2004, p.2

- viii) T. R. Beard, R. B. Ekelund Jr., and G.S. Ford, *Pursuing Competition in Local Telephony: The Law and Economics of Unbundling and Impairment* (November 2002)([www.telepolicy.com](http://www.telepolicy.com));
  - ix) T. R. Beard, G. S. Ford, and T.M. Koutsky, *Mandated Access and the Make-or-Buy Decision: The Case of Local Telecommunications Competition* (December 2002) ([www.telepolicy.com](http://www.telepolicy.com));
  - x) R. D. Willig, W. H. Lehr, J. P. Bigelow, and S. B. Levinson, *Stimulating Investment and the Telecommunications Act of 1996*, Unpublished Manuscript (October 2002);
  - xi) K A. Hassett and L. J. Kotlikoff, *The Role of Competition in Stimulating Telecom Investment*, AEI PUBLICATION (October 2, 2002) ([www.aei.org/publications/pubID.14873/pub\\_detail.asp](http://www.aei.org/publications/pubID.14873/pub_detail.asp)). Hassett *et al.* (2002) perform a simulation rather than using actual data. *See also, Does Unbundling Really Discourage Facilities-Based Entry? An Econometric Examination of the Unbundled Local Switching Restriction*, Z-TEL POLICY PAPER NO. 4 (February 2002)([www.telepolicy.com](http://www.telepolicy.com));
  - xii) *Competition at the Crossroads: Can Public Utility Commissions Save Local Telephone Competition?*, Consumer Federation of America (October 2003) (<http://www.consumerfed.org/pr10.07.03.html>).
- 1.6 Optus submits that effective access regulation does not discourage efficient investment in infrastructure, and Telstra's proposed ULLS undertaking will not encourage such investment.