

**Access Dispute Between
Chime Communications Pty Ltd (Access Seeker)
and
Telstra Corporation Limited (Access Provider)**

Line Sharing Services (LSS)

**Publication of Interim Determination and associated statement of reasons
under Section 152CRA of the *Trade Practices Act 1974***

INTRODUCTION

On 21 December 2006, the Australian Competition and Consumer Commission made an interim determination in this dispute that provided for the following LSS annual charges to apply prospectively between the parties:

Except where the parties subsequently agree otherwise, the LSS Annual Charges payable by Chime to Telstra for the LSS are \$38.40 per LSS per annum (\$3.20 per LSS per month).

This interim determination also specified charges to apply prospectively between the parties for the connection or disconnection of LSS.

This interim determination took effect as and from 21 December 2006, and will remain in force until 2 November 2007, unless:

- (i) a final determination comes into effect; or
- (ii) the LSS ceases to be a declared service; or
- (iii) this interim determination is revoked or taken to be revoked under the Act;

in which case this interim determination will cease to have effect on the day that the relevant event occurs.

Having consulted the parties, the Commission has decided to publish its reasons for making this Interim Determination dealing with LSS annual charges.

At the request of the parties, certain information relating to LSS connection charges, or to the parties' respective financial circumstances or business plans, has not been reproduced here.

The ACCC has not yet made a decision regarding whether to separately publish extracts from the Interim Determination and associated statement of reasons dealing with LSS connection and disconnection charges.

REASONS FOR INTERIM DETERMINATION

EXECUTIVE SUMMARY

1. The Line Sharing Service (LSS) has been regulated since 2002. It allows the copper wires that provide voice telephony to also be used to supply broadband internet services, by using the low frequency part of the copper line spectrum for voice and making the high frequency spectrum portion available to access seekers for supplying ADSL services. Telstra retains the ability to provide voice services and obtain line rental revenue and voice call revenue.

2. The Commission has determined to make an interim determination that specifies annual charges for the LSS to apply between the parties to this dispute until a final determination is made (and in any event for no more than one year).

3. In reaching this decision, it is noted that Telstra has continued to charge Request LSS annual charges at the rate of \$9 per month notwithstanding that the Commission (2005) and the Australian Competition Tribunal (June 2006) has each ruled that it is not satisfied that a charge of this amount is reasonable.

4. In setting the LSS annual charges, the Commission has applied its long-standing LSS pricing principles (2002), and also the previous rulings that have been made by the Commission (2005) and the Australian Competition Tribunal (June 2006) concerning a reasonable approach to setting LSS annual charges.

5. Consistent with the Commission's published approach since declaration of the LSS (August 2002), a contribution to line costs has not been included in LSS annual charges, as line costs are being fully recovered in other charges. It is noted that from 2000 Telstra has progressively increased its line rental prices (such as from \$11.65 to \$27.23 (GST exclusive) for the majority of its retail residential customers) so as to recover line costs from line rental revenues.

6. In these circumstances, to allow a contribution to line costs in LSS charges would permit Telstra to double-dip from revenues earned on downstream fixed-voice and ADSL services in over-recovering line-related costs, to the detriment of efficiency and competition and the long term interests of end-users.

7. While Telstra has to date chosen to set line rental charges at a level that fully recovers line costs, following the making of a draft interim determination in this dispute (October 2006), Telstra raised for consideration an alternative approach to the recovery of its line-related costs, that would have consequences for the pricing of the LSS and for the wholesale line rental (WLR) service.

8. Under Telstra's proposal, a contribution to the recovery of line-related costs would be included within LSS annual charges, with a reduction in charges for the WLR service.

9. While Telstra's willingness to reconsider its approach to the recovery of line costs is welcome, the initial suggestion of Telstra as how to implement this initiative requires further work, as

- it results in charges across LSS and WLR that are too high; and
- an immediate introduction of a new price construct could unduly harm competition, due to the consequences for competitors who have relied on Telstra's previous price constructs in making investment decisions.

10. The Commission does not consider it is appropriate for Request to continue to pay LSS annual charges at the rate of \$9 per month while this further work is undertaken by the parties. It is noted that Telstra has been able to implement a rebalancing of LSS and WLR charges but did not seek to do so prior to the making of the draft interim determination.

11. Accordingly, while the Commission remains open to considering further approaches for the purposes of setting prospective LSS annual charges in a final determination, and is also strongly encouraging the parties to negotiate a resolution of the dispute that has regard to charges applying across the LSS and WLR service, it considers that an interim determination should be made that reflects current circumstances, including Telstra's long-standing approach to the recovery of line costs.

12. The Commission intends to progress the dispute towards a final determination as a matter of priority, and is looking to make final determinations by no later than 31 March 2007. In considering the final determination, the Commission would be interested in adopting an appropriate proposal for the rebalancing of annual charges for the LSS and the WLR service, provided that an appropriate approach to this rebalancing can be developed by this time.

1. BACKGROUND

On 3 February 2006 Chime Communications Pty Ltd (Chime) submitted an amended access dispute notification to the Commission in relation to the supply, by Telstra, of the LSS (the notification). (Chime's initial notification of 25 November 2005 originally included iiNet as a party to the dispute, however, iiNet was removed as a party to the dispute in the amended notification). Chime provided its LSS notification to the Commission pursuant to section 152CM(1) of the *Trade Practices Act 1974* (the Act).

The notification states that Telstra has made the LSS available to Chime on terms specified in a Customer Relationship Agreement (CRA 191) entered into between the parties on 9 October 2003. CRA 191 relates to single orders of the LSS. Amongst other things it provided for an LSS monthly rental charge of \$13 per service. Chime advised on 3 February 2006, that, amongst other terms, the LSS monthly charge was in dispute between the parties (Chime reaffirmed this advice on 21 July 2006 in response to the Commission's queries about the status of the terms in dispute). Chime subsequently advised on 27 September 2006 that the LSS monthly charge applying between the parties is currently \$9 per service. In correspondence of 13 February 2006, 24 March 2006 and 27 September 2006, Chime requested an interim determination be made in relation to the LSS monthly charge.

Consultation regarding an interim determination on LSS annual charges

On 6 October 2006, the Commission provided a draft ID that proposed LSS annual charges, and an accompanying Issues Paper (the Issues Paper) to the parties for comment. Responses were provided to the Commission from the parties by way of initial written submissions, lodged by each party on 30 October 2006. Parties made written submission in reply to the submission of the other party on 3 November 2006.

Current decision

Subsection 152CPA(1) of the Act provides that a determination may be expressed to be an interim determination. The Commission has decided to make an ID on the price-related terms and conditions for the provision of the LSS (copy attached). The Commission has done this by revoking the interim determination made in this dispute on 2 November 2006 and replacing it with a new instrument that includes new terms relating to annual charges.

The Commission's reasons for the ID are set out below. The reasons address the issues of:

- whether the Commission should make an interim determination in this dispute; and
- if so, what the content of that determination should be.

2. SHOULD THE COMMISSION MAKE AN INTERIM DETERMINATION IN RESPECT OF THE LSS ANNUAL CHARGE?

Part XIC of the Act does not specify the matters that the Commission is required to take into account in deciding whether to make an interim determination. While the Commission is free to have regard to the matters that it would be required to take into account in making a final determination when making an interim determination, it is not required to take those matters into account, and does not have a duty to consider whether to take those matters into account.

In accordance with the matters set out in section 7.1 of the Commission's Dispute Resolution Guidelines, in deciding whether to issue an interim determination, the Commission has considered the following factors:

- whether the Commission is satisfied that it has sufficient information on which to make an interim determination
- whether the Commission is satisfied in all the circumstances, it is appropriate to make an interim determination.

3. HOW HAS THE COMMISSION DERIVED THE CHARGES SPECIFIED IN THE INTERIM DETERMINATION?

Introduction

The basis upon which the proposed charges have been derived would appear to be relevant to considering whether the Commission should be satisfied that it holds sufficient information and that in all the circumstances it is appropriate to make an interim determination dealing with these charges.

First, whether sufficient information is held will depend upon how the proposed charges are to be derived, and the nature of the calculations that are thereby required.

Also, the basis upon which the proposed prices have been derived is relevant to deciding whether it is appropriate to make an interim determination that specifies those prices.

Pricing Principles

The proposed charges have been derived by applying the LSS pricing principles.¹ In essence, these principles require that LSS prices should comprise the forward-looking efficient costs of supplying the LSS. Further, in principle, LSS prices should be geographically de-averaged, however, averaged prices can be justified where the distortionary effect of an averaged charge is not significant.²

In applying these principles to LSS ‘specific-costs’ (which is relevant to the derivation of LSS Annual Charges), the Australian Competition Tribunal has confirmed that LSS ‘specific-costs’ should be pooled with the equivalent costs that Telstra incurs when it provides access to the higher spectrum on its copper lines (to itself or others) – i.e., when supplying retail ADSL, wholesale ADSL and ULLS – and unitised having regard to downstream demand of at least all DSL services (and possibly by demand for all CAN lines or ADSL capable CAN lines).³

Source materials

The source documents relied upon in deriving the interim determination’s charges are specified in Appendix A to this interim determination.

The source materials that the Commission has had regard to includes information provided in connection with Telstra’s LSS access undertaking.⁴

The Commission has also had regard to the parties’ submissions made in the course of consulting on the making of the ID.

Any information over which Telstra has claimed confidentiality (or derived data) has not been reproduced in this explanation and has instead been recorded in Appendix B (and provided to Telstra only).

Derivation of proposed LSS annual charges

¹ ACCC, *Line Sharing Service – Final decision on whether or not a Line Sharing Service should be declared under Part XIC of the Trade Practices Act 1974*, August 2002, Chapter 5.

² ACCC, *Assessment of Telstra’s LSS undertaking relating to connection and disconnection charges – final decision*, April 2006, at pp 56-57

³ Telstra Competition Limited [2006] ACompT 4.

⁴ ACCC, *Assessment of Telstra’s LSS undertaking relating to connection and disconnection charges – final decision*, April 2006.

In the issues paper, the Commission explained the basis upon which the proposed LSS annual charges had been derived. For convenience, this explanation is reproduced in the discussion below.

In deriving the proposed LSS annual charges, the Commission has considered whether or not to include a contribution to line cost component and a 'specific-cost' component.

Contribution to line cost component

Consistent with the Commission's previous consideration of this issue, the proposed LSS annual charge does not include a contribution to the costs of the line. This is because efficient line costs are being recovered through other charges imposed in respect of the line, such as line rental charges, and, in the absence of reductions in these other charges, to recognise a contribution to line costs as a cost component in LSS annual charges would lead to an over-recovery of efficient line costs.

LSS-specific cost component

The proposed LSS annual charge reflects efficient 'LSS-specific costs', as estimated based upon available information.

For the purposes of the interim determination, efficient 'LSS-specific costs' have been estimated having regard to efficient 'ULLS-specific costs' as estimated on a 'stand-alone basis'. (The term 'stand-alone basis', as here used in respect of 'ULLS-specific costs', describes the approach to cost attribution whereby 'ULLS-specific costs' are estimated on the premise that the only occasions in which Telstra provides access to the higher spectrum on its copper lines was when Telstra supplies the ULLS to external access seekers.)

The Commission estimates these costs at around \$3.20 per line per month, based upon:

- a cost model that Telstra has supplied on 14 March 2006 for measuring (on a stand-alone basis) ULLS 'specific costs' that appears generally robust;
- the Commission's preferred WACC values being substituted into this cost model; and,
- a rounding up of the resulting cost estimate to the nearest 20 cents.

The Commission has otherwise not sought to adjust this cost model with the exception of applying the Commission's preferred WACC values. These values and underlying parameter values are provided in Table 1 below.

The use of this cost model for the purposes of proposing the interim determination should not be seen as an acceptance of all of the variables and underlying assumptions of the model beyond the interim determination.

Confidential information extracted from the Telstra 'ULLS-specific cost' model and contained in confidential Appendix B to this interim determination comprises claimed 'ULLS-specific costs' for 2005-06 (2H), 2006-07 and 2007-08 (as adjusted for the Commission's preferred WACC value), and ULLS demand forecasts reflected in the model for 2002-03 and following years to 2007-08.

Table 1 The Commission's preferred WACC values

	2000/01	2001/02	2002/03	2003-04	2004-05	2005-06	2006-07	2007-08
D/V ratio	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40
E/V ratio	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60
Risk-free (r_f)	0.06	0.06	0.06	0.05	0.06	0.05	0.06	0.06
Risk premium	0.06	0.06	0.06	0.06	0.06	0.06	0.06	0.06
Asset beta	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Equity beta	0.83	0.83	0.83	0.83	0.83	0.83	0.83	0.83
Tax Rate (e)	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
Debt Premium	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.01
Issuance cost	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Gamma	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
CAPM								
R_{equity}	0.1122	0.1086	0.1089	0.0982	0.1080	0.1013	0.1063	0.1063
R_{debt}	0.0723	0.0687	0.0690	0.0583	0.0682	0.0615	0.0664	0.0664
WACC								
$WACC_{pre-tax}$	10.37%	9.99%	10.02%	8.88%	9.93%	9.21%	9.74%	9.74%
Vanilla WACC	9.62%	9.26%	9.30%	8.23%	9.21%	8.54%	9.03%	9.03%

The Commission sought parties' submissions on the following:

- Whether the Commission's LSS pricing principles should be used in deriving the charges for the purposes of an interim determination?
- Does the Commission's approach represent a reasonable application of those principles for the purposes of making an ID?
- Is it appropriate for the purposes of an ID for the Commission to not include a contribution to line costs?; and,
- Is it appropriate for the purposes of an ID for the Commission to assume that LSS specific costs are approximate to the ULLS specific costs as estimated on a stand-alone basis.

Parties' submissions

Telstra submits that although it is appropriate for the Commission to be guided by its LSS pricing principles to derive the monthly charge, it would be inappropriate for the Commission to make an ID on the same terms as the draft ID as Telstra has a new and more equitable pricing construct for LSS.⁵

Telstra proposes a new pricing construct (which in Telstra's opinion better reflects the LSS pricing principles) providing for:

- a monthly charge to recover service specific costs, plus a contribution to the costs of the local loop; and

⁵ Telstra, Submission on the draft interim determination on monthly charges, 30 October 2006, p. 2.

- a rebate to the retail provider of the voiceband PSTN service to the end user customer on an LSS line.⁶

Telstra contends that this pricing construct promotes the LTIE better than the Commission's draft ID because it improves allocative efficiency and is consistent with the Commission's stated desire to promote facilities based competition.⁷

Telstra submits that this approach follows the costing approach proposed by the Tribunal in its recent LSS decision. Telstra states that based on the Tribunal's comments (which Telstra does not necessarily agree with) Telstra developed an ADSL equivalent unit cost model that pools relevant costs incurred by Telstra across its retail ADSL services, wholesale ADSL services, ULLS and LSS. This cost estimates (of \$6.68 per service per month) was provided to the Commission as part of Telstra's ULLS monthly charge undertaking.⁸

Telstra's proposed geographically de-averaged LSS prices are set out below.⁹

Band	Approach 1 notional LSS monthly charge (\$)	Approach 2 notional LSS monthly charge (\$)	Proposed LSS monthly charge – rounded to nearest 10c (\$)
1	5.27	8.06	6.70
2	10.52	11.49	11.10
3	18.77	16.99	18.00
4	88.52	63.49	76.10

Telstra has derived its proposed prices by taking the average of two approaches, set out in Appendix A of its 30 October 2006 submission. Telstra has calculated loop costs by subtracting ULLS specific costs from the ULLS monthly prices recently determined by the Commission. For the first approach, Telstra has attributed 50% of the loop cost to the LSS and then added the ACCC's LSS specific cost estimate from the draft ID (\$3.20). For the second approach, Telstra has attributed 33.33% of loop costs to the LSS and then added Telstra's ADSL equivalent costs (\$6.68).¹⁰

Telstra's pricing construct also provides for a rebate to the retail voiceband PSTN provider of not more than \$15.00.¹¹ That is, where the provider of the retail voiceband PSTN service is a wholesale customer of Telstra, that service provider would receive a rebate on the wholesale line rental (WLR) charge.

Telstra submits that the Commission's derivation of LSS-specific costs is arbitrary and unsafe because:

- It is based on a cost model that Telstra provided in relation to a different service and this cost model is inapplicable with respect to LSS. Telstra argues that instead the Commission should seek to inform itself regarding LSS specific costs;¹²
- It is based on inappropriate WACC estimates. Telstra argues the WACC used to calculate ULLS specific costs should be estimated just for this purpose having regard to the risks entailed in the relevant assets (i.e., different WACCs should apply in respect of ULLS

⁶ Telstra, Submission on the draft interim determination on monthly charges, 30 October 2006, p. 3.

⁷ Telstra, Submission on the draft interim determination on monthly charges, 30 October 2006, pp. 3-4.

⁸ Telstra, Submission on the draft interim determination on monthly charges, 30 October 2006, Appendix A p. 8-9.

⁹ Telstra, Submission on the draft interim determination on monthly charges, 30 October 2006, Appendix A, p. 9.

¹⁰ Telstra, Submission on the draft interim determination on monthly charges, 30 October 2006, Appendix A, p. 8-9.

¹¹ Telstra, Submission on the draft interim determination on monthly charges, 30 October 2006, Appendix A, p. 10.

¹² Telstra, Submission on the draft interim determination on monthly charges, 30 October 2006, p. 4.

specific costs and ULLS network costs). Telstra submits that it appears that the Commission has calculated ULLS specific costs using an asset beta and associated WACC data that was originally intended for the PSTN OTA context and these should not be applied in a ULLS (or LSS) context. Telstra submits the Commission should seek detailed submissions from the parties on these issues;¹³ and

- It fails to take into account the direct costs of the LSS and allocates costs across services that are not the subject of the Commission's jurisdiction. Telstra argues that the allocation of service specific costs across a wider pool of services (including DSL) is contrary to the Commission's statutory obligations under section 152CR(1)(d)(i) of the Act to take into account the direct costs of access to the service. Telstra also argues it is beyond the Commission's power to allocate service specific costs across services that are not the subject of the arbitration.¹⁴

Chime supports the Commission's use of its LSS pricing principles to derive the proposed LSS annual charges. Chime submits that:

- The Commission should not include in the LSS annual charges a contribution to the costs of the line as Telstra already recovers efficient line costs through other charges, such as line rental charges; and
- It is appropriate for the Commission to assume that LSS-specific costs are approximate to the ULLS specific costs as estimated on a stand-alone basis.¹⁵

In response, Telstra disagrees with Chime's contention that it is appropriate for the Commission to assume that LSS specific costs approximate ULLS specific costs and Telstra submits that the Commission has not made conservative assumptions because the Commission's proposed monthly charges are less than the LSS specific costs which Telstra estimates using the Tribunal's approach set out in the LSS decision.¹⁶

In its response submission, Chime submits that:

- It is not reasonable for an ID to be delayed or abandoned whilst Telstra's proposed pricing construct is considered, but, if the Commission is inclined to consider it, this should be done after an ID is made;
- It disagrees with Telstra's interpretation of the pricing principles and considers that the principles recognise that Telstra already fully recovers its line-related costs, such that the price of Telstra's LSS should only equal its LSS specific costs;
- Under sections 152CR(2) and (3) the commission has a broad discretion as to the matters it can consider when making an ID;
- the ULLS cost model is relevant to this arbitration and that it is appropriate for the Commission to refer to it and the ULLS specific costs represent a reasonable proxy of LSS specific costs and can be relied upon for the purposes of an ID;
- for the purpose of an ID the Commission should be able to vary WACC input assumptions from those submitted by the access provider, where available information allows the Commission to do so with confidence;

¹³ Telstra, Submission on the draft interim determination on monthly charges, 30 October 2006, pp. 5-6.

¹⁴ Telstra, Submission on the draft interim determination on monthly charges, 30 October 2006, p. 6.

¹⁵ Chime, Submission in response to the Commission's proposed new interim determination and issues paper, 27 October 2006, p. 1.

¹⁶ Telstra, Reply to Chime's submission on the draft ID on monthly charges, 3 November 2006, p. 1.

- the Commission does not need to take into account the direct costs of access to the service in section 152CR(1)(d)(i) because this relates to the making of a final determination;
- Telstra's ADSL equivalent cost model, on which it has based its LSS estimates, should not be given any weight because Chime has not been provided with a copy of the model and has not had an opportunity to scrutinise or test the veracity of it;
- Given the higher demand for ADSL services as compared to forecast demand for ULLS/LSS services, pooling of costs across these services should result in substantially lower LSS specific unit costs.¹⁷

Commission's views

- Telstra's proposed rebalancing of annual LSS and WLR charges

Consistent with the Commission's published approach since declaration of the LSS (August 2002), a contribution to line costs has not been included in the specified LSS annual charges, as line costs are being fully recovered in other charges. In these circumstances, to allow a contribution to line costs in LSS charges would permit Telstra to double-dip from revenues earned on downstream fixed-voice and ADSL services in over-recovering line-related costs, to the detriment of efficiency and competition and the long term interests of end-users.

In this regard, it is noted that from 2000 Telstra has progressively increased its line rental charges (e.g., from \$11.65 to \$27.23 per month (GST exclusive) for the majority of its retail residential customers) so as to recover line costs from line rental revenues.

While Telstra has to date chosen to set line rental charges at a level that fully recovers line costs, following the making of a draft interim determination in this dispute (October 2006), Telstra raised for consideration an alternative approach to the recovery of its line-related costs, that would have significant consequences for the pricing of the LSS and for the wholesale line rental (WLR) service. Adopting this approach would not only vary the level of charges paid, but would also alter the pricing construct more generally as different prices would apply in each of the geographic bands.

While Telstra's willingness to reconsider its approach to the recovery of line costs is welcome, the initial suggestion of Telstra as how to implement this initiative requires further work, as

- it results in charges across LSS and WLR that are too high; and
- an immediate introduction of a new price construct could unduly harm competition, due to the consequences for competitors who have relied on Telstra's previous price constructs in making investment decisions.

The Commission does not consider it is appropriate for the access seeker to continue to pay LSS annual charges at the rate of \$9 per month while further work is undertaken by the parties. It is noted that Telstra has been able to implement a rebalancing of LSS and WLR charges at any time since it commenced supplying the LSS, but did not seek to do so prior to the making of the draft interim determination in this dispute.

Accordingly, while the Commission considers that Telstra's proposed approach to pricing is worthy of detailed consideration, the Commission does not consider that it would be appropriate to make such a significant change in approach to pricing of the LSS by way of an interim determination in this access dispute.

That said, the Commission strongly encourages the parties to take this opportunity to engage in meaningful negotiations around access to each of the LSS and WLR, and will write to the parties

¹⁷ Chime, Submission in response to Telstra's submission on the proposed interim determination, 3 November 2006, pp. 1-3.

asking them to report to the Commission on the outcome of those negotiations as soon as possible, and in any event by no later than 21 January 2006.

To reinforce the importance that the Commission places on the pending negotiations, parties should note that the Commission would intend to have regard to the reasonableness of the commercial offer that Telstra makes in these negotiations (and the reasonableness of any decision by the access seeker not to accept that offer) in determining:

- whether or not the Commission will explore Telstra’s proposed rebalancing of LSS and WLR annual charges for the purposes of the final determination, or defer any consideration of the proposal until the Commission reviews the LSS declaration and associated pricing principles later in 2007; and,
- whether and if so the extent to which the Commission will backdate the final determination.

Although it is not necessary for the purposes of the present decision to provide detailed comment on particular aspects of Telstra’s proposed approach, to facilitate subsequent negotiations between the parties the Commission notes that it has already provided guidance on the level of charges that is considered reasonable for the independent supply of the LSS and WLR (as per the LSS annual charges specified in the ID and the model WLR prices that have been published by the Commission).¹⁸

The Commission anticipates that in addition to the overall level of charges to apply prospectively to the LSS and WLR, it would be important for the parties to seek to reach agreement on:

- (i) the proportion of line costs that should be recovered from fixed voice and ADSL services, and the consequent rebalancing of prospective annual charges between the LSS and WLR;
- (ii) from when the rebalanced charges for the LSS and WLR should apply, having regard to the potential for downstream competitive services to be disrupted should any change in approach to those charges be implemented too quickly; and
- (iii) the amount of already received LSS annual charges to be repaid by Telstra to the access seeker.

In this regard, it is noted that LSS access seekers have made investment and business decisions on the basis of the currently applying approach to LSS pricing (which has applied since 2002), and to simply move to another approach to pricing without a transitional period would risk harming efficient investment and competition, to the detriment of the LTIE. The Commission notes that where it has previously had cause to adjust its approach to pricing, it has only done so following detailed consultation and by applying a transitional price path (over which price adjustments were made).¹⁹

Should the parties be unable to reach agreement on LSS annual charges, the Commission will proceed to make a final determination at its earliest opportunity (and by no later than 31 March 2007). The Commission will write to the parties shortly commencing this consultation process.

As noted above, at this time, unless the Commission considers that an unconditional offer that had been made by Telstra across the LSS and WLR was reasonable having regard to the long term interests of end-users and to the matters outlined above, the Commission would intend to proceed

¹⁸ ACCC, *Pricing Principles and indicative prices - local carriage service, wholesale line rental and PSTN originating and terminating access services*, 29 November 2006.

¹⁹ ACCC, *Mobile Terminating Access Service, Final Decision*, June 2004 pp 214-222; ACCC, *Final determination for model price terms and conditions of the PSTN, ULLS and LCS services*, October 2003, pp 60-66

to make a final determination that specified a LSS annual charge of no more than \$38.40 (i.e., \$3.20 per month).

- *Whether 'LSS specific-costs' would approximate 'ULLS specific costs' as measured on a stand-alone basis*

Telstra contends that 'LSS specific-costs' are unlikely to approximate the 'ULLS specific-costs' as measured on a stand-alone basis because different costs and demands are associated with the ULLS and LSS. Telstra contends that the Commission should instead inform itself of the 'LSS specific-costs'.

This submission misunderstands the approach to pricing of the LSS (and the ULLS) that the Commission applies, and which the Tribunal endorsed in the LSS review. Under this approach, the (efficient) 'specific-costs' incurred when Telstra supplies the LSS or the ULLS to access seekers, and line-sharing to itself (i.e., when it shares a line in order to supply retail or wholesale DSL services), are aggregated and recovered across all associated lines.²⁰ The Issues Paper explains why under this approach 'LSS specific-costs' would be expected to be approximate to 'ULLS specific-costs' as those costs (i.e., 'ULLS specific-costs') are measured on a stand-alone basis, as follows:

The Commission considers on available information that the *stand-alone* ULLS 'specific-cost' estimate is a reliable benchmark for the *upper bound* of the range of efficient LSS 'specific-costs' that the Commission could consider appropriate when making a *final determination* that fully applied the Tribunal's decision regarding the attribution of 'specific costs'.

While *stand-alone 'specific-costs' measures* (i.e. measures derived without adopting the approach to cost attribution that the Tribunal has recommended) may differ to a small extent in absolute terms, the LSS 'specific-costs' measure that is derived once the Tribunal's decision is applied will likely fall to below the *stand-alone* ULLS 'specific-costs' measure.

This is because:

- While *stand-alone* efficient unit costs for LSS and ULLS 'specific-costs' may differ to some extent, this divergence would not be expected to be overly significant in absolute terms given the limited size of the cost base, and the ULLS 'specific-costs', LSS 'specific-costs' and ADSL equivalent costs involving the same cost categories.
- Most importantly, the Tribunal's LSS decision requires a pooling of LSS 'specific-costs' with equivalent costs incurred in supplying ULLS and ADSL services, and any such divergences between *stand-alone* ULLS and LSS 'specific-costs' would be diluted by that approach. Further, given ULLS forecast demand is higher than LSS forecast demand, and demand is the key determinant of these unit costs, the specific-costs measure derived by pooling only 'LSS and ULLS specific costs' would tend to approach the stand-alone ULLS 'specific-cost measure'. In this regard, demand data for the ULLS and LSS (as provided by Telstra in cost models it has submitted to the Commission) are recorded in confidential Annexure B.
- Further, when robust ADSL equivalent unit cost data become available and are also taken into account, efficient 'LSS-specific' unit costs would be expected to fall below those estimated for ULLS 'specific-costs' on a stand-alone basis, given the

²⁰ Telstra Corporation Limited (ACN 051 775 556) [2006] ACompT 4, at paragraphs 121 - 166

much higher demand for ADSL services²¹ as compared to forecast demand for ULLS/LSS services, and the presence of fixed costs within the relevant cost base.

Telstra further contends that the 'LSS specific-costs' are unlikely to approximate the 'ULLS specific-costs' as measured on a stand-alone basis because the 'ADSL equivalent costs' are higher (rather than lower as the Commission's approach suggests) than the 'ULLS specific-costs'.

To fully investigate Telstra's 'ADSL equivalent costs' claim will require detailed analysis, which the Commission will undertake for the purposes of the final determination. This assessment will consider whether the claimed 'ADSL equivalent costs' are representative of efficient costs, and are of the same level and order as the 'LSS specific-costs' and 'ULLS specific-costs'.

As noted in the Issues Paper, it would not be appropriate to include costs of sales associated with downstream services in this cost claim for 'ADSL equivalent costs'. Allowing such costs would in effect require access seekers to contribute to Telstra's costs of sales for downstream services and thereby, for example, pay Telstra's marketing and billing costs associated with those downstream services. It is noted that the marketing and billing costs for the downstream services that access seekers supply are outside the cost categories that comprise the 'LSS specific-costs' and 'ULLS specific-costs'.

In this regard, in the Issues Paper, the Commission noted that these 'ADSL equivalent costs' can be summarised for present purposes as the costs incurred in:

- providing computer systems for the ordering of access to the higher frequency spectrum of copper lines in connection with retail and wholesale ADSL orders (but not ordering systems more generally, such as those used in the supply of downstream retail or wholesale services)
- having staff check that these orders are properly completed and that the line in question is capable of supporting access to the higher frequency spectrum; and,
- performing associated management functions.

An initial review of the limited material that Telstra has provided in support of its 'ADSL equivalent costs' claim is strongly indicative however of the inclusion of costs associated with sales of downstream services. This information cites cost categories such as 'marketing', various 'billing' related costs (support, administration, development), 'bad debts', 'sales costs' and 'retail level capex'.²²

Accordingly, it would not appear that the information that Telstra has provided to date is reflective of its 'ADSL equivalent costs' but rather is an attempt to measure the costs of sales of downstream services.

Further, on the information that has been provided to date, the Commission remains of the view that efficient 'ADSL equivalent costs' are likely to be lower than 'ULLS specific-costs' as those costs are measured on a stand-alone basis. As a consequence, the Commission considers that its assumption made for the purposes of the ID that 'LSS specific-costs' are approximate to 'ULLS specific-costs' as measured on a stand-alone basis is a conservative assumption.

²¹ As at 30 June 2006, Telstra was supplying 2,549,900 ADSL services (either wholesale or retail) – see, ACCC, *Snapshot of broadband deployment as at 30 June 2006*

²² Supplementary Statement of *Telstra employee*, 11 August 2006 at Annexure F

- *Whether efficient 2006-07 'ULLS specific-costs' measured on a stand-alone basis are \$3.20*

Telstra raises a number of concerns regarding the \$3.20 measure that the Commission has adopted for these costs.²³

Adjusting the WACC value

Telstra submits that it is inappropriate for the Commission to alter the WACC value in the relevant cost model from the value that Telstra initially specified in that model, as altering one variable of a complex costing model means the resulting measure is prone to an unacceptable risk of error.

The Commission does not agree that for the purposes of an interim determination it should refrain from changing input values from those advocated by the access provider where, as is the case here, the available information allows the Commission to do so with a reasonable degree of confidence.

Adjusting the WACC value leads to a relatively modest reduction in the derived unit cost measure, and the costs derived from Telstra's unadjusted cost model is below the charges currently applicable to the LSS. Applying the Commission's WACC adjustment merely results in a further decrement to derived unit costs.

Use of current values for WACC parameters

Telstra contends that the Commission should update the WACC parameter values, and in particular, the values for the risk free rate and debt risk premium.

The Commission considers that it remains appropriate to use the risk-free rate values that the Commission proposed to the parties for the purposes of the ID. The charges specified in the ID rely upon WACC values for 2000-01 through to 2007-08, and it is only in respect of 2006-07 and 2007-08 that more current observations of the risk free rate could lead to changes in the WACC value adopted. In this regard, the risk free rate (as represented by the 10 year Commonwealth government bond yield) as at 30 June 2006, and as at 30 October 2006 (the most up-to-date observation available) remains proximate to the value adopted by the Commission for 2006-07 and 2007-08.²⁴

Accordingly, the Commission considers that updating the 2006-07 and 2007-08 risk free rate values for the purposes of the interim determination would not have a material effect on the derived charges. The Commission will however update these values when it comes to consider a final determination in the matter.

The Commission has not accepted Telstra's approach in relation to the appropriate debt risk premium in previous matters.²⁵ However, it is noted that even if the Commission adopted the approach advocated in Telstra's submission, this would have little or no effect on the derived cost measure.

Use of a modified asset beta in calculating the WACC

Telstra contends that a modified asset beta should be used in calculating its WACC to reflect differences between the ULLS and the PSTN.

In determining the appropriate asset beta for the ULLS, the Commission needs to consider the assets employed by the service and the cash flows that result from the final use of these assets. The cash flows that have traditionally recovered the costs of the ULLS are those resulting from the

²³ Telstra submission 30 October 2006, p. 5.

²⁴ Source: Reserve Bank of Australia, *F02 Capital Market Yields - Government Bonds*, www.rba.gov.au accessed 4 December 2006

²⁵ See for example ACCC, *Assessment of Telstra's ULLS monthly charge undertaking: final decision*, August 2006, pp. 106-107.

sale of PSTN products such as line rental, local and long distance calls. Therefore, the Commission considers that the asset beta relevant for PSTN originating and terminating access is also relevant for the ULLS.

Broadband is a recent addition to the list of services that can be supplied over the ULLS. Provision of broadband over the ULLS is not necessary for Telstra to recover the costs of ULLS and as such the Commission's current view is that it should not be considered when determining the appropriate asset beta. If anything, the consideration of the provision of broadband in addition to the provision of PSTN services would appear to make it more likely that Telstra would recover the costs of the ULLS (as broadband provides additional revenue) and as a consequence would tend to lower systematic risk associated with Telstra's asset base, compared to when broadband was not supplied.

Use of a 'ULLS-specific WACC'

Telstra contends that a ULLS-specific WACC should be used (which is higher than the WACC used for the PSTN).

Consistent with its view as expressed in recent undertaking assessments,²⁶ the Commission considers that the same WACC is appropriate for both ULLS network and 'ULLS-specific' costs. As noted above, cash flows that recover a particular cost need to be considered when determining the asset beta for the cost. The same cash flows (PSTN cash flows) recover both ULLS network and 'ULLS-specific' costs, so one WACC is appropriate for both components of the ULLS charge.

4. DOES THE COMMISSION HAVE SUFFICIENT INFORMATION ON WHICH TO MAKE AN INTERIM DETERMINATION FOR LSS ANNUAL CHARGES

Introduction

In its issues paper, the Commission suggested it was relevant to consider whether the available information would provide a reasonable basis for the new interim determination. It was noted the information would need to be:

- reasonably complete, having regard to all of the significant matters which are taken into consideration in applying the pricing principles to the issues
- reasonably robust, in the sense that critical assessment has not to date disclosed a fundamental error – that is, an error such that the resulting cost measures could not reasonably be considered to be broadly indicative of efficient unit costs

The Commission noted that some areas where information did not appear to be sufficiently complete or robust *for the purposes of making a final determination*, but, proposed that by making conservative assumptions in respect of them, these information limitations could be reasonably overcome *for the purposes of making an interim determination*.

In its issues paper the Commission identified particular instances where further or better information would assist in preparing a final determination dealing with LSS annual charges concern, namely:

- the 'LSS-specific cost base' – while Telstra has supplied a 'specific-cost' model to support the charges it proposed in its 2004 LSS monthly charge access undertaking, that cost model was shown not to be robust in the Tribunal proceedings brought in connection with that undertaking; and,
- the 'ADSL equivalent cost base' – where a cost model has not been proposed.

²⁶ *Ibid.*, p. 154.

Parties' submissions on LSS annual charges

Telstra submits that the Commission does not have sufficient information to make an ID in the form proposed because in the absence of model price terms, there is no pricing benchmark that can be readily applied. Telstra argues that this insufficiency of information is evidenced by the Commission's own statement that the information received by it in the LSS undertaking process was insufficiently robust and the fact that the Commission's ID is based on 'analogy and speculation'.²⁷

Chime submits that the Commission does have sufficient information on which to make an interim determination in relation to LSS annual charges. Chime agrees with the Commission that any limitations in relation to ADSL equivalent cost information can be overcome by making conservative assumptions that efficient LSS-specific costs are approximate to efficient ULLS-specific costs, as estimated on a stand alone basis.²⁸

In its reply submission, Telstra submits that the Commission does not have sufficient information to make an ID (and that the Tribunal's approach in the LSS monthly charge undertaking decision is flawed). In addition, Telstra submits that if the Commission is minded to make an ID, Telstra submits the Commission should take into account Telstra's ADSL equivalent cost base information.²⁹ Telstra maintains its view that the information on ULLS specific costs is insufficient for the purposes of estimating the costs of providing a different service, even in the context of an ID. Telstra argues ULLS-specific cost information is not applicable.³⁰

In its response submission, Chime noted that Telstra provided a redacted submission of 30 October 2006 to Chime. Chime submits that to avoid delay Chime will not seek access to the information Telstra claims is confidential for the purposes of consultation on the ID. Chime submits that the Commission should give little weight to the information Telstra has claimed as confidential as Chime has not had the opportunity to scrutinise and test the veracity of that material.³¹

²⁷ Telstra, Submission on the draft interim determination on monthly charges, 30 October 2006, p. 1.

²⁸ Chime, Submission in response to the Commission's proposed new interim determination and issues paper, 27 October 2006, p. 2.

²⁹ Telstra, Reply to Chime's submission on the draft ID on monthly charges, 3 November 2006, p. 1.

³⁰ Telstra, Reply to Chime's submission on the draft ID on monthly charges, 3 November 2006, p. 2.

³¹ Chime, Submission in response to Telstra's submission on the proposed interim determination, 3 November 2006, p. 4.

Commission's views

The Commission considers that, for the purposes of making an interim determination, it does not need to have in front of it all of the information that it would need for the purposes of the final determination.

Further, the Commission does not believe that it needs to have reached a view on all outstanding issues in an access dispute before it can make an interim determination. To set the information threshold at a level equivalent to that necessary to issue a final determination would restrict the Commission's ability to make an interim determination in a way that was not intended by the Parliament. Subsections 152CR(3) and (4) confirm that requiring the Commission to take into account matters that it must consider in making a final determination would detract from the utility of interim determination arrangements. Subsection 152CR(4) provides that, in making or varying an interim determination, the Commission does not have a duty to consider whether to take into account a matter specified in subsection 152CR(1) of the Act.

While there is the potential for further or better information to become available in the course of the arbitration, the Commission considers that the information now available is reasonably complete and robust for the purposes of an interim determination.

Dealing with the information available to support the LSS annual charges, on the analysis undertaken to date, the efficient 'ULLS-specific costs' measure (as estimated on a stand-alone basis) that the Commission has used for the purposes of the ID appears to be reasonably robust.

The Commission considers that, in relation to the informational limitations identified in the issues paper, these can and should be overcome for the purposes of making a timely interim determination by making the conservative assumption that efficient 'LSS-specific costs' are approximate to efficient 'ULLS-specific costs' as estimated on a stand-alone basis.

The Commission does not consider that it should have regard to Telstra's 'LSS equivalent costs' claim in this regard, as it is not reflective of the costs that Telstra efficiently incurs in providing line sharing to itself, but rather appears to be a measure of actual costs incurred regarding the sale of downstream services.

The method by which the charges were derived is set out in full in the Issues Paper provided to the parties, and discussed in these reasons above. The Commission does not agree that this method involves speculation or analogy.

Accordingly, the Commission's considers that there is sufficient information before the Commission on which to make an interim determination in the terms and conditions set out in this interim determination.

5. WHETHER THE COMMISSION IS SATISFIED THAT, IN ALL THE CIRCUMSTANCES, IT IS APPROPRIATE TO MAKE AN INTERIM DETERMINATION?

The Dispute Resolution Guidelines note that in considering if an interim determination is appropriate, in all the circumstances, the Commission considers a range of matters including:

- The nature of any contractual arrangement between the parties
- Whether backdating a final determination would provide an adequate alternative to making an interim determination
- The likely impact of an interim arrangement on end-users
- The timing of the final determination

- International treaty obligations
- Other matters.

These are considered in turn.

5.1 Nature of any contractual obligations

In accordance with the Guidelines, the Commission has considered the nature of the contractual arrangements between Chime and Telstra.

In the Issues papers, the Commission suggested that while Part XIC of the Act encourages commercial negotiation and the application of terms and conditions of supply that have been commercially negotiated, it also recognises that in some instances commercial negotiation could not be expected to give rise to outcomes that would promote the long term interests of end-users. This is especially the case where there is a significant disparity of bargaining position between the parties to the negotiation.

The parties were requested to make submissions on the nature of the contractual relations between the parties and as to why it may or may not be appropriate for the currently applicable prices to be varied by way of an ID.

Parties' submissions

Chime states that the parties have not agreed on a contractual arrangement in lieu of an interim determination and, that because parties have been unable to agree on pricing for the services, the relevant contractual arrangements between the parties remain unsettled and create uncertainty. Chime submits there continues to be a significant disparity in the bargaining power between the parties.³²

In response, Telstra states that there is certainty as to LSS monthly charges, such as those charges set out in the LSS schedule to the CRA between the parties dated 9 October 2003, as varied from time to time. Telstra submits that an ID merely changes the prices between the parties, it does not improve certainty.³³

Commission's views

The Commission is of the view that the existing contractual arrangements between Chime and Telstra do not militate against the making of an interim determination for LSS monthly charges. The Guidelines provide in section 7.1.1:

... there may be a case for making an interim determination if the terms of the arrangement reflect a significant disparity in bargaining position of the parties which is unlikely to be ameliorated through the making of a final determination in the near future.

The Commission notes that the contractual arrangements that were in place when the dispute was notified have been modified in some respects (as they relate to certain connection charges) by negotiations between the parties. The Commission does not consider, however, that there is any evidence of a reduction in the significant disparity in the bargaining power of the parties. The disparity appears unlikely to be remedied by a final determination in the near future.

In this regard, Chime has continued to seek an interim determination regarding LSS annual charges.

³² Chime, Submission in response to the Commission's proposed new interim determination and issues paper, 27 October 2006, p. 2.

³³ Telstra, Reply to Chime's submission on the draft ID on monthly charges, 3 November 2006, p. 2.

Telstra has continued to impose LSS Annual Charges of \$9 per month notwithstanding that the Commission and the Australian Competition Tribunal has each ruled that they were not satisfied that a \$9 per month charge was reasonable.

As a consequence of reaching the above view that on the facts there has been no agreement between the parties, it is not strictly necessary for the Commission to consider Telstra's submissions around the nature of the Commission's powers to make a determination. However, the Commission would not agree that section 152CM of the Act (which deals with the pre-requisites for notifying a dispute) limits its power to make a determination. Rather, the Commission considers that its power to make a determination is as provided by section 152CP of the Act.

The consultation on a draft ID in the current arbitration (of the LSS access dispute), and the making of the ID, does not prevent the parties from negotiating over different terms and conditions to apply between them. Further, terms and conditions subsequently agreed between the parties would apply in preference to those specified in the ID.

In conclusion, the Commission considers that the contractual circumstances between the parties does not militate against the making of an ID and, if anything, lends weight to the Commission making an ID.

5.2 Whether backdating a final determination would provide an adequate alternative to make an interim determination

The Commission has considered whether in the circumstances backdating may represent an adequate alternative to the making of an interim determination.

In the Issues Paper, the Commission suggested that, while backdating can reimburse a party to an access dispute for any additional payments over and above what it would have been required to make under the final determination, it could be expected that the potential for backdating may not always represent an alternative to the making of an interim determination. This could be due to:

- a lesser degree of commercial certainty that will apply until the final determination, and a decision as to whether or not to backdate, have been made; and/or,
- the respective financial position of the parties to the dispute and their ability to fund the additional payments without compromising their business operations.

The Commission sought from the parties their advice as to:

- What additional payments are likely to be involved with and without the making of the interim determination—which includes an assessment of the difference in the prices that would apply up until final determination with and without the making of the interim determination, the number of services involved and the length of time until final determination?
- What is the ability of each of the parties to fund this quantum (either in the form of extra payments made or payments forgone) without compromising their current and future business plans with and without the making of the interim determination?

In the issues paper, the Commission also suggested that, from the relative size of the parties (as measured, for instance, by their respective annual revenues), it would appear that Telstra is in a significantly better position to absorb (at least until a final determination) any shortfalls that may be associated with any difference between charges that may be specified in an interim determination and in a final determination respectively.

Parties' submissions

Chime states that it is currently re-examining its forecasts for the remainder of the financial year in light of the pricing changes proposed by the Commission and expects that overall numbers would be revised upwards.

However, based on Chime's current forecasts, Chime estimates it would save [c-i-c] per annum based on the proposed terms for LSS annual charges. Chime notes that, depending on the outcome of its ULLS dispute with Telstra, it may migrate LSS services to the ULLS, which would reduce its savings on LSS annual charges to [c-i-c]. Chime submits both amounts to be material savings.³⁴

Chime submits that given the revenues earned by the companies in 1H06 (\$120 million for Chime and \$11,439 billion for Telstra) Telstra is better placed than Chime to absorb (until a final determination) any shortfalls associated with the reduced annual charges in the proposed ID.³⁵

Chime also submits that the price reductions in the proposed ID will have a significant impact on the range, price and quality of the services Chime is able to offer end-users, in particular Chime states that it is currently developing [c-i-c business plans]. However, Chime states that the opportunity to develop [c-i-c these business plans] will likely be lost if Chime is required to wait for final determinations, even if those determinations are backdated.³⁶

Telstra submits that backdating a final determination could remedy any possibly adverse impact on Chime should the final determination lower the monthly charges for LSS.³⁷ Telstra also argues that if the Commission makes an ID on the same terms as the draft ID and then chooses to apply Telstra's proposed pricing construct (for LSS annual charges) in a final determination, an access seeker may be required to repay substantial sums to Telstra and/or increase its prices, which would have an adverse impact on the LTIE.³⁸

In its response submission, Chime states that the Commission's price in a final determination is likely to be closer to \$3.20 than the current price of \$9.00, and therefore, if an ID is made, any amount payable by one party to another as a result of backdating, will be significantly reduced. Chime reiterates its arguments that Telstra is better placed than Chime to absorb any differences in price until a final determination is made.³⁹

In response to Chime's submission, Telstra submits that given the adequacy of backdating, it is more appropriate for the Commission to refrain from making an ID until it receives further and better information particularly when the basis of the propose ID is, in Telstra's view, unreasonable.⁴⁰

Commission's views

In the Commission's view, the backdating of a final determination does not represent an adequate alternative to the making of an ID in this matter. This is because of the potential for delay in the making of a final determination, and the reduced certainty to the parties regarding LSS annual charges to be paid for the intervening period in the absence of an ID. In these circumstances, while the lower prices specified in the ID would be expected to benefit end-users (through a

³⁴ Chime, Submission in response to the Commission's proposed new interim determination and issues paper, 27 October 2006, pp. 2-3.

³⁵ Chime, Submission in response to the Commission's proposed new interim determination and issues paper, 27 October 2006, p. 3.

³⁶ Chime, Submission in response to the Commission's proposed new interim determination and issues paper, 27 October 2006, p. 3.

³⁷ Telstra, Submission on the draft interim determination on monthly charges, 30 October 2006, p. 7.

³⁸ Telstra, Submission on the draft interim determination on monthly charges, 30 October 2006, p. 7.

³⁹ Chime, Submission in response to Telstra's submission on the proposed interim determination, 3 November 2006, p. 3.

⁴⁰ Telstra, Reply to Chime's submission on the draft ID on monthly charges, 3 November 2006, p. 2.

greater variety of services, improvements in service quality and/or reduced prices), a failure to make the ID would defer these benefits at least until the final determination was made.

The Commission considers that the interim determination will increase, not decrease, certainty in relation to LSS pricing going forward. Although the final decision on key issues remains subject to further consideration, the interim determination (and associated reasons) gives parties some indication as to the direction the Commission might take in relation to key issues. Given that a final determination is likely to be some months away, the Commission considers that it is appropriate to provide LSS monthly charges in the interim. The timing of the final determination is discussed further below.

The Commission believes that Telstra has the superior ability to absorb any reductions in revenues arising from lower ID charges in the period up until a final determination is made - in the event that higher charges were specified in a final determination and were backdated - compared to Chime having to absorb higher current charges until a final determination was made. These factors combined suggest that an ID should be made rather than placing reliance on a backdated final determination.

It would be unlikely for the Commission, should it subsequently decide to alter the approach to deriving LSS Annual Charges for the purposes of the final determination (to reflect the approach that Telstra has now proposed), to backdate the higher LSS Annual charges that would result. As noted previously, it is the Commission's practice in such situations to transition to new pricing levels by adopting a price path. Backdating a final determination that involved a change in approach would be inconsistent with that prior practice.

5.3 The likely impact of the interim determination on end-users

The Commission has considered the likely effect of an interim determination on the interests of end-users.

In the issues paper, the Commission suggested to the parties that an interim determination is likely to promote the long-term interests of end-users where it would encourage efficiency in use or in investment in the facilities that are or in future would be used to supply the services, or promotes competition for the supply of services such that end-users are offered a greater variety of services, or services that are of a higher quality or of a lower price.

Parties' submissions

Chime points to [c-i-c business plans that it is developing], and submits that the opportunity to [c-i-c implement these business plans] would be compromised if IDs were not made in its access disputes.⁴¹ Chime's submissions made in relation to backdating (set out previously) addressed the likely impact of the ID on end users.

Telstra submits that Chime has made only vague claims around how the ID would promote the interests of end-users [c-i-c] and that it should be directed by the Commission to supply further information on those claims.⁴² Telstra also submits that iiNet's [c-i-c business plans are] irrelevant to a dispute between Chime and Telstra.⁴³

Commission's views

As noted above, the Commission and the Australian Competition Tribunal have considered in detail the LSS annual charge that has applied between the parties, and each has ruled that they are not satisfied that this charge of \$9 per month is reasonable having regard to the LTIE.

⁴¹ Chime, 27 September 2006, p. 5.

⁴² Telstra, 10 November 2006, p. 2.

⁴³ Telstra, Reply to Chime's submission on the draft ID on monthly charges, 3 November 2006, p. 2.

Accordingly, the Commission considers that, on current information, making the interim determination will be beneficial to the continued development of competition and economic efficiency, and therefore is likely to promote the interests of end-users.

By indicating the Commission's current understanding on key issues, it will provide more certainty to Chime on the LSS charges that it might face, and will tend to encourage Chime in progressing its plans for new services and further network build (which Chime submits has been dependant on achieving certainty in relation to both the ULLS and LSS).

Notwithstanding Telstra's objection, the Commission considers that the prices in the interim determination are more likely to reflect efficient unit costs than the prices currently applying between the parties. As noted in the issues paper, conservative assumptions that bias *upwards* the derived unit costs were used in formulating the interim determination prices.

While Telstra may provide new information which results in upwards adjustments to some costs, on balance the Commission considers it more likely than not that, after more comprehensive analysis has been completed for the purpose of a final determination, the LSS charges will remain closer to the charges specified in the ID than those currently applying between the parties.

The Commission also notes that Chime is a wholly owned subsidiary of iiNet, and as such considers it reasonable to believe that iiNet's [c-i-c business plans] will be informed by the terms upon which Chime can access the upstream LSS. Although Telstra questions whether the foreshadowed [c-i-c business plans] will eventuate, the Commission is satisfied that making the ID will lead to circumstances that will better facilitate investment [c-i-c].

While this limited LTIE analysis suggests that the new interim determination is justified, it should be noted that, unlike consideration of a final determination, the Commission is not required to have regard to all the reasonableness and LTIE criteria before making an interim determination.⁴⁴

5.4 Timing of the final determination

The Commission has considered the likely timing of a final determination in deciding whether or not to make an interim determination.

In the Dispute Resolution Guidelines, the Commission indicates that the timing of an interim determination is relevant in two ways. First, if the period of time between notification of the dispute and the making of a final determination is likely to be substantial, then an interim determination may be appropriate. Second, the period of time between the interim determination and the final determination should be considered. If a final determination is to be made within a relatively short period of time (say 2 to 3 months), then the case for making an interim determination is likely to be weaker, especially given that an interim determination uses resources that could otherwise be used to finalise the arbitration.

Parties' submissions

Chime submits that the completion of all steps necessary for making a final determination may take several months and it is, therefore, appropriate that an ID be made that is more likely to reflect the prices that will apply under the final determination than the ID that is currently in place.^{45 46}

In its response submission in the LSS annual charges consultation, Chime submits that if the Commission analyses Telstra's proposed new pricing construct this would likely substantially

⁴⁴ See section 152CR(4) of Part XIC.

⁴⁵ Chime, Submission in response to the Commission's proposed new interim determination and issues paper, 27 October 2006, p. 4.

⁴⁶ Chime, 3 November 2006, p. 6.

delay the making of a final determination. Therefore, in the meantime, Chime believes it is appropriate that an interim determination be made.⁴⁷

Commission's views

The Commission notes that eight months have already elapsed since Chime notified the LSS access dispute. In the present circumstances, there is likely to be a need for additional information and analysis in order to derive efficient cost measures that are sufficiently robust as a basis for the making of a *final determination*. It is envisaged that obtaining further information and detailed submissions from the parties would take a considerable period, which could extend to a number of months.

Further, there appear to be additional matters that have the potential to delay the Commission somewhat in conducting the arbitration and making a final determination, including:

- Some of the information may not be available to the access seeker due to claims of confidentiality.
- Some of the information may not be available to the access seeker because of the material having been obtained in the course of another arbitration, and the TPA provides for formal consultation processes to be followed in determining whether the Commission should disclose this material to the access seeker; and,
- There are other matters in addition to LSS annual charges that are in dispute between the parties.

As such, it would appear reasonable to expect that a final determination in the arbitration would not be made within a reasonably short period (say 2 to 3 months), of making an interim determination. Indeed, thorough examination of Telstra's proposed pricing construct will take considerable time and require substantive submissions from both parties. Therefore, given this, a final determination will not be made before the end of 2006.

On the other hand, the Commission is in a position to make this interim determination without delay, which will provide certainty to the parties for some time. The Commission therefore considers that it is appropriate to make the interim determination given the likelihood that a final determination will not be made in the near future.

5.5 International Treaty Obligations

The Commission considers international treaty obligations are not relevant to the issue of whether or not an ID should be made in this dispute.

6. CONCLUSION

The Commission considers that:

- the information before it provides a reasonable basis on which to make the new interim determination
- it is appropriate in all the circumstances to revoke the current interim determination and make the new interim determination.

Accordingly, the Commission has revoked the interim determination made in this dispute on 2 November 2006 on disconnection charges and replaced it with a new interim determination that also includes the LSS Annual Charges proposed in the draft ID sent to parties on 6 October 2006.

⁴⁷ Chime, Submission in response to Telstra's submission on the proposed interim determination, 3 November 2006, p. 4.

Appendix A

Document	Note on availability
ACCC, <i>Snapshot of broadband deployment as at 30 June 2006</i>	This document is publicly available on the ACCC's website
Telstra Corporation Limited (ACN 051 775 556) [2006] ACompT 4	A (public) version of this document is publicly available
ACCC, <i>Line Sharing Service – Final decision on whether or not a Line Sharing Service should be declared under part XIC of the Trade Practices Act 1974</i> , August 2002, Chapter 5	This document is publicly available on the ACCC's website
ACCC, <i>Final report on the assessment of Telstra's undertaking for the Line Sharing Service (confidential version)</i> , August 2004	A (public) version of this document is publicly available on the ACCC's website
ACCC, <i>Assessment of Telstra's ULLS and LSS monthly charge undertakings (confidential version)</i> , December 2005	A (public) version of this document is publicly available on the ACCC's website
ACCC, <i>Assessment of Telstra's LSS undertaking relating to connection and disconnection charges – final decision</i> , April 2006	A (public) version of this document is publicly available on the ACCC's website
Telstra, LSS-specific cost model	Model is not publicly available
Telstra's 'Telstra ULLS Specific Costs FINAL (ACCC).xls' model, as submitted to the Commission on 14 March 2006	Model is not publicly available
Reserve Bank of Australia, <i>F02Capital Market Yields - Government Bonds</i> , accessed 4 November 2006	Publicly available at www.rba.gov.au
Statement of <i>Telstra employee*</i> , 11 August 2006 * Telstra claims that the name of its employee should not be disclosed	Public version of this document is publicly available on the ACCC's website titled 'Specific costs input sup statement (11 Aug 06)' http://www.accc.gov.au/content/index.phtml/itemId/771159/fromItemId/743667