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Via:

Mr Grahame O'Leary and Mr David Hinitt
Communications Group
Australian Competition and Consumer Commission

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Dear Mr O'Leary and Mr Hinitt

ACCC DTCS FAD Inquiry 2014: Discussion Paper - Primary Prices

We refer to the ACCC's discussion paper entitled *Domestic Transmission Capacity Service, Final Access Determination Discussion Paper - Primary Prices, July 2014 (DTCS FAD Discussion Paper)*. In that Discussion Paper the ACCC raised question 39 as follows:

39 Should the 2015 DTCS FAD maintain an uplift on pricing to Tasmania to reflect the higher costs associated with the route? If so, does 40% remain appropriate?

Basslink Telecoms Pty Ltd (**Basslink**) provides the following response to question 39 in the DTCS FAD Discussion Paper.

Introduction

Basslink operates a domestic transmission capacity service (**DTCS**) between Melbourne and Hobart which consists of both a land component and a submarine component. Relevant characteristics of the network include the following:

- The submarine component is 300km long and represents approximately half of the distance which makes up the Basslink network.
- On the Victorian land component, which represents 160km of the 300km land component, Basslink uses third party providers to offer DTCS services.

The only other carrier that is reliant on an undersea cable to provide the DTCS is Telstra. However, unlike Telstra, Basslink does not own its network from end-to-end having instead to rely on third party service providers. Also Basslink does not provide any other telecommunication services which help subsidise its DTCS service between Tasmania and the mainland. Basslink's DTCS business is a completely stand-alone telecommunications business offering a single wholesale product. The use of third party providers in conjunction with the operation of an undersea cable means that Basslink's business model is unlike that of any other DTCS provider in Australia.

Background

The current DTCS final access determination which was made on 21 June 2012 and will expire on 31 December 2014 (**2012 DTCS FAD**) determines regulated prices for transmission services between the mainland and Tasmania by classifying those services as regional services¹ and using an additive term to apply a 40 per cent uplift to the prices of those services for a nominal 300km undersea cable component.²

The ACCC considered that it was appropriate to classify services from mainland Australia to Tasmania and within Tasmania as regional services because services on those routes were more likely to have cost features akin to regional services, such as lower utilisation.³ Further, the ACCC considered that it was appropriate to apply the 40 per cent uplift to the prices of services on those routes to reflect the higher cost of deployment, maintenance and repair of undersea cables.⁴ The uplift is based on a comparison of prices for undersea cable routes with mainland inter-capital routes and only applies to the 300km undersea component of the service between the mainland and Tasmania.⁵ The ACCC considered it appropriate to apply the uplift to a notional length of the undersea component of 300km for any service between the mainland and Tasmania to reflect the radial distance of the longest link currently available. This was intended to ensure that regulated prices captured the cost of the longest service provided between the mainland and Tasmania.⁶

Submission

Basslink submits that the 2015 DTCS final access determination (**2015 DTCS FAD**) should maintain an uplift on pricing for transmission services between the mainland and Tasmania to reflect the higher costs associated with those services. At this stage of the 2015 DTCS FAD process, without knowing the pricing for transmission services between the mainland and Tasmania which is likely to apply in the 2015 DTCS FAD, it is difficult for Basslink to be definitive on the percentage uplift which should apply. However, assuming that the ACCC

¹ ACCC, *Final Access Determination No. 1 of 2012 (DTCS)*, clause 1.5(g) of Schedule 1; ACCC, *Final Access Determination for the Domestic Transmission Capacity Service Explanatory Statement*, June 2012, p23.

² ACCC, *Final Access Determination No. 1 of 2012 (DTCS)*, clause 1.5(h) of Schedule 1; ACCC, *Final Access Determination for the Domestic Transmission Capacity Service Explanatory Statement*, June 2012, p23.

³ ACCC, *Final Access Determination for the Domestic Transmission Capacity Service Explanatory Statement*, June 2012, p23.

⁴ ACCC, *Draft Final Access Determination for the Domestic Transmission Capacity Service (DTCS) Explanatory Statement*, December 2011, p34; ACCC, *Final Access Determination for the Domestic Transmission Capacity Service Explanatory Statement*, June 2012, p23.

⁵ ACCC, *Final Access Determination for the Domestic Transmission Capacity Service Explanatory Statement*, June 2012, p23.

⁶ ACCC, *Draft Final Access Determination for the Domestic Transmission Capacity Service (DTCS) Explanatory Statement*, December 2011, p34; ACCC, *Final Access Determination for the Domestic Transmission Capacity Service Explanatory Statement*, June 2012, p24.

adopts a similar approach to pricing in the 2015 DTCS FAD as applies in the 2012 DTCS FAD, Basslink submits that 40 per cent is the minimum uplift which should be applied to pricing for transmission services between the mainland and Tasmania.

Basslink considers that it is appropriate that an adjustment be made to the price for transmission services between the mainland and Tasmania due to the substantial costs associated with deploying and maintaining the submarine cable required to deliver those services and Basslink's unique cost structure. There is no reason why the current uplift of 40 per cent on prices to those services implemented by the ACCC in the 2012 DTCS FAD should be reduced for the purposes of the 2015 DTCS FAD. Rather, Basslink submits that a 40 per cent uplift on prices is the minimum uplift which should be applied to account for the higher submarine cable costs and the unique attributes of Basslink's business model.

This submission is made on the basis that the ACCC will adopt a similar approach to pricing in the 2015 DTCS FAD as to that which currently applies in the 2012 DTCS FAD. If the ACCC proposes to adopt a different approach for transmission services between the mainland and Tasmania from that in the 2012 DTCS FAD, Basslink will seek to make a further submission, at the appropriate stage of the 2015 DTCS FAD process, on the appropriate uplift factor which should apply to that pricing.

Costs of deploying and maintaining submarine cable

The difference in the costs associated with deploying and maintaining submarine cables and those associated with terrestrial cables results from:

- the additional cost in manufacturing cables capable of withstanding the different environmental factors in a marine location;⁷ and
- the high costs associated with marine deployment and maintenance of the cable, particularly the significant costs associated with hiring cable laying and cable maintenance ships.⁸

Unique characteristics of mainland to Tasmania transmission routes

Basslink's Melbourne to Hobart transmission route differs from all other inter-capital cities routes in that it is a "thin" demand route that consists of undersea components and has different cost structures to mainland routes. The following factors distinguish the Melbourne to Hobart transmission route from other inter-capital routes:

⁷ Telstra also notes this in its submission to the ACCC during the 2012 DTCS FAD process entitled *Telstra's Response to the Commission's Discussion Paper - Price Terms and Conditions*, 29 August 2011, p42.

⁸ Telstra also notes this in its submission to the ACCC during the 2012 DTCS FAD process entitled *Telstra's Response to the Commission's Discussion Paper - Price Terms and Conditions*, 29 August 2011, p42.

- Tasmanian routes utilise an undersea cable with cost-structures that are greatly different to terrestrial routes - including additional capex and opex requirements.

- Tasmanian transmission routes are very "thin" in demand and capacity terms. The addressable market size accessible to Basslink to meet business case objectives is extremely limited, due to a wholesale focus and the nature of the infrastructure it owns. Tasmanian transmission routes are "thin" in capacity terms due to:
 - the fledgling IT industry in Tasmania;

 - the relative absence of Top 500 corporate head offices;

 - the absence of nationally significant data centre operators;

 - Tasmania has a small population with a higher than average unemployment and retiree base;

 - Tasmania has a dispersed population;

 - there is limited DSLAM penetration;

 - there is limited on-island backhaul competition (particularly Launceston).

- Basslink does not have the ability to provide total spend discounts, subsidies or rebates across other product sets, such as mobile or voice, that can subsidise any below cost pricing for the DTCS in the FAD. Further, Basslink must be able to operate as a commercial enterprise and still generate an acceptable return to shareholders while meeting its original business case objectives.⁹

- Basslink does not own all of the end-to-end components that make up the Melbourne to Hobart transmission route. Basslink only owns and operates the undersea component across Bass Strait comprising roughly one-third of the entire Melbourne to Hobart route. Basslink has to rely on third party service providers for the other segments of the route.

- There are no significant break-out points on the Melbourne to Hobart transmission route which would present an opportunity for additional revenue, such as there are on other mainland routes. The assets cannot be repositioned to take advantage of emerging dynamic demand. It is not valid to compare alternative routes that are wholly terrestrial or even of the same length.

⁹ Subsection 152BCA(1)(b) of the *Competition and Consumer Act 2010*.

As noted in the introduction to this submission, the only other carrier that is reliant on an undersea cable to provide the DTCS is Telstra Corporation Limited (**Telstra**). In their respective submissions in response to the ACCC's price terms in the draft 2012 DTCS FAD both Basslink and Telstra asserted that a 40 per cent uplift on pricing for transmission services between the mainland and Tasmania was insufficient to enable them to earn a normal commercial return on their investment. Telstra asserted that the 40 per cent uplift was aligned with the cost of deploying a non-geographically diverse submarine cable, such as that supplied by Basslink, however, it did not capture the higher costs associated with supplying undersea cable services using a geographically diverse submarine cable path.¹⁰ Basslink submitted that the 40 per cent uplift failed to take into account Basslink's unique cost structure.¹¹ Accordingly, in the last DTCS FAD process both Basslink and Telstra submitted that a higher uplift than 40 per cent should be applied to pricing for their respective transmission services between the mainland and Tasmania.

Basslink continues to maintain that while it uses a non-geographically diverse submarine cable, it is exposed to different costs in providing the DTCS than Telstra.

Unlike Telstra, Basslink does not own its network from end-to-end. Rather, as noted above, Basslink has to rely on third party service providers. Given that Telstra owns its network outright, the added expense associated with engaging third party providers is not an expense that is relevant to Telstra. Unlike Basslink, Telstra does not have to account for the commercial return of third party providers.

Further, as noted above, unlike Telstra Basslink does not provide any other telecommunication services which could help subsidise its DTCS service between Tasmania and the mainland. Basslink's DTCS business is a completely stand-alone telecommunications business offering a single wholesale product. In contrast, Telstra offers numerous telecommunication services that can subsidise the operation of its undersea cable, if necessary.

Necessary considerations when making a final access determination

Section 152BCA(1) of the *Competition and Consumer Act 2010 (CCA)* requires the ACCC to take into account a range of matters when making the 2015 DTCS FAD. Some of these matters are addressed below, noting the significance of ensuring an appropriate uplift factor for Basslink and affected end-users.

Whether the determination will promote the Long Term Interest of End Users

Section 152BCA(1)(a) requires the ACCC to take into account whether the 2015 DTCS FAD will promote the long-term interests of end-users of carriage services or of services supplied by means of carriage services (**LTIE**). Section 152AB(1) of the CCA notes that in determining

¹⁰ Telstra, *Response to the Commission's price terms in the draft final access determination for the Domestic Transmission Capacity Service*, 9 March 2012, p21.

¹¹ Basslink, *Confidential submission concerning the draft final access determination for the Domestic Transmission Capacity Service (DTCS)*, 2 February 2012.

whether a particular thing promotes the LTIE regard must be had to the objective of promoting competition in markets for carriage services and for services supplied by means of carriage services.

It is likely that a failure to achieve a normal commercial return would ultimately force Basslink to cease providing the DTCS. In turn, this would be likely to result in Telstra achieving monopoly provider status between Tasmania and the mainland. Furthermore, the absence of genuine competition in the DTCS space would be likely to increase prices on relevant downstream markets which include data services, mobile services, and general telecommunication services delivered over transmission networks.

Promotion of the LTIE also requires that regard be had to the economically efficient investment in the infrastructure by which telecommunication services are provided. Accordingly, it is important that the prices in the 2015 DTCS FAD encourage economically efficient investment and enable an efficient service provider to obtain a normal commercial return on its investment. An uplift which is less than 40 per cent would discourage Basslink to undertake further investment. The need to increase capacity is both an inevitable and necessary factor for any telecommunications business given the continuing growth in the scope of telecommunication services. For instance, the most immediate capacity requirement will arise with the introduction of the NBN. As a result, it is imperative that Basslink be able to increase its capacity without suffering a decrease in its rate of return.

Basslink's legitimate business interests

Under subsection 152BCA(1)(b) of the CCA, in making the 2015 DTCS FAD the ACCC is required to take into account the legitimate business interests of a carrier or carriage service provider who supplies, or is capable of supplying, the declared service, and the carrier's or provider's investment in facilities used to supply the declared service.

An uplift on prices which is less than 40 per cent would prevent Basslink from earning a normal commercial return on its investment, having regard to the relevant risks of the investment, and therefore be contrary to Basslink's legitimate business interests.

Direct costs of providing access to a declared service

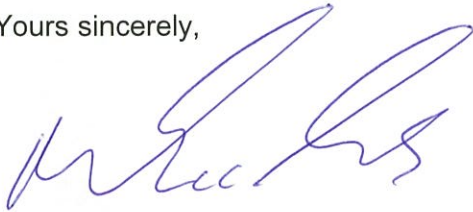
Subsection 152BCA(1)(d) of the CCA requires the ACCC, in making the 2015 DTCS FAD, to take into account the direct costs of providing access to a declared service, encompassing those costs that are necessarily incurred in providing access. In this context the phrase 'direct costs' is interpreted to mean that an access price should cover the direct incremental costs incurred in providing access, including contribution for indirect costs. This would include both Basslink's costs in relation to third party service providers as well as the cost of repairing and maintaining the undersea cable. As such, in determining the uplift to apply to prices for transmission services between the mainland and Tasmania the ACCC should take into account Basslink's costs in relation to third party service providers and the costs of repairing and maintaining the undersea cable.

Conclusion

Accordingly, Basslink submits that assuming the ACCC adopts a similar approach to pricing for transmission services between the mainland and Tasmania in the 2015 DTCS FAD as applies in the 2012 DTCS FAD, 40 per cent is the minimum uplift which should be applied to pricing for transmission services between the mainland and Tasmania. As noted above, if the ACCC proposes to adopt a different approach for transmission services between the mainland and Tasmania from that in the 2012 DTCS FAD, Basslink will seek to make a further submission, at the appropriate stage of the 2015 DTCS FAD process, on the appropriate uplift factor which should apply to that pricing.

If you have any questions regarding the above submission, please do not hesitate to contact me.

Yours sincerely,



Malcolm Eccles
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Basslink Telecoms Pty Ltd