



Australian  
Competition &  
Consumer  
Commission

# **Interim access determinations for the declared fixed line services**

## **Statement of Reasons**

**March 2011**



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## List of abbreviations and acronyms

ABS	Australian Bureau of Statistics
ACCC	Australian Competition and Consumer Commission
AD	access determination
BBM	building block model
CAN	customer access network
CBD	central business district
CCA	<i>Competition and Consumer Act 2010</i>
CACS Act	<i>Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Act 2010</i>
CPI	consumer price index
DAC	depreciated actual cost
DHC	depreciated historic cost
DORC	depreciated optimised replacement cost
DSLAM	digital subscriber line access multiplexer
ESA	exchange service area
FAD	final access determination
FLSM	fixed line services model
IAD	interim access determination
LCS	local carriage service
LSS	line sharing service
MEAs	modern equivalent assets

Model Terms	<i>Model Non-Price Terms &amp; Conditions Determination 2008</i>
NBN	national broadband network
ORC	optimised replacement cost
PIE II	Telstra's PSTN Ingress Egress model (version 2)
PSTN	public switched telephone network
PSTN OA	public switched telephone network originating access
PSTN TA	public switched telephone network terminating access
RAF	regulatory accounting framework
RAB	regulatory asset base
RKRs	record keeping rules
RMRC	retail minus retail cost
SAOs	standard access obligations
SIOs	services in operation
TEA model	Telstra's Efficient Access model
Tribunal	Australian Competition Tribunal
TSLRIC+	total service long-run incremental cost
ULLS	unconditioned local loop service
WACC	weighted average cost of capital
WLR	wholesale line rental

# 1 Summary

The *Competition and Consumer Act 2010* (CCA) was recently amended to change the operation of Part XIC from an ex-post negotiate/arbitrate access regime to an ex-ante price and non-price terms and conditions access regime.<sup>1</sup> These changes took effect from 1 January 2011.

Under the new access regime, the Australian Competition and Consumer Commission (ACCC) must make final access determinations (FADs) for declared services. The ACCC can, in some circumstances, make interim access determinations (IADs) to operate before FADs are made. The ACCC is no longer required to make pricing principle determinations.

The ACCC has decided to issue IADs under sections 152BC and 152BCG of the CCA for the following six declared fixed line services (together, the declared fixed line services):

- unconditioned local loop service (ULLS)
- wholesale line rental (WLR)
- line sharing service (LSS)
- public switched telephone network originating access (PSTN OA)
- public switched telephone network terminating access (PSTN TA)<sup>2</sup>
- local carriage service (LCS).

The IADs apply from 1 January 2011 to 31 December 2011. The IADs will be automatically revoked when the ACCC issues FADs. The ACCC considers that making IADs to commence from 1 January 2011 will provide the industry with certainty in the transition to the new access regime.

The IADs contain both price and non-price terms. The IADs also incorporate the effect of the exemption determinations made under the previous access regime.

The price terms in the IADs are based on prices calculated using a building block model (BBM) approach, taking into account the best information currently before the ACCC, including material received as part of the recent review of the declared fixed line services pricing principles.<sup>3</sup> The ACCC has also had regard to other relevant matters when determining the prices for the IADs, including regulatory certainty and consistency. The BBM approach represents a change from the ACCC's historic approach to pricing, which was based on:

- retail minus retail cost (RMRC) pricing for the WLR and LCS, and
- total service long run incremental cost (TSLRIC+) pricing for the ULLS, LSS and PSTN OTA.

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<sup>1</sup> The amendments were made by the *Telecommunications Legislation Amendment (Competition and Consumer Safeguards)* Act 2010. From 1 January 2011 the *Trade Practices Act 1974* was renamed the *Competition and Consumer Act 2010*.

<sup>2</sup> PSTN OA and PSTN TA are together referred to as 'PSTN OTA'.

<sup>3</sup> Review of Access Pricing Principles for Fixed Line Services, <http://www.accc.gov.au/content/index.phtml/itemId/904344>.

All industry submissions to the ACCC's review of the declared fixed line services pricing principles have indicated broad acceptance of the ACCC's proposed change in its pricing approach.

The ACCC has the power to amend the IADs at any time before it issues FADs.

As required under the CCA, the ACCC will commence a public inquiry before making FADs in relation to the declared fixed line services. The ACCC proposes to issue a discussion paper when the public inquiry commences, which will set out relevant issues and seek further comment from industry. In developing the discussion paper (to be released at the commencement of the FAD public inquiry), the ACCC will have regard to information received as part of the recent pricing principles review.

## **2 Legislative framework**

Part XIC of the CCA was amended with effect from 1 January 2011 by the *Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Act 2010* (CACS Act). This section briefly outlines the changes to the Part XIC access regime.

### **2.1 Previous access regime: negotiate/arbitrate model**

Prior to the commencement of the CACS Act, the now repealed Division 8 of Part XIC set out arbitration provisions. If parties could not agree on the terms of access to a declared service, either party could notify the ACCC of a dispute. The ACCC would then arbitrate the dispute and determine the terms and conditions of access between those two parties.

The ACCC was required to make pricing principle determinations and price related terms and conditions for declared services under the now repealed section 152AQA. The ACCC was also required to make a written determination setting out model terms and conditions relating to access for certain declared services.<sup>4</sup> The ACCC was required to have regard to the pricing principle determinations and model terms when arbitrating access disputes.

The ACCC's 1997 document *Access Pricing Principles – Telecommunications: a guide* (1997 Access Pricing Principles) has generally guided the ACCC when determining pricing principles and indicative prices for declared fixed line services. In December 2009 the ACCC commenced a review of the 1997 Access Pricing Principles. In September 2010 the ACCC issued draft pricing principles and draft indicative prices for consultation (see sections 3.2 and 3.3 below).

Following the repeal of sections 152AQA and 152AQB, the ACCC is no longer required to issue pricing principle determinations and model terms and conditions for declared services. Because of this legislative change, the review of the 1997 Access Pricing Principles was suspended as the power to make such principles has been removed.

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<sup>4</sup> Repealed section 152AQB of the CCA. These services were PSTN OA, PSTN TA, ULLS and LCS.

Under the previous access regime, the ACCC had the power to make exemption determinations which had the effect of exempting access providers from the standard access obligations (SAOs) in relation to the supply of declared services. The exemption determinations could be unconditional, or could apply subject to conditions and limitations. Following the repeal of sections 152AS and 152AT of the CCA, the ACCC no longer has the power to make exemption determinations.

The transitional provisions in the CACS Act state that once an access determination (AD) (including an IAD) in relation to a service commences, a determination made under the repealed sections 152AS and 152AT ceases to have effect.<sup>5</sup>

## **2.2 New access regime: up-front price and non-price terms model**

The CACS Act replaced the previous negotiate/arbitrate model with a model which enables the ACCC to set default price and non-price terms in ADs. An AD will only apply where there is no commercial agreement between the access seekers and access provider. They create a benchmark which access seekers can fall back on while still allowing parties to negotiate different terms.

ADs can be interim (IADs) or final (FADs). Where ADs specify terms and conditions of access they must include terms and conditions relating to price (or a method of ascertaining a price) and may also contain non-price terms, although this is not compulsory.<sup>6</sup> Compliance with IADs and FADs is a carrier licence condition<sup>7</sup> and a service provider rule.<sup>8</sup> The IADs and FADs do not apply to the extent they are inconsistent with various other instruments and agreements, including access agreements between parties.<sup>9</sup>

Under the new access regime, the ACCC is able to incorporate provisions in ADs which provide that the SAOs are not applicable (either unconditionally or subject to conditions or limitation). Similarly, it may include provisions that restrict or limit the application of any or all of the SAOs.<sup>10</sup>

### ***Interim access determinations***

The CCA allows the ACCC to make IADs in various circumstances, including where a service is declared and no FAD has previously been made in relation to that service.<sup>11</sup>

The ACCC is not required to consult with industry,<sup>12</sup> or observe any requirements of procedural fairness when making an IAD.<sup>13</sup> The CCA does not specify any matters that the ACCC must take into account when making an IAD.<sup>14</sup>

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<sup>5</sup> Items 202 (class exemptions) and 203 (individual exemptions) of the CACS Act.

<sup>6</sup> See section 152BC of the CCA.

<sup>7</sup> Section 152BCO of the CCA.

<sup>8</sup> Section 152BCP of the CCA.

<sup>9</sup> Section 152BCC of the CCA.

<sup>10</sup> Paragraphs 152BC(3)(h) and (i) of the CCA.

<sup>11</sup> Subsection 152BCG(2) of the CCA.

<sup>12</sup> Subsection 152BCH(2) of the CCA.

<sup>13</sup> Subsection 152BCG(4) of the CCA.

<sup>14</sup> Subsection 152BCA(4) of the CCA.



An IAD for a declared service is automatically revoked when an FAD is made by the ACCC for that declared service.<sup>15</sup>

The ACCC has the power to amend an IAD at any time before an FAD is made.<sup>16</sup>

### **3 Background on pricing principles and indicative prices**

In August 2009, the ACCC made pricing principles and indicative prices for the declared fixed line services which expired on 31 December 2010.<sup>17</sup>

The ACCC had been in the process of consulting with industry on new pricing principles and indicative prices to apply from 1 January 2011. As part of that consultation, the ACCC proposed a substantial shift from its previous pricing methodologies (TSLRIC+ and RMRC) to a new BBM pricing methodology. The ACCC proposed that the BBM methodology would be used to calculate indicative prices for all the declared fixed line services. The consultation process and a description of the proposed pricing methodology are outlined below.

#### **3.1 1997 Access Pricing Principles**

For over a decade the ACCC was generally guided by its 1997 Access Pricing Principles when determining pricing principles and indicative prices for declared fixed line services. The 1997 Access Pricing Principles used a forward looking TSLRIC+ approach to determining prices for access to the relevant declared services.<sup>18</sup>

In telecommunications, both in Australia and internationally, the application of TSLRIC+ for fixed line services involved continually revaluing the existing sunk assets used in providing these services. This revaluation was based on the asset's optimised replacement cost and occurred each time a pricing determination was made.

##### ***TSLRIC+ pricing for ULLS, LCS and PSTN OTA***

In accordance with the 1997 Access Pricing Principles, a forward looking TSLRIC+ pricing approach had consistently been adopted as the pricing principle for the ULLS, the LSS and the PSTN OTA, and indicative prices were calculated for those services based on that pricing principle.

##### ***RMRC based pricing for WLR and LCS***

Due to the absence of a reliable cost model, in the past the ACCC has adopted a RMRC pricing approach to calculate indicative prices for WLR and LCS services.<sup>19</sup>

However, the ACCC had indicated to industry that it would seek to implement a cost-based pricing approach for those services once a robust cost model, capable of

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<sup>15</sup> Subsection 152BCF(9A) of the CCA.

<sup>16</sup> Subsection 152BCN(1) of the CCA.

<sup>17</sup> ACCC, *Pricing principles and indicative prices for LCS, WLR, PSTN OTA, ULLS, LSS, 1 August 2009 to 31 December 2010*.

<sup>18</sup> TSLRIC+ is the incremental or additional costs the firm incurs in providing the service, assuming all of its other production activities remain unchanged. It includes a mark up for common costs.

<sup>19</sup> Under an RMRC methodology, the access price is determined by deducting the access provider's avoidable costs of retailing a given service to end-users from the retail price paid for that service.

producing reliable estimates, was available.<sup>20</sup> The ACCC has also previously indicated that retail prices and RMRC prices for WLR and LCS currently exceed cost-based prices, particularly for WLR.<sup>21</sup>

### **3.2 Consultation on new pricing principles and indicative prices: December 2009 Discussion Paper**

In the 13 years since the release of the 1997 Access Pricing Principles, there has been significant debate among industry participants on the appropriate approach to determining access prices for the declared fixed line services and the appropriateness of a TSLRIC+ methodology for valuing the fixed line network. Issues included:

- The continual revaluation of network assets means that there has been ongoing uncertainty over the level of access prices.
- Calculating forward looking costs involves estimating the cost of providing the relevant service using modern equivalent assets (MEAs). However, there is considerable debate and uncertainty over what constitutes MEAs.

In December 2009, the ACCC released the *Review of 1997 Guide to Telecommunications Access Pricing Principles for Fixed Line Services: Discussion Paper* (December 2009 Discussion Paper).<sup>22</sup> The December 2009 Discussion Paper signalled that consideration of a new pricing approach was timely, given the dynamic nature of the communications market and developments that had taken place in the industry since 1997. The December 2009 Discussion Paper suggested adopting a BBM approach to calculating prices for all the declared fixed line services.

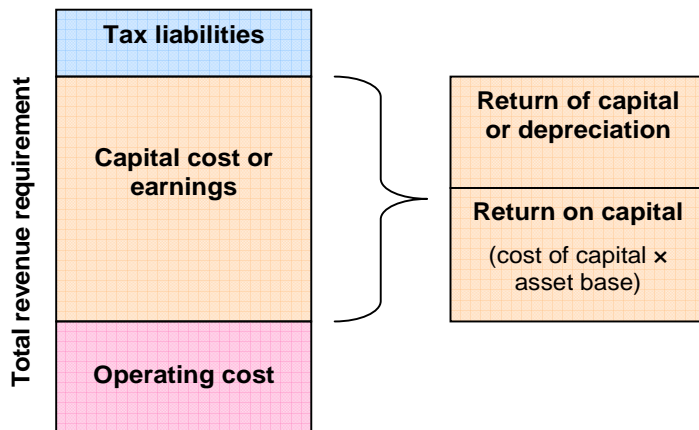
To implement a BBM, the ACCC must establish an initial value of the regulated asset base (RAB). Once the initial RAB value is established, it is 'locked-in' and rolled forward from one year to the next. The BBM accounts explicitly for each cost category or 'building block' faced by the regulated business. Each of the building blocks are added together to determine the business's total revenue requirement. This is illustrated in the diagram below:

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<sup>20</sup> See for example, ACCC, *Pricing Principles and indicative prices for LCS, WLR, PSTN OTA, ULLS, LSS 1 August 2010 to 31 December 2010*, December 2009, Appendix 1 under 'LCS' and 'WLR'.

<sup>21</sup> ACCC, *Local carriage service and wholesale line rental – final pricing principles and indicative prices for 2008-2009*, August 2008.

<sup>22</sup> The December 2009 Discussion Paper can be found at the ACCC website: [www.accc.gov.au](http://www.accc.gov.au).



Revenues calculated using a BBM cover a service provider's efficient costs, including a commercial return on investments that is commensurate with its legitimate commercial interests.

Six submissions were received in response to the December 2009 Discussion Paper.<sup>23</sup> All of the submissions supported a move to using a BBM with a locked in RAB to set prices for the fixed line services.

### 3.3 Consultation on new pricing principles and indicative prices: September 2010 Draft Report

Having regard to the submissions made on the December 2009 Discussion Paper, on 17 September 2010 the ACCC released the *Draft Report – Review of the 1997 Telecommunications Access Pricing Principles for Fixed Line Services*, which incorporated draft pricing principles and draft indicative prices (September 2010 Draft Report).<sup>24</sup>

The September 2010 Draft Report proposed to adopt a BBM with a locked-in RAB calculated using a depreciated actual cost (DAC) valuation methodology (DAC is also referred to as depreciated historic cost, DHC). It proposed to use data contained in Telstra's Regulatory Accounting Framework (RAF) to estimate the value of the RAB.

Draft indicative prices for five of the declared fixed line services—ULLS, WLR, LCS and PSTN OA and TA—were estimated using a BBM pricing model initially developed by Ovum Pty Ltd and revised by the ACCC (the Fixed Line Services Model (FLSM), referred to in the September 2010 Draft Report as the Ovum BBM). An indicative price for the LSS was estimated from a separate pricing model (outside the BBM framework).

The ACCC received submissions from 15 interested parties on various issues in relation to the September 2010 Draft Report, the FLSM and the LSS specific cost model.<sup>25</sup>

<sup>23</sup> Submissions can be found at the ACCC website: [www.accc.gov.au](http://www.accc.gov.au).

<sup>24</sup> ACCC, *Review of the 1997 telecommunications access pricing principles for fixed line services, Draft Report*, September 2010. The Draft Report can be found on the ACCC website: [www.accc.gov.au](http://www.accc.gov.au).

<sup>25</sup> Submissions can be found at the ACCC website: [www.accc.gov.au](http://www.accc.gov.au).

### 3.4 Suspension of pricing principles inquiry

In December 2010, the ACCC suspended its review of the 1997 Access Pricing Principles as the power to make such principles has been repealed with the amendments to the CCA. The ACCC indicated that it would make IADs for the declared fixed line services in early 2011.<sup>26</sup>

## 4 IADs for fixed line services

The ACCC has decided to issue IADs for each of the declared fixed line services to commence from 1 January 2011.

The ACCC considers that it is desirable for industry participants to have interim price and non-price terms for all the declared fixed line services. These terms will provide a default position for access seekers, while still allowing parties to negotiate different terms. The ACCC considers that this will provide some certainty for industry until the ACCC makes FADs for the declared fixed line services.

The IADs for all the declared fixed line services include price and non-price terms. The IADs for WLR, LCS and PSTN OA also incorporate the effect of the exemption determinations which were originally made under the now repealed exemption provisions in the CCA.

The IAD does not specify price terms to apply to WLR that uses the NBN as an input. This is because it would be premature for an IAD to address the price of such a service. The ACCC intends to consider these services in the course of the FAD inquiry.

### 4.1 Material the ACCC has taken into account when making the IADs

The ACCC has taken the following material into account when making the IADs for the declared fixed line services.

#### *Price terms*

- submissions in response to the December 2009 Discussion Paper
- the September 2010 Draft Report
- submissions in response to the September 2010 Draft Report
- additional information requested and received from Telstra and other industry participants in order to address some of the issues identified in the submissions in relation to the FLSM
- information that Telstra provides to the ACCC under record keeping rules (RKR), including:
  - the telecommunications regulatory accounting framework RKR (RAF RKR), and
  - the customer access network RKR (CAN RKR) (a summary of which is periodically published at [www.accc.gov.au](http://www.accc.gov.au))

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<sup>26</sup> ACCC media release: NR 282/10, *ACCC to issue Interim Access Determinations for telecommunications fixed line pricing in early 2011*, 21 December 2010.

- previous pricing principle determinations made by the ACCC under repealed section 152AQA of the CCA

### *Non-price terms*

- decisions of the ACCC in previous arbitration determinations made under repealed Division 8 of the CCA
- information provided by parties to access disputes under the repealed Division 8 of the CCA
- previous non-price model terms and conditions determinations made by the ACCC under the repealed section 152AQB of the CCA

### *Exemptions*

- exemption determinations made under the repealed sections 152AS and 152AT.

The ACCC's approach to setting the price and non-price terms and conditions in the IADs is set out below.

## **5 Price terms**

For the purpose of the IADs, the ACCC has decided to adopt price terms for the IADs which are based on the FLSM, and take other factors into account. The ACCC has made a number of amendments to the FLSM provided to industry in the September 2010 Draft Report, and has also revised its approach to estimating the RAB value, which is a component of the FLSM.

The ACCC has also decided to average Band 1 to 3 ULLS prices, and round up the resulting estimated prices for the Bands 1 to 3 ULLS, the WLR and the LSS, for the purpose of the IADs.<sup>27</sup>

Reasons for these adjustments are set out below.

### **5.1 Amendments to the Fixed Line Services Model (FLSM)**

As a result of the submissions received in response to the September 2010 Draft Report and additional information received from Telstra, the ACCC has made a number of amendments to the FLSM.

A summary of the ACCC's revisions to the FLSM and the model inputs since the release of the September 2010 Draft Report is at **Appendix A**. The major revisions to the FLSM are:

- Changes to the asset classes included in the FLSM, most significantly the inclusion of additional 'building and support assets' and 'indirect capital assets'.
- Indexation of land asset values by the CPI.
- Incorporation of the LSS into the FLSM.
- Revisions to the ACCC's operating and capital expenditure and demand forecasts, reflecting more recent data and additional information from Telstra.

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<sup>27</sup> Bands are geographical classifications of exchange service areas (ESAs). Generally, Band 1 includes ESAs in CBD areas; Band 2 includes ESAs in metropolitan areas; Band 3 includes ESAs in regional areas; and Band 4 includes ESAs in rural areas.

- Updating of the weighted average cost of capital (WACC) parameters.

## 5.2 Adjustment to CAN cost allocations for geographic cost differentials

The ACCC has also revised its methodology for determining the cost allocation factors for ‘ducts and pipes’ and ‘copper cables’ to the ULLS and the WLR. The September 2010 Draft Report noted that the method used to set these cost allocation factors “does not take into account the different distribution of the ULLS, the WLR and other services across the geographic bands”.<sup>28</sup> While recognising that the costs allocated to the ULLS could be over-estimated by this approach, the September 2010 Draft Report stated that:

the ACCC does not have cost information by band to enable it to take into account any potential difference in unit costs ... However, should better cost information be made available, the ACCC will review the cost allocation factors for ULLS, WLR and other services.<sup>29</sup>

In submissions to the September 2010 Draft Report, the ACCC received information that assisted it in developing a methodology for adjusting the cost allocation factors for ‘ducts and pipes’ and ‘copper cables’ to reflect estimated geographic cost differentials. The methodology applies cost relativities between the bands for ‘ducts and pipes’ and ‘copper cables’ derived from the Analysys Cost Model.<sup>30</sup> These adjustments reduce ULLS band prices compared to the WLR price and allow the ACCC to set a price for Band 4 ULLS for the first time.

## 5.3 RAB valuation

In the September 2010 Draft Report, the ACCC noted that potential values for the initial RAB ranged from scrap value to optimised replacement cost (ORC). There is no uniquely ‘correct’ value for the initial RAB. An element of judgement is therefore required to determine a suitable range of potential RAB values for Telstra’s sunk investments in network assets and then to settle on a value within this range that forms a sound basis for estimating prices to be included in IADs.

### *ACCC’s assessment of the suitable range of RAB values*

The ACCC considers that a suitable range of RAB values is set by the depreciated historic value of Telstra’s investments in network assets (that is, their depreciated actual cost or DAC value) and by depreciated optimised replacement cost (DORC). In determining this range, the ACCC took into account that:

- a DAC value would allow Telstra to recoup its actual investment costs and achieve a commercial return on those investments. A valuation method that valued sunk assets at less than their actual costs could, by creating a risk of ‘regulatory opportunism’, deter future investments in sunk assets by regulated businesses.<sup>31</sup> Therefore, a DAC value sets the lower bound for the range of suitable RAB values.

<sup>28</sup> September 2010 Draft Report, p. 90.

<sup>29</sup> *ibid.*, p. 91.

<sup>30</sup> The Analysys Cost Model was commissioned by the ACCC in August 2007 to estimate the cost of providing the declared fixed line services in Australia. The model was designed with specific reference to Australian conditions.

<sup>31</sup> See September 2010 Draft Report, p. 24.

- a DORC value would be compatible with the previous TSLRIC+-based approach to calculating ULLS prices, which used estimated ORC values for Telstra's assets. To ensure consistency with the actual cost foundation of the building block approach, an ORC value must be depreciated to reflect the age of Telstra's actual assets—therefore a DORC value must be used rather than ORC.<sup>32</sup> DORC values have been adopted in setting initial RAB values in other regulated industries, including the energy industry. Since DORC values derived from existing models are based on continued use of outdated copper-based technologies, and less-than-full optimisation of the network, the ACCC considers that currently available DORC values form an upper bound for the range of suitable RAB values.

After determining the suitable range of RAB values, the ACCC considered whether a RAB value based on either end of this range would provide a sound basis for estimating prices for the purposes of making IADs. The ACCC has concluded that both valuation methods have considerable limitations.

A DAC valuation of Telstra's assets would necessarily be based on Telstra's RAF accounts because, as noted in the September 2010 Draft Report, the RAF data generally represent the most complete and accurate record of the historic costs for the fixed line network.<sup>33</sup> In that report, however, the ACCC recognised the limitations of Telstra's RAF data, particularly for assets that were put in place many years ago when account keeping was generally less robust and Telstra was subject to less stringent accounting obligations and disclosure rules. The ACCC has in the past expressed concerns about the incomplete nature of Telstra's records on its long-lived network assets, particularly its ducts, pipes and copper cables.<sup>34</sup>

Use of a DORC valuation method would require the ACCC to make many subjective judgements about the appropriate level of optimisation and the modern equivalent assets for the copper network. The ACCC has noted the criticisms by the Australian Competition Tribunal of existing TSLRIC+ models. It considers that, if a suitable model was available, a DORC value would be calculated using a fibre network, with a discount for the much higher service quality potential of fibre and a substantial depreciation allowance to take into account the age and deterioration of the existing copper network (compared to a new fibre network). No such model currently exists and timely development of such a model is not feasible.

Taking these considerations into account, the ACCC concluded that neither the DAC nor DORC approaches taken alone would in themselves provide a sufficiently robust or reliable method for determining an initial RAB value for the purposes of estimating IAD prices. The ACCC then considered whether Telstra's current cost accounting

<sup>32</sup> In applying its previous TSLRIC+ approach, the ACCC used estimates of the hypothetical cost of replacing Telstra's network with new modern equivalent assets. Since these hypothetical assets were assumed to be new, there was no depreciation. In contrast, a building block approach requires a value to be placed on the actual assets being used to provide the services. This requires an allowance for depreciation to reflect the age of the actual assets in use.

<sup>33</sup> See September 2010 Draft Report, p. 28. The asset values in the RAF accounts generally use information from Telstra's asset register, which provides a more disaggregated record of historic costs. The main exception is land assets, which, in Telstra's asset register, have been revalued from time to time and indexed by the CPI to reflect the typical appreciation of land assets over time. In addition, land assets are not depreciated in Telstra's asset register.

<sup>34</sup> See September 2010 Draft Report, p. 26.

valuation of its assets could provide a reliable basis for setting an initial RAB value. However, since these accounts provide indexed values for Telstra's assets calculated from the RAF accounts, they are subject to the same limitations as the RAF accounts as well as any shortcomings in the indexation methodology applied by Telstra.<sup>35</sup>

Given the inherent limitations in DAC, DORC and current cost accounting approaches in determining a RAB value, the ACCC considered a number of other factors to assist it in settling on an initial RAB value within the suitable range of potential values.

### ***ACCC's decision on an initial RAB value for estimating IAD prices***

In setting an initial RAB value for the purpose of estimating IAD prices, the ACCC used the DAC value that forms the lower bound of the suitable range as a starting point from which it developed a suitable RAB value. The more substantial limitations associated with obtaining a DORC value ruled it out as a starting point. The ACCC has made two adjustments to the DAC value. In making these adjustments, the ACCC has taken into account submissions to the September 2010 Draft Report and two additional considerations set out in the next section.

The first adjustment is that the ACCC has accepted that the value of land assets should be indexed to reflect the appreciation of land values over time. For the purposes of this IAD, the ACCC has adopted the land values provided by Telstra which Telstra has indexed by the CPI since its last revaluation of land assets in 1991-92.<sup>36</sup> No depreciation has been allowed for land assets in the FLSM. A DAC value with indexed land asset values results in a RAB estimate of \$16.31 billion.

The second adjustment is that the ACCC has increased the value assigned to the 'ducts and pipes' asset class by \$1.44 billion above its value in Telstra's RAF accounts. Details of the basis for this adjustment are set out below.

The resulting RAB value of \$17.75 billion falls within the range identified by the ACCC as suitable for the purposes of setting prices for the IADs.

### ***Reasons for adjusting the value assigned to 'ducts and pipes' assets***

In reaching its decision to adjust the DAC value of the CAN 'ducts and pipes' asset class by an increment of \$1.44 billion, the ACCC was guided by the principle that pricing stability is desirable to the extent that it supports past investments and promotes industry confidence in making future investment decisions.

In its previous regulatory decisions, the ACCC has consistently sought to promote competition by encouraging access seeker infrastructure investments. As a result, there has been significant growth in digital subscriber line access multiplexer (DSLAM) investments as access seekers have increasingly competed on price and service offerings.

Infrastructure competition has, to date, occurred predominantly in Band 2 ESAs, with access seeker DSLAMs overwhelmingly located in Band 2 ESAs. As at December

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<sup>35</sup> Telstra's indexation methodology in its current cost accounts is not transparent so the ACCC is unable to assess its appropriateness.

<sup>36</sup> Telstra Corporation Ltd, *Pricing Principles for Fixed Line Services: Response to the ACCC's Draft Report*, October 2010, p. 78.



2010, approximately 76 per cent of all Band 2 ESAs were served by one or more competitor DSLAMs (that is, DSLAMs other than Telstra's), and 94 percent of total ULLS services in operation (SIOs) are provided in Band 2 ESAs.<sup>37</sup>

The ACCC considers that, in determining an initial RAB value for the CAN and Core assets, it is important to protect the legitimate business interests of both access seekers and Telstra. This consideration led the ACCC to conclude that a clear justification is required for any significant change in existing prices. Based on this view, the ACCC decided to maintain a \$16 ULLS price in Band 2. In addition, for the reasons set out in section 5.4 below, the ACCC decided that a single ULLS price of \$16 should apply in Bands 1 to 3.

To determine a RAB valuation consistent with this decision, the ACCC calculated the net present value of the cash flows expected from applying an SIO-weighted \$16 Band 1 to 3 ULLS averaged price and adopting prices for the other fixed line services estimated by the FLSM as being consistent with the \$16 ULLS price and the costs of providing those services.<sup>38</sup>

The net present value calculation implies a RAB value of \$17.75 billion, when the increment above the RAB estimate of \$16.31 billion (based on a DAC value with indexed land asset values) is allocated to the 'ducts and pipes' asset class. Since this value falls within the suitable range of potential RAB values, the ACCC determined that this value represents an appropriate value for Telstra's CAN and Core assets used to provide the fixed line services.

In deciding to allocate the increment to the 'ducts and pipes' asset class, the ACCC took the view that the economic value of these assets is likely to be substantially higher than their depreciated historic values as recorded in the RAF accounts. Since these assets are long-lived, they are more susceptible to the limitations of past accounting practices than other network assets in establishing a value based on accounting records. In addition, these assets represent infrastructure that will be of use beyond the life of the current copper network. In particular, ducts and pipes are likely to be of continuing economic value for a fibre based network.

In regard to the WLR, LCS and LSS prices estimated by the FLSM as being consistent with the \$16 ULLS price for Bands 1 to 3, the ACCC notes that the main factor causing the structure of prices across services to differ from the previous indicative prices is lower costs of providing WLR, LCS and LSS relative to ULLS.

Falling investment in some of the equipment used to provide the fixed line services (for example, switching equipment) has reduced the costs of providing WLR and LCS. The costs of providing those two services have also been reduced by removing the monopoly profits built into the previous RMRC-based indicative prices. As mentioned in section 3.1 above, the ACCC has previously signalled to industry its

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<sup>37</sup> Telstra CAN RKR data, December 2010.

<sup>38</sup> Using a net present value approach to determine asset values is an accepted valuation method. See Steering Committee on National Performance Monitoring of Government Trading Enterprises, *Guidelines on Accounting Policy for Valuation of Assets of Government Trading Enterprises: Using Current Valuation Methods*, Commonwealth of Australia, State and Territory Governments, 1994.

intention to move away from the RMRC pricing approach that has caused WLR and LCS prices to exceed cost-based prices, particularly for WLR<sup>39</sup>

For LSS, the cost of providing the service has fallen because the LSS-specific assets are now fully depreciated.<sup>40</sup>

#### 5.4 Averaging Band 1 to 3 ULLS prices

The ACCC has decided to average Band 1 to 3 ULLS prices.<sup>41</sup> In reaching this decision, the ACCC has had regard to a number of factors.

Although the ACCC has rejected national averaging of ULLS prices in the past, it has previously considered greater averaging of the lower cost ULLS Bands. Most recently this was considered in the context of the Zone A and Zone B proposals associated with the indicative price consultation based around the Analysys Cost Model during 2009.<sup>42</sup> The arguments from that time are still relevant today.

It could be argued that Bands 1 to 3 share similar characteristics and the aggregation of these geographic regions is appropriate and will not have a distortionary impact on investment or competition. This view is supported by the significant narrowing of the price differential between Bands 2 and 3 that results from the adoption in the FLSM of band cost differentials derived from the Analysys Cost Model. Previously, price differentials were calculated on the basis of the previous PIE II model relativities,<sup>43</sup> which the ACCC considers overstated the actual band cost differentials.

Averaging the Band 1 to 3 ULLS prices into a single price simplifies the ULLS price structure and may reduce administrative costs.<sup>44</sup>

Setting a separate Band 4 price ensures that the much higher costs of providing services in rural areas is reflected in prices. It also recognises that in Band 4, the small scale of markets, and the greater risks associated with attracting sufficient customers to recoup DSLAM investment costs, are likely to be more important to investment decisions than the ULLS/WLR price differential. This is consistent with the ACCC's argument in the September 2010 Draft Report that national averaging of ULLS prices would not promote competition in remote areas 'given that the ULLS is not

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<sup>39</sup> ACCC, *Local carriage service and wholesale line rental – final pricing principles and indicative prices for 2008-2009*, August 2008.

<sup>40</sup> See ACCC, *Statement of reasons for the final determination made in access dispute between Chime Communications Pty Ltd and Telstra Corporation Limited in relation to the LSS*, pp. 37-38. The statement of reasons is available on the ACCC website: [www.accc.gov.au](http://www.accc.gov.au).

<sup>41</sup> In averaging the Bands 1 to 3 prices estimated by the FLSM, the ACCC has weighted the estimated Band prices by the share of SIOs in each Band.

<sup>42</sup> ACCC, *Draft principles and indicative prices for LCS, WLR, PSTN OTA, ULLS, LSS*, August 2009, p. 21.

<sup>43</sup> The PIE II model is a model developed by Telstra for network cost estimation. Telstra has used this model to support several submissions to the ACCC. The ACCC has held concerns about the accuracy of the results generated by the model: see ACCC, *Assessment of Telstra's ULLS monthly charge undertaking*, Draft Decision, June 2006, p. 37.

<sup>44</sup> It would also tend to reduce any market distortions said to be caused by having a de-averaged ULLS price and a nationally averaged WLR price. While retaining a separate Band 4 ULLS price with a nationally averaged WLR price could be argued to distort investment decisions, it is more likely that the small scale of markets in remote areas, and the greater risks associated with attracting sufficient customers to recoup DSLAM costs, are more important to investment decisions in remote areas than the ULLS/WLR price differential.

technically viable for delivering high speed data services in large parts of rural areas.<sup>45</sup>

The ACCC recognises that its decision to average ULLS prices for Bands 1 to 3 will result in a price increase in Band 1. However, for most access seekers the Band 1 price increase will be more than offset by the lower Band 3 ULLS price and lower prices for other declared fixed line services such as the WLR and LSS.<sup>46</sup>

The ACCC considers that the reduction in price charged in Band 3 may promote further investments in DSLAMs in those ESAs. The ACCC is currently addressing the issue of backhaul pricing, which has previously been identified as one of the obstacles to DSLAM roll-outs in Band 3 ESAs.<sup>47</sup> These two measures could potentially increase in competition in Band 3, where currently only 1.4 per cent of ULLS lines are located.<sup>48</sup>

The ACCC has also had regard to the changing nature of the telecommunications industry and NBN Co's stated intention to charge uniform national wholesale prices for the National Broadband Network (NBN).<sup>49</sup> The ACCC considers that averaging of Band 1 to 3 ULLS prices at this time will ease industry's transition to national wholesale pricing for the NBN. The ACCC notes that Band 4 ESAs are largely outside the fibre footprint and are likely to be served by wireless technologies. This provides a further basis for the ACCC decision to set a separate ULLS price in Band 4.

In the absence of bypass of the CAN, greater averaging of ULLS prices will not lead to the possibility of inefficient duplication of the CAN network. In the current situation, the NBN will displace rather than duplicate the CAN. Averaging of ULLS prices may assist a smooth transition to the NBN and promote industry stability.

## 5.5 Rounding prices

The ACCC has decided to round up the prices estimated by the FLSM for the Bands 1 to 3 ULLS, the WLR and the LSS.

The ACCC considers that this will simplify the rate structure and ensure a seamless transition from the previous indicative price for Band 2 ULLS.

## 6 Non-price terms and conditions

The ACCC has decided to include certain non-price terms and conditions in the IADs for all the declared fixed line services.

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<sup>45</sup> September 2010 Draft Report, p. 52.

<sup>46</sup> Access seekers may also benefit from any reduced administrative costs consequent on the simplification of the ULLS price structure.

<sup>47</sup> Other obstacles include the small scale of markets in many Band 3 ESAs and the resulting greater risks associated with attracting sufficient customers to recoup DSLAM costs.

<sup>48</sup> Telstra CAN RKR data, December 2010.

<sup>49</sup> NBN Co has announced that it intends to: "Provide nationwide access to high-speed broadband through uniform national wholesale access pricing and competitive price offerings." See NBN Co Ltd, *NBN Co Wholesale Access Service: Product and Pricing Overview for Access Seekers*, December 2010, p. 5, available at [www.nbnco.com.au/wps/wcm/connect/main/site-base/main-areas/publications-and-announcements/publications/product-and-pricing-overview](http://www.nbnco.com.au/wps/wcm/connect/main/site-base/main-areas/publications-and-announcements/publications/product-and-pricing-overview).

The ACCC considers that this will provide industry with default terms and conditions in the interim period before FADs are made. The inclusion of these terms in the IADs may reduce the number of access disputes between parties in the transitional period for areas covered by the non-price terms and conditions. The non-price model terms and conditions cover the following areas:

- (a) billing and notification
- (b) creditworthiness and security
- (c) general dispute resolution procedures
- (d) confidentiality provisions
- (e) communication with end-users
- (f) network modernisation and upgrade provisions
- (g) suspension and termination
- (h) changes to operating manuals, and
- (i) ULLS ordering and provisioning.

All of the above areas incorporate the wording of the *Model Non-Price Terms & Conditions Determination 2008* (2008 Model Terms) except for (f) and (i). For the network modernisation and upgrade provisions, the ACCC had regard to final determinations made in April 2010 in relation to various ULLS and LSS access disputes.<sup>50</sup> Similarly, for the ULLS ordering and provisioning terms (in particular, the LSS to ULLS transfer process), the ACCC has had regard to final determinations made in August 2010 in various ULLS access disputes.<sup>51</sup>

The ACCC consulted with industry before making the 2008 Model Terms. Similarly, the ACCC consulted with various parties in making the final determinations in relation to areas (f) and (i) above. The ACCC considers that the terms adopted in both the 2008 Model Terms and the final determinations in the relevant access disputes represent the best information before the ACCC at the time of making these IADs.

It is relevant to note that, for the purposes of the IADs, the ACCC has excluded the following clauses contained in the 2008 Model Terms:

- the liability (risk allocation) provisions which are contained in clause C of the 2008 Model Terms
- the intact vacant ULLS (iVULLs) provisions which are contained in clauses J.20 to J.24 and annexure 2 of the 2008 Model Terms, and
- the facilities access provisions which are contained in clause K of the 2008 Model Terms.

In determining the non-price terms of the IADs, the ACCC has decided to take a conservative approach and limit the scope of some of the 2008 Model Terms. This is because there is no requirement for consultation before making an IAD, and breach of

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<sup>50</sup> Some of these final determinations are available on the ACCC website: [www.accc.gov.au](http://www.accc.gov.au).

<sup>51</sup> A copy is available on the ACCC website: [www.accc.gov.au](http://www.accc.gov.au).

an IAD results in a breach of carrier licence condition<sup>52</sup> and a service provider rule.<sup>53</sup> Both breaches may involve substantial pecuniary penalties of up to \$10 million.<sup>54</sup>

In relation to the iVULLs and the facilities access provisions, the ACCC also understands that there have been recent industry developments in relation to that process.

The ACCC will consult with industry on the content of non-price terms and conditions, including those provisions of the 2008 Model Terms that were excluded from the IADs, when it commences its FAD inquiry.

## **7 Incorporation of the effect of exemption determinations**

As noted above, the transitional provisions in the CACS Act state that once an AD (including an IAD) in relation to a service commences, a determination made under the exemption provisions ceases to have effect.<sup>55</sup>

Before the commencement of the IADs, there were eight exemption determinations which affected the WLR, LCS and PSTN OA services:

### ***Tribunal's Metropolitan Determinations***

- Australian Competition Tribunal's (Tribunal) 2009 WLR Individual Exemption Order made on 24 August 2009
- Tribunal's 2009 LCS Individual Exemption Order made on 24 August 2009
- Tribunal's 2009 PSTN OA Individual Exemption Order made on 9 September 2009 (in relation to the supply of the PSTN OA in metropolitan ESAs)

### ***ACCC and Tribunal's CBD PSTN OA Determinations***

- ACCC's Individual Exemption Order No. 6 of 2008 made on 30 October 2008, affirmed and varied by the Tribunal's 2009 PSTN OA CBD Individual Exemption Order made on 9 September 2009 (in relation to the supply of the PSTN OA in CBD ESAs)

### ***ACCC's Class Exemption Determinations***

- ACCC's Class Exemption Determination No. 1 of 2008 made on 22 August 2008 (in respect of the LCS)<sup>56</sup>
- ACCC's Class Exemption Determination No. 2 of 2008 made on 22 August 2008 (in respect of the WLR)<sup>57</sup>
- ACCC's Class Exemption Determination No. 3 of 2008 made on 29 October 2009 (in respect of the PSTN OA)<sup>58</sup>

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<sup>52</sup> Section 152BCO of the CCA.

<sup>53</sup> Section 152BCP of the CCA.

<sup>54</sup> Sections 68 and 101 and Part 31 of the *Telecommunications Act 1997*.

<sup>55</sup> Items 202 (class exemptions) and 203 (individual exemptions) of the CACS Act.

<sup>56</sup> This determination was subsequently varied by the ACCC's Class Exemption (Variation) Determination No. 2 of 2009.

<sup>57</sup> This determination was subsequently varied by the ACCC's Class Exemption (Variation) Determination No. 1 of 2009.

(together, the Exemption Determinations).

The Exemption Determinations made access providers exempt from the SAOs in relation to the WLR, LCS, and PSTN OA in certain ESAs, subject to conditions and limitations.

The ACCC and Tribunal's CBD PSTN OA Determinations made Telstra exempt from the SAOs in relation to the supply of the PSTN OA in 17 CBD ESAs, subject to conditions and limitations. The ACCC's Class Orders in relation to the PSTN OA mirrored the ACCC and Tribunal's orders, and made the exemption apply to all access providers (not just Telstra).

The Tribunal's Metropolitan Determinations specified that Telstra was exempt from SAOs in relation to the supply of the WLR, LCS and PSTN OA in certain metropolitan ESAs, subject to conditions and limitations. The ACCC's Class Orders mirrored the Tribunal's Orders and made the exemption apply to all access providers (not just Telstra).

The ACCC has decided to incorporate the effect of the Exemption Determinations into the IADs for the WLR, LCS and PSTN OA services. The ACCC considers that this approach promotes regulatory consistency in the transition to the new access regime and is also consistent with the Tribunal's assessment that the Exemption Determinations in relation to those services was in the long-term interests of end-users.

### ***Calculations of Exemption ESAs***

The Tribunal's Metropolitan Determinations required the ACCC to calculate which of the 380 ESAs listed in those determinations would become 'Exemption ESAs' on a six monthly basis. In order to become an Exemption ESA the ESA was required to satisfy three conditions listed in the determination. The ACCC was required to publish a list of those ESAs on its website, and the exemption in relation to the ESAs would take effect approximately six months after the publication.

On 30 December 2010, 129 ESAs took effect as Exempt ESAs under the Tribunal's Metropolitan Determinations. Those ESAs are published on the ACCC's website.

The IADs make all access providers exempt from the SAOs in relation to the supply of the WLR, LCS and PSTN OA in those 129 ESAs from 1 January 2011. This is because the IADs incorporate the effect of the Tribunal's Metropolitan Orders and the ACCC's Class Orders in their entirety.

Under the Tribunal's Metropolitan Determinations, a further 52 ESAs would have become exempt from 30 June 2011. Those ESAs are published on the ACCC website. If the IADs are still in effect on that date, the exemption in relation to those additional 52 ESAs will take effect at that date.

Under the IADs, the ACCC will still be required to collect information from ULLS acquirers and from Telstra on a six monthly basis in order to calculate which ESAs will become Exemption ESAs in future periods.

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<sup>58</sup> This determination was subsequently varied by the ACCC's Class Exemption (Variation) Determination No. 3 of 2009.

The ACCC will consult with industry on the issue of exemptions from the SAOs in certain areas or in certain circumstances when it commences its FAD inquiry.

## **8 Commencement and expiry**

The IADs will be backdated to commence on 1 January 2011. The ACCC considers that it is desirable that IADs apply from this date to give industry certainty by setting default (or benchmark) price related terms from the expiry of the pricing principles determinations on 31 December 2010.

The CCA requires IADs to specify an expiry date. As such, the ACCC has specified that the IADs should expire on 31 December 2011. When an FAD commences, the IAD for that service will automatically be revoked.<sup>59</sup>

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<sup>59</sup> Section 152BCF(9A) of the CCA.

## Appendix A: Revisions to the Fixed Line Services Model (FLSM) and ACCC forecasts

Revision	Submission reference*	Comment
<b><i>Assets included in FLSM</i></b>		
Inclusion of some assets incorrectly omitted from the FLSM and removal of some assets incorrectly included	Telstra main submission (pp. 108-109)	<p>Asset classes added to the RAB, based on information provided by Telstra, are:</p> <ul style="list-style-type: none"> <li>• ‘other communications plant and equipment’ added to CAN – to account for CAN radio systems and some network support assets</li> <li>• ‘network land’ and ‘other non current assets’ – include relevant land assets</li> <li>• ‘network buildings and support assets’ – include relevant building and support assets</li> </ul> <p>Asset classes removed from RAB, based on information provided by Telstra, are ‘satellite equipment’ and ‘international network cables’</p>
Treatment of land assets	Telstra main submission (pp. 59-60)	<p>To reflect the appreciation of land, the value of land assets is indexed by increasing the closing value of land assets by forecast CPI inflation to obtain the following year’s opening value when rolling over the RAB.</p> <p>To prevent land assets being depreciated in the FLSM, very long asset lives (10,000 years) have been used to ensure that annual depreciation is negligible. This is consistent with the approach adopted by many other regulators.</p>
Revision of asset lives for some asset classes	Telstra main submission (pp. 108-109) and Schedule 7	<p>The following asset lives have been increased on the basis of information provided by Telstra:</p> <ul style="list-style-type: none"> <li>• ‘ducts and pipes’ (from 30 to 35 years)</li> <li>• ‘transmission equipment’ (from 10 to 15 years)</li> <li>• ‘radio bearer equipment’ (from 10 to 16 years).</li> </ul> <p>Asset lives for newly added asset classes were obtained from Telstra’s Schedule 7.</p>
<b><i>Inclusion of LSS in FLSM</i></b>		
Inclusion of LSS in FLSM	Frontier Economics (pp.	Estimates of the specific costs of providing the LSS, including an allowance



<b>Revision</b>	<b>Submission reference*</b>	<b>Comment</b>
	25-33), Herbert Geer (pp. 3-7), Optus (p. 37) and Telstra main submission (p. 121)	for overheads, were included in the FLSM following Telstra's provision of information on the costs it allocates to the LSS, in response to a request by the ACCC. Network costs allocated to the LSS by Telstra were excluded as these are recovered through the WLR prices.
<b><i>Cost allocation factors</i></b>		
Increased transparency in cost allocation factors	Macquarie Telecom (p. 3), RBS (p. 4), Herbert Geer (p. 12).	New spreadsheet showing the calculations for cost allocation factors added to the FLSM.
Use of 2008-09 Analysys allocation factors as starting point		Correction of error caused by using 2009-10 Analysys allocation factors instead of 2008-09 Analysys allocation factors.
PSTN OTA transmission allocation factors	Frontier Economics (pp. 19-20)	Calculation error corrected. Use of historical growth in PSTN minutes, packet switch data and ISDN traffic to determine cost allocation factors.
Allocation factors included for added asset classes 'network land' and 'network building and support assets'		For the ULLS and the WLR, the factors are Analysys Cost Model factors adjusted for actual 2008-09 demand and for demand forecasts in subsequent years. For PSTN OTA and LCS, the factors are a weighted average of the cost allocation factors for all other asset classes (excluding 'network land' and 'network building and support assets') used by those services.
Allocation factors for 'other plant and equipment' and 'indirect capital assets'		'Indirect capital assets': The factors are calculated by taking a weighted average of the allocation factors for the other asset classes. 'Other communications plant and equipment': For ULLS and WLR, a weighted average of the CAN 'radio bearer equipment' and 'network building and support assets' factors are used. For PSTN OTA and LCS, the 'network building and support assets' allocations are used.
Adjustment of cost allocation factors for 'ducts and pipes' and 'copper cables' for ULLS and WLR to take account of geographic cost differentials	Optus (pp. 30-35, 53-56), CEG (on behalf of Optus)	Cost relativities between the bands for 'ducts and pipes' and 'copper cables' have been derived from the Analysys Cost Model.
<b><i>Operating expenditure</i></b>		
Revisions to total operating expenditure		Revisions reflect the changes in asset classes included in the RAB.

<b>Revision</b>	<b>Submission reference*</b>	<b>Comment</b>
Removal of operating expenditure for 'customer equipment', 'satellite equipment' and 'international network cables' asset classes		Telstra has advised that these asset classes are not used to provide the regulated fixed line services.
Mark-up for indirect operating costs increased	Telstra main submission (p. 61)	Increased from 10 per cent to 80 per cent based on analysis of Telstra's RAF accounts and Analysys Cost Model assumptions.
Use of better inflator for telecommunications assets	Frontier Economics (p. 11)	ABS producer price index - Communication equipment manufacturing.
Operating expenditure for 'other communications plant and equipment' reduced		Updated to reflect better information from Telstra on the proportion of 'other communications plant and equipment' assets used to provide the fixed line services.
Lower forecasts for CAN operating expenditure	Frontier Economics (pp. 10-12), Optus main submission (pp. 8-19)	Use of the most recent actual operating expenditure value instead of the 5-year average.
<b><i>Capital expenditure</i></b>		
Use of better inflator for telecommunications assets	Frontier Economics (p. 6)	ABS producer price index - Communication equipment manufacturing.
Inclusion of forecast capital expenditure for 'network land' and 'network building and support assets'		Forecasts determined using a five year (FY2005-2009) historical average of expenditures indexed to 1 June 2009. Historical capital expenditures obtained from Telstra's asset register.
Inclusion of capital expenditure for 'indirect capital assets'		Annual capital expenditure has been assumed to equal annual depreciation.
Lower forecasts for CAN capital expenditure	Frontier Economics (pp. 6-10), Optus main submission (pp. 8-19)	Extrapolation of the declining trend in capital expenditure over the past 5 years.
<b><i>WACC parameters</i></b>		
Updated risk free rate	Telstra main submission (p. 84)	Increased to 5.61 per cent (from 5.36 per cent), based on 20 day average for 6 December 2010 to 31 December 2010.

<b>Revision</b>	<b>Submission reference*</b>	<b>Comment</b>
Updated expected inflation		Based on updated inflation forecasts issued by the Reserve Bank. The updated expected inflation rate is 2.63 per cent; compared to 2.59 per cent in the September 2010 Draft Report.
Revised gamma	Telstra main submission (pp. 87–90)	Economy-wide gamma estimate of 0.45 adopted.
Use of debt risk premium for benchmark A-rated 10-year bonds	Vodafone Hutchison (p. 8), Telstra main submission (p. 84)	The nominal debt risk premium has been updated to 2.19 per cent, based on 20 day average for 6 December 2010 to 31 December 2010 using Telstra's Australian bond issues with 10 years to maturity. Telstra is understood to currently be the only A-rated company issuing 10-year bonds. As a result, the Telstra 10-year bond issues were used as the benchmark at this time.
<b><i>Regulatory period</i></b>		
IADs have been set for one calendar year (2011)	Telstra main submission (p. 110), Optus main submission (pp. 18-19)	IADs are interim and apply until FADs are made. The ACCC will consult on the length of the regulatory period for FADs.
<b><i>Forecast demand</i></b>		
Use of actual 2009-10 demand figures for PSTN OTA and LCS	Telstra supplementary submission, November 2010 (p. 32).	For PSTN OTA., actual 2009-10 data now available from Telstra's Schedule 8 RAF data. For LCS, demand data provided by Telstra (9 months of actual and 3 months of forecasts).
Updated demand forecasts	Optus main submission (p. 39-42), Macquarie Telecom (p. 7) Frontier Economics (p. 13-15), Herbert Geer (p. 13), Telstra supplementary submission, November 2010 (p. 32).	Revisions based on actual demand trends and internal projections provided by Telstra in November 2010.

<b>Revision</b>	<b>Submission reference*</b>	<b>Comment</b>
<b><i>Roll-forward</i></b>		
2009-10 RAB roll-forward calculation	Telstra main submission (pp. 63-64)	Correction of calculation for net capital additions in 2009-10.
<b><i>RAB</i></b>		
Revision of RAB values included in FLSM		Asset values reconciled with Telstra's asset register and Telstra's November submission providing disaggregated values for assets included in the RAF.
Allocation of 'network building and support assets' to CAN and Core RABs	Telstra supplementary submission, November 2010 (pp. 8-14)	Allocation between the CAN and Core based on depreciated TEA model values for 'network building and support assets' included in the CAN. The residual value is allocated to the Core.
Value for 'other CAN' asset class		'Other CAN' is made up of pair gains systems equipment. The depreciation level for the 'pair gains' asset class has been applied to 'other CAN'.
Allocation of 'other communications plant and equipment' to CAN and Core RABs		'Other communications plant and equipment' is made up of CAN Radio bearer equipment and network buildings/support assets. The CAN Radio bearer equipment in this asset class is allocated entirely to the CAN. The remaining 'other communications plant and equipment' assets (network buildings/support-type assets) are allocated in the same proportion as the 'network building and support' asset class is allocated between the CAN and Core.
Allocation of 'indirect capital assets' to CAN and Core RABs		'Indirect capital assets' have been allocated to the CAN and Core RABs in the same proportions as direct network assets (59% for the CAN, 41% Core).
<b><i>Pricing</i></b>		
Averaging of ULLS band prices		ULLS band 1 to 3 prices have been averaged by using the proportion of SIOs in each of the three bands to obtain a weighted average price.

\*Where relevant, the submissions taken into account by the ACCC in deciding on revisions are listed. In some cases, the ACCC has made revisions based on its own analysis since releasing the September 2010 Draft Report.