Submission by AAPT Limited to the Australian Competition and Consumer Commission's draft report titled *Review of the 1997 telecommunications access pricing principles for fixed line services*, dated September 2010

Introduction

1. AAPT Limited (**AAPT**) welcomes the opportunity to comment on the Australian Competition and Consumer Commission's (the **ACCC's**) release of the draft report titled *Review of the 1997 telecommunications access pricing principles for fixed line services*, dated July 2010 (**Draft Report**).

2. AAPT makes this submission to the Draft Report alongside the report by Frontier Economics commissioned by the Competitive Carriers Coalition (**CCC**) (the **Frontier Economics Draft Pricing Report**). AAPT fully supports the comments made by Frontier Economics in that report.

Executive summary

Shift from TSLRIC+ to BBM

3. AAPT welcomes the ACCC's proposed shift from a total service long run incremental cost plus an allocation for common costs (**TSLRIC+**) pricing methodology for public switched telephone network originating and terminating access (**PSTN OTA**) and unbundled local loop service (**ULLS**) and a retail minus retail costs (**RMRC**) pricing methodology for wholesale line rental (**WLR**) and local carriage service (**LCS**) to a building block model (**BBM**) approach. AAPT also supports the continued use of the line sharing service (**LSS**) specific cost model.

4. AAPT considers that such an approach will promote the long term interests of end users (**LTIE**).

Use of DAC and the RAF accounts to establish the initial RAB

5. AAPT supports the ACCC's proposal to use depreciated actual cost (**DAC**) and the use of the regulatory accounting framework (**RAF**) accounts to establish the initial regulated asset base (**RAB**). However, AAPT considers that the straight line depreciation used in the RAF accounts should be replaced with a method which reduces the assets in those accounts by the actual compensation Telstra has received against those assets (as detailed in the report by Frontier Economics commissioned by the CCC in response to the ACCC's earlier discussion paper on this issue (the **Frontier Economics Discussion Paper Report**)).

6. If the ACCC continues to use the straight line depreciation in the RAF accounts to establish the initial RAB then AAPT considers that the ACCC's initial RAB estimate should be considered to be an extreme high end estimate.

7. In AAPT's view, the ACCC's initial RAB estimate should be considered to be a high end estimate in any event because it hasn't been adjusted for inefficient investments by Telstra in its customer access network (**CAN**) and core network.

The WACC

8. AAPT considers that a WACC of 9.14% is more than an adequate return on Telstra's sunk assets which in AAPT's view have probably already paid for themselves many times over.

Individual prices and a four year regulatory period

9. AAPT supports the ACCC's proposal to set prices for each individual service.

10. AAPT also supports the adoption of a four year regulatory period, however, AAPT considers that indicative pricing should be assessed against international

benchmarks during this period to ensure access pricing in Australia does not become expensive relative to the rest of the world as AAPT submits has in fact happened with the ACCC's current indicative prices for mobile terminating access (**MTAS**).

11. AAPT also considers that indicative pricing should also be reassessed once Telstra has finalised its deal with NBN Co. In AAPT's view, the payment of $9B from NBN Co to Telstra as specified in the financial heads of agreement between Telstra and NBN Co (the **FHOA**) should be factored into and result in a significant reduction in indicative access prices in order to avoid the situation where Telstra is effectively compensated more than once for its network investments.

Pricing structure

12. AAPT supports:

  - a national WLR and LCS price due to the fact that at a retail level both line rental and local calls are priced on a national basis and because there is no geographical break up of costs available;

  - a national LSS price on the basis that the only costs involved in providing the LSS are provisioning costs which are not dependent on geography;

  - a geographically de-averaged ULLS price because an average ULLS price would not promote competition the LTIE as it would involve a significant departure from the real underlying costs of the provision of the ULLS; and

  - a geographically de-averaged PSTN OTA price because an average PSTN OTA price would not promote the LTIE as it would involve a significant departure from the real underlying costs of provision of PSTN OTA. AAPT agrees with the Optus letter dated 23 September 2010 which advocated a revision of the PSTN OTA pricing break up using more current data including the need to factor in shorter call holding times, however, AAPT strongly disagrees with the alternative proposition made in that same letter that the ACCC should consider setting a nationally averaged PSTN OTA rate because there are significant price differences between geographic bands.

Draft prices

13. AAPT considers that the draft indicative prices are too high because:

- they are all (except for LSS) based on an initial RAB which is set too high;
- in the case of WLR, LCS and ULLS specifically, prices have been rounded up significantly and unnecessarily (particularly given that AAPT considers that the BBM estimates should be considered as providing high end estimates);
- in the case of WLR, ULLS and LSS specifically, prices appear expensive by international standards, eg in the UK (based on the exchange rate as of 15 October 2010) the current price in the UK for WLR is AUD$13.45 pm, for ULLS is AUD$11.63 pm and for LSS is AUD$2.10 pm. This is particularly concerning for AAPT given that the ACCC is proposing to effectively lock in indicative prices for four years;
- in the case of PSTN OTA specifically, AAPT agrees with many analysts including the highly regarded Wik-Consult and Ovum which both predict that interconnection pricing for both fixed and mobile networks is ultimately heading towards bill and keep (ie zero) and that as a result AAPT considers that interconnect pricing should be trending that way. Increasing PSTN OTA by 10% as is proposed in the Draft Report will not promote

competition or the LTIE and is at odds with the anticipated trend to zero and may (as argued by Wik-Consult) even cause delay to industry migration away from circuit switched interconnection to IP based interconnection resulting in inefficiencies which are not in the LTIE; and

- in the case of LCS specifically, prices are based on an assumed call holding time of 4 minutes when AAPT considers that industry wide call holding times for local calls are closer to 3 minutes.

In conclusion

14. AAPT urges the ACCC to:

    - reconsider the way it measures depreciation when determining the initial RAB;

    - treat the BBM price estimates as being high end estimates and therefore the ACCC should not round these numbers up as has been done with WLR, LCS and ULLS. In AAPT's view, this is further supported by current pricing for equivalent services in overseas jurisdictions;

    - re-assess the LCS price based on a call holding time closer to three minutes, instead of four minutes;

    - decrease (not increase) PSTN OTA prices given the anticipated international trend towards bill and keep; and

    - make an express provision in the indicative price determination for the re-assessment of indicative prices once the FHOA between Telstra and NBN Co has been finalised and when the indicative prices begin to appear expensive by international standards.

Moving from TSLRIC+ to BBM

15. The ACCC states in the Draft Report that it intends to adopt a BBM approach with a locked-in RAB when determining principles relating to the price of access to the declared services, excluding LSS where prices will be estimated using a model specific to providing those services[1].

16. Some of the main arguments in favour of the shift from TSLRIC+ and RMRC to BBM approach are stated to be[2]:

    - the continual revaluation of network assets has caused ongoing uncertainty over the level of access prices;

    - TSLRIC+ based pricing may have resulted in the past depreciation of existing assets not being taken into account resulting in over recovery by the access provider; and

    - Telstra's CAN appears to display enduring bottleneck characteristics rather than a network likely to be bypassed and therefore one of the primary reasons for adopting TSLRIC+ methodology in the first place is simply not applicable.

17. The ACCC notes that it considers that moving to a BBM approach will promote the LTIE and that locking in a value for the RAB will improve certainty for access seekers and access providers, promote predictable revenue and price paths and minimise the risk of windfall gains or losses, reduce the risk that

[1] Draft Report, page 17
[2] Draft Report, page 15

efficient investment will not be recovered, promote efficient investment in infrastructure and promote competitive entry and competition[3].

18. AAPT welcomes the shift from TSLRIC+ and RMRC to a BBM approach and agrees with the ACCC that this approach will promote the LTIE.

19. AAPT also supports the decision to continue to price LSS using a separate specific cost model (established and fully tested during the recent LSS arbitrations) and agrees with the ACCC that this approach will promote the LTIE.

Setting the initial RAB

DAC is the right choice

20. The ACCC notes in the Draft Report that the main issue in setting the initial RAB is determining how to assign a value to Telstra's sunk network assets with potential values for the initial RAB ranging from scrap value to optimised replacement cost[4].

21. The ACCC also noted that while scrap value could be justified by reference to the sunk nature of the copper network, setting the initial RAB on this basis would be inconsistent with Telstra's legitimate commercial interests and could mean that access providers may be unwilling to make sunk investments in the future[5].

22. AAPT disagrees with the ACCC's approach on this issue and would have welcomed a determination that set the initial RAB by reference to the sunk

[3] Draft Report, page 18
[4] Draft Report, page 21
[5] Draft Report, page 21

nature of Telstra's copper network. AAPT considers that the copper network has paid for itself many times over and, consequently, does not believe that such an approach would be inconsistent with Telstra's **legitimate** commercial interests.

23. The ACCC proposes to adopt a single RAB from which infrastructure costs can then be allocated to various services using cost allocation rules[6].

24. AAPT agrees that a single RAB is simple, practical and avoids the complexity associated with multiple RABs.

25. The ACCC proposes to include assets from Telstra's network in the initial RAB, including assets from the CAN (eg ducts and copper cables) and the core network (eg switching equipment) used to provide services, including non-declared services. A portion of these shared costs is then allocated to the declared fixed line services[7].

26. The ACCC proposes to use a DAC valuation method on the basis that it[8]:

   - encourages efficient use of and investment in infrastructure (as Telstra will be able to recover its actual costs);
   - promotes competition (by ensuring that access seekers face wholesale prices for bottleneck services which reflect the actual cost of service provision);
   - is relatively simple and objective (values for actual costs can be derived from regulatory and/or general ledger accounts);
   - promotes Telstra's legitimate commercial interests; and

[6] Draft Report, page 22
[7] Draft Report, page 22 & 23
[8] Draft Report, page 25, 26 & 27

- is well known (having being used in other regulated industries over the past decade).

27. AAPT supports the ACCC's decision to adopt a DAC valuation method. AAPT considers that the depreciated optimised replacement cost (**DORC**) approach advocated by Telstra is not in the LTIE because:

    - the underlying rationale for the use of a replacement cost approach (ie to promote efficient build versus buy decisions) does not apply as Telstra's CAN is an enduring bottle neck which is unlikely to be bypassed; and

    - the replacement cost approach has a high level of subjectivity in comparison to a DAC approach.

Depreciation

28. The ACCC considers that past compensation received by Telstra up to the date of setting the initial RAB should be taken into account when valuing the initial RAB because this ensures that access seekers and ultimately end-users are not charged more than once for Telstra's costs of investing in the existing assets[9]. The ACCC proposes to take into account the past depreciation as that depreciation is outlined in the RAF accounts provided by Telstra[10].

29. AAPT supports the use of the RAF accounts to establish an initial RAB but considers that the depreciation recorded in the RAF accounts has been based on straight-line depreciation when the gross value of the historic costs from

[9] Draft Report, page 23
[10] Draft Report, page 23

Telstra's RAF accounts should be reduced by the actual compensation that Telstra has received against those assets to date[11].

30. If the ACCC continues to use the straight line depreciation in the RAF accounts to establish the initial RAB then AAPT considers that the ACCC's initial RAB estimate should be considered as being an extreme high end estimate.

31. In addition, the ACCC acknowledges that the DAC could be adjusted downwards[12]:

    - to remove or write down assets which were inefficient; and

    - by using different estimates for the remaining assets lives of existing ducts and pipes and copper cables since much of the network would have already been fully depreciated,

    however, it does not in fact make these adjustments because it considers that reliable information on which to base these adjustments is not available[13].

32. Consequently, AAPT considers that, in any event, the ACCC's estimate of the initial RAB should be considered to be a high end estimate.

33. AAPT urges the ACCC to:

    - make adjustments to the RAF account data when calculating the initial RAB by replacing the straight line depreciation set out in the RAF account data and replacing it with the actual compensation received by Telstra; and

[11] These arguments were detailed on page 19 of the Frontier Economics Discussion Paper Report
[12] Draft Report, page 28
[13] Draft Report, page 28

- reconsider its decision to not make adjustments for Telstra's inefficient investments and asset lives.

34. AAPT considers that if these things are not done then the ACCC's initial RAB estimate should be considered to be very much a high end estimate and therefore the ACCC should not round these numbers up in any circumstances.

The FHOA

35. The ACCC has also decided not to take into account the migration payments to be paid to Telstra under the FHOA between NBN Co and Telstra, although it does note that it will take this into account in subsequent regulatory periods[14].

36. AAPT considers that these payments should be considered to be revenue received by Telstra against its investment in its CAN and core network and should be taken into account when setting access prices so as to avoid Telstra being compensated twice. AAPT considers that four years is too long a period to ignore such a large compensation payment from NBN Co to Telstra.

Determining the revenue requirement

37. The ACCC notes that the revenue requirement for each year is determined by assessing the forecast opex, WACC on the RAB, depreciation and forecast tax liabilities[15].

Depreciation

38. Once the initial RAB is established using the RAF accounts, the ACCC then notes that it proposes to apply a straight-line depreciation schedule because[16]:

[14] Draft Report, page 29
[15] Draft Report, page 30

- it will allow the access provider to recover the cost of prudently incurred investment over the life of the asset;
- it is likely to promote price stability for end users and therefore greater certainty over the regulatory period;
- it is consistent with the ACCC's and AER's approach in regulating other industries; and
- it is the simplest and most widely adopted method of calculating depreciation.

39. AAPT agrees with this approach but reiterates the point about how depreciation should be measured when setting the initial RAB, ie by taking into account the revenue received by Telstra against those assets to date.

The WACC

40. AAPT considers that a WACC of 9.14% is more than an adequate return on Telstra's sunk assets providing yet another reason why the BBM's indicative price estimates should be considered to be high end estimate and therefore should not be rounded up in any way.

Capex and opex

41. The ACCC notes that it needs to forecast capex and opex during the regulatory period and that it intends to build incentive mechanisms into the regulatory

[16] Draft Report, page 31 & 32

framework to ensure only prudently incurred capex and opex expenditure is included in the revenue requirement[17].

42. The ACCC considers that Telstra should provide capex and opex forecasts to the ACCC and that it will then assess whether they are efficient and necessary[18].

43. The ACCC intends to make a RKR for this purpose which will be the subject of a separate consultation process[19].

44. AAPT is concerned that this process is open to gaming. TLS will clearly face incentives to over estimate its capex and opex forecasts and argue against efficiency adjustments.

45. AAPT supports the approach of building inventive mechanisms to ensure that only prudently incurred capex and opex is included, particularly given that forecast opex has been identified by the ACCC as being a highly sensitive input[20]. Consequently, any forecast provided by Telstra needs to be carefully scrutinised by the ACCC.

46. However, AAPT urges the ACCC to considers an alternative approach whereby a CPI-X cap is applied to individual service prices (as is done in the UK, for example) as this will have a higher level of certainty and in AAPT's view will be less susceptible to gaming[21].

[17] Draft Report, page 37
[18] Draft Report, page 38 and 39
[19] Draft Report, page 39 and 40
[20] Draft Report, page 56
[21] Frontier Report, page 30

Setting prices for specific services

Individual price caps for each declared service

47. The ACCC proposes to set individual price caps for each declared service which reflect Telstra's costs of providing the service, a reasonable rate of return on capital and depreciation.

48. The ACCC considers that an individual price cap is the most effective means of promoting the LTIE as it[22]:

    - provides less flexibility for access providers to move away from cost-based pricing for specific services which promotes competitive neutrality;

    - ensures access providers can't price discriminate (eg by increasing the price for ULLS to prevent or inhibit infrastructure based competition); and

    - promotes efficient build versus buy decisions.

49. AAPT supports the ACCC's proposal to set indicative price caps for each individual service.

Four year regulatory period

50. The ACCC proposes an initial regulatory period of four years (1 January 2011 to 31 December 2014) but notes that the length of any subsequent regulatory periods will be based on industry developments and the applicable legal framework[23].

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[22] Draft Report, page 47
[23] Draft report, page 48

51. The ACCC considers that a four years regulatory period will be in the LTIE as it gives certainty to prices and allows participants to plan investments[24].

52. AAPT welcomes the stability and certainty that comes with a longer regulatory period, however, AAPT is concerned that four years is quite a long period of time and that international pricing may continue to progress down over time (eg AAPT believes that PSTN OTA is heading towards bill and keep) while the ACCC is proposing to hold prices flat for 4 years. This could make prices in Australia appear very expensive by international comparisons by the end of 2014, if not well before.

53. AAPT is also concerned that during the four year regulatory period the deal between NBN Co and Telstra will be finalised resulting in a $9B payment from NBN Co to Telstra. AAPT considers that such a payment should trigger an immediate review of indicative access prices.

54. Consequently, AAPT considers that indicative prices:

- should be assessed against international benchmarks during the regulatory period to ensure that access prices in Australia do not become expensive by international comparisons; and

- should be re-assessed once the FHOA has been finalised between Telstra and NBN Co and that such a re-assessment should not be delayed into the next regulatory period.

Structure of the indicative prices

55. The ACCC proposes to set[25]:

[24] Draft Report, page 48
[25] Draft Report, page 52

- de-averaged prices for ULLS, keeping the existing four band structure;
- de-averaged prices for PSTN OTA, keeping the existing structure; and
- averaged prices for WLR, LCS and LSS.

De-averaged ULLS pricing

56. The ACCC considers that average prices for ULLS will not promote competition or the economically efficient use of and investment in infrastructure and that average pricing would depart significantly from the real underlying costs of the ULLS[26].

57. AAPT agrees and considers that there are significant price differences between the geographic bands (Band 1 through to Band 4) and that averaging the price of ULLS would therefore result in a significant departure from the underlying costs of supply which is clearly not in the LTIE.

Averaged price for WLR

58. The ACCC notes that since retail prices for line rental are set on a national averaged basis, WLR prices should also be set on a nationally averaged basis[27].

59. The ACCC also notes that there is an absence of geographically disaggregated cost date and so the ACCC is not able to determine a cost based de-average price[28].

60. AAPT agrees with this approach adopted by the ACCC.

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[26] Draft Report, page 53
[27] Draft Report, page 53
[28] Draft Report, page 53

Averaged price for LCS

61. The ACCC notes that it does not have reliable geographically de-averaged cost data to set de-averaged LCS prices and so proposes to continue to set prices on a nationally averaged basis[29].

62. AAPT agrees and notes that retail prices are also set on a nationally averaged basis.

Averaged price for LSS

63. The ACCC notes that it does not have reliable geographically de-averaged cost data to set de-averaged LSS prices and so proposes to continue to set prices on a nationally averaged basis[30].

64. AAPT agrees that LSS pricing should be set on a national average basis and notes that the only costs of providing the LSS are the costs of provisioning the LSS which are not dependent on geography.

De-averaged PSTN OTA pricing

65. The ACCC proposes to use the existing banded structure for PSTN OTA as it is in the LTIE[31].

66. AAPT agrees with this approach adopted by the ACCC and considers that there are significant price differences between the geographic bands (CBD, Metro, Provincial and Rural) and that averaging the price of PSTN OTA would involve

[29] Draft Report, page 54
[30] Draft Report, page 54
[31] Draft Report, page 52

a significant departure from the real underlying costs of provision and is therefore not in the LTIE.

67. AAPT agrees with the Optus letter dated 23 September 2010 which advocated a revision of the PSTN OTA pricing break up using more current data including the need to factor in shorter call holding times, however, AAPT strongly disagrees with the alternative proposition made in that same letter that the ACCC should consider setting a nationally averaged PSTN OTA rate because there are significant price differences between geographic bands.

Draft indicative prices

68. AAPT has a number of concerns with each of the draft indicative prices as set out below.

Draft prices for ULLS

69. The ACCC has proposed the following set of ULLS prices based on the current geographically disaggregated band structure[32]: $6.50 pm for B1, $16 pm for B2 and $31 pm for B3.

70. AAPT considers that these prices are higher than they should be because:

   - the initial RAB is set too high;

   - the ACCC has rounded these prices up without any real justification for doing so. The BBM estimates a national average ULLS price of $15.00 whereas the indicative prices proposed by the ACCC appear to be based on a

[32] Draft Report, page 55

national average ULLS price of around $15.75 this equates to a rounding up of around 5%; and

- they appear expensive by international standards. For example in the UK the price for the equivalent service is 15.60 British Pounds pa[33] and based on the exchange rate as of 15 October 2010 this equates to around AUD$11.63 pm.

Draft prices for LSS

71. The ACCC is proposing to leave LSS pricing unchanged at $2.50 pm[34], a decision based (among other things) on the costs associated with the specific operational support systems in place to facilitate LSS provisioning.

72. AAPT supports the continued use of the LSS specific cost model developed during recent LSS arbitrations. This model was fully tested during those arbitrations and therefore should be considered reliable.

73. However, AAPT can recall from its own experience in the LSS arbitrations that the price for LSS should start to fall significantly once Telstra has recouped its initial investment in IT infrastructure required to establish the relevant provisioning system. AAPT is concerned that a price of $2.50 pm for the next four years is likely to mean that Telstra will be over compensated for its investment in the LSS provisioning system.

74. In addition, AAPT notes that the proposed LSS indicative price does appear to be expensive by international standards. For example, in the UK the price for

[33] Ofcom, Openreach Financial Framework, Local Loop Unbundling Charge Control, dated 14 October 2010
[34] Draft Report, page 55

the equivalent service is 15.60 British Pounds pa[35] and based on the exchange rate as of 15 October 2010 this equates to around AUD$2.10 pm.

Draft prices for WLR

75. The ACCC has proposed a WLR indicative price set at $20 pm[36].

76. AAPT is concerned that $20 pm is higher than it should be given:

- the initial RAB is set too high;
- the outputs of the model have been rounded up quite significantly and, in AAPT's view, without justification. The ACCC appears to have rounded up the WLR estimates from the BBM from around $18.75 pm to $20 pm (ie an increase of around 6.7%). In AAPT's view this is not justified given that the BBM estimates should be considered to be high end estimates; and
- $20 pm appears expensive on an international basis. For example, in the UK, Ofcom has set WLR pricing at 100.68 British Pounds pa[37] for the period up to March 2010 and based on the exchange rate as of 15 October 2010 this equates to around AUD$13.36 per month.

Draft prices for LCS

77. The ACCC has proposed an indicative price for LCS of 7 cents per call[38].

78. AAPT is concerned that 7 cents per call is higher than it should be because:

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[35] Ofcom, Openreach Financial Framework, Local Loop Unbundling Charge Control, dated 14 October 2010
[36] Draft Report, page 55
[37] Ofcom, Charge Controls for Wholesale Line Rental and related service, dated 26 October 2009
[38] Draft Report, page 55

- the initial RAB is set too high;

- the outputs of the model have been rounded up unnecessarily; and

- it has been based on a call holding time of 4 minutes. AAPT's local call holding time is around [***cic cic***] and AAPT considers that the industry standard would be much closer to 3 minutes than 4 minutes. AAPT estimates that applying a 3 minute call holding time would reduce the LCS indicative price down to around 5.2 cents per call.

Draft prices for PSTN OTA

79. The ACCC has proposed an indicative price for PSTN OTA at a headline rate of 1.1 cpm[39]. AAPT notes that this is effectively a 10% increase on the current indicative price for PSTN OTA of 1 cpm.

80. AAPT is concerned that 1.1 cpm is higher than it should be because the initial RAB is set too high.

81. In addition, AAPT considers that PSTN OTA and in fact interconnect prices in general should be falling, not increasing.

82. In support of this, AAPT notes that Ovum anticipates the demise of per minute interconnect charging arrangements as noted in a recent report[40]:

> ***End of the minute is approaching***
> *We believe it is inevitable that charging for wholesale (and possibly retail) voice traffic will move from per-minute to a new regime that relates more*

[39] Draft Report, page 55
[40] Ovum, VOIP interconnect: the end of the minute is approaching, dated 9 February 2010, page 4.

closely to the resources used. This is likely to be some form of capacity-based charging, such as per-megabyte.

83. In addition, Ovum also anticipates a move to zero interconnect rates (or bill and keep arrangements) as noted in a recent report[41]:

> *In 2020, developments in network technology will of course have impacted the regulatory regime for the interconnection of fixed and mobile networks. The migration to NGN, increased use of mobile broadband and convergence are all important factors driving significant changes. Two of the most likely future charging principles will be capacity-based charging (CBC) and 'bill and keep' (**BaK**).*
>
> *………*
>
> *BaK is the more likely option in the long term. Given that most NRAs will likely impose symmetric termination rates for fixed and mobile at very low levels, and the expense associated with tracking and billing for small increments is not worthwhile, BaK will probably become the common choice for most operators.*

84. In further support of this, AAPT notes that a recent WIK-Consult report made the following observations[42]:

> *IP based NGNs represent the convergence of the Internet and the traditional switched PSTN/PLMN network. The inevitable question is, should interconnection of future NGNs be based on the Internet economic model, the switched network model or some third model (possibly a blend of the two)?*
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> *………*

[41] Ovum, Telecoms in 2010: regulation, dated 24 December 2009, page 7 and 8
[42] The Future of IP Interconnection: Technical, Economic and Public Policy Aspects, Wik-Consult, dated 29 January 2008, page XI

For reasons explained more fully in the report, it is clear that current CPNP arrangements already have a substantial negative effect on welfare, especially for the mobile network, in a number of respects:

- *They tend to lead to inefficiently high wholesale termination fees, even when the fees are regulated;*
- *High wholesale mobile termination fees in effect create collusory incentives to maintain high per-minute (mobile) retail prices;*
- *The high retail prices depress use of the service to levels far below those that are efficient, and may in some cases depress use below the level of efficient monopoly price s for the operators as well.*

………

All of these considerations lead us to feel that interconnection fees should be much lower than they are today, ***preferable zero****. [*emphasis added*]*

85. Wik also stated in the same report that that if interconnect fees remain as high as they are to day that mobile operators and some fixed operators may choose not to evolve their networks to IP based interconnection. In other words, leaving interconnect rates as high as they are to day will be a self defeating strategy[43]:

If termination fees were to remain at current levels, we anticipate that many mobile operators and some fixed operators might chose not to evolve their networks to IP based interconnection. They might perceive the migration as an unacceptable regulatory risk. Alternatively, they might chose an IP interconnection strategy that attempts to lock in the current inefficient arrangements, or a modernized version of them, rather than enabling IP-based interconnection arrangements to evolve in a healthy and natural way. These concerns suggest that waiting for the migration to IP based NGNs to implement changes might be a self defeating strategy.

[43] The Future of IP Interconnection: Technical, Economic and Public Policy Aspects, Wik-Consult, dated 29 January 2008, page XI

86. AAPT considers that these comments support the view that interconnect charges are expected to and in fact should, for efficiency reasons, trend downwards towards zero or bill and keep.

87. AAPT understands that Telstra will argue that because voice minutes over the PSTN are falling that interconnect rates must as a direct consequence increase because the per-minute price for a given asset base will increase.

88. AAPT considers that these arguments should be dismissed because:

- while the BBM estimates a PSTN OTA price of 1.1 cpm (a 10% increase on current interconnection arrangements), these estimates should be considered to be very much a high end estimate and in AAPT's view the actual cost should be very much lower; and

- there are real efficiency risks in maintaining interconnect rates at current levels let alone increasing them, including the possibility that it may stall network operators from making the shift from circuit switched interconnection to IP based interconnection.