

Dr Richard Chadwick
General Manager | Adjudication Branch
Australian Competition & Consumer Commission

Dear Dr Chadwick

NBN Co Limited - Authorisations - A91290 - A91292 - Summary Determination

I am pleased to accept your advice regarding the eligibility to submit an opinion at this point. Like many observers, we had become weary of what had seemed a lost cause, and had failed to see the ACCC opportunity to actually review and place on record what we and all colleagues in the profession that I have canvassed, view as a strong case for restoring wholesale and “infrastructure” competition in the broadband and information market. These views are despite legislated payment facilitation in the case of NBN to Telstra, and the failure to allow a testing of the natural monopoly case for the NBN. Colleagues in the field agree the case fails.

Legislation can change, whereas asset destruction tends to be terminal, tipping the case I argue, strongly in favour of ACCC preservation in the market of competitive assets that make information more generally and cheaply available.

Unusually for these issues, as noted in my summary remarks, there has been no discernable challenge to the views expressed here, with a tendency to blame politics, hung parliaments, and the GFC for a climate where analysis has not been called for or where proffered, not listened to. So I greatly value the opportunity provided by the ACCC, as customers and taxpayers know an announced but slow NBN in one dimension of telecommunications rapidly stalled private investment all over, as commented by every independent party in the business - all waiting for NBN!

I attach below my general summary comments and separately the associated personal annotations on the draft summary determination of the ACCC.

Kind regards

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OVER-ARCHING COMMENT - by Professor Michael G Porter,

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DETERMINATION ii A91290 – A91292

Summary

In this draft determination the ACCC proposes to grant authorisation to NBN Co Limited to give effect to particular provisions contained in the Optus HFC Subscriber Agreement.

The ACCC proposes to grant authorisation for 20 years.

Comment by Prof Michael G Porter

Technology changes so fast that there can be little assurance that a similar ACCC decision would be made next year, owing to dynamic developments typical of telecommunications, information markets and broadband in particular. As the ACCC interim decision wisely notes, the dynamic issues are a key, hard to predict, and the essence of previous failures of government policy and regulation worldwide. What is yet to come in wireless and fibre competition, of a collaborative and competitive kind, is truly dramatic, as countless lectures and seminars, eg from Massachusetts Institute of Technology free on the internet, make quite clear. We want all assets at play for public benefit, not tied up by formerly illegal cross payments across companies.

In the last 24 hours our converging information market has changed yet again, with the prospect of News Ltd owning 50% of Foxtel assets with Telstra at 25%. The Optus HFC cable assets are thus, absent abnormal payments between companies such as NBN and Optus, an option to be maintained or sold under new arrangements, past legislation notwithstanding.

Legislation from Senator Conroy made it possible, or possibly obligatory, to allow a 20 year sequence of payments totalling perhaps \$20 billion from NBN to Telstra to reduce competition from HFC cable and copper to fibre, propping up a business plan of NBN deliberately not subject to public scrutiny (say by Productivity Commission). Similarly new technology and government legislation from government could yet support initiatives from other levels of government, like our active coastal communities along the Great Ocean Road, many denied fibre until almost 2020. Thus certainly technology and possibly governments may all create opportunities that are helped not hindered by a decision that encourages the Optus HFC assets not to be de-commissioned in exchange for payments adding over time to about \$2 billion.

No reason to act now.

My friend and colleague Professor Stephen Littlechild now of Cambridge University, who advised the UK government on these matters from the reforming Thatcher era and to this day around the globe including the ACCC, has noted that in almost all cases telecommunications regulators had significantly underestimated technical change and competitive technologies back when from he was the key regulatory adviser on telecoms and actual regulator of electricity (OFFER) in UK. Technology has been changing more rapidly since then as fibre optics, internet protocol, and “Moore’s Law” transform the world of communications and information. Reasons for allowing today such a long series of payments to “decommission” assets for 20 years are hard to fathom, and while the ACCC makes a balanced attempt, the dynamic imponderables and the ACCC charter should make for a decision to not allow payments to withdraw assets.

A letter circa 23/5/12 in the Australian Financial Review by Optus in a response to my OpEd piece in AFR on 21/5/12 that they could compete better with the money coming in (up to \$2 billion) payments from NBN to decommission those HFC assets is hardly neutral advice and is not backed up by any significant experts.

It is also clear that the assets of HFC companies delivering pay TV (Foxtel) are being constantly upgraded, eg by C-COR, something that will continue following announcements on 20/6/12 from News Ltd, given that the F in HFC cable is fibre. (Cisco documents those transition strategies, and the US and Europe benefits from cable competition with fibre and copper and wireless.)

In terms of my credentials on this matter, I note with pride that a former think tank I founded (Centre of Policy Studies, Monash University, a sole winner of a Commonwealth Centre of Excellence Award in economics in Australia, 1982-87), produced one of the first volumes on telecommunications reform, regulation and privatisation back in 1982 (with Baumol and Littlechild and others as contributors). We received many questionable approaches and offers not to advocate competition or even privatisation in telecommunications, which we rejected in favour of promoting competition and unbundling.

The money bound up in this topic is vast, the opportunities unbounded and always changing, and therefore the priority of preserving competition wherever is clear. Competition has happened more properly in Victorian electricity post our and other research, modelling and advice, but sadly not in telecommunications, with varying governments understating the benefits of competition under emerging technology.

As one who has since followed the Telecom, broadband and cable pay TV and satellite (AUSSAT) debate closely and publicly (see my recent CEDA “Four Doors to Digital Competition” paper and volume, and associated conference at the Sydney Hilton, Dec 2008, where ACCC Commissioner Ed Willett was a valued contributor 2008, along with top executives from Telstra,

Optus, C-COR and many related professionals), I note that the decision to allow payments to competitors to remove any assets from competition is easily regarded as a travesty of economics and undermines a competitive pro-investment strategy in Australia.

Government legislation including the most recent, left the ACCC in an invidious position, but just as legislation from government was anticipated as inhibiting competition, so new legislation from the next government could reverse the trend, noting the 10+ year NBN rollout. Thus we need all assets reasonably facilitating competition to be available, unless there is an overwhelming case the other way, which the ACCC interim decision indicates is not the case.

More to the point, the ACCC reputation in implementing its charter and legislation as the pro-competition agency and enforcer of government pro-competition laws and public interest tests, is most important of all, as the essence of quality in a market economy stems from full, competitive and independent information embodied in markets, essentially so in the case of telecommunications.

To allow assets to be used for all time for one purpose (pay TV in case of Telstra) but not others (broadband), starting now, where the “other” (not pay TV) is the heart of information competition in information, is deeply inconsistent. At least in the case of the Telstra outcome pay TV will still be provided and cables maintained, for possibly a decade or more, or awaiting better future legislation perhaps, legislation facilitating an alternative to overbuild of cable by fibre. Many cables are being re-conditioned for Foxtel this year.

While there is commercial scope for switching pay TV over to NBN fibre and closing cable, but at a huge cost to metropolitan consumers who could or should be able to obtain cheaper services via that same cable, measured in actual cost of provision (no digging, no new wires, or boxes). An earlier than optimal rollover of all HFC clients to the NBN fibre is not a priority, or even a necessity, as the US and Europe and Cisco prove.

Even a delay in NBN fiberising the areas with HFC cable for five year or ten years, with joint use of existing HFC assets for both pay TV (where Foxtel services purchased) and broadband (with speeds in my own case with Telstra Ultimate [Netgear or Cisco] DOCSIS 3.0 delivering over 100Mbps for ethernet and 70Mbps wireless, which can also be available to at least 2.6 million cable-passed homes) will allow NBN to only have to service those areas in metropolitan Australia that do not have cable Foxtel. This cost saving should be encouraged, by not killing the HFC market with termination of yet more cable modems.

Leaders of major companies engaged in the rollout continue to confirm to me, as do expert IT heads in key entities and local governments, that they would prefer an area by area tender of assets with the criteria being broadband speed and asset leasing or purchase cost, not pre-scripting or pro-scripting technology, allowing the mass of fibre, cable, copper and wireless options to be optimised at a way lower unit cost to the area wholesale provider (NBN or sub-

contractor) and so to customers. A key to the logic of their position is some restricted knowledge of where fibre (including Nexgen and other private fibre, and HFC cable) is located.

A future government could legislate to prioritise NBN tender areas, with priority rollouts in areas that do not have HFC cable or will not overbuild existing fibre (as NBN has already been discussing in some cases). All made easier by an ACCC decision to prevent NBN payments to Optus for decommissioning HFC cable assets.

One inhibitor of sound understanding of how real competition will work in broadband in Australia given an ACCC decision towards competition, and against payments not to compete, is that the map of exactly where fibre and cable is in Australia is kept secret, allegedly on security grounds. A current or future government should almost certainly reverse that security interpretation with an in-between position allowing eligible commercial tenderers access to information in their areas of interest.

In the view of independent experts in the broadband rollout area, this fibre map information, and resulting tendering, will slash broadband costs, as the technologies don't overbuild but complement each other, and allow packaging and linking together where it can be done commercially. With digital data, just (0,1)'s, you don't actually need "grand central" NBN to get the data around. That is why some of the worst governed areas of the world still have fast broadband at consumer level!

But NBN could well have the license to tender the wholesale areas, with Optus HFC assets being some of those, like Nexgen and ideally Telstra, tendering in perhaps with some facilitating new legislation.

That commercial relaxing of rollout pressure, and use of Optus HFC and all tendered assets, with area-by-area tenders, can make it easier and more affordable for NBN to prioritise remote, slow or dark areas of broadband service, and skip my street and many others in metropolitan Australia who have HFC cable capable of getting to 500Mbps or even 1 gigabyte! (see Cisco and other technical data). Yes the HFC model requires a dynamic investment model for local network equipment as cable broadband usage expands, but that is properly a commercial matter, where the NBN will and should experience competitive tension.

Most informed economists in my experience understood it was politics and power not economic logic that explain the Telstra HFC payments being given legislative exemption from the normal relevant ACCC acts. The then ACCC Chairman openly admitted it was all politics not economics. Clearly a pro-competitive agency would and did generally oppose a practice of enabling one company, a state owned enterprise, to pay a private firm not to compete. It took legislation over-riding ACCC freedoms to allow cross company cartel-like payments that could otherwise mean jail terms in the private sector. The natural monopoly defence of such payments was never tested, because all independent economists new it would fail.

I have expressed these views publically since 2008 in many respected media (Australian, AFR, CEDA) and open conferences and have yet to have a single response not in agreement, apart from self-interested parties such as Optus claiming, in effect, that receipts of such money enable them to be more competitive. We would all like such payments to compete, but first we have to be a “Tiger Woods”, a standout competitor!!

Thus while the ACCC can, regrettably, stand back from the anticompetitive outcomes legislated by the current government in relation to NBN – Telstra payments, it should indicate its standards by not acting consistently with such anti competitive actions.

The anti-cherry picking laws and payments to decommission assets, basically serve to prop up a business model for a new and supposedly natural monopoly NBN, without any party having established the natural monopoly status of the NBN. The KPMG McKinsey report, as confirmed on page 1, were hired and jointly paid \$25 million not to comment on an alternative model to the NBN. Their report was about how it might work, not “whether” or “why” or “what if”? It was not meant in any way as supporting that rollout model, and they were restricted from looking at alternatives. The Productivity Commission was also not invited to evaluate, but evidently made negative comments when asked by the media to discuss the NBN model. All we know is that the speed of light is fast, and glass fibre can do smart things with upgrades by colour of light, modulation variations and so forth. But fibre is the F in HFC, as already noted. Suppressing HFC cable for a huge fee, of a form not replicated in any other country, and not subject to any independent support or analysis, should make it possible for the ACCC to freely express their best judgements.

The wording of the ACCC draft determination reflects real understanding of these points and is a sound basis for a negative decision.

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