Submission to the Australian Competition and Consumer Commission

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Response to Hutchison's Undertakings
with respect to the supply of its
Mobile Terminating Access Service (MTAS)
Draft Decision
May 2006

Contents

1. Introduction

1.1 Vodafone welcomes the opportunity to comment on the Hutchison Mobile Terminating Access Service (MTAS) Undertaking Draft Decision released by the Australian Competition and Consumer Commission (the Commission) on 21 April 2006.

1.2 Hutchison lodged undertakings with the ACCC to supply MTAS in the following three classes:

- Public Mobile Telecommunications Service (PMTS) ‘Single Rate’
- PMTS ‘Dual Rate’
- Non-PMTS

1.3 Each class is presented as a separate undertaking for both Hutchison Telecommunications (Australia) Limited (HTAL) (2G network) and Hutchison 3G Australia Pty Ltd (H3GA) (3G network) so Hutchison has six ordinary MTAS undertakings in total.

1.4 The PMTS undertakings are presented as alternatives, although Hutchison believes the Dual rate undertaking combined with the Non-PMTS undertaking is more beneficial to the long term interests of end users than the PMTS single rate undertakings.

1.5 Hutchison requested the Commission to consider the PMTS undertakings as alternatives in combination with the non-PMTS undertakings.

1.6 The Commission has assessed the six undertakings individually against the statutory criteria and found the price terms and conditions of the single rate undertaking are reasonable, although the non-price terms and conditions were found to be unreasonable. The PMTS Dual rate undertaking and Non-PMTS undertakings were both found to be unreasonable. Overall Hutchison’s undertakings to supply MTAS were rejected by the Commission.

1.7 Consistent with the submission made by Vodafone to the Commission’s discussion paper on the Hutchison undertakings, Vodafone remains of the view that the Commission cannot be satisfied that any or all, or any combination of Hutchison’s undertakings are reasonable in the terms of section 152AH of the *Trade Practices Act* 1974 (the TPA). As such, Vodafone considers that it is not open to the Commission to accept any or all, or any combination of the Hutchison undertakings under section 152BV of the TPA.

1.8 The Commission's first broad pricing principle for telecommunications is that access prices should be cost based[1]. Hutchison has not provided cost modelling or any relevant analysis demonstrating that the undertakings are based on the costs for supplying MTAS. To the extent that Hutchison seeks to rely upon the Commission's pricing principles for the MTAS , these pricing principles are indicative only and were not derived from Australia specific cost modelling or analysis.

1.9 Given the absence of cost modelling and substantive cost analysis by Hutchison and the Commission, Vodafone holds firmly the view that the Commission cannot determine that the price terms and conditions of any of the six undertakings are reasonable.

1.10 In making this submission Vodafone has followed, where possible, the Commission's draft decision on Hutchison's undertaking for MTAS. As a result of Hutchison's lack of analysis to support their undertakings, it has been difficult for Vodafone to provide in-depth comments on the Hutchison undertakings. Vodafone's response is therefore confined to a limited number of areas. It should also be noted that Vodafone has limited its comments in this submission to the price terms and conditions in the Hutchison undertakings, which should not be taken as Vodafone agreeing that the non-price terms and conditions are reasonable.

2. Undertakings

PMTS Single Rate Undertaking

2.1 Vodafone remains of the view that the Commission cannot be satisfied by the price terms and conditions of the single rate undertaking are reasonable. Hutchison has not provided cost modelling or any relevant analysis demonstrating that the undertakings are based on Hutchison's costs for supplying MTAS.

2.2 Hutchison supports the reciprocal rate of 12cpm for PMTS calls by using the Commission's empirical benchmarking exercise undertaken as part of the Mobile Services Review 2004. Notably, 12cpm is also the Commission's rate covering the 1 January 2007 to 30 June 2007. Hutchison proposes the 12cpm PMTS single rate to apply from 1 January 2006 to 31 December 2007.

[1] Australian Competition and Consumer Commission (1997) *Pricing Principles Telecommunications - A guide*, p14

2.3 To the extent that Hutchison relies upon the Pricing Principles to support the rate in the PMTS Single Rate Undertaking, Vodafone notes that these prices were indicative only and were not based on any Australia specific cost modelling or analysis. The Commission target price of 12cpm was based on unadjusted overseas cost benchmarks (other than for currency) and also Telstra's Regulatory Accounting Framework reports and to a lesser extent, those of Optus. Vodafone submits that this methodology is not consistent with the LTIE and is not a robust or reasonable methodology for calculating or estimating TSLRIC+ or producing an estimate of the range of TSLRIC+ for MTAS. Hutchison has arbitrarily chosen the Commission's indicative prices without itself demonstrating that the basis of these prices are such that it is reasonable and consistent with the statutory criteria.

2.4 In the draft decision the Commission contends that 12cpm is the best available estimate of the upper bound of TSLRIC+ and hence a relevant direct cost of supply at this point in time[2].

2.5 Since 2004, the Commission has not conducted any further analysis to support the assertion that 12cpm represents the upper bound of the TSLRIC+ of providing the MTAS in Australia. However, Optus and Vodafone have undertaken in-depth cost modelling based on the costs of operating a 2G network in Australia that has been subject to extensive analysis by the Commission, other providers of the MTAS and consultants, and believe that the cost of providing the MTAS on their respective networks is higher than 12cpm.

2.6 Economically efficient investment in infrastructure for mobile termination is not promoted by MTAS rates that are not based on forward looking efficient costs of supplying the service. In the absence of forward looking efficient prices, a misallocation of resources will occur, whereby there will be an under or over investment in the service depending on the mobile termination rate.

2.7 An MTAS rate of 12 cpm, is below the estimated forward looking efficient cost of Vodafone providing mobile termination, which is 16.15 cpm.

[2] Australian Competition and Consumer Commission, *Hutchison's undertaking with respect to the supply of its Mobile Terminating Access Service (MTAS) Draft decision,* 24 April 2006, p. 57.

2.8 Vodafone does not agree with the Commission that the single rate undertaking will promote competition in the fixed to mobile market, if the single rate undertaking is accepted rather than rejected. The PMTS single rate undertaking does not provide a rate of MTAS for fixed to mobile calls. It is unlikely, as the Commission argues, that the single rate PMTS undertaking will stimulate fixed to mobile substitution and hence put pressure on retail prices for fixed to mobile calls at a rate faster than outlined in the MTAS pricing principles determination.

Dual rate undertaking

2.9 Hutchison has arbitrarily chosen prices to support the PMTS dual rate undertaking without demonstrating that the basis of these prices are such that it is reasonable and consistent with the statutory criteria.

2.10 Hutchison itself claims that the rate of 21 cpm is not reflective of the underlying cost of providing the MTAS[3]. Hutchison simply selected the 21 cpm rate for MTAS based on their last commercially negotiated rate, a rate which is not, on the basis of the material which Hutchison has provided in the supporting material to the undertakings, derived from TSLRIC+ pricing principles.

Non PMTS undertaking

2.11 Hutchison has not provided any cost modelling or analysis as to why MTAS for mobile calls originating within Australia should be differently priced from those originating from outside Australia.

2.12 The cost of providing mobile termination to a mobile call from another carrier should be the same whether the call originated from inside or outside Australia, regardless of the technology used to originate calls.

2.13 A higher rate for non-PMTS services, compared with PMTS carriers is not in the interest of fixed-line carriers or international mobile carriers.

3. Direct Costs

3.1 Under 152AH(1) of the TPA, in determining reasonableness of the terms and conditions of an access undertaking the Commission must have regard to the direct costs of providing access to the declared service concerned.

[3] Hutchison, Submission *to the ACCC Access undertakings, Domestic Digital Mobile Terminating Access service*, 19 December 2005, p 6.

3.2 The Commission states that:

> *at a minimum an access price should cover the direct incremental costs incurred in providing access and should not exceed the stand-alone costs of providing the service, where this is defined to mean: costs an access provider will incur in producing a service assuming the access provider produced no other services*[4].

3.3 Vodafone recognises that there is a need to balance each of the criteria in section 152AH, and that, at times, there may be a tension between the direct costs of providing access to the declared service, and the economically efficient operation of a carriage service, a telecommunications network or a facility. However, it is not apparent from the Commission's draft decision on the Hutchison undertaking that it has attempted to weight or balance these considerations – rather, the Commission has not assessed Hutchison's direct costs (and indeed, Hutchison has not provided any evidence in this process of its direct costs) and has placed too great a weight on the costs that it considers (on the basis of relatively 'thin'[5] evidence, being the MTAS pricing principles) to be 'efficient'. It is not at all clear that the Commission has (or that it even could given the lack of evidence provided by Hutchison as to its direct costs) had regard to the direct costs of providing access to the MTAS in considering Hutchison's undertakings.

3.4 In short, the Commission cannot be satisfied that the price terms and conditions in any or all, or any combination, of the Hutchison undertakings are reasonable under section 152AH of the Act because it has insufficient information before it upon which to make an assessment of the reasonableness of the price terms and conditions.

4. Cost of 3G

4.1 Hutchison's undertakings do not distinguish between the costs of providing mobile termination on a 3G network and on a 2G network. However, the Commission's target MTAS rate of 12cpm, which Hutchison uses to support the rates in the PMTS undertakings, is based on benchmarked overseas termination rates for 2G only.

[4] Australian Competition and Consumer Commission, *Hutchison's undertaking with respect to the supply of its Mobile Terminating Access Service (MTAS) Draft decision,* 24 April 2006, p. 18.

[5] The Productivity Commission has previously commented that 'international benchmark data provide thin evidence about the appropriate levels of regulated access prices': Productivity Commission, *Telecommunications Competition Regulation: Inquiry Report*, 20 September 2001, p 395.

4.2 Hutchison states that 3G is a lower cost technology than its 2G network so 12cpm is a conservative estimate of an efficient cost of providing MTAS[6]. Hutchison also submits that by terminating calls on its 3G network, it is providing termination services at the minimum of costs.

4.3 Neither Hutchison nor the Commission have provided any evidence to support the assertions that terminating calls on a 3G network are lower than terminating calls on a 2G network.

4.4 It is important for the Commission to acknowledge that carriers in Australia and around the world are rolling out 3G networks because 3G provides:

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- spectral efficiency in capacity for growth in voice and non-voice services (2G networks will be ultimately capacity constrained – by cell site shortage if nothing else);

- higher bandwidth services not possibly under 2G (data cards, video, TV);

- potentially better quality for voice transmission, comparable to that of a fixed network; and

- efficient provision of the portfolio of lower bandwidth services (voice and SMS) and higher bandwidth services over an integrated network.

MTAS prices after 1 July 2007

4.5 In finding the price terms and conditions of the PMTS undertaking reasonable, the Commission believes that it is reasonable for Hutchison to supply MTAS at 12cpm to the end of 31 December 2007, which is beyond the time period in which the Commission's indicative prices apply.

4.6 However, the Commission has indicated that prices for MTAS after 30 June 2007 could be lower than 12cpm. The Commission states:

> *Without attempting to pre-empt the outcome of any future modelling of the cost of providing MTAS, the Commission anticipates that it is likely that the price of the MTAS (based on the previous empirical work contained in the MTAS final report) will be lower rather than higher than 12cpm[7].*

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[6] Australian Competition and Consumer Commission, *Hutchison's undertaking with respect to the supply of its Mobile Terminating Access Service (MTAS) Draft decision,* 24 April 2006, p76.
[7] ibid p29.

4.7 Vodafone is concerned that the Commission is already pre-empting the outcome of modelling work that may be used by the Commission to determine pricing principles and indicative prices to apply after the expiry of the current pricing principles and indicative prices on 30 June 2007.

5. Fixed to Mobile Market

5.1 Vodafone's views regarding retail price levels in the fixed to mobile market and the lack of pass through of lower MTAS rates to lower retail prices for fixed to mobile prices have been outlined in previous Vodafone submissions.

5.2 At a principled level, Vodafone agrees with Hutchison – regulated lower rates of MTAS are unlikely to be significantly passed through to fixed to mobile prices and in this way lower MTAS prices merely result in a value transfer from mobile operators to fixed line operators.

5.3 However, Vodafone is of the view that Hutchison's differential pricing structure for PMTS and non-PMTS is inappropriate for promoting fixed to mobile pass through. The differential pricing is not based on any cost modelling or substantial evidence as to how a differential price between PMTS and non- PMTS calls could be sustained.

5.4 Hutchison argues the pricing differential for non-PMTS of 18cpm compared with 12cpm PMTS is a practical means of testing whether or not an appropriate degree of pass through will occur in the absence of a specific pass through mechanism[8].

5.5 Vodafone has argued previously that differential pricing between MTAS for PMTS and Non-PMTS may frustrate pricing agreements through arbitrage opportunities. Carriers could disguise calls and make them appear to be mobile calls when in fact they are coming from a fixed line to take advantage of the termination pricing differential.

5.6 The differential pricing structure advocated by the dual rate undertaking is not a targeted response to the lack of pass through of lower MTAS rates in the fixed to mobile market.

[8] Hutchison, Submission *to the ACCC Access undertakings, Domestic Digital Mobile Terminating Access service*, 19 December 2005, p11.

5.7 Vodafone recommends a targeted approach to the lack of pass through of lower MTAS prices to retail fixed to mobile prices, such as F2M safeguard, outlined in the Vodafone access undertaking. Targeting fixed to mobile retail prices directly results in a net increase in consumer welfare and economic efficiency, rather than simply a value transfer from providers of the service to fixed originating operators.