

nbn submission

in response to ACCC's consultation paper in relation to nbn's revised variation to the NBN Co Special Access Undertaking

25 August 2017





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1. Introduction and executive summary

1. **nbn** appreciates the opportunity to respond to the ACCC's consultation paper dated 2 August 2017 (**Consultation Paper**) in relation to **nbn**'s application to vary its Special Access Undertaking dated 27 June 2017 (**Revised SAU Variation**).
2. Securing the timely approval of the Revised SAU Variation is a key priority for **nbn** and **nbn** is keen for this process to be concluded as soon as possible with the ACCC's acceptance of the Revised SAU Variation.

Non-price terms

3. **nbn** welcomes the ACCC's statements in the Consultation Paper in relation to non-price terms. The Revised SAU Variation addresses the key concerns identified by the ACCC in its draft decision (**Draft Decision**) in relation to **nbn**'s original application to vary the SAU (**Original SAU Variation**).
4. In addition to **nbn**'s decision to revert to its original approach in the SAU to the definition of NBN Co Network and the definition of network boundary points, **nbn** submits that its further changes to the co-existence and remediation provisions for FTTB and FTTN satisfy the Category B SAOs and are reasonable.

Price terms

5. **nbn** submits that the proposed MTM related price terms are consistent with the Category B SAOs and are reasonable.
6. While the ACCC has sought further comments on **nbn**'s overall approach to pricing, we note that the ACCC's role in assessing the Revised SAU Variation is limited to determining if the Revised SAU Variation, incorporating these MTM related price terms, is reasonable and consistent with the Category B SAOs. It is not within the scope of the ACCC's assessment to review or re-open aspects of the pricing construct that are not related to the additional MTM services, or which relate to existing services covered by the SAU.
7. **nbn** is encouraged by the ACCC's acknowledgement that **nbn**'s current pricing review, known as the pricing evolution review (**Pricing Evolution Review**), is an ongoing process and independent of the SAU variation.¹ **nbn** is also supportive of the ACCC's statement that commercial outcomes are likely to be preferable to any regulatory outcome.²
8. However, it is critical for the ACCC to let this process run its course without intervention or interference. This is necessary to ensure that **nbn** can work constructively with access seekers to develop an optimal pricing construct for **nbn** services.

¹ ACCC, Consultation Paper, page 25.

² Ibid, page 25.



9. Intervention through the SAU variation on **nbn's** broader pricing construct is out of scope of the ACCC's assessment powers. In any event, **nbn's** significant incentives, augmented by the regulatory backstops within the existing structure of the SAU, will ensure the reasonableness of **nbn's** current review of its pricing construct and allow for the achievement of economically efficient outcomes.
10. The effectiveness of **nbn's** incentives in practice is evident in **nbn's** approach to pricing to date.
11. **nbn** has already voluntarily reduced the effective price per Mbps of CVC for TC-4 capacity on several occasions and has also implemented modifications in how those reductions have been implemented to drive more efficient outcomes. **nbn's** current Pricing Evolution Review reflects **nbn's** commitment (consistent with its incentives) to optimise its pricing approach over time.
12. A supplementary expert report, prepared by Professor Ordovery and Dr Shampine, confirms that **nbn's** incentives are working as intended in practice and that experimentation with price levels and pricing structures, to better gauge the state and responsiveness of downstream demand and its likely evolution, is to be expected in such an environment.
13. Accepting the Revised SAU Variation will ensure that all MTM services become subject to the same regulatory framework, meaning that the ACCC's regulatory backstop powers can work as intended across **nbn's** entire suite of services. This will not be possible if the ACCC does not accept the Revised SAU Variation. Such an approach will also ensure that a technologically neutral approach to regulation of **nbn** services is preserved.
14. **nbn's** approach of direct engagement with access seekers on pricing matters is superior to any other options that have been canvassed so far, such as regulatory intervention in relation to MTM prices (where not covered by the SAU as it currently applies).
15. Alternative approaches are not at all straightforward and raise significant practical issues, including:
 - (a) disparate regulatory approaches across different regulatory instruments;
 - (b) different regulatory approaches depending on the **nbn's** access technology, with pricing matters for additional MTM services (i.e. HFC, FTTB and FTTN) potentially falling outside of the SAU pricing construct; and
 - (c) a heightened risk of regulatory error, driven by information asymmetry and the complexities in setting wholesale prices in a dynamic and fast-moving market; and
 - (d) undermining investment incentives in relation to network technologies that are regulated outside of the scope of the SAU and increased uncertainty in relation to how future services, such as FTTC, will be regulated.
16. To the extent that there are other matters contributing to current issues in the sector, such as margin erosion from retail pricing strategies focussed on preserving market share, then these are



matters that can be considered and addressed separately by the ACCC as part of its market review. **nbn** has previously made submissions to the ACCC Market Study, identifying its concerns in relation to downstream markets.

17. Accordingly, it is possible for the ACCC to accept the Revised SAU Variation to bring the additional MTM technologies within the scope of the SAU while the Pricing Evolution Review runs its course.
18. To the extent that eventual changes to **nbn**'s pricing construct or levels are incompatible with the SAU pricing framework, then this will entail the lodgement of a further SAU variation that would permit the ACCC to assess the reasonableness of any changes to the price terms. **nbn** will have strong incentives to submit a further SAU variation, if required, to ensure that it is able to obtain regulatory protection in relation to any changed approach to pricing.

Structure of this submission and next steps

19. This submission is structured as follows:
 - (a) submission on non-price terms – section 2;
 - (b) submission on price terms – section 3;
20. Given the length of the original variation process and the small number of substantive changes to the non-price terms that remain the focus of assessment by the ACCC, **nbn** encourages the ACCC to proceed promptly to accept the Revised SAU Variation and to do so on expedited basis.
21. This submission is intended to augment (and be read together with) the supporting material and submissions to our Revised SAU Variation and the Original SAU Variation.
22. **nbn** may provide supplementary submissions to assist the ACCC in its consideration of the Revised SAU Variation, including in response to any further industry submissions.



2. Non-price terms

2.1 Definition of NBN Co Network and network boundary point

23. We are supportive of the ACCC's statement in relation to **nbn's** position on the definition of NBN Co Network and the network boundary point:³

"NBN Co has addressed the concerns of the ACCC and stakeholders on matters relating to service description by adopting the recommendations proposed by the ACCC in the draft decision. NBN Co has now reinstated the network boundary point definition and removed the reference to 'any other telecommunications network' from the definition of NBN Co Network. The ACCC considers the proposed changes in the revised variation on service description provides a high degree of certainty to access seekers about the services provided by NBN Co over the term of the SAU"

24. As **nbn** has not included the previously proposed changes in the Revised SAU Variation, these issues do not require any further assessment by the ACCC. Accordingly, **nbn** does not have any further submissions to make in relation to the definition of NBN Co Network and the definition of network boundary point in Attachment A of the SAU.

2.2 Co-existence and remediation provisions

25. **nbn** welcomes the ACCC's comments on the **nbn's** proposed approach to the co-existence and remediation provisions.

26. The ACCC has stated:

- (a) **nbn** has "addressed a key concern of the ACCC and stakeholders on the duration for which the provisions would be locked in";⁴ and
- (b) "Considering that the disconnection of special services will not begin until 2019 and that the expected timeframe for final disconnection of special services is three years following this date, having the co-existence provisions apply for the duration of module 1, with the option of including co-existence provisions after this date through the replacement module process, could be appropriate. Further, the fact that no cases of remediation have been recorded could be evidence that the current arrangements are working effectively and issues with copper lines are being addressed at an earlier stage, which lends further support to having the provisions apply for the duration of module 1, as opposed to a shorter period".⁵

³ ACCC, Consultation Paper, page 13.

⁴ Ibid, page 17.

⁵ Ibid, page 17-18.



27. **nbn** submits that its proposed changes are consistent with the Category B SAOs and the reasonableness criteria. **nbn** submits that the limitation of the proposed terms and conditions to Module 1 would promote **nbn**'s legitimate business interests, while also meeting the interests of persons who have a right to use the services.
28. As the ACCC recognised in the ACCC Draft Decision,⁶ **nbn** already faces significant incentives to minimise co-existence time and to undertake remediation. These incentives are highly likely to persist for the duration of Module 1.
29. The end of Module 1 also represents a logical point to "sunset" the proposed co-existence and remediation provisions and this coincides with a range of other significant changes to the SAU (e.g. a move to Replacement Modules).
30. To the extent that co-existence and remediation issues persist beyond the end of Module 1, it is open for **nbn** to use the Replacement Module Application regime to separately address the issues as they exist at that time. **nbn** has previously indicated that it expects remediation to be a long-term issue associated with degradation of cables and joints in the copper network.⁷
31. We also consider that the additional refinements we have made, including to narrow the scope of services that can be covered by the co-existence provisions and the refinement of the remediation provisions to address interference management (and consequential changes), are reasonable.
32. In response to the ACCC's question as to whether there are other ways outside the SAU that **nbn** could provide further information to access seekers regarding the number of services affected by the co-existence and remediation provisions,⁸ **nbn** notes that it already faces incentives to address co-existence and remediation issues in a timely manner and, consistent with this, to provide relevant information to access seekers. These incentives are being realised in practice.

⁶ ACCC, Draft Decision, p.34.

⁷ **nbn**, Submission to ACCC consultation paper 26 August 2016, p.5.

⁸ ACCC, Consultation Paper, page 18.



3. nbn pricing matters

3.1 Overview

33. This section 3 sets out **nbn's** responses to the matters for consultation raised by the ACCC in section 4.4 of the Consultation Paper. We have not directly responded to matters that have previously been addressed in our supporting submission, or interested party submissions that were made in response to the Draft Decision.
34. **nbn** submits that the proposed MTM related price changes are consistent with the Category B SAOs and are reasonable. In particular:
- (a) **The scope of ACCC's assessment powers are limited to MTM-related price changes:** While the ACCC has sought to seek further comments on **nbn's** overall approach to pricing in its Consultation Paper, **nbn** notes that the ACCC's role in assessing the Revised SAU Variation is limited to determining if the incorporation of these MTM related price changes are reasonable and consistent with the Category B SAOs. It is not within the scope of the ACCC's assessment to review or re-open aspects of the pricing construct that are not related to the additional MTM services, or which relate to existing services covered by the SAU.
 - (b) **The Pricing Evolution Review is separate to the SAU variation process:** **nbn** is encouraged by the ACCC's acknowledgement that the Pricing Evolution Review is an ongoing process and independent of the SAU variation. **nbn** is also supportive of the ACCC's statement that commercial outcomes are likely to be preferable to any regulatory outcome. However, it is critical for the ACCC to let this process run its course without intervention or interference, to maximise the possibility of **nbn** working constructively with access seekers to develop an optimal pricing construct. Intervention, for which there is no reasonable basis, would involve the ACCC cutting across an existing review of **nbn's** pricing and will undermine, rather than augment, that initiative by creating an environment that may divert some access seekers into regulatory arbitrage and posturing rather than commercial engagement with **nbn**.
 - (c) **nbn's incentives are working in practice:** Intervention through the SAU variation process on **nbn's** broader pricing construct is out of scope of the ACCC's assessment powers. In any event, as a wholesale only, single service firm facing substantial sunk costs that need to be recovered, **nbn** has strong incentives to price efficiently and to drive the uptake and usage of higher bandwidth services. This is being borne out in practice through **nbn's** strong track record of proactively reducing the effective CVC price per Mbps for TC-4 capacity and adopting a more economically efficient method for implementing the CVC pricing construct. **nbn's** Pricing Evolution Review takes matters further, potentially resulting in more substantive changes to **nbn's** pricing construct and/or levels to drive more efficient outcomes in the market. These initiatives have occurred voluntarily, and



demonstrate the operation of **nbn's** incentives, and without the need for any direct regulation of **nbn** services.

- (d) **Not incorporating the additional MTM services within the SAU will create inconsistencies in the regulatory framework for nbn services:** if the additional MTM services are not incorporated into the SAU pricing framework, then the various regulatory protections or backstops afforded by the SAU (including maximum regulated prices and the ACCC's revenue neutral price rebalancing power) will not apply to FTTB, FTTN and HFC services. This would also entail different forms of price regulation for the additional MTM services versus those services that were originally incorporated into the SAU. It will create two different pricing approaches based on technology even though the underlying service construct and services are the same across technologies. The better approach would be to include the additional MTM services within the scope for the SAU to have a single and consistent regulatory approach across technologies.
- (e) **Alternative forms of regulatory intervention are not straightforward:** Intervention by the ACCC in the wholesale pricing of the additional MTM services would be premature and give rise to significant risks. In addition to cutting across the Pricing Evolution Review, the consequences of intervention include a significant risk of regulatory error. This will increase the costs associated with regulation, heighten the prospects of regulatory gaming and skew investment away from technologies that are not covered by the SAU.
- (f) **Future changes to be nbn's pricing construct are likely to require ACCC review:** While it is difficult (and unnecessary, in this context) to speculate how **nbn's** pricing construct and/or levels may change following the Pricing Evolution Review, it is likely that if any changes to the **nbn** pricing construct cannot be accommodated within the current SAU framework, then this would require **nbn** to submit a further SAU variation for such changes to gain the benefit of the regulatory protection afforded by the SAU. As the ACCC would need to be satisfied that those structural changes are consistent with the applicable statutory criteria, the ACCC would have a critical role in assessing structural changes to **nbn's** pricing through any future SAU variation that may be required if the Pricing Evolution Review entails more structural changes.
- (g) **Developments in the retail market are separate to the SAU variation process and should be addressed as part of the ACCC's Market Study:** Emerging retail market issues, such as falling retail margins and consequential trade-offs between price and quality, are attributable to a range of factors, not just the CVC charge for TC-4 capacity (as has been alleged by some access seekers). This includes the current "land grab" as access seekers seek to maintain or capture market share in the transition to the **nbn** and the failure of access seekers to take steps that could potentially increase ARPU. It is vital that these developments, which are independent of the SAU, to be given greater attention by the ACCC as part of its Market Study. These should not delay acceptance of the Revised SAU Variation.



3.2 nbn's incentives in relation to pricing are working in practice

35. In our supporting submission to the Revised SAU Variation, we provided extensive commentary on **nbn's** incentives to price efficiently to achieve cost recovery. This included the existence of significant 'long term revenue sufficiency risk' that will extend well beyond the initial rollout and migration, along with the emergence of potential inter-modal competition from other networks (including competing fixed line builds, fixed wireless, 4G and eventually 5G services).
36. When these incentives are combined with the maximum regulated prices established through the SAU and the additional protections that have been built within the regulatory architecture of the SAU (e.g. the ACCC powers to undertake a revenue neutral price rebalancing, etc.), **nbn** faces a strong set of incentives to:
- (a) incur costs and invest efficiently;
 - (b) price efficiently to drive the uptake and usage of higher value services; and
 - (c) ultimately, increase the prospects of long term cost recovery.
37. These incentives work together as a package to produce economically efficient outcomes that also promote **nbn's** legitimate business interests, the interests of access seekers and ultimately the interests of end users.
38. Critically, **nbn's** incentives are not merely theoretical based on **nbn's** status as a wholesale only company. These incentives can now be seen operating in practice in a material way and will continue to be seen for the foreseeable future as **nbn** seeks to increase take up and usage for the benefit of the whole sector.
39. To date, these incentives have manifested:
- (a) as reductions in the CVC charges;
 - (b) as modifications in how those reductions have been implemented to drive more economically efficient outcomes (e.g. greater scope for competitive differentiation and trade-offs between price and quality); and
 - (c) as a comprehensive review of the pricing construct to determine whether there is a better approach for realising efficient outcomes as the sector evolves and develops.
40. These incentives have culminated in a progressive reduction of effective prices per Mbps of CVC TC-4 capacity, notwithstanding the fact that **nbn** has had the ability to charge higher prices. This includes:



- (a) a reduction in the CVC charge per Mbps for all traffic classes by 12.5% from an initial price of A\$20.00 to A\$17.50;⁹
- (b) the introduction (for all network types except satellite¹⁰) a further set of discounts for the CVC (TC-4) charge, known as dimension based discounts (DBD), to provide higher levels of future price certainty to service providers and to create incentives on service providers to increase their usage of the **nbn** to promote higher speed services;¹¹ The initial implementation of the DBD scheme saw the effective CVC (TC-4) charge being reduced to A\$15.75 in June 2016 and further down to \$15.25 per Mbps in December 2016 (for all service providers on an industry wide basis);¹²
- (c) the introduction of a service provider specific dimension-based discount scheme on 1 June 2017, which allows for even deeper discounts for higher levels of CVC dimensioning based on the capacity usage of each RSP.¹³ This approach links the CVC price to the amount consumed by each service provider (rather than taking the industry average) and is intended to create greater scope for competitive differentiation of downstream services based on appropriate trade-offs between price and service quality. Based on current usage levels, the average effective unit price is A\$14.40 per Mbps of CVC capacity,¹⁴ with much heavier discounts for more aggressive dimensioning.¹⁵

41. Ordover and Shampine have made the following observations in relation to **nbn**'s pricing conduct in their supplementary expert report:¹⁶

"We note that all of the price changes discussed are reductions and discounts, and conclude that these behaviors are consistent with nbn being subject to and responsive to market signals. It is not surprising that the need to stimulate incrementally profitable take-up leads to discounting. These are precisely the behaviors we would expect to see a firm like nbn engage in to encourage take-up and usage of its services and achieve its cost recovery objectives".

⁹ This price is contractually specified as part of WBA2. From 1 July 2017, A\$17.50 (plus CPI – 1.5%) has also been the maximum regulated price for the CVC price under the SAU.

¹⁰ For **nbn**'s satellite service, an access seeker needs to purchase CVC capacity that is separate from that used in respect of all other **nbn**TM network types. This is related to the management of the scarce capacity on the satellite network

¹¹ The initial implementation of the DBD scheme was through the use of an industry wide, industry average approach, where the discount on CVC per Mbps increased (in steps) as the CVC dimensioning (CVC per AVC) increased.

¹² nbn, Media Release: New CVC pricing model to drive enhanced broadband service, 17 February 2017. Available at, <http://www.nbnco.com.au/corporate-information/media-centre/media-releases/New-CVC-pricing-model-to-drive-enhanced-broadband-service.html>

¹³ nbn, Discount Notice: CVC Dimension Based Discount, 27 February 2017. Available at, http://www.nbnco.com.au/content/dam/nbnco2/documents/sfaa-cvc-dimension-based-discount-notice_effective_1_June_2017_2016_20170227.pdf

¹⁴ nbn CEO, Position Paper: Why are data speeds sometimes lower than what consumers were expecting? Is nbn to blame with its infamous CVC charge?, page 2. See, <http://www.nbnco.com.au/content/dam/nbnco2/documents/is-nbn-cvc-charge-to-blame-position-paper-170731.pdf>

¹⁵ nbn, Discount Notice: CVC Dimension Based Discount, 27 February 2017. Available at, http://www.nbnco.com.au/content/dam/nbnco2/documents/sfaa-cvc-dimension-based-discount-notice_effective_1_June_2017_2016_20170227.pdf. See discount table on page 2.

¹⁶ Supplementary Expert Report of Janusz A. Ordover and Allan L. Shampine, 24 August 2017, paragraph 15.



42. The outcomes from **nbn's** implementation of the current DBD scheme appear positive, with the ACCC recently noting in the context of its latest NBN Wholesale Market Indicators Report that *"the average CVC capacity acquired per user has increased by almost 10 per cent during the quarter"*.¹⁷
43. These developments show that **nbn's** incentives are working in practice (and as intended).

3.3 The Pricing Evolution Review confirms our incentives are working and needs to be allowed to run its course

44. **nbn** is currently undertaking the Pricing Evolution Review, including in response to industry concern on CVC pricing levels and other market developments utilising the Product Development Forum (**PDF**).
45. Consistent with its customer engagement approach to date, **nbn** is taking a collaborative approach with this review, consulting extensively with PDF participants and using a co-design approach to develop and validate the various pricing options that are being considered. The use of such techniques is a demonstration of **nbn's** incentives to develop a pricing construct that promotes the interests of access seekers, in addition to **nbn's** own legitimate business interests.
46. Some of the pricing options that are currently being considered by **nbn** include (amongst other options):
- (a) a rebalancing of the AVC and CVC charge;
 - (b) changes to AVC price steps; and
 - (c) AVC-only pricing.
47. **nbn's** willingness to undertake a comprehensive review of its pricing construct shows the use of price experimentation by **nbn** to drive higher levels of uptake and demand in relation to **nbn** services, which in turn is likely to produce a more economically efficient outcome relative to **nbn** leaving its prices static (or where prices are locked in for a fixed period by regulatory fiat).
48. **nbn's** consideration of such options, and approach to date with price experimentation, is consistent with the observations made by Ordover and Shampine in their supplementary report:¹⁸
- "We expect that this would entail experimenting with price levels and price structures (e.g., finding the proper balance between fixed and variable components of a multi-part pricing scheme) to better gauge the state and responsiveness of downstream demand and its likely evolution, subject to the price caps in the SAU. That is, given the dynamic nature of the industry, we would expect both the*

¹⁷ ACCC, Media Release, ACCC releases quarterly report on the NBN wholesale market, 11 August 2017. See, <https://www.accc.gov.au/media-release/accc-releases-quarterly-report-on-the-nbn-wholesale-market-3>

¹⁸ Supplementary Expert Report of Janusz A. Ordover and Allan L. Shampine, 24 August 2017, paragraph 13.



prices and price structures set by a firm like nbn to change over time, and, to the extent permitted, across different geographic areas. A firm in nbn's position has strong incentives to encourage take up and overall usage of its network. Such behavior especially makes sense in the presence of joint and common fixed costs, provided, of course, that the firm can earn positive net income on the incremental demand".

49. It is critical for the ACCC to let the Pricing Evolution Review process run its course, without any intervention or interference.
50. This is consistent with the ACCC's decision to accept the original SAU. The ACCC has previously recognised that **nbn** will be self-motivated *"to invest in and operate its network efficiently and to encourage efficient use of its network."*¹⁹ These factors have already been recognised by the ACCC in accepting the SAU, as being capable of motivating **nbn** *"to set new prices efficiently of its own accord."*²⁰
51. The ACCC has also previously noted the existence of these incentives in relation to **nbn**'s observed behaviour in the development of new prices (which would be analogous to the situation that would exist if **nbn** made substantive changes to the price construct as part of the Pricing Evolution Review):²¹

*"Importantly, while the SAU permits the ACCC to determine new prices, **if NBN Co's observed behaviour indicates that it is responding to the incentives mentioned above, the ACCC expects that it would not be necessary for it to determine initial maximum regulated prices.** As noted above, the ACCC considers that it is appropriate for NBN Co to have a degree of pricing flexibility for new products, and that allowing this flexibility can lead to efficient outcomes".* (our emphasis)

52. **nbn** also supports the ACCC's statement in its Consultation Paper that it *"welcomes"* nbn's announcement of its Pricing Evolution Review and that it *"considers any agreed outcome on pricing between NBN Co and its customers is likely to be preferable to any regulatory outcome"*.²²
53. However, we also note that the ACCC has suggested *"if a commercial outcome cannot be achieved, the ACCC will consider whether changes to NBN Co's pricing could be made that would promote more efficient outcomes for NBN Co, RSPs and for consumers"*.²³
54. **nbn** is encouraged by the ACCC's acknowledgement that **nbn**'s current pricing review is an ongoing process and independent of the SAU variation. **nbn** also acknowledges the role of the ACCC's

¹⁹ ACCC, "ACCC Draft Decision on the Special Access Undertaking lodged by NBN Co on 18 December 2012", April 2013, section 5.3.1, p. 99.

²⁰ Ibid, 5.4.2.2, p. 121. See also ibid, 5.3.1, p. 100 and 5.3.3, p. 120.

²¹ ACCC, NBN Co Special Access Undertaking, Final Decision, 13 December 2013, page 87.

²² ACCC, Consultation Paper, page 25.

²³ Ibid, page 25.



backstop powers under the SAU. However, **nbn** also considers that the ACCC needs to ensure that **nbn** has sufficient space to constructively engage with access seekers prior to considering intervention (i.e. that the ACCC does not take any steps that could compromise **nbn**'s ability to do so).

55. Regulatory arbitrage and posturing by access seekers would be suboptimal. Regulatory intervention in relation to pricing matters also has significant complexities, as further described in section 3.5 below.

3.4 Not incorporating MTM services within the SAU will create inconsistencies in the regulatory framework

56. A key aspect of the SAU pricing framework is that **nbn**'s incentives provide the basis for **nbn** to realise efficient outcomes without the need for intervention by the ACCC in pricing decisions.
57. However, the SAU pricing framework still provides the ACCC with the power, which is intended to operate as a regulatory backstop, to undertake revenue neutral price rebalancing²⁴.
58. The regulatory certainty facilitated by the rebalancing mechanism will be significantly lower if FTTB, FTTN and HFC services are not included within the SAU because the ACCC would also need to utilise its other powers under Part XIC of the CCA to address the pricing of those services.
59. Accordingly, acceptance of the Revised SAU Variation will have the positive effect of extending the operation of the various regulatory price protections that are available under the SAU to the bulk of **nbn**'s services. This will complement the incentives that **nbn** currently has in respect of those MTM services and provide regulatory certainty.
60. Such an approach would also facilitate a continued technologically neutral approach to the regulation of **nbn** services. It would avoid a situation (discussed further in section 3.5 below) where potentially two different pricing approaches could apply to the services currently covered by the SAU and to FTTB, FTTN and HFC services even though the underlying service construct and services are the same across technologies. The better approach would be to include the additional MTM services within the scope of the SAU to have a single and consistent regulatory approach across technologies.
61. On this basis, **nbn** submits that the extension of the SAU to include the additional MTM related price terms is reasonable, relative to the counter-factual where the current scope of the SAU is maintained without any variation and the additional MTM services are addressed through an alternative regulatory instrument. It would promote:
- (a) the LTIE, notably by promoting competition in markets for listed services by creating a more consistent and predictable regulatory environment across all **nbn** technologies – it

²⁴ The ACCC also has the reserve power under the SAU to intervene in regard to new product pricing.



would do this by adopting a single regulatory approach to all **nbn** services, regardless of technology. In doing so, it would avoid different approaches to price regulation across technologies, which in turn will avoid some of the significant issues identified in section 3.5 below; and

- (b) the interests of persons who have rights to use the declared service by subjecting all prices for the additional MTM services to the overarching price protections set out in the SAU, including the powers available to the ACCC to undertake revenue neutral price rebalancing.

3.5 Alternative methods of regulation of **nbn** pricing for MTM raises significant risks for sector and the ACCC

- 62. If the ACCC did not accept the Revised SAU Variation and sought to intervene separately in relation to the price of the additional MTM services (e.g. through an access determination), **nbn** submits that this counter-factual is not at all straightforward and will raise some significant complications in the regulatory framework.
- 63. First, the ACCC will expose the sector to significant risk of regulatory error due to the inevitably blunt nature of its alternative regulatory powers and information asymmetry issues (e.g. around demand elasticities and willingness to pay). **nbn** needs flexibility and the ability to experiment to ensure it can innovate and act on its incentives to increase take up and usage in an environment where end user willingness to pay is evolving.
- 64. It is critical to note that price setting in relation to **nbn** services is fundamentally different to setting prices in a legacy context, particularly for products that have limited bandwidth capabilities and relatively static demand profiles. Pricing in an **nbn** context is less well suited to regulatory intervention on a periodic basis than traditional legacy services, due to the faster pace of change and evolving forms of usage and demand. This is evident in the frequency of changes in the effective price per Mbps of TC-4 CVC capacity since the commencement of the rollout.
- 65. Ordover and Shampine have observed in their supplementary report:²⁵

"Direct price regulation would be a significant burden on both the ACCC and nbn, would raise significant concerns about regulatory opportunism (as discussed above), and would lack the flexibility of the present structure. In recent years, nbn has repeatedly lowered its prices and experimented with different pricing structures. It is implausible that such flexibility could be accomplished if were prices being directly set by the ACCC through an ongoing regulatory process. Indeed, one of the great advantages of the downward pricing flexibility contained in the SAU structure is that a firm like nbn can respond to new information and industry dynamism in ways and in a timely manner that a price-setting regulator cannot".

²⁵ Supplementary Expert Report of Janusz A. Ordover and Allan L. Shampine, 24 August 2017, paragraph 25.



66. Secondly, **nbn** strongly agrees with the view expressed by the ACCC in the Draft Decision that the use of a single regulatory instrument that applies for all **nbn** network types (as compared to a counter-factual in which the SAU is not varied and the ACCC potentially intervenes via an access determination in relation to FTTB, FTTN and HFC) is likely to promote the interest of access seekers by providing long-term certainty and clarity around **nbn**'s commitments and obligations.²⁶
67. In the alternative situation, **nbn**'s pricing would effectively become split between two regulatory instruments based on technology, with potentially disparate approaches to prices emerging for the additional MTM services even though the overarching service construct and services are the same as for the services currently covered by the SAU.
68. This would occur notwithstanding the fact that all revenues and costs associated with the additional MTM services are already captured by the LTRCM. Therefore, if the price related aspects of the SAU were not extended to cover FTTB, FTTN and HFC, the cost recovery aspects of the SAU would continue to apply to **nbn** on a whole of business basis, with the pricing aspects of FTTB, FTTN and HFC operating outside of the overarching regulatory construct established by the SAU. This would increase the regulatory burden on **nbn**, access seekers and the ACCC, which would need to administer more than one regulatory regime that effectively governs the same subject matter.
69. Thirdly, any disparate regulatory or pricing treatment of certain technologies would skew future investments in those technologies, with **nbn** having to consider the extent to which it prioritises investment in services where it has the benefit of regulatory protection. Critically, as the additional MTM services will most likely undergo further upgrades over time (e.g. a shift to DOCSIS 3.1 on HFC and copper acceleration technologies, such as G.Fast, on FTTB, etc.), a regulatory intervention outside of the SAU framework may have broader unintended consequences in relation to **nbn**'s incentives to undertake such upgrades in respect of MTM services. Such an outcome would also raise significant issues around investment certainty for new services, such as FTTC, as it would not be readily apparent which regulatory framework would apply to these new services.
70. These adverse consequences were identified by Ordover and Shampine in their supplementary report:²⁷

"However, imposing direct price regulation on the MTM and not including it in the SAU is another matter entirely. Direct price regulation of the MTM would undermine the operation of the entire SAU, as the cost and revenue elements of the SAU would continue to apply to nbn's whole business, but pricing elements would not. At a minimum, such a patchwork regulatory structure – with pricing of some services under the SAU and some under direct price regulation – would seriously undermine incentives for efficient network construction choices, as the differences in regulatory regimes covering different options would become an important consideration for innovation, investment, and pricing. That is, nbn would have to consider not just whether a particular construction decision was

²⁶ ACCC, Draft Decision, p.64.

²⁷ Supplementary Expert Report of Janusz A. Ordover and Allan L. Shampine, 24 August 2017, paragraph 20.



efficient from an engineering perspective, but whether different regulatory treatment compared to alternatives make it less desirable from a regulatory perspective. We understand that a primary motivation for the MTM is to allow more cost-effective provision of network services across Australia, and imposing more onerous direct price regulation on the MTM would undermine that goal of using the MTM technologies in the first place. More generally, creating a new pricing regulatory structure for the MTM while otherwise wedging its construction into the other SAU constructs and maintaining the pricing regulatory structure already in place for FTTP, fixed wireless and satellite builds threatens to create a variety of distortions and undermine the operation of the SAU in providing efficient incentives for construction and pricing”.

71. Similarly, in the context of investment incentives in relation to new services, Ordovery and Shampine have observed:²⁸

“Investment-depressing risk is also created by the problem of regulatory opportunism (or regulatory creep), in which additional regulations are imposed ex post, after sunk investments are made. As above, this is highly relevant as nbn has already been investing in MTM deployment, and, we understand, fiber to the curb (“FTTC”) that nbn is currently trialing. A series of ongoing access determinations imposing increasingly greater restrictions on pricing for MTM and potentially new services could create risks that directly impact investment decisions such as whether to bring out new services at all, given the uncertainty in their regulatory treatment. Such a process would also increase the consequent distortions over time flowing from the initial decision to split out the method of regulation.”

72. When the above considerations are taken together, **nbn** submits that any intervention by the ACCC in relation to the additional MTM services will result in suboptimal, uncertain and complex outcomes
73. Intervention does not represent a viable option relative to acceptance of the Revised SAU Variation and is fundamentally at odds with the regulatory structure that the ACCC has endorsed through its acceptance of the SAU as it currently applies.

3.6 Regulatory counter-factual associated with **nbn**'s Pricing Evolution Review

74. As **nbn** is undertaking a significant review of its current pricing construct as part of its Pricing Evolution Review, it is important to consider the regulatory counter-factual that would apply if the Revised SAU Variation was not accepted and the Pricing Evolution Review resulted in a change to **nbn**'s pricing construct.
75. While it is difficult (and unnecessary, in this context) to speculate at this point as to how **nbn**'s pricing construct may change given the current stage of the consultation process and the number of

²⁸ Ibid, paragraph 23.



alternative options being considered, two regulatory counter-factual scenarios are possible if the Revised SAU Variation is not accepted by the ACCC at this time.

76. It is likely that if any changes to the **nbn** pricing construct:
- (a) can be accommodated within the current SAU framework, then the current SAU framework would continue to apply and any changes arising from the Pricing Evolution Review would be subject to the overarching protections of the SAU, once such changes are settled. However, there would be a lack of regulatory certainty if the SAU framework did not apply to the additional MTM services in such a circumstance; or
 - (b) cannot be accommodated within the current SAU framework, then this would require **nbn** to submit a further SAU variation for such changes to gain the benefit of the regulatory protection afforded by the SAU. The lodgement of a further SAU variation would entail further consultation with access seekers and would require the ACCC to be satisfied that those structural changes are consistent with the applicable statutory criteria. Therefore, the ACCC will have a critical role in assessing structural changes to **nbn**'s pricing through any future SAU variation that may be required if the Pricing Evolution Review entails more structural changes. The assessment of any such future SAU variation would be significantly more straightforward in a situation where MTM services were already included in the SAU.
77. With reference to either scenario, it would be reasonable for the scope of the SAU to be expanded now to include the additional MTM services.

3.7 Impact of other industry developments on the ACCC's approach to the SAU variation

78. In its Consultation Paper, the ACCC has alluded to a number of concerns expressed by access seekers as part of the previous SAU variation process and through the ACCC's separate market study process.
79. This includes the suggestion (**nbn** notes the absence of supporting evidence provided by the relevant access seekers) that:²⁹
- (a) **nbn**'s pricing construct, and the CVC price specifically, is constraining the uptake of higher value services; and
 - (b) due to increasing end-user demand for data (i.e. concurrent busy-hour usage), the CVC price makes it uneconomic for RSPs to supply adequate bandwidth at prevailing retail

²⁹ ACCC, Consultation Paper, pages 23-24.



prices, which in turn has impacted RSP margins and resulted in trade-offs being made on quality.

80. While **nbn** is addressing CVC pricing as part of its Pricing Evolution Review and is canvassing several potential changes to its pricing construct (which it is developing and validating using a co-design approach with access seekers), it is important to stress that developments at the retail level of the market are complex and multi-faceted.
81. It is certainly not the case, as has been suggested by some access seekers, that the CVC charge is solely to blame (or even largely to blame) for the current situation in the retail market.
82. **nbn's** public statements³⁰ and a recent white paper³¹ provide a summary of the current market dynamics and **nbn's** views in relation to these matters and the CVC price specifically. It is clear to **nbn** that there are a variety of factors that have contributed to, and exacerbated, the issues at the retail level.
83. As **nbn** has stated publicly, the other main determinant of the current situation being faced at the retail level is the "land grab" phenomenon as access seekers fight for market share as end-users transition to the **nbn**.³² This has resulted in access seekers competing away retail margins that they are now looking to recoup by lobbying for a reduction in **nbn's** wholesale prices.
84. Access seekers who claim that CVC prices should be lower without identifying alternative revenue models or acknowledging the impact of such pricing decisions on **nbn's** cost recovery are simply arguing in favour of increasing their own profits at the cost of the Australian taxpayer. While this is commercially rational behaviour by access seekers, their assertions need to be tested, and **nbn** encourages the ACCC to do this.
85. The effect of access seekers' arguments to simply lower CVC prices, without addressing broader cost recovery and industry considerations, is to require **nbn** to fund 'race to the bottom' pricing in the downstream market whilst access seekers embark on an aggressive marketing campaigns to retain and attain market share. It is not the role of **nbn** (or Australian taxpayers) to guarantee the margins that RSPs have historically obtained on legacy networks, particularly as they take steps to preserve market share in the transition to the **nbn** by competing that margin away.

³⁰ <http://www.nbnco.com.au/blog/the-nbn-project/getting-the-balance-right-on-the-nbn-network.html>

³¹ nbn CEO, Position Paper: Why are data speeds sometimes lower than what consumers were expecting? Is nbn to blame with its infamous CVC charge? See <http://www.nbnco.com.au/content/dam/nbnco2/documents/is-nbn-cvc-charge-to-blame-position-paper-170731.pdf>

³² Bill Morrow, "Why are data speeds sometimes lower than what consumers were expecting? Is nbn to blame with its infamous CVC charge?", (31 July 2017), p. 5.



86. As Ordover and Shampine have observed in their supplementary report, such outcomes in the retail market should not impact **nbn**'s ability to achieve cost recovery and delivers an economically beneficial outcome for end-users:³³

"With respect to the levels of prices, it is important to bear in mind that cost recovery for the network is an important policy goal, and the NBN Offers cap nbn's prices. Cost causality also indicates that end-consumers using the service should, to the extent possible given the cross-subsidization policy, bear the costs for the infrastructure serving them, rather than investors in nbn (through regulatory expropriation of their investments) or taxpayers generally. That is, claims that prices are "too high" must be considered in light of the costs of providing that service. Building out and maintaining the nbn network is extremely costly. The network was built based on the regulatory expectation that the investors (the Commonwealth of Australia) would have the opportunity to recover those costs and earn a reasonable rate of return. The presence of aggressive downstream competition, which squeezes downstream margins, is not an economic problem, nor would it be sensible to reduce nbn's rates by regulatory fiat in an attempt to increase downstream margins. Intense downstream competition among nbn's customers ensures low profitability, which benefits Australian telecommunications customers, no matter what the wholesale price is, given the non-discrimination requirements applicable to nbn".

87. Indeed, it is clear that RSP pricing strategies so far have "focused on price with little mention of data speed or quality during the peak of the day,"³⁴ and have driven down prices for internet plans to a price which may not reflect what end users are prepared to pay.³⁵

88. However, it is also clear that RSPs are benefitting from the discounts that are available under the DBD scheme and that this will increase as RSPs build further scale on the **nbn**TM network as the rollout continues. For example, while the CEO of Vocus has recently noted that its margins on the **nbn** are lower than that on legacy networks and that they "expect to see some further increases in wholesale costs over the course of FY18", he also observed that CVC costs would not grow at the rate they did in FY17, in part, due to the DBD scheme which took effect on 1 June:³⁶

"The discount tier structure will have some benefits as we step up capacity but the ability to manage the amount of CVC you're provisioning [also] becomes stronger the larger the portfolio."

89. Therefore, whilst the CVC charge has a role to play in access seeker economics (as would any other wholesale input), it is not the only contributing factor and the picture is inherently more complex

³³ Supplementary Expert Report of Janusz A. Ordover and Allan L. Shampine, 24 August 2017, paragraph 18.

³⁴ Bill Morrow, "Why are data speeds sometimes lower than what consumers were expecting? Is nbn to blame with its infamous CVC charge?", (31 July 2017), p. 2. Available at: <http://www.nbnco.com.au/content/dam/nbnco2/documents/is-nbn-cvc-charge-to-blame-position-paper-170731.pdf>.

³⁵ Sid Maher, "NBN chief Bill Morrow asks who will by the \$49bn debt", (14 August 2017), *The Australian*. Available at: <http://www.theaustralian.com.au/national-affairs/nbn-chief-bill-morrow-asks-who-will-by-the-49bn-debt/news-story/8fe4e66edbea363e60d8d49a7b4611db>.

³⁶ Ry Crozier. Vocus sees NBN margins slip further behind ADSL, IT News, 23 August 2017. See, <https://www.itnews.com.au/news/vocus-sees-nbn-margins-slip-further-behind-adsl-471528>



than many interested parties would suggest, particularly as subscriber numbers on the **nbn** continue to increase and the discounts implemented on 1 June 2017 begin to take effect.

90. It is critical for these developments, which are independent of the SAU, to be given greater attention by the ACCC as part of its Market Study. These developments should not delay acceptance of the SAU and do not justify a change in approach in terms of how **nbn** should be regulated. In addition to being technically separate to the SAU from a legal process perspective, **nbn's** Pricing Evolution Review is also technically separate to the SAU variation process.
91. **nbn** has incentives to ensure that access seekers remain economically viable and that they maximise their usage of the **nbn**. This is being addressed through the operation of **nbn's** incentives outside of the SAU via **nbn's** Pricing Evolution Review, but with **nbn** ultimately being constrained by the regulatory backstops that are included in the SAU. These will be further enhanced if the SAU is varied to include the additional MTM services.

3.8 Current model is appropriate for the additional MTM services

92. The ACCC has requested views in its Consultation Paper on whether the current pricing model is reasonable for the additional MTM services given there is more variability and uncertainty about the speeds that can be achieved.³⁷ It is unclear to **nbn** as to why the ACCC is actively entertaining such an unsubstantiated assertion as part of its SAU variation assessment process.
93. The purpose of the SAU is to capture all technologies that **nbn** may deploy, both from a cost recovery (LTRCM) and pricing perspective.
94. The arguments that have been made by access seekers about treating the additional MTM technologies differently from a CVC pricing perspective conflate speed with usage. They are incorrect and should be disregarded by the ACCC.
95. The ACCC already has data that usage on MTM networks is significantly higher than on legacy copper networks. In April 2016, end users on the nbn™ network consumed around 35% more data than non-**nbn** end users.³⁸ This increased usage is supported by **nbn's** customers provisioning an average of 1.04Mbps of TC-4 CVC capacity per end user as compared to Telstra's wholesale DSL customers provisioning an average of only 0.23Mbps of AGVC capacity per end user.³⁹

³⁷ ACCC, Consultation Paper, page 25.

³⁸ In April 2016, this amounted to 112GB used per month compared to 83GB per month. **nbn**, "Aussies watching 13 billion hours of online content a year", (6 April 2016). Available at: <http://www.nbnco.com.au/corporate-information/media-centre/media-releases/aussies-watching13billionhoursofonlinecontentayearabs.html>. Note that in March 2017, the amount of data being used per month on the **nbn**™ Network has increased to 148GB. **nbn**, "Aussie binge boom continue to grow", (28 March 2017). Available at: <http://www.nbnco.com.au/corporate-information/media-centre/media-releases/Aussie-binge-boom-continues-to-grow.html>.

³⁹ ACCC, *Communications Report 2015-16*, (February 2017), p. v.



96. Therefore, it is not credible to suggest that a key element of **nbn**'s pricing construct should not apply to FTTB, FTTN and HFC services, given the high levels of usage that are being seen across all of **nbn**'s fibre based technology variants.
97. Such an argument also ignores the fact that **nbn** makes tools made available to access seekers enable them to ensure that CVC capacity is acquired at an appropriate level for the AVC bandwidth throughput that can be achieved on the relevant connection. This includes "birth certificates" and weekly speed reports in relation to end-user connections.
98. In addition, any speed issues on the additional MTM services are likely to be far more short-lived than the period over which **nbn** expects it will need to recover its initial losses through a CVC charge. As the ACCC is aware, network speeds in the FTTB and FTTN footprints remain affected by the co-existence of legacy services during the co-existence period with Telstra.
99. Subject to continued testing and trials, **nbn** is currently also planning to deploy G.fast technology in the future to provide an upgrade path for its fibre-to-the-curb (FTTC) and FTTB networks, which has the potential to significantly increase wholesale speed capabilities above 100Mbps per premises.⁴⁰ To date, **nbn** has trialled wholesale FTTB speeds above 600Mbps using G.fast on 100m of 20-year old copper lines,⁴¹ whilst operators in other jurisdictions such as BT and Deutsche Telecom are capable of using G.fast and other technologies like Super Vectoring to deliver speeds of up to 300Mbps to end users on FTTN technology.⁴² Further technology paths also exist beyond G.fast and **nbn** is actively exploring these technologies as they become available. Further information about the technology roadmap of these technologies has been provided in the Analysys Mason report previously commissioned by **nbn** in relation to its Original SAU Variation.⁴³
100. Accordingly, any speed concerns that an access seeker may have as a reason for removing CVC charges are not supported by existing data, are likely to be short-lived and, in any case, are being actively addressed by **nbn**.

⁴⁰ **nbn**, "DSL Upgrade paths: The difference between G.fast and XG.FAST", (14 July 2017), accessed 28 July 2017. Available at: <http://www.nbnco.com.au/blog/the-nbn-project/the-difference-between-g-fast-and-xg-fast.html>.

⁴¹ **nbn**, "**nbn**tm technology 101: What is FTTB?" (28 April 2017), accessed 28 July 2017. Available at: <http://www.nbnco.com.au/blog/the-nbn-project/nbn-technology-101-what-is-fttb.html>.

⁴² **nbn**, "Setting the facts straight on Fibre-to-the-Node" (8 March 2017), accessed 28 July 2017. Available at: <http://www.nbnco.com.au/blog/the-nbn-project/setting-the-facts-straight-on-fibre-to-the-node.html>.

⁴³ Analysys Mason, Report for Webb Henderson, Review of nbn's network selection methodology and the efficiency and prudence of the design of its FTTN, FTTB and HFC networks, Public version, April 2016, pages 58-73, See, <https://www.accc.gov.au/system/files/Analysys%20Mason%20expert%20report%20%28Public%20version%20-%20redacted%29.pdf>