

# Draft Determination for model price terms and conditions of the PSTN, ULLS and LCS services

## Submission by PowerTel Limited

PowerTel Limited (**PowerTel**) welcomes the opportunity to comment on the Australian Competition and Consumer Commission's (**the Commission's**) *Draft Determination for model price terms and conditions of the PSTN, ULLS and LCS services*, dated June 2003 (**draft determination**).

This is a critical issue for PowerTel because Telstra's Domestic PSTN Originating and Terminating Access (**PSTN O/T**), Unconditioned Local Loop Service (**ULLS**) and Local Carriage Service (**LCS**) services (**core services**) are fundamental building blocks to the competitive supply by PowerTel of a number of retail and wholesale services in Australia.

Consequently, the price that Telstra charges for the core services has a direct and significant impact on the ability of PowerTel and other competitive carriers to compete in the provision of these retail and wholesale services with significant flow on effects to the long term interests of end users (**LTIE**).

## Executive summary

PowerTel agrees with the Commission that:

- a total service long run incremental cost (**TSLRIC**) approach should be adopted for the PSTN O/T and the ULLS services; and
- a retail-minus approach should be adopted for the LCS service, at least while the TSLRIC based cost of a local call is above that of retail prices.

However, PowerTel does not agree with the Commission that:

- the PIE II model should be used to determine the TSLRIC of PSTN O/T and ULLS services. PowerTel considers that the Commission should adopt an independently developed cost model; and
- the access deficit contribution (**ADC**) should be gradually removed from PSTN O/T charges over a 3 year time frame (2003/04 to 2005/06). PowerTel considers that the ADC should be immediately removed from PSTN O/T charges.

## A pricing comparison

The tables below compare the pricing proposed by Telstra for PSTN O/T, ULLS and LCS services in its most recent access undertaking with the Commission's indicative pricing specified in the draft determination.

### PSTN O/T pricing comparison

Year	Commission	Telstra
2003/04	1.2 cpm – 1.25 cpm	1.7 cpm
2004/05	1.1 cpm – 1.15 cpm	1.7 cpm
2005/06	0.9 cpm – 1.0 cpm	1.7 cpm

### ULLS pricing comparison<sup>1</sup>

Band	Commission <sup>2</sup>	Telstra
B1	\$11 - \$14	\$20
B2	\$19 - \$22	\$40
B3	\$35 - \$40	\$40
B4	\$80 - \$100	\$40

### LCS pricing comparison

Year	Commission	Telstra
2003/04	12.81 cents – 13.61 cents	17 cents

## Pricing analysis

Compared to Telstra's proposed pricing, the Commission's indicative pricing for PSTN O/T and LCS appears, on the surface, to be favourable to access seekers.

However, PowerTel considers that this is misleading because the prices proposed by Telstra in its most recent access undertaking:

- are very high; and
- in any event, are much higher than the prices which Telstra has commercially negotiated in the market.

<sup>1</sup> The prices in this table relate to the years 2003/04 to 2005/06.

<sup>2</sup> The Commission's proposed indicative prices are based on an assumed demand of around 140,000 lines by 2005.

PowerTel also considers that Telstra's proposed ULLS pricing is very high. In addition, PowerTel agrees with the Commission that:

- Telstra's proposed ULLS pricing is unlikely to promote broadband infrastructure competition. As a result, PowerTel considers that Telstra's proposed prices are unlikely to promote growth in the take up of broadband services; and
- the Commission's indicative pricing for ULLS is a step closer to what is required to stimulate broadband demand and competition in city and metropolitan (B1 and B2) areas where DSL technology is most suited.

Little, if any, DSL technology will be used in B3 and B4 because other technologies (eg wireless) are likely to be more suitable for the provision of broadband services in these areas. Consequently, averaging the price for ULLS over B2, B3 and B4 will lead to an increased price for B2 which is where services such as ADSL is likely to be most effective. This will act as an inhibitor to increased broadband penetration rates through competitive offerings

## **TSLRIC of PSTN O/T and ULLS**

The Commission, despite expressing some reservations, used Telstra's PIE II model to determine the TSLRIC of supplying the PSTN O/T and ULLS services. The Commission justified its use of the model on the basis that:

- PIE II is superior to the Commission's n/e/r/a/ model because it maps the locations of each end-user and network points in order to model the PSTN network;
- a preliminary assessment of the model revealed outcomes (particularly call conveyance costs) not unlike those of the n/e/r/a model; and
- the prices being determined are only indicative and will be used to guide the industry in negotiations rather than setting actual prices.

The Commission accepted all of Telstra's inputs to the PIE II model (although this was only on a preliminary basis and subject to further scrutiny) except for trench sharing in new estates, the WACC and network planning costs.

PowerTel does not agree with the Commission's use of the PIE II model to determine the TSLRIC of PSTN O/T and ULLS services because:

- Telstra has developed the PIE II cost model as a tool to help it further its own commercial interests by claiming the costs of providing these services are higher than they actually are;
- the PIE II model is not a true TSLRIC model as it adopts a scorched node instead of a scorched earth approach; and

- there are a number of significant flaws with the PIE II model, each of which will be addressed in PowerTel's submission to the Commission on Telstra's most recent access undertaking.

PowerTel considers that the Commission should adopt a cost model that nurtures competition, is in the LTIE and which can not be criticised for its lack of independence. This can only be achieved through use of an independently developed cost model.

## The Access Deficit Contribution

PowerTel agrees with the Commission's decision to reject proposals to:

- increase the ADC through allowing a local call surcharge; and
- apportion a higher percentage of the access deficit (**AD**) to calls rather than to minutes.

In addition, PowerTel is encouraged by the Commission's conclusion that it is difficult to justify the continued need for an ADC on PSTN access charges and that it should be removed.

Having decided to remove the ADC on PSTN O/T charges, the Commission then needed to decide between the following two ways to remove the ADC:

- redefine the AD to incorporate other line revenues from the CAN (eg ISDN and leased lines to name a few) – this would lead to a significant initial reduction in the ADC; or
- remove the ADC more gradually.

The Commission noted that the ADC could not be immediately removed (or reduced substantially) without certain negative impacts on:

- Telstra's legitimate business interests in being able to rely on the Commission's previous access pricing approach (which accepted an ADC) for its business planning; and
- some access seekers who have current contracts extending to at least 2004 and 2005 may find themselves stranded at significantly higher rates if immediate changes to the ADC were made.

The Commission concluded that a phasing out of the ADC over a 3 year period (2003/04 to 2005/06) was the preferred approach.

The Commission noted that the two main competing interests that needed to be balanced when making this decision were:

- competition and efficiency outcomes (ie the LTIE) will be promoted by removing the ADC from PSTN O/T charges more immediately; and
- the interests of Telstra and some access seekers are likely to be better met by phasing out the ADC over a 3 year period.

PowerTel suggests that most (if not all) access seekers would prefer the immediate removal of the ADC.

PowerTel considers that it is unlikely that many access seekers (if any) would have agreed rates with Telstra for PSTN O/T services beyond the end of 2003 or early 2004. Even if there were such arrangements in place, the access seekers involved could simply use a transit provider to avoid being stranded at a higher rate. While agreements for the supply of PSTN O/T may specify a rate for a certain period they very rarely (if at all) commit the access seeker to any level of traffic volume. As a result, an access seeker could simply switch traffic via another access seeker that had agreed a lower rate with Telstra.

Consequently, PowerTel considers that the competing interests to be balanced are competition and efficiency (ie the LTIE) on the one hand and Telstra's commercial interests alone on the other.

In deciding to phase out the ADC over 3 years, PowerTel considers that the Commission has given greater weight to Telstra's commercial interests than to the promotion of competition and efficiency (ie the LTIE). The industry has fought for many years now to have the AD properly defined. The Commission now recognises and agrees with these arguments but has chosen not to act to rectify the problem immediately and will instead gradually rectify the problem over time because it is concerned about Telstra's commercial interests.

Telstra is one of the most vertically integrated telecommunications companies in the world and continues to be the dominant wholesale and retail supplier of telecommunications services in Australia, including local, national, long-distance, international and mobile telephony, dial-up and broadband Internet, data, printed and on-line directories and pay TV (through its 50% ownership interest in Foxtel). The extent of Telstra's dominance of the sector is demonstrated by the fact that it receives almost 60% of total industry revenue, which is almost four times the revenue of Optus, its nearest rival, and over 90% of total industry profits.

PowerTel considers that any concern about Telstra's commercial interests should be given as little weight as possible and that the Commission should reconsider its decision not to immediately remove the ADC from Telstra's PSTN O/T charges.