

Report of Andrew Bailey

16 June 2017

“Build it and they will come?” The Role of Capital Efficiency in Telecommunications Competition

This Report

I have been instructed by Gilbert + Tobin, on behalf of Telstra Corporation Limited (Telstra), to provide a report setting out my expert opinion with respect to the Australian Competition and Consumer Commission’s (ACCC) inquiry into whether to declare domestic mobile roaming, in particular:

1. the draft decision of the ACCC dated May 2017;
2. the various submissions and supporting evidence provided by Vodafone Hutchison Australia Pty Ltd (VHA) and Singtel Optus Pty Ltd (Optus) in respect of the inquiry.

A copy of my instructions is set out at Annexure A. I have read the Harmonised Expert Witness Code of Conduct (Annexure A to Federal Court of Australia Practice Note GPN-EXPT) and agree to be bound by it.

My report has been written from the perspective of a senior executive who has worked in a mobile network operator but who also understands the broader telecommunications sector. I have had first-hand experience with many of the issues raised in the Inquiry. I joined Optus just a week before it entered the fixed line and mobile markets. My executive roles there commenced as head of the regulatory division and subsequently I headed corporate strategy, the wholesale business unit and finally the mass market business unit (consumer and small business). I was also, for a short period, Acting Chief Operating Officer. Subsequently I was Managing Director of Crown Castle Australia, a shared infrastructure company (and now part of Broadcast Australia). Overall, my executive roles at Optus and elsewhere spanned over 10 years. I have also been a board member – both ex officio as a CEO and as an independent member – of several telecommunications companies. I have thus worked as both a competitor of Telstra and in partnership with them. I have wrestled with the capital productivity issues that feature prominently in my report from several perspectives – regulatory as well as commercial, as a business unit head as well as sitting in the corporate centre. I have been on the receiving end of decisions about how scarce capital is to be spent as well as having been involved in making such decisions.

This report has three parts. The first, in Section 1, argues that infrastructure-based competition between telecommunications MNOs can helpfully be viewed from the perspective of companies vying to maximize their capital efficiency. Sections 2 - 6 consider whether, from this perspective, VHA has actually established the necessary minimum arguments for its case. Section 7 then considers the impact roaming would have on the network investment incentives faced by the MNOs.

1. The Primacy of Capital Efficiency in Telecommunications

Telecommunications is a capital intensive business. That means it is a business where product costs are characterised by high fixed capital costs but low marginal costs. To generate \$1m in revenue, Telstra deploys \$0.81m in capital. This is remarkably high compared to many other businesses. Service companies – such as consulting firms - are at the other extreme, using very little capital alongside a highly skilled workforce. Companies that make things – for example CSR who manufacture building materials – are in the middle. To generate \$1m in revenue CSR uses only \$0.38m in capital.

With so much capital needed network operators worry, first and foremost, about using their stock of capital efficiently. Capital efficiency means maximising the revenue for every dollar of capital used. Expressed in operational terms capital efficiency requires a network with high capacity utilization (thus generating economies of scale) and a user base paying sensible prices for its network services. Using capital in an efficient manner is the only way that MNO's can generate the profits needed to compensate investors for the risks involved in such a fast moving technology intensive business.

Providing reliable network services at a reasonable cost and then attracting sufficient customers is thus the unremitting focus of most telco executives. A casual joke among telco executives is that, for the billions on the balance sheet, the company has acquired just one product – “the network”. An MNO can get itself into financial difficulties in lots of ways but low capital efficiency is the most insidious and difficult to correct. When it occurs, it is usually the result of one or both of two factors:

1. the network has been poorly designed or dimensioned; or
2. there are insufficient customers using the network or their usage patterns don't suit its capabilities.

Mobile networks, because they have relatively short technology cycles and relatively high swap out costs, presents these challenges in a particularly acute way.

The centrality of capital efficiency in driving MNO's competitive behaviour makes it a useful lens through which to consider the issues in this regulatory determination. In particular it helps explain why the MNO's have built the networks they have built and attracted the types of customers that they have.

2. How mobile operators build an infrastructure - based business

A new entrant into a newly de-regulated mobiles market, such as Australia had in the mid-1990s, faces some critical decisions about network development – what technology to choose, where to build the network and how much capacity to install. Without the reassurance of steady positive cashflows “wrong” network build decisions can seem like a crisis. Disappointed shareholders take drastic action where a new venture fails to quickly build revenues and become capable of funding its own capital expenditures.

To minimise the acute financing costs in the early years of its operation a new entrant usually starts with a smaller core network in metro areas, thus maximising potential revenue per dollar of network spend. Further network expansion proceeds as customer preferences are better understood. Over a period of years this turns into an iterative process of “fitting” a network to a customer base. The three operational levers that are most influential are:

1. capacity expansion in the existing network to meet customer expectations on key performance measures such as traffic congestion, dropout rates and call quality;
2. geographic network expansion to capture new customers and serve existing customers better; and
3. targeted marketing to build usage in new areas.

Even though there are areas where all MNOs have a network presence, there should not be an expectation that MNOs converge to having identical networks. There will be some areas where later entrants just don't want to build. There will be some areas where an MNO's distribution channels are stronger or weaker compared with its competitors. There is no reason to expect that the customer base of Optus or VHA will be identical to the customers who use Telstra. Differences in per-customer profitability and different customer usage patterns will exert divergent influences on network configurations. Even if there is, say, 90% congruence in the geographic footprint of the three MNO networks that remaining 10% can significantly influence capital efficiency.

Network development issues are not abstract matters being decided by strategists or network planners, in isolation from the business. As often as not they mirror the pressing daily realities of those executives who carry revenue generating responsibilities. Such executives strive to meet revenue targets from which are deducted internal imputed charges (or, equivalently, an allocated capital charge) for the network usage of their products or customers. Executives wanting specific network enhancements to land

particular deals may face further capital charges related to these projects. Such internal charging mechanisms can easily tip a deal from profitability to loss-making. These deals often impact the achievement of performance targets, so the decisions are hard fought. Over time they help shape the network.

This process of fitting together a network and a customer base means that, over time, each carrier ends up with the network they want. Over even longer time frames the process is reinforced by evolving mobile technology. New generations of technology offer a superior set of customer benefits to the one they replace, giving the operator an opportunity to fix (or at least dilute) aspects of past network decisions that, for whatever reason, have been less than satisfactory. Over successive generations of mobile technology, telcos should arrive at a good fit between their network and a set of customers who like the price – service package that is being offered. And inevitably, over an extended time period, the initial advantages of the incumbent get diluted by competition.

Different network configurations may persist indefinitely. Mobile network operators are not locked into a particular network – or market strategy. Both the deployment of annual increments of capital spending and the periodic emergence of new network technologies to which I have referred in the paragraph above allow an operator to give effect to new strategic priorities. I see evidence of this in Optus' increased capital expenditure, including on regional and rural coverage, in recent years. But there is also some inertia provided by the operator's customer base. Naturally enough, operators tend to stick with what has worked to date. Mostly these types of changes are a function of time. Given enough time an operator can choose to significantly alter their market strategy and the network configuration that gives expression to it.

Network development is a more subtle process than simply expanding a network's geographic footprint. The appearance of smartphones a decade ago has transformed network usage. The diverse capabilities of these phones has driven spectacular growth in data traffic.¹ What were once "nice to have" network attributes such as in-building coverage and network capacity have become much more important aspects of network quality, as experienced by users.² (Needless to say, providing additional capacity or high quality in-building coverage with distributed antennae systems involves yet more capital expense.) Such dramatic usage changes makes it likely that customers discriminate between MNOs on coverage and capacity, even in areas where all three networks operate side by side.

All this summarises to make four fundamental points:

1. the network of an MNO is the cumulative expression of the customer growth opportunities it has chosen to pursue. Mobile networks do not have a pre-ordained configuration so it is not as simple as "build it and they will come". More accurately it should be expressed as "build it, market it, and they will come and try it";
2. MNOs have ample opportunities, through successive network development decisions and successive generations of cellular technology to optimise the fit between the network and their customer base. Telstra and Optus have both provided evidence that what works for one network won't necessarily work for another.³ In a very real sense, each MNO ends up with the network that they think makes sense for the customer base they have attracted;
3. Coverage is not a one dimensional issue of geographic footprint. It seems intuitively obvious that day-to-day usability is what matters to customers and this requires a variety of network attributes; and

¹ Telstra Response to the ACCC's Discussion Paper on the declaration of a wholesale domestic mobile roaming service Public version, p. 19

² Optus, for example, cite evidence about growing customer demand for data speed. See Analysys Mason, p.14

³ For example, see Telstra pp. 10 - 14

4. It is important not to assume that the differences between networks are somehow fixed. Networks change with technologies and with customer behaviours and preferences. Even if the geographic footprint is stable each operator is continually optimising network performance as well as planning how and when new technologies should be introduced.

These points bear directly on VHA's case. It claims that Telstra's various sources of advantage have prevented VHA having a network that allows it to compete effectively. But because VHA's network is the end result of some decades of its own decision making, its case must go deeper than simply asserting that Telstra has 'unfair advantages'.

VHA does indeed make its argument more specific. It puts forward several propositions that spell out exactly how Telstra is able to compete unfairly. It claims:

- mobiles competition in Australia is "inherently regional"
- customers are greatly influenced by coverage in regional and rural areas; and
- Telstra uses the demand for regional and rural coverage among metro customers to exploit its "monopoly position" in regional and rural areas

I will now consider these arguments.

3. Is mobiles competition regional?

In its draft decision, the ACCC concludes that there is a national market for retail mobile services⁴. In contrast, VHA claim that mobile competition is "inherently regional"⁵. Testimony from VHA's expert Dr Ritzmann explores this idea extensively. He asserts that "Telstra holds a monopoly over an astounding 60% of the mobile coverage area" and argues that much of this area is a "natural monopoly. In such areas, no other mobile operator can profitably invest to duplicate Telstra's infrastructure and effectively compete."⁶ I understand this argument to be a supply-side argument – an argument that competition can be characterised just by MNO profitability in specific geographic areas covered by the network.

I have a number of difficulties with VHA's characterisation of mobiles competition. Let's look first of all at the demand side of the mobiles market. Saying that competition is regional seems inconsistent with the essential value proposition of a mobile service. A mobile service offers customers not just connectivity in and around the places they live but also the option of connectivity in other areas. From a consumer's perspective, that optionality is a key reason for purchasing (and paying a premium for) connectivity in the form of a mobile service.

Telstra's marketing of its mobile service clearly plays to this customer perspective. Undoubtedly it uses the 'superior coverage' theme as marketing shorthand for a second message – Telstra has the best network, including in areas of overlapping coverage with the other MNO's. But the fact that it uses coverage to carry this important second message reinforces the point that customers pay attention to the quality of the coverage option they are buying – national, not regional coverage.

This seems to point to another significant inconsistency in the VHA case. Its proposed "spillover effect" envisages exactly this customer buying behaviour - metro customers being influenced by the option of remote area coverage. How then can competition be "inherently regional" when, at least on the demand side of the market, customers don't think in this way?

Turning to the supply side of the market, 'regionality' sits uneasily with how mobile network costs are allocated. Without doubt there are important network costs (base stations, backhaul links and so on) that can be attributed to a specific geography. I do not want to deny this reality. But many substantial mobile

⁴ ACCC draft decision, May 2017, section 4

⁵ Vodafone pp. 9

⁶ Vodafone p. 8

network costs are shared across the whole network – spectrum costs, marketing and branding, billing and customer service, some core network elements, handset deals, distribution arrangements and more. The whole idea of a network is that multiple users of a shared infrastructure all share the task of covering its fixed costs and generating a profit. Obviously individual cell sites or groups of cell sites can have lower or higher usage but to extrapolate from this to saying competition is regional seems to me an exaggeration.

Looking at demand and supply side arguments together yields yet another difficulty of the regionality concept. Let's say that, knowing its metro customers value the coverage option, Telstra (or any other MNO) advertises its coverage on, for example, the Birdsville Track. In marketing such a remote location it would be promoting both its geographic coverage and, using a kind of marketing shorthand, the quality of its network in general. This marketing may well attract additional customers in Sydney and Melbourne (and even better persuade them to pay a higher price). In a meaningful sense then, Birdsville Track coverage is profitable, irrespective of usage occurring in those specific cell sites. To me this looks like whole-of-network competition, not regional competition. The ACCC, in its draft decision, arrives at this same conclusion.⁷

4. Coverage and the “Spillover Effect”

VHA seems to focus its concerns on a quite specific alleged competition defect:

- it is focused on “urban users who value coverage greatly and who are prepared to pay higher prices to obtain it.”⁸ This group is being denied reasonable competitive choice because of regional areas where Telstra is the only MNO; and
- it is not focused on urban users who do not value coverage⁹ nor rural users.

These propositions are, in my opinion, difficult to reconcile with what I consider to be the observable behaviour of metro mobile users. In my experience, there are a range of factors that influence consumers' choice of service provider. As the ACCC observes, price is a primary factor on which MNOs compete.¹⁰ Optus has also noted that data speed is a growing customer priority. This sits uneasily with VHA's assertion that a large number of metro consumers are singularly influenced by regional and remote coverage. VHA support their contention by quoting Telstra evidence that “71% of customers churning to Telstra do so for better coverage”¹¹ To me, this evidence is ambiguous. What coverage are we talking about? How do we know that the survey respondents were referring to regional and rural coverage? In the absence of specific information about the framing of this question in the survey instrument, surely a more plausible interpretation is that respondents were not referring to regional coverage but rather the coverage quality they experience on a daily basis – coverage in tunnels, high rise buildings, outer suburban areas and on major roads. It is also possible that they were using “coverage” as shorthand for metro network quality - the frequency of drop outs, ability to handle peak traffic loads and so on.

Optus offers a particularly helpful discussion of this point. They note that VHA has significantly fewer base stations in metro areas, compared to Telstra.¹² Further, when VHA encountered network quality problems in 2010 and 2011, there was a shift in market share to Telstra that was unrelated to any changes in regional and remote area coverage. The Optus expert concludes that Telstra's market share and the price premium it commands, relative to VHA, reflects the fact that it has “superior network quality and depth of coverage”.¹³ Lastly they note that coverage is declining in importance as an influence on customers relative to data speed.¹⁴

⁷ ACCC draft decision, May 2017, section 4

⁸ Feasey p. 4

⁹ Richard Feasey Response to Professor George Yarrow's submissions to the ACCC in the Domestic Mobile Roaming Enquiry 2016 p. 3

¹⁰ ACCC draft decision, May 2017, section 5.2.3

¹¹ Vodafone p.4

¹² Analysys Mason p.12

¹³ Analysys Mason, p.13

¹⁴ Analysys Mason, p.13

But let us put these doubts aside and follow VHA's development of its spillover idea. The "coverage" they think fuels the spillover effect is not the patchy coverage users might encounter in outer metro areas, interstate highways or even regional centres. VHA's expert is quite specific - "small pockets of monopoly" are not a problem.¹⁵ I think this means that their concern is with the large contiguous areas where Telstra is the sole supplier. This makes VHA's argument an odd one indeed. Metro customers, we are told, are in thrall to Telstra's service because it has a presence in the places they rarely visit - perhaps just a few days each year when "going bush" or on their annual holidays. Why would coverage for a few days of holidays be more important than coverage for the remaining 362 days of the year? Perhaps there is the odd user who thinks this but it is difficult to imagine that such behaviour characterises a large customer segment. Optus arrives at a similar conclusion.¹⁶

VHA is making the case here that spillovers affect a large number of consumers. But this implies another set of oddities about the customer behaviour being proposed. Specifically, if as VHA alleges, there is a large customer segment who want a service offering badly but are unhappy with the premium they would have to pay Telstra for that service, workarounds and second best solutions inevitably emerge. I would argue that a workaround to the problem of 'denied coverage choice' is already available to these users.

Given that remote area travel is unlikely to be a "last minute" decision why would these consumers simply not avail themselves of Telstra coverage by buying a Telstra SIM for the few days they are travelling? Doing this, they could access Telstra's remote area network for the few times it is needed, but still use VHA most of the time. They would not have to choose between Telstra's superior coverage and VHA's more economical pricing. No doubt some will think such a scenario is unrealistic because of its inconvenience. (I note that it is a commonplace behaviour during international travel.) My response would be that this objection does not deny the relevance of the scenario. Rather it points to the small size of the customer group that conforms to VHA's description. Were there the large, highly motivated group of consumers that VHA alleges, such SIM switching behaviour would be recognised as commonplace. As far as I am aware, it is not.

For these reasons, I agree with the ACCC's conclusions in its draft decision that:

- "while network coverage does certainly appear to be a factor in choosing a service provider for many who live in metropolitan areas, there is evidence to suggest that there are other factors which are more important to these consumers."
- "competition over network quality, and the importance of network reliability, depth of coverage, and service quality to consumers, is a factor which has contributed to Telstra's position in the national mobile market. There is a perception held by many consumers that Telstra provides high quality mobile services, will provide a more reliable and better quality service. The investment that Telstra has made in its network in the past has contributed to this consumer perception."
- MNOs do not need coverage in regional areas with 0.8% of the population to compete in the metro market.

5. Are VHA's arguments consistent with its own past competitive behaviour?

I argued earlier that when a new entrant (in particular) is developing its business it is making what might be described as "conjoined" decisions – network capabilities and targeting particular types of customers. Thus, if one looks at the characteristics of VHA's customers, it may indirectly tell us about the network that VHA really wants. What does the past record show about the types of customers that VHA has targeted?

VHA has spent decades with less geographic coverage than the two other MNOs¹⁷. It has found large numbers of customers happy with that type of network service. Telstra¹⁸ has provided evidence that these

¹⁵ Feasey, p. 7

¹⁶ Analysys Mason, p.14

¹⁷ Telstra p. 10

VHA customers spend less than those using Telstra or Optus. These are not the customers likely to pay the higher prices that a geographically larger network would require. So, there seems to be a disconnect between the network it has developed and the network service it now says many customers want. Furthermore, when network assets relevant to a bigger network have come up for sale at attractive prices – such as the dark fibre network of Pipe Networks in 2009-10, and the 700 MHz spectrum auction prior to 2017 – VHA chose not to purchase them.

6. Competition defects or just competition outcomes?

VHA's case is centred on an alleged "spillover" of Telstra's regional "monopoly" coverage to unfairly compete in metro areas. The conclusion I draw from the above discussion is that VHA has not conclusively demonstrated that its case is consistent with the competitive realities of the Australian market.

It has had the opportunity to develop a network that best gives it competitive traction. The network it has chosen targets lower spending mobile users. Now it appears to want to change its long-standing value proposition to its customers. Specifically, it seems to want to offer more premium network features like enhanced coverage. Surely the logical response is that it is free to spend its own capital to provide these additional features.

There are, of course, other value propositions that VHA could pursue that would not require extensive regional coverage. Aiming to be best-in-class in terms of network speed, metro capacity or metro coverage are all strategies that would build on the network presence that it has and be of considerable appeal to its metro customer base. There is no inevitable market logic about expanding geographic coverage.

Neither the customer side nor the supplier side of the mobiles market offers strong evidence that competition is regional. If this is really how customers think, it would seem to undermine VHA's claimed spillover effect. But there is no evidence – or market behaviour – I am aware of that supports the notion that a large group of metro customers feel they are denied reasonable choice of coverage.

Telstra has gone to great lengths to make its regional and rural coverage commercially attractive to metro customers. VHA can hardly cry foul now if Telstra has found a way to convert the liability of broad coverage expectations into a commercial virtue. The observable differences between the three mobile networks is, in my view, simply the outcome of competition and is not an expression of unfair competition on the part of Telstra.

7. Impact of Roaming Declaration on Network Investment Incentives

VHA advocates roaming onto the Telstra and Optus networks as an appropriate remedy for the alleged competitive defect in the mobiles market. Given the importance of capital efficiency in shaping mobiles competition, I have included some comments on the merits of roaming as a remedy to the problems VHA perceives.

The expert witnesses of Telstra (Professor Yarrow) and VHA (Mr Feasey) both consider the possible impacts on retail prices in the event of a roaming declaration. Mr Feasey says this:

It is self-evidently in the LTIE if the same level of coverage could be supplied at a lower price than the price charged by Telstra today. Indeed, I think this is the central question which the ACCC should be asking itself in this enquiry.¹⁹

¹⁸ Telstra p. 34

¹⁹ Feasey p.7

I think there is room to take a different view of what is in the long term interests of consumers. The ACCC is obliged, of course, to look more widely than immediate price impacts – it also needs to consider “encouraging efficient use of, and investment in, infrastructure”.

A declaration of domestic roaming by the ACCC would have a highly asymmetrical effect across the three MNOs. Besides strengthening VHA’s competitiveness among metro customers a declaration would significantly impact investment incentives. Would this be a good thing?

Telstra and Optus will face diminished profitability in regional coverage areas. Regional customers leaving them for VHA would mean the loss of a (larger) retail margin for a slim wholesale margin. (The rationale of wholesale business in metro areas – that it can bring in large additional sales of network minutes – does not apply because of the limited regional population.²⁰) In metro areas, a bigger adverse customer response may be anticipated because VHA would now be able to offer best-in-market coverage.

Whether this is in the long term interests of consumers depends on one’s view of what has happened to regional investment incentives. Telstra and Optus would both have a diminished ability to exploit their investments in regional coverage among regional and metro customers. These weaker returns would permanently reduce the capital efficiency of new regional capital investments. In such circumstances it is hard to expect any outcome other than a scaling back of regional coverage investments by Telstra and Optus. Analysys Mason, an expert witness instructed by Optus, arrives at this same conclusion.²¹

A roaming declaration would also complicate the risk assessment associated with regional network investments. Because it would face a simple per-minute roaming charge, VHA would not have to worry about aligning its marketing to regional coverage capacity. Telstra and Optus, on the other hand, would still have to cover their fixed network costs but now with a diminished ability to match network capacity to customer usage. It is easy to imagine all MNOs starting to second guess investment decisions that may be impacted by regulatory decisions. I thus find it difficult to share Mr Feasey’s confidence that such a state of affairs is “self-evidently” in the long term interest of consumers.

The regulatory remedy sought by VHA would have a highly asymmetrical effect across the three MNOs. These effects would start with the immediate metro customer responses to VHA’s strengthened service offering. It would directly impact the network investment incentives faced by Telstra and Optus and most likely have a chilling effect on future regional network investments.

At the level of telecommunications regulation I expect the impression will form that VHA, who to date has spent the least of the three MNOs on regional and rural coverage, is being allowed to piggyback on the risks taken by its competitors. It is thus hard not to see a roaming declaration as other than a major departure from the policy of infrastructure-based competition that seems to have served the Australian market so well.

²⁰ Optus make a similar argument: see Analysys Mason, p.15

²¹ Analysys Mason, p.15 - 16

ANNEXURE A

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15 June 2017

By email

Andrew Bailey

Email: ac.bailey@outlook.com

Dear Mr Bailey

Response to the Australian Competition and Consumer Commission regarding potential declaration of a wholesale domestic roaming service on behalf of Telstra Corporation Limited

1 Background

- 1.1 We act for Telstra Corporation Limited (**Telstra**).
- 1.2 On 5 September 2016, the Australian Competition and Consumer Commission (**ACCC**) commenced an inquiry into whether to declare a wholesale domestic mobile roaming service (**ACCC Inquiry**). As part of that inquiry, on 26 October 2016, the ACCC released a Discussion Paper seeking views on a range of issues it considers relevant to whether such a declaration should be made. Set out in the ACCC's Discussion Paper is a description of the legal framework and the assessment approach.
- 1.3 Submissions on the Discussion Paper were provided by a number of mobile network operators including Telstra, Singtel Optus Pty Ltd (**Optus**) and Vodafone Hutchison Australia Pty Ltd (**VHA**).
- 1.4 On 5 May 2017, the ACCC published its Draft Decision not to declare wholesale domestic roaming (**Draft Decision**).
- 1.5 In accordance with section 152AL under Part XIC of the *Competition and Consumer Act 2010* (Cth) (**CCA**), the ACCC may only declare a telecommunications services if (among other things) it is satisfied that doing so will be in the long-term interests of end-users (**LTIE**). Under section 152AB of the CCA, in deciding whether the declaration will promote the LTIE, the ACCC must consider whether declaration is likely to result in the achievement of the following three objectives:
 - (a) the objective of promoting competition in markets for telecommunications services;
 - (b) the objective of achieving any-to-any connectivity in markets for telecommunications services; and
 - (c) the objective of encouraging the economically efficient use of, and investment in, telecommunications infrastructure.
- 1.6 In determining the likelihood to which a particular thing is likely to result in the achievement of promoting competition in markets for telecommunication services, regard must be had to the

extent to which the thing will remove obstacles to ensure users of telecommunications services gain access to those telecommunications services.¹

- 1.7 In determining the likelihood to which a particular thing is likely to result in the achievement of encouraging the economically efficient use of, and investment in, telecommunications infrastructure, regard must be had to the following matters:²
- (a) whether it is, or is likely to become, technically feasible for the services to be supplied and charged for, having regard to:
 - (i) the technology that is in use, available or likely to become available; and
 - (ii) whether the costs that would be involved in supplying, and charging for, the services area reasonable or likely to become reasonable; and
 - (iii) the effects, or likely effects, that supplying, and charging for, the services would have on the operation or performance of telecommunications networks;
 - (b) the legitimate commercial interests of the supplier or supplier of the services, including the ability of the supplier or suppliers of services to exploit economics of scale and scope;
 - (c) the incentives for investment in:
 - (i) the infrastructure by which the services are supplied; and
 - (ii) any other infrastructure by which the services are, or are likely to be become, capable of being supplied.
- 1.8 In determining incentives for investment, regard must be had to the risks of making the investment³.
- 1.9 We have been instructed to engage you, on behalf of Telstra, to prepare a report based on your expert opinion, for use by Telstra in relation to the ACCC Inquiry. Telstra may seek to rely upon your report in any subsequent review of the ACCC's final decision. If that occurs, we will contact you.
- 1.10 By this letter, we set out our written instructions to you.

2 Scope of work

- 2.1 You are retained to provide an expert report which comments on:
- (a) the ACCC's Draft Decision;

¹ See section 152AB (4) of the CCA, noting that this subsection does not limit the matters to which regard may be had (see section 152AB(5) of the CCA).

² See section 152AB(6) of the CCA, noting that this subsection does not limit the matters to which regard may be had (see section 152AB(7) of the CCA)

³ See section 152AB(7A), noting that this subsection does not limit the matters to which regard may be had (see section 152AB(7B) of the CCA)

- (b) the submissions and supporting material from VHA; and
- (c) the submissions and supporting material from Optus.

3 Guidelines for preparing your report

3.1 While you have not been engaged in respect of any legal proceedings, Telstra is seeking a robust and rigorous independent expert report. We request that you prepare your report in accordance with Federal Court of Australia *Harmonised Expert Witness Code of Conduct*. A copy of the Code of Conduct is enclosed at **Attachment A**.

3.2 In particular, in preparing your report, we ask that you please:

- (a) identify your relevant area of expertise and provide a curriculum vitae setting out the details of that expertise;
- (b) only address matters that are within your expertise;
- (c) where you have used factual or data inputs please identify those inputs and the sources;
- (d) if you make assumptions, please identify them as such and confirm that they are in your opinion reasonable assumptions to make;
- (e) if you undertake empirical work, please identify and explain the methods used by you in a manner that is accessible to a person not expert in your field;
- (f) confirm that you have made all the inquiries that you believe are desirable and appropriate and that no matters of significance that you regard as relevant have, to your knowledge, been withheld from your report; and
- (g) do not provide legal advocacy or argument and please do not use an argumentative tone.

4 Confidentiality and legal professional privilege

4.1 Presently, your report and all correspondence between us (excluding this letter) is subject to legal professional privilege. In addition, the information we have provided to you is commercially sensitive and confidential. For these reasons, we request you do not disclose or discuss your report, our correspondence or any information we provide to you with any third parties.

Yours faithfully
Gilbert + Tobin



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Attachment A

Harmonised Expert Witness Code of Conduct **(Annexure A to Federal Court of Australia Practice Note GPN-EXPT)**

APPLICATION OF CODE

1. This Code of Conduct applies to any expert witness engaged or appointed:
 - (a) to provide an expert's report for use as evidence in proceedings or proposed proceedings; or
 - (b) to give opinion evidence in proceedings or proposed proceedings.

GENERAL DUTIES TO THE COURT

2. An expert witness is not an advocate for a party and has a paramount duty, overriding any duty to the party to the proceedings or other person retaining the expert witness, to assist the Court impartially on matters relevant to the area of expertise of the witness.

CONTENT OF REPORT

3. Every report prepared by an expert witness for use in Court shall clearly state the opinion or opinions of the expert and shall state, specify or provide:
 - (a) the name and address of the expert;
 - (b) an acknowledgment that the expert has read this code and agrees to be bound by it;
 - (c) the qualifications of the expert to prepare the report;
 - (d) the assumptions and material facts on which each opinion expressed in the report is based [a letter of instructions may be annexed];
 - (e) the reasons for and any literature or other materials utilised in support of such opinion;
 - (f) (if applicable) that a particular question, issue or matter falls outside the expert's field of expertise;
 - (g) any examinations, tests or other investigations on which the expert has relied, identifying the person who carried them out and that person's qualifications;
 - (h) the extent to which any opinion which the expert has expressed involves the acceptance of another person's opinion, the identification of that other person and the opinion expressed by that other person;
 - (i) a declaration that the expert has made all the inquiries which the expert believes are desirable and appropriate (save for any matters identified explicitly in the report), and that no matters of significance which the expert regards as relevant have, to the knowledge of the expert, been withheld from the Court;
 - (j) any qualifications on an opinion expressed in the report without which the report is or may be incomplete or inaccurate;
 - (k) whether any opinion expressed in the report is not a concluded opinion because of

insufficient research or insufficient data or for any other reason; and

- (l) where the report is lengthy or complex, a brief summary of the report at the beginning of the report.

SUPPLEMENTARY REPORT FOLLOWING CHANGE OF OPINION

4. Where an expert witness has provided to a party (or that party's legal representative) a report for use in Court, and the expert thereafter changes his or her opinion on a material matter, the expert shall forthwith provide to the party (or that party's legal representative) a supplementary report which shall state, specify or provide the information referred to in paragraphs (a), (d), (e), (g), (h), (i), (j), (k) and (l) of clause 3 of this code and, if applicable, paragraph (f) of that clause.
5. In any subsequent report (whether prepared in accordance with clause 4 or not) the expert may refer to material contained in the earlier report without repeating it.

DUTY TO COMPLY WITH THE COURT'S DIRECTIONS

6. If directed to do so by the Court, an expert witness shall:
 - (a) confer with any other expert witness;
 - (b) provide the Court with a joint-report specifying (as the case requires) matters agreed and matters not agreed and the reasons for the experts not agreeing; and
 - (c) abide in a timely way by any direction of the Court.

CONFERENCE OF EXPERTS

7. Each expert witness shall:
 - (a) exercise his or her independent judgment in relation to every conference in which the expert participates pursuant to a direction of the Court and in relation to each report thereafter provided, and shall not act on any instruction or request to withhold or avoid agreement; and
 - (b) endeavour to reach agreement with the other expert witness (or witnesses) on any issue in dispute between them, or failing agreement, endeavour to identify and clarify the basis of disagreement on the issues which are in dispute.