Access Dispute Between
Primus Telecommunications Pty Ltd (Access Seeker)
and
Telstra Corporation Limited (Access Provider)
Line Sharing Services (LSS)
Publication of Final Determination and associated statement of reasons under Section 152CRA of the *Trade Practices Act 1974*

INTRODUCTION

On 1 August 2007, the Australian Competition and Consumer Commission made a final determination in this dispute (copy appended). Having consulted the parties, the Commission has decided to publish this Final Determination and the reasons for making it. At the request of a party, commercial-in-confidence information has been redacted prior to the publication of this statement of reasons for decision.

STATEMENT OF REASONS

EXECUTIVE SUMMARY

The Commission has specified certain of the terms on which Telstra supplies the Line Sharing Service ('LSS') to Primus. These are the terms on which LSS services are connected or disconnected, either individually or as part of a 'network migration', including charges payable for service qualifications. This follows the parties being unable to agree on them, and Primus notifying the dispute for Commission arbitration.

The Commission has reduced the charges that apply when connecting or disconnecting a LSS (either individually or as part of a network migration), and also reduced the timeframes to migrate in bulk wholesale ADSL services to the LSS. The specified charges are to apply for the period from 1 February 2004 until 31 December 2007.

The charges result from applying the Commission's long–standing pricing principles for the LSS (August 2002).

1. INTRODUCTION

1.1 Purpose

Primus and Telstra have been in dispute over certain terms of access to the Line Sharing Service ('LSS'). This dispute was notified to the Commission for arbitration, and the Commission has made a final determination in that arbitration. This document sets out the reasons for making this final determination.

1.2 Background to arbitration and final determination

Primus notified the Commission of its dispute with Telstra on 21 December 2004. A case management meeting between the parties followed on 8 February 2005, with submissions on matters arising out of the meeting received on 22 February 2005. The Commission advised its views on preliminary matters on 17 March 2005. During 2005, the Commission consulted the parties on various other matters, including the appointment of Dr Paul Brooks as a technical expert to assist the Commission.

The Commission commenced consultations on an interim determination on 19 January 2006, and made an interim determination on 12 July 2006.

The parties remained unable to resolve the dispute, and the Commission commenced consultation on the making of a final determination.

The terms of access that were raised for consideration in the final determination are as follows:

1. Charges for LSS 'single' connections and disconnections
2. Terms and conditions relating to Managed Network Migrations (MNM) as follows:
   (a) LSS Connection charges for MNMs involving 50 or more services
   (b) LSS Connection charges for MNMs involving up to 20 services and between 20 and 49 services
   (c) LSS Disconnection charges where the disconnection occurs as part of a MNM
   (d) Minimum number of LSS connections as a precondition for requesting a MNM
   (e) Minimum MNM charge per exchange
   (f) MNM cancellation charges (which are referred to in the interim determinations as 'standard cancellation charges' and 'pre-jumpering cancellation charges' (also known as 'pre-wiring charges).
3. Charges for LSS service qualifications

1.3 Current Consultation Process

On 2 February 2007, the Commission commenced consultations on the making of a final determination.

The Commission first sought the parties' submissions on procedural matters, which were received on 9 February 2007 and 16 February 2007. On 7 March 2007, the Commission provided its views on these procedural matters, and also sought parties' views on further procedural matters. These submissions were received on 9 March 2007, 12 March 2007 and 14 March 2007. On 14 March 2007, the Commission notified the parties of its decision on the additional procedural matters.

Other access disputes had been notified in respect of the LSS, and there was overlap in the terms of access that were disputed. After seeking the parties' views, the Commission held a joint hearing to consider the terms of access that were commonly disputed in three LSS access disputes. This was done as it was considered that holding a joint hearing on these matters was likely to result in the disputes being resolved in a more efficient and timely manner. And so, these reasons for decision on occasion refer to submissions that were advanced by other LSS access seekers in the joint hearing. Terms of access that were in dispute in a single arbitration only were dealt with in a separate hearing involving the relevant parties.

The Commission provided to the parties a draft final determination, and an accompanying discussion paper to assist the parties in providing their submissions, on 30 March 2007. The draft final determination reflected the Commission's preliminary views pending consideration of the parties' submissions.

Following a request from Telstra, the timetable for parties' submissions was extended to 4 May 2007 (for principal submissions) and 14 May 2007 (for response submissions). Telstra also provided additional material to the Commission dated 30 May 2007, 5 June 2007, 6 July 2007 and 10 July 2007.

2. PRELIMINARY MATTERS

2.1 The Line Sharing Service ('LSS')

The LSS allows two carriers to provide separate services over a single metallic pair or line. The higher frequency part of the line is used by the access seeker to supply broadband (DSL) services, while the access provider supplies a PSTN voice service over the same line.

The LSS is a declared service. The Commission declared the LSS on 30 August 2002, pursuant to subsection 152AL(3) of the Act. A copy of the declaration was published in the *Commonwealth of Australia Gazette* No. GN41, 16 October 2002.

The LSS declaration is currently due to expire in October 2007, although the Commission may, after holding a public inquiry, determine to extend the expiry date or make a new declaration or let the declaration lapse (section 152ALA of the TPA). A public inquiry has commenced.

2.2 Access obligations and existence of dispute relating to access

The Commission sought the parties' views on whether access obligations are owed and whether a dispute exists in relation to access.

Primus is of the view that access obligations are owed, and that an access dispute exists. [Request, 4/5, p.1]

Telstra disputes that it owes access obligations on the basis of its view that Part XIC of the TPA is invalid. Subject to this claim, Telstra acknowledges that access obligations would otherwise exist, and that there is a dispute over access to the LSS. [Telstra 4/5, Pt 1, p.4].

The Commission has formed the view that, with respect to the access dispute, the requirements of subsection 152CM(1) of the Act are satisfied. That is:

- Telstra is a carrier;
- Telstra supplies the declared LSS;
- Telstra has an obligation under subsection 152AR(3) of the Act to supply the LSS to the access seeker; and
- The access seeker is unable to agree with Telstra about the terms and conditions of access to the LSS addressed in the final determination.

2.3 Whether the Commission has jurisdiction to arbitrate the access dispute

Although Telstra accepts that an access dispute exists between Primus and Telstra, Telstra refers to earlier raised concerns as to whether the Commission has jurisdiction to arbitrate the dispute. [Telstra 4/5, Pt 1, pp.3, 5]

These earlier raised concerns relate to whether the parties are 'unable to agree' on the relevant terms of access, and in particular in regards to LSS service qualification charges. Telstra raised these concerns in February 2005.

The Commission responded to these views on 17 March 2005. The Commission advised the parties that it was satisfied that a dispute existed (i.e., the parties were unable to agree) on LSS connection and disconnection charges. The Commission further advised that it was not then satisfied that the dispute that existed on LSS service qualification charges would warrant arbitration. LSS service qualifications have been addressed in the final determination as discussed later in these reasons.

The Commission continues to hold the view that a dispute exists in respect of the matters addressed in the final determination.

2.4 Whether to proceed to make a final determination

Telstra submits that the Commission should not at this time make a final determination in the arbitration, and should instead await decisions in other proceedings Telstra has commenced. These proceedings concern:

- A legal challenge to the validity of Part XIC of the *Trade Practices Act 1974* (High Court of Australia, proceedings s.42 of 2007); and,
- A review of the Commission decision to reject Telstra's most recently proposed access undertaking for the Unconditioned Local Loop Service (Australian Competition Tribunal, No.8 of 2006). [Telstra 4/5, Pt 1, pp.7, 15]

The Commission is of the view that it is appropriate for it to proceed to make a final determination in this arbitration. As previously advised to the parties, the Commission considers that it is entitled to proceed on the basis that the legislation is validly enacted. Further, the Commission considers that the consequences of suspending the arbitration (including the impact delays would be likely to have on end-users) make it inappropriate not to proceed on the basis that Telstra has commenced proceedings challenging the validity of relevant legislative provisions.

Further, the Commission does not consider that it should defer making a final determination on the terms of access to the LSS because of the ULLS proceedings commenced in the Tribunal. The Tribunal handed down its decision in the ULLS proceeding on 17 May 2007. Views expressed in those proceedings could have had some implications for the LSS also. However, in this instance, the Tribunal has provided recent views specifically on access to the LSS, and this decision has informed the Commission's approach. [*Re Telstra Corporation Ltd* [2006] ACompT 4]

3. General approach

3.1 Use of pricing principles

Introduction

The Commission has determined pricing principles for the LSS under section 152AQA of the TPA. This determination, as well as reasons for making it, is contained in ACCC, *Final Decision on whether or not a Line Sharing Service should be declared under Part XIC of the Trade Practices Act 1974*, August 2002.

The pricing principles require that prices reflect the Total Service Long Run Incremental Cost (plus a contribution to indirect cost) ('TSLRIC+) of providing access to the LSS. (ACCC, *Final Decision on whether or not a Line Sharing Service should be declared under Part XIC of the Trade Practices Act 1974*, August 2002, pp 83-84). They also require that LSS access prices should not include a contribution to costs that are recovered in other charges. (ACCC, August 2002, at pp 97-98)

The Commission is required to apply these long-standing pricing principles in determining prices to apply in respect of the LSS unless it would not be appropriate to do so. [Sub-section 152AQA(6) of the TPA] The Commission sought the parties' views on whether it should apply the LSS pricing principles.

Parties' submissions

The parties are generally supportive of the use of the LSS pricing principles. Access seekers support their use. [Chime 14/5, p.1] [Primus 14/5, p.1] [Request 14/5, p.3] Telstra also supports their use, except that it considers that LSS access prices should be averaged, and should not in any circumstances be de-averaged. That is, the same charges should always apply in each of the four geographic bands. Telstra also confirms its view that LSS access prices should include a contribution to the recovery of indirect and overhead costs. [Telstra 14/5, Part 1, pp.8-9]

Commission's views

The Commission is required to have regard to the LSS pricing principles, and considers that it should in this arbitration determine access prices for the LSS that reflect the Total Service Long Run Incremental Cost (plus a contribution to indirect cost) ('TSLRIC+') of providing access to the LSS.

A detailed discussion of the TSLRIC+ methodology, can be found in ACCC, *Access Pricing Principles – Telecommunications - a guide*', 1997.

The Australian Competition Tribunal expressed its general agreement with the approach to applying the long term interests of end-users ('LTIE') test (established by the Commission in its *Access Pricing Principles, Telecommunications – a guide*)[1] and the Commission's use of TSLRIC pricing. In the Tribunal's view, the key principles include:

> *The price of a service should not exceed the minimum costs that an efficient firm will incur in the long-run in providing the service.*
>
> *The costs are the forward-looking costs, including a normal return on efficient investment (which takes into account the risk involved).*
>
> *Forward-looking means prospective costs using best-in-use technology. The access provider should only be compensated for the costs it would incur if it were using this technology, not what it actually incurs, for*

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[1] ACCC, *Access Pricing Principles, Telecommunications – a guide* (*Access Pricing Principles Guidelines*), July 1997.

> *example in using out-of-date technology which is more costly. Of course, a firm may be using older technology because it was the best available at the time the investment was made and replacing it cannot be justified commercially. In a competitive market, however, that firm would only be able to charge on the basis of using the most up-to-date technology because, if it did not (in this hypothetical competitive market) access seekers would simply take the service from an alternative service provider.*
>
> *The cost of providing the service should be the cost that would be avoided in the long-run by not having to provide it. Thus, it is the additional or incremental costs necessarily incurred, assuming other production activities remain unchanged.*[2]

Further, the Tribunal noted that '… in the general case where access prices need to be regulated, unless pricing is on a TSLRIC basis, efficient investment is unlikely to be encouraged.'[3] The Commission notes that the Tribunal went on to state that:

> *This discussion should not be taken to suggest that TSLRIC pricing should be imposed at every opportunity. It will often be the case that regulation, including regulated pricing, is not appropriate in given circumstances. It does mean, however, that, in our view, it would generally not be in the LTIE to depart from TSLRIC pricing where access is regulated. Accordingly, where an access regime requires, or creates an unacceptable risk, of non-TSLRIC pricing, the Tribunal considers that such a regime is unlikely to encourage the efficient use of, and investment in, infrastructure.*[4]

Similarly, the Tribunal has also stated that, in respect of the LSS, a proper application of the criteria relevant to the assessment of an access undertaking (and which significantly overlap with the section 152CR(1) criteria) would require that prices reflect the efficient costs of providing access to the LSS:

> *. . . we would point out that whenever an access provider seeks approval of an access undertaking from the Commission which involves a consideration of a price term by comparing it with costs, it would be necessary, in order to satisfy the statutory framework, that the access provider establish that its costs are efficient costs.*[5]

The LSS pricing principles require that access prices should be de-averaged. In considering LSS access prices in other regulatory decisions, the Commission has acknowledged that, in practice, an average access price can be appropriate where the distortionary effect of averaged prices is not likely to be material. That is, where the TSLRIC+ of supplying the LSS does not vary materially between geographic bands. [ACCC, *Assessment of Telstra's LSS undertaking relating to connection and disconnection charges, Final decision*, April 2006, at pp: 56-57]

The Commission remains of the view that LSS access prices should be de-averaged except where the distortionary effect of an average LSS access price is not likely to be material. Whether an averaged access price is likely to cause a material distortion is a matter discussed below in considering LSS connection and disconnection charges, and charges associated with LSS managed network migrations.

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2 *Seven Network Limited (no 4)* [2004] ACompT 11 at [135].

3 ibid., at [136].

4 ibid., at [137].

5 *Re Telstra Corporation Ltd* [2006] ACompT 4 at para 46

3.2 Relevant legislation

Introduction

The Commission sought the parties' advice on legislation that is relevant to the making of the final determination.

Parties' submissions

The parties identify Part XIC of the TPA, and Division 8 of this Part in particular, as relevant to the making of the final determination.

Telstra submits that the Utilities (Network Facilities Tax) Act 2006 (ACT), and any legislation of a similar purpose that may be passed in future in other states, is also relevant to the final determination. [Telstra 14/5, Pt 1 page 14]

Primus submits that it is not aware of other States passing an Infrastructure Tax Act, and disputes that the ACT legislation could have a material bearing on costs for the LSS. Primus also points to the existence of carrier immunities from certain State laws under the Telecommunications Act as providing a possible shield from the ACT charges. [Primus, 14/5, Part 1, p.6]

Commission's views

The Commission considers that Part XIC of the TPA is relevant to the making of the final determination. The Commission considers that the following sections are of direct relevance to the making of a final determination:

- Section 152CP(1) of the Act, which provides that unless the Commission terminates the arbitration, the Commission must make a written determination on access by the access seeker to the declared service.
- Section 152CP(2) of the Act, which provides that the determination may deal with any matter relating to access by the access seeker to the declared service, including matters that were not the basis for notification of the dispute.
- Section 152CP(4) of the Act, which requires that before making a determination, the Commission must give a draft determination to the parties.
- Section 152CP(5) of the Act, which requires that when the Commission makes a determination it must give the parties to the arbitration its reasons for making the determination.
- Section 152CQ of the Act, which sets out restrictions on access determinations.
- Section 152CR(1) of the Act, which requires that in making a final determination, the Commission must take certain matters into account. :
- Section 152CR(2) of the Act, which provides that the Commission may take into account any other matters that it thinks are relevant.
- Section 152DNA of the Act, which concerns backdating and interest.
- Section 152AQA(6) of the Act, which requires that the Commission must have regard to a pricing principles determination (made in accordance with section152AQA(1)) if the Commission is required to arbitrate an access dispute under Division 8 in relation to the declared service.

The Commission considers that the *Utilities (Network Facilities Tax) Act* 2006 (ACT) could potentially be relevant to the setting of LSS access prices, to the extent that Telstra is liable to a charge under that Act, and that any such cost relates to Telstra's supply of the LSS. However, it is uncertain that these conditions are satisfied.

Further, Telstra has not made a cost claim in respect of any liability arising under this Act, but rather seeks the ability to require access seekers to make unspecified contributions should a liability accrue in future. The Commission does not consider that this would be appropriate, as it denies access seekers certainty as to the charges that they face for using the LSS and impedes competition, and is unnecessary to ensure cost recovery. Accordingly, the Commission has not specified in the final determination that liabilities under the ACT Act should be passed-through.

Further, given that the expiry date of the final determination is relatively soon (as discussed below), the Commission does not consider that it is necessary to make allowance for the possible introduction of other laws to which Telstra may become liable in respect of its supply of the LSS.

3.3 Section 152CR(1) criteria

Introduction

The Commission must have regard to the criteria specified in section 152CR(1) of the TPA in making a final determination. These criteria are:

a. whether the determination will promote the long term interests of end-users (LTIE) of carriage services or of services supplied by means of carriage services;

b. the legitimate business interests of the carrier or provider, and the carrier's or provider's investment in facilities used to supply the declared service;

c. the interests of all persons who have rights to use the declared service;

d. the direct costs of providing access to the declared service;

e. the value to a party of extensions, or enhancement of capability, whose cost is borne by someone else;

f. the operational and technical requirements necessary for the safe and reliable operation of a carriage service, or a telecommunications network or a facility;

g. the economically efficient operation of a carriage service, a telecommunications network or a facility.

The Commission provided the parties with draft views on how these criteria should be interpreted and sought the parties' comment.

Section 152CR(1)(a) Whether the determination will promote the long-term interests of end-users (LTIE) of carriage services or of services supplied by means of carriage services

Parties' submissions

Telstra considers that in order for the final determination to promote the long term interests of end-users (LTIE), the final determination should ensure that Telstra's costs will be recovered in both the short-term and long-term. Telstra considers that access prices that are too low would also fail to promote the LTIE, as they would deter Telstra from investing in its facilities, and will also deter carriers from investing in competing facilities where it would be efficient to do so. Telstra also cautions that prices for the LSS can affect demand for the ULLS, and lead to carriers choosing the LSS in circumstances where this will lead to higher costs of supply. [Telstra 14/5, Part 1, pp.10-11] Telstra also submits that incentives for it to invest in a fibre to the node network (FTTN) should also be considered. [Telstra, 14/5, Part 2, p.2]

Access seekers consider that charges that reflect the efficient cost of supplying the LSS will best promote the LTIE, and consider regard should be had to the likely effect of access charges on the supply of downstream services.

Each access seeker identifies broadband (DSL) services as a relevant downstream service. Chime also refers to the possible effect of LSS access prices on downstream voice services (voice over internet protocol supplied over an LSS).

Access seekers consider regard should be had to investment in DSLAM networks [Primus 14/5, p.2] [Request 14/5, pp.3-7] [Chime pp.2-3, 9], and for efficient use of and investment in access networks. Access seekers contend that LSS access charges that are too high could lead to inefficient duplication of access networks (such as would be the case if suppliers were required to deploy a by-pass access network, or use an entire copper pair to supply DSL to end-users). [Chime 18/5, p.3] [Primus 14/5, p.3] [Request 21/5, p.6]

Commission's views

The Commission has published a guideline explaining what it understands by the phrase 'long-term interests of end-users' in the context of its declaration responsibilities.[6] The Commission considers that a similar interpretation is appropriate to making a final determination in this arbitration.

In the Commission's view, particular terms and conditions promote the interests of end-users if they are likely to contribute towards the provision of goods and services at lower prices, higher quality or towards the provision of greater diversity of goods and services.

The Commission also notes that the Tribunal has offered guidance in its interpretation of the phrase 'long term interests of end-users' (in the context of access to subscription television services):

> *Having regard to the legislation, as well as the guidance provided by the Explanatory Memorandum, it is necessary to take the following matters into account when applying the touchstone – the long-term interests of end-users:*
>
> **End-users: "end-users" include actual and potential [users of the service] …*
>
> **Interests: the interests of the end-users lie in obtaining lower prices (than would otherwise be the case), increased quality of service and increased diversity and scope in product offerings. …[T]his would include access to innovations … in a quicker timeframe than would otherwise be the case …*
>
> **Long-term: the long-term will be the period over which the full effects of the … decision will be felt. This means some years, being sufficient time for all players (being existing and potential competitors at the various functional stages of the … industry) to adjust to the outcome, make investment decisions and implement growth – as well as entry and/or exit – strategies.*[7]

As explained further below, the Commission considers that LSS access prices that reflect the efficient (as opposed to actual) cost of supplying the LSS will best promote the LTIE.

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6 ACCC, *Telecommunications services — Declaration Provisions: A Guide to the Declaration Provisions of Part XIC of the Trade Practices Act*, July 1999.

7 *Seven Network Limited (no 4)* [2004] ACompT 11 at [120].

To consider the likely impact of particular terms and conditions on the LTIE, the Act requires the Commission to have regard to whether the terms and conditions are likely to result in:

- promoting competition in markets for carriage services and services supplied by means of carriage services;
- achieving any-to-any connectivity; and
- encouraging the economically efficient use of, and economically efficient investment in:
  - the infrastructure by which listed carriage services are supplied; and
  - any other infrastructure by which listed services are, or are likely to become, capable of being supplied.[8]

In determining the extent to which terms and conditions are likely to result in the objective of promoting competition, regard must be had to the extent to which the terms and conditions will remove obstacles to end-users of gaining access to listed services.[9]

The Commission considers that, in assessing whether particular terms and conditions will promote competition, it is relevant to consider markets in which DSL services are supplied (retail and/or wholesale), and to consider whether the terms and conditions will remove obstacles to end-users gaining access to DSL services.

This is because the LSS is an input to the provision of carriage services on the non-voiceband frequency spectrum of the line, and this spectrum is typically used to provide DSL services. This approach is consistent with the approach adopted by the Australian Competition Tribunal. (Re Telstra Corporation Ltd ACompT 4 [2006] at [97], [149])

Obstacles to accessing DSL services could be in the nature of DSL infrastructure not being available in the end-user's area, or the price of services that are available being too high, or their quality (measured by reference to, for instance, data transfer rates) being too low.

It is also possible that service providers will offer voice over internet protocol services over an LSS. However, the Commission does not consider that, over the period to which the final determination relates, the LSS will be commonly used in order to supply voice over internet protocol services. This is due to the specification that Telstra is only obliged to supply the LSS where a PSTN voice service is already being supplied on the line. While this does not preclude a VoIP service also being supplied to the end-user, it does limit the value to end-users of competing VoIP services supplied over the LSS, and reduces the class of end-users for whom such services would be attractive. This is because line rental charges would not be avoided.

The Commission considers that prices that reflect efficient forward-looking costs of supply will best promote effective competition in the supply of broadband/DSL services. This is because such prices best enable access seekers to compete on an equal footing with other suppliers, including the access provider, in the supply of downstream DSL services.

The Commission considers that the terms of access addressed in this final determination do not directly affect the objective of achieving any-to-any connectivity.

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8 *Trade Practices Act 1974*, section 152AB(2).

9 ibid., section 152AB(4).

In determining the extent to which terms and conditions are likely to result in the achievement of the objective of encouraging the economically efficient use of and investment in infrastructure, regard must be had to:

- whether it is technically feasible for the services to be supplied and charged for with regard to technology that is in use, available or likely to become available; and the costs involved in supplying and charging for, the services that are reasonable or likely to become reasonable; and the effects or likely effects that supplying and charging for the services would have on the operation or performance of telecommunications networks;
- the legitimate commercial interests of the supplier or suppliers of the services, including the ability of the supplier or suppliers to exploit economies of scale and scope;
- incentives for investment in the infrastructure by which services are supplied; and any other infrastructure by which services are or likely to become capable of being supplied; and
- the risks involved in making the investment.[10]

In the Commission's view, the phrase 'economically efficient use of, and economically efficient investment in ... infrastructure' refers to the concept of economic efficiency that consists of three components:

- Productive efficiency – This is achieved where individual firms produce the goods and services that they offer at least cost;
- Allocative efficiency – This is achieved where the prices of resources reflect their underlying costs so that resources are then allocated to their highest valued uses (i.e. those that provided the greatest benefit relative to costs); and
- Dynamic efficiency – This reflects the need for industries to make timely changes to technology and products in response to changes in consumer tastes and in productive opportunities.

The Commission considers that it is relevant to here consider use of, and investment in, infrastructure used to supply the LSS (e.g, ordering and provisioning systems and access networks), as well as infrastructure used to supply carriage and/or content services over the LSS, e.g., DSL access multiplexers ('DSLAMs'). This is consistent with the approach adopted by the Australian Competition Tribunal. (Re Telstra Corporation Ltd ACompT 4 [2006] at [104])

Again, the Commission considers that access charges that reflect the efficient, forward-looking costs best meet these considerations. Such charges are consistent with the access provider's legitimate commercial interests and, in particular, enable access providers to exploit economies of scale and scope. These charges also provide correct incentives for the access provider and access seekers to make efficient investments in infrastructure used to supply the LSS and downstream services. By promoting competition, these charges also encourage dynamic efficiency.

3.3.2 Section 152CR(1)(b) The legitimate business interests of the access provider, and the carrier's or provider's investment in facilities used to supply the declared service

Parties' submissions

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10 *Trade Practices Act 1974*, section 152AB(6) and (7A).

Telstra emphasises that it is legitimate for it to seek to earn a normal commercial return on its investment, and that this requires that access prices enable cost recovery plus a return on investment that is commensurate with risk. [Telstra 14/5, Part 1, p.11]

Access seekers submit that it is a legitimate interest for the access provider to receive a normal commercial return, but that higher returns would not be legitimate. [Primus 14/5, p.3] [Chime 14/5, p.3] Request also submits that, under this criterion, it is only forward-looking efficient costs that should be considered. [Request 14/5, p.8]

Commission's views

As outlined in the Commission's *Access Dispute Guidelines*, the Commission considers it is a legitimate interest for an access provider to earn a normal commercial return on its investment.[11] In this regard, the Commission is of the view that the concept of 'legitimate business interests' should be interpreted in a manner consistent with the phrase 'legitimate commercial interests' used elsewhere in Part XIC of the TPA.

For completeness, the Commission notes that it would be a legitimate interest for an access provider to seek to recover its costs as well as a normal commercial return on investment having regard to the relevant risk involved.

The Commission further notes that an access price should not be inflated to recover any profits the access provider (or any other party) may lose in a dependent market as a result of the provision of access.[12]

Similarly, the Australian Competition Tribunal has stated that:

> *The expression "legitimate business interests" is a general expression and is somewhat open-textured. What is "legitimate" conduct or a "legitimate" interest in business may be open to a number of differing interpretations. We consider that a carrier's "legitimate business interests" is a reference to what is regarded as allowable and appropriate in commercial or business terms. In the context of s 152AH(1)(b), the expression connotes something which is allowable and appropriate when negotiating access to the carrier's infrastructure. When looked at through the prism of a charge term and condition of access and its relationship to a carrier's cost structure, it is a reference to the interest of a carrier in recovering the costs of its infrastructure and its operating costs and obtaining a normal return on its capital. (Re Telstra Corporation Ltd [2006] ACompT 4 at [89])*

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[11] ACCC, *Resolution of telecommunications access disputes – a guide (Access Dispute Guidelines)*, March 2004 (Revised), p. 56.

[12] ACCC, *Access Pricing Principles Guidelines*, p. 10.

3.3.3 Section 152CR(1)(c) the interests of all persons who have the right to use the service

Parties' submissions

In Telstra's view, the class of persons who have rights to the LSS includes persons with 'indirect rights' to use the LSS such as end-users that purchase a retail service from Telstra. [Telstra 14/5, Part 1, p.12] Telstra further submits that it is the interests of the entire class, and not those of a single acquirer of LSS, that should be had regard to. [Telstra 14/5, Part 1, p.3]

Request submits that the main interest of persons with rights to use the LSS is their interest in being able to compete in the supply of downstream services. Request considers this interest is best served by access prices that reflect efficient, forward-looking costs. [Request 14/5, p.8] Chime and Primus also submit that such pricing will promote the interests of these persons. [Chime 4/5, p.3] [Primus 4/5 p.3]

Primus further submits that the criterion calls for a consideration of the rights of access seekers. However, in its view, proper regard for these rights would also promote the interests of all retail customers of downstream services. [Primus 14/5, Part 1, p.4]

Commission's views

The Commission notes Telstra's submission concerning Telstra's retail customers having rights to indirectly use line sharing by acquiring a retail service. While the Commission agrees that retail services supplied to end-users involve the use of line sharing, it does not consider that this gives them a right to use the LSS. The Commission considers that it is only LSS access seekers that the criterion contemplates. The interests of end-users are already to be considered under other criteria.

The Australian Competition Tribunal has also provided views on this criterion (in assessing whether an approach that led to a higher LSS Annual Charge should be adopted):

> *s 152AH(1)(c) requires us to have regard to the interests of persons who have rights to use Telstra's LSS, that is, access seekers. . . A higher monthly charge would not be in the interests of an access seeker because it would raise its costs and inhibit its ability to compete with Telstra over the provision of retail services to end-users that could be provided using the LSS. (Re Telstra Corporation Ltd [2006] ACompT 4 at [91])*

As noted in the *Access Dispute Guidelines,* people who have rights to currently use a declared service will generally use that service as an input to supply carriage services, or a service supplied by means of carriage services, to end-users. In the case of the LSS, the access service could also be used to provide a wholesale service to another service provider.

The Commission considers that this class of persons has an interest in being able to compete for the custom of end-users on the basis of their relative merits. Terms and conditions that favour one or more service providers, including the access provider, over others and thereby distort the competitive process may prevent this from occurring and consequently harm those interests.[13]

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[13] ACCC, *Resolution of telecommunications access disputes – a guide,* (*Access Dispute Guidelines*), p. 57.

3.3.4 Section 152CR(1)(d) the direct cost of providing access to the declared service

Parties' submissions

Telstra refers to the Tribunal's views expressed in *Re Telstra Corporation Ltd* [2006] ACompT 4 and *Application by Optus Mobile Pty Limited and Optus Networks Pty Limited* [2006] ACompT 8 that this criterion is concerned with ensuring that the costs of providing the service are recovered. Further, that the term 'direct costs' includes a contribution to the indirect costs associated with providing access, i.e., fixed and common costs, Lastly, the appropriate cost concept to have regard to here is the long-run, such that distinctions between fixed and variable cost are not relevant. [Telstra 14/5, Part 1, p.13]

Request submits that cost-based access prices are consistent with the criterion, and that it is long-run costs that should be considered. Request is of the view that efficiently incurred costs should be considered, arguing that TSLRIC methodology is the best way to derive cost-based charges. [Request 4/5, p.9] Primus is also of the view that prices should reflect the costs of an efficient operator. [Primus 4/5, p.3] Chime identifies incremental costs only as being relevant under this criterion. [Chime 4/5, p.3]

Commission's views

The Commission considers that the direct costs of providing access to a declared service are those incurred (or caused) by the provision of access, and includes the incremental costs of providing access.

Consistent with the Tribunal's view, the Commission has interpreted this criterion, and the use of the term 'direct costs', as not excluding consideration being given to a contribution to indirect costs. (*Application by Optus Mobile Pty Limited and Optus Networks Pty Limited* [2006] ACompT 8 at [137]) A contribution to indirect costs can be supported by other of the criteria also.

However, the criterion does not extend to permitting compensation for loss of any 'monopoly profits' that occurs as a result of increased competition.

In this regard, the *Explanatory Memorandum for the Trade Practices Amendment (Telecommunications) Bill 1996* states:

> *... the 'direct' costs of providing access are intended to preclude arguments that the provider should be reimbursed by the third party seeking access for consequential costs which the provider may incur as a result of increased competition in an upstream or downstream market.*[14]

The Commission also notes the Tribunal considers the direct costs criterion 'is concerned with ensuring that the costs of providing the service are recovered.'[15]

More recently, the Tribunal has noted that direct costs could conceivably be allocated (and hence recovered) in a number of ways, and that adopting any of those approaches would be consistent with this criterion.

> *Telstra's approach to estimating a per unit cost is likely to be consistent with ensuring recovery only of direct costs. However, while direct costs will be incurred by Telstra in order to provide the declared service, there are a number of cost allocation methods other than that adopted by Telstra (including those suggested by the Commission and other interveners in this*

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14 *Explanatory Memorandum for the Trade Practices Amendment (Telecommunications) Bill 1996*, p. 44.

15 *Telstra Corp Ltd [2001]* ACompT 4 (7 Dec 2001) at paragraph 92.

matter) that would enable it to recover the direct costs of investment in infrastructure necessary to provide a LSS. (Re Telstra Corporation Ltd [2006] ACompT 4 at [139]

3.3.5 Section 152CR(1)(e) the value to a party of extensions, or enhancement of capability, whose cost is borne by someone else

Parties' submissions

Telstra and Primus raised this criterion as relevant to certain costs associated with the LSS. The other parties did not comment on this criterion.

Primus considers that correction of Telstra's cable records was of value to Telstra, but that Primus was bearing the cost of making these corrections. [Primus 4/5, p.4] Telstra considers that the development of different procedures for the connection or disconnection of LSS as part of a managed network migration was of value to access seekers, and it had borne this development cost. [Telstra 14/5, Part 1, p.3]

Commission's views

The Commission has previously noted its view that:

> *This criterion requires that if an access seeker enhances the facility to provide the required services, the access provider should not attempt to recover for themselves any costs related to this enhancement. Equally, if the access provider must enhance the facility to provide the service, it is legitimate for the access provider to incorporate some proportion of the cost of doing so in the access price.*[16]

The Commission remains of this view, and has applied this approach in setting access prices in the final determination.

3.3.6 Section 152CR(1)(f) the operational and technical requirements necessary for the safe and reliable operation of a carriage service, or a telecommunications network or a facility

Parties' submissions

Telstra considers that this criterion can be relevant to setting access prices as operational and technical requirements can have cost implications, and access prices should permit the recovery of costs that are necessarily incurred to meet these requirements. [Telstra 14/5, Part 1, pp.12-13] Primus is also of the view that terms of access should reflect safe and reliable work practices. [Primus 4/5, p.4]

Commission's views

The Commission considers that this criterion requires that terms of access should not compromise the safety or reliability of carriage services and associated networks or facilities, and that this has direct relevance when specifying technical requirements or standards to be followed.

The Commission suggested to the parties that this criterion is generally unlikely to be relevant to disputes relating only to the price of access to a service. This is because the access price will have little direct bearing on the adoption of operational and technical requirements necessary for the safe and reliable operation of a carriage service, or a telecommunications network or a facility. However, this criterion may be more relevant to non-price terms and conditions attaching to the supply of the LSS that are in dispute (if any).

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16 ACCC, *Access Pricing Principles Guidelines*, p. 11.

That said, the Commission acknowledges that, in the long-run, access prices that are persistently below the efficient costs of supplying a service can, indirectly, compromise the safe and reliable supply of the service. Accordingly, the Commission considers that efficient costs should be based upon a method of supply of the LSS that meets the relevant operational and technical requirements necessary for the safe and reliable operation of the LSS and facilities used to supply the LSS.

3.3.7 Section 152CR(1)(g) the economically efficient operation of a carriage service, a telecommunications network or a facility

Parties' submissions

Telstra submits that the criterion requires a balancing of interests, and that proper regard to this criterion means that access prices should not be set at a level that is below cost. [Telstra 4/5, Part 1, p.13] Telstra considers that investment in the infrastructure that underlies the LSS is promoted by access charges that are based on efficient costs, but cautions that access charges that do not permit it to recover its costs will deter it from making investments. [Telstra 14/5, Part 1, p.5]

Access seekers raise for consideration the services, networks and facilities of both the access provider and the access seeker. They also conclude that access prices based on forward-looking efficient costs are required by this criterion. [Chime 4/5, p.4] [Primus 4/5, p.4]

Chime and Primus submit that access charges that are too high will impede efficient investment by both Telstra and access seekers, and lead to under-utilisation of infrastructure used to supply services. [Chime 18/5, p.4] [Primus 14/5, Part 1, p.5]. Chime states that the LSS annual charges that applied up until the making of the interim determination contributed to it being unable to invest more in the network it uses when supplying DSL and VoIP over the LSS. [Chime 18/5, pp.6-7]

Commission's views

As noted in the Commission's *Access Dispute Guidelines,* the phrase 'economically efficient operation' embodies the concept of economic efficiency as discussed earlier under the LTIE. That is, it calls for a consideration of dynamic, productive and allocative efficiency. [17]

Further, consistent with the approach adopted by the Tribunal, the Commission considers that in applying this criterion, it is relevant to consider:

- the economically efficient operation of downstream services provided by access seekers using Telstra's LSS, or by Telstra itself in competition with those access seekers; and,
- the telecommunications networks and infrastructure used to supply these services. (Re Telstra Corporation Ltd [2006] ACompT 4 [94-95])

The *Access Dispute Guidelines* note that in the context of a determination, the Commission may consider whether particular terms and conditions enable a carriage service, telecommunications network or facility to be operated efficiently. The Commission considers that, in the context of access prices, prices that reflect the efficient forward-looking costs of the service best meet this criterion.

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[17] ACCC, *Access Dispute Guidelines*, p. 57.

3.4 Additional matters and information to which the Commission intends to have regard in making the final determinations

Section 152CR(2) of the TPA allows the Commission to have regard to additional matters. The Commission sought the parties' views on whether it should have regard to additional matters.

The parties nominated decisions of the Australian Competition Tribunal, the pricing principles, previous decisions made by the Commission in respect of Telstra's LSS access undertakings and the ACT Infrastructure Tax Act and the possibility of similar legislation eventuating in other jurisdictions. [Telstra 4/5, Part 1, p.14] [Request 4/5, p.10] [Primus 4/5, p.4] [Chime 4/5, p.4]

The Commission has had regard to these additional matters. For completeness, the Commission also has had regard to the various documents and matters that are referred to in this statement of reasons.

3.5 Period to which the final determination should apply

3.5.1 Commencement date

Introduction

The provisions of a final determination (either all or some) may be expressed to take effect earlier than the date on which the determination takes effect, provided that this date is no earlier that the date on which the parties commenced negotiations with a view to agreeing on the terms and conditions of access (s. 152DNA(2)).

The Commission proposed to backdate certain of the terms of access in dispute to the date of notification of the access dispute. The Commission advised the parties that it would consider backdating to an earlier time where it could be established that the parties commenced negotiations at a time materially earlier than the date of notification. The Commission sought the parties' views.

Parties' submissions

Telstra submits that backdating is not appropriate because:

(a) it would not promote the rationale for backdating (which it describes as removing incentives to delay arbitrations), as Telstra's conduct has not been a cause for delay in the arbitration;

(b) an interim determination was made in the dispute, negating the need for backdating; and

(c) backdating would otherwise not be in the LTIE. [Telstra 4/5, Part 3, p 14]

In the alternative, Telstra submits that the commencement date should be no earlier than the date of notification because:

(a) it would be impossible to determine with certainty the dates on which negotiations between Telstra and each of the parties began in respect to each of the different issues, and

(b) it would be highly unfair to backdate to an earlier date in light of the lengthy arbitrations which have ensued due to delays which have not been in Telstra's control.

Telstra claims that some of the issues in dispute were not included in a party's notification, and that it would be contrary to section 152DNA(2) to backdate related terms and conditions to a time earlier than the date on which such issues were introduced into the dispute. [Telstra 4/5, Part 3, p 15]

Telstra also submits that it had made numerous reasonable offers to Primus *[c-i-c redaction]* including offers made before it commenced supplying the LSS to

Primus. *[end c-i-c redaction]* These offers were made in good faith and the charges in them reflected Telstra's estimated direct costs at the time at which they were made. Further, Telstra continued to seek to negotiate with Primus throughout the period of the arbitration. The delays that did occur, Telstra considers, were due to Primus and the Commission. Under such circumstances, Telstra submits, it would be unfair for the Commission to decide to backdate. [Telstra 14/5, Part 5, pp.1-6]

Primus submits that it is appropriate to backdate the price-related terms because:

(a) it considers that Telstra was reluctant to negotiate,

(b) it believes that backdating would create an incentive for Telstra to negotiate reasonably in the future, and

(c) backdating would recompense Primus for the amounts it has overpaid and the business opportunities lost through not having access to the excess funds paid to Telstra.

Primus argues that the Commission should backdate to when negotiations first began; or the date of first supply where this occurred after negotiations commenced. Primus submits that while negotiations concerning the terms of Primus's access to the LSS commenced earlier, the appropriate commencement date of the final determination is 1 February 2004 [Primus 4/5, pp 4-6].

Primus also submits that Telstra has significant commercial reasons for delaying the progress of arbitrations and has done so. Further, Primus contends that an interim determination is not an alternative to backdating of a final determination; and that backdating is to encourage Telstra to set reasonable terms of access sooner, and could not be described as a punishment. Lastly, Primus advises that it does not seek backdating for service qualification charges. [Primus 14/5, Part 1, p 5; Part 3, pp 6-8; Part 4, p.5; Primus, Part 6, p.2]

Commission's views

The Commission is required to formulate guidelines about its approach to backdating (s. 152DNA(8)), and to have regard to those guidelines, as well as any such matters as the Commission considers relevant (s.152DNA(7)).

The guidelines are set out in sections 7.4.2 to 7.4.6 of the Commission's Telecommunications Dispute Resolution Guidelines.

As noted in the explanatory memorandum the backdating provisions are intended to:[18]

> *...encourage commercial agreement and co-operation during access arbitrations by removing incentives for delay and to ensure a considered and reasonable outcome is ultimately applied to the interim period which may otherwise be covered by an interim determination or a commercial agreement which one or more parties may be disputing.*

Consistent with this, the guidelines aim to improve incentives to reach commercial agreement and co-operate during access arbitrations.

The guidelines provide that the Commission will, in general, be inclined to backdate determinations. However, each case will be considered on its merits. In particular, the Commission is likely to consider whether the manner in which the parties have conducted themselves before and during the arbitration provides grounds for not backdating the determination.

[18] Supplementary explanatory memorandum for the Telecommunications Legislation Amendment Bill 1998, p. 33.

If, for example, prior to the notification of the dispute the access provider offered the access seeker price and non-price terms and conditions that are substantially similar to those determined by the Commission and the access seeker refused, then it may not be appropriate to backdate. Similarly, if the access seeker has been tardy in responding to offers put forward by the access provider, then it may not be appropriate to backdate to the start of negotiations.

The Commission considers that Telstra and Primus have been in dispute regarding LSS 'single' connections and disconnections and MNM charges since at least 1 February 2004, when Telstra commenced supply of the LSS to Primus.

Prior to the notification of the dispute, Telstra did not offer Primus terms of access substantially similar to those that have now been determined by the Commission. Nor does the Commission consider that Primus delayed in responding to offers put forward by Telstra, or acted to delay the arbitration.

The Commission does not consider that the making of an interim determination means that it should not backdate in this instance.

Consequently, the Commission has determined to backdate the terms for LSS 'single' connections and disconnections and MNM connection charges to 1 February 2004, when Telstra first supplied the LSS service to Primus. The parties did not seek backdating of LSS service qualification charges.

The Commission did not backdate the other MNM terms that are addressed in the final determination as it did not consider that doing so would have a practical effect (forecasting timeframes, migration plan amendment terms, minimum numbers of services to connect, minimum exchange charge, and disconnection charge), and/or because it did not consider that they should take effect prior to being advised to the parties (MNM cancellation charges).

3.5.2 Expiry date

Introduction

A provision of a determination may be expressed to terminate on a specified date (s. 152DNA(4)). Although not currently a requirement of the legislation, the Commission would usually expect to limit the duration of a determination to a certain period in this way. The Commission proposed to the parties an expiry date for the final determination of 31 December 2007, and sought the parties' views.

Parties' submissions

Primus submits that 30 June 2008 is an appropriate expiry date for all provisions of the final determination. Primus points to the duration of the current dispute, and anticipates difficulties in obtaining either a negotiated agreement with Telstra or an arbitrated outcome for the period following the final determination's expiry. [Primus 4/5, p 6].

Telstra did not object to the expiry date that the Commission proposed. [Telstra, 4/5, Part 3, p.17; Part 4, p.15] In response, Telstra refers to previously expressed concerns should the expiry date extend beyond the current expiry date of the LSS declaration (31 October 2007). [Telstra 14/5, Response to Primus, Part 5, p.7].

Commission's views

The Commission has decided to maintain the position proposed to the parties, and to specify an expiry date for the final determination of 31 December 2007.

Section 152DNC of the Act provides that a final determination can continue to operate notwithstanding the expiry of a declaration. Further, the LSS declaration could be extended, or the LSS could be re-declared. As such, the Commission does not consider that it should restrict the expiry of the final determination to no later than the current expiry date of the LSS declaration.

The Commission considers that an expiry date of 31 December 2007 will provide an adequate overlap between the finalisation of the inquiry into the future regulation of the LSS (that the Commission is conducting ahead the 31 October 2007 expiry date of the LSS declaration).

The terms of this final determination, and the Commission's finding in the LSS inquiry should provide a reasonable basis for the parties to reach a negotiated outcome for access to the LSS from 1 January 2008.

The Commission does not consider that a later expiry date would be appropriate as there is the potential for the outcome of this inquiry (which will include a review of the associated pricing principles) to suggest that the current regulatory approach to LSS pricing may not remain appropriate for the period beyond 31 December 2007.

3.5.3 Interest

Introduction

Section 152DNA(6) of the TPA provides the Commission with a discretion to require interest to be paid in instances of backdating at a rate specified in the determination. The Commission proposed to the parties that interest should be included on under or over payments, and suggested this be at the Reserve Bank of Australia (RBA) Large Business Variable Indicator Rate. The Commission sought the parties' views.

Parties' submissions

Consistent with its views on backdating, Telstra submits that interest should not be imposed [Telstra 4/5, Part 1, p 15].

Telstra further states that in regards to connections and disconnections, Telstra has made several attempts to negotiate with the parties on a commercial level and that the only purpose of interest charges would be to 'punish' Telstra. Telstra also claims that the opportunity cost to access seekers associated with any overpayments would be minimal, as the costs to access seekers of connecting the LSS have decreased over the period the dispute has continued. [Telstra 4/5, Part 4, p 14]

In its response submission, Telstra submits that a backdated payment that includes interest would be inappropriate, as Telstra did not fail to negotiate acceptable charges reflective of cost, and the long period of arbitration. In the alternative, Telstra submits:

- the 90-day bank bill rate is the appropriate rate, and not an internal rate of return that may be used for business planning,
- interest should be payable from the interim determination date of 12 July 2006, and
- interest should not be compounded. [Telstra 14/5, Response to Primus, Part 5, p.8]

Primus considers that the backdated payment should include an interest component so as to ensure that Telstra does not benefit from the delays in resolving the dispute. [Primus 4/5, pp 6-7] Initially Primus proposed that:

- the interest rate should be that applicable to debt financing, as determined by the Reserve Bank of Australia Large Business Variable Indicator Rate; and

- interest is to be calculated on the amounts of money overpaid to Telstra for each of the disputed price terms, commencing from the date on which the overpayments were made, and finishing 21 days after the final determination is made.

Primus also submitted that a higher interest rate should apply; either an internal rate of return of around 15% should be used, or else the *[c-i-c redaction]* rate specified in the customer relationship agreement with Telstra for late payments, or overpayments, should be used. *[end c-i-c redaction]* [Primus 14/5, Part 3, p.11]

Commission's views

Under section 152DNA(7) of the TPA, the Commission is required to have regard to its guidelines and such other matters as it considers relevant in determining whether or not interest should be charged.

The *Access Disputes Guidelines* provide that the Commission 'will generally' provide for the payment of interest on 'backdated amounts' (the amounts underpaid or overpaid by an access seeker having regard to the charges and the period of backdating that are specified in the final determination).[19] The interest component is used in conjunction with backdating to remove the incentive for delay.

However, the Commission evaluates interest on a case-by-case basis and does not consider that interest is automatically payable in every circumstance in which backdating of a final determination occurs.

As specified in the Guidelines, where interest is to be paid, it will be calculated on the amounts of money that have been overpaid (or underpaid), and will usually be calculated by reference to;

- the volume of services supplied by the access provider to the access seeker over the backdating period; and,
- the charges that that are specified in the final determination.

Further, the rate of interest should reflect the opportunity cost of the overpayment (or underpayment) and, in general, daily compounding will be appropriate. Lastly, the guidelines also suggest that the opportunity cost could be assessed by reference to the rate applicable to debt financing.

In the current arbitration, the Commission considers that it is appropriate to specify that interest is charged on the overpayments that have occurred. Given the time value of money, the access seeker would be denied the full benefit of the determination in the absence of an award of interest.

Consistent with the approach suggested by the guidelines, the Commission has specified that the RBA's Large Business Variable Indicator Rate should be used to calculate interest, and interest shall be charged on a daily basis and compounded. Interest is to be paid from the date of each overpayment, and ending 21 days after the final determination is made.

The Commission considered the parties alternative rates of interest. The Commission was not satisfied that all overpayments would necessarily have been used to fund long-held investments, as opposed to being used to meet expenses or retire existing debt, or that any such investments would in fact yield a rate of return of around 15% per annum. The 90 day bank bill rate does not represent the opportunity cost of money to the access seeker.

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19 ACCC, *Access Dispute Guidelines*, p. 63.

Use of the contractually agreed rate (which would have *[c-i-c redaction]* resulted in a higher rate being specified *[end c-i-c redaction]*) was considered, but on balance was not adopted, as the information before the Commission did not suggest that Primus was in default, or that its cost of debt was of this order.

3.5.4 Specification of settlement amounts

Primus submits that the Commission should specify the exact amounts owing in the determination, inclusive of interest, in order to avoid potential for dispute over these calculations. [Primus, 4/5, p.7] Telstra opposes the Commission doing so. [Telstra, 14/5, Response to Primus, Part 5, p.7]

The Commission has chosen not to specify the settlement amounts to be paid by Telstra. The Commission considers that the parties should be able to agree the outstanding amounts themselves, given that the Commission has specified the charges to apply, the period to which they are to apply, and provided particulars regarding how interest is to be calculated (i.e., daily interest rates to apply, on a daily compounding basis). The Commission also considers that specifying the settlement amount in the determination could be problematic, and has the potential to delay the making of the final determination.

4. TERMS AND CONDITIONS ADDRESSED IN JOINT HEARING

4.1 LSS annual charges

Although these terms are now in dispute between Telstra and Primus, the Commission is arbitrating that dispute in a separate proceeding. Hence these charges are not addressed in this final determination.

4.2 LSS 'single' connection and disconnection charges

4.2.1 Background

A LSS connection or disconnection can be made using:

- Telstra's standard ordering systems and processes; or,
- a managed network migration process.

A LSS 'single' connection or disconnection is when Telstra's standard ordering system and processes are used, and comprise all LSS connections and disconnections that occur outside of a managed network migration process.

Telstra, Primus and Request participated in the joint hearing on the terms to apply to LSS 'single' connections and disconnections.

4.2.2 Current charges

Primus and Request are each in dispute with Telstra over LSS 'single' connection and disconnection charges. The charges are addressed in CRA Table 191.5 and CRA Table 191.6. The charge currently applying is specified in an interim determination

4.2.3 Prior consideration

LSS 'single' connection and disconnection charges have been considered by the Commission in a number of proceedings –ACCC, *Assessment of Telstra's LSS undertaking relating to connection and disconnection charges – final decision*, April 2006; ACCC, *Statement of reasons relating to an interim determination*, 12 July 2006 (Primus dispute); *Reasons for interim determination*, 2 November 2006 (Request dispute).

The Commission has published an extract of the decision to make an interim determination in the Telstra / Request LSS arbitration that discusses how the LSS 'single' connection and disconnection charges were calculated for the purposes of that determination. (www.accc.gov.au)

4.2.4 Principles to apply

The Commission proposed to the parties that LSS 'single' connection and disconnection charges should be determined having regard to the LSS pricing principles. The parties' submissions regarding the use of these principles are discussed previously.

The parties are supportive of the use of the LSS pricing principles; the area of contention here is whether to specify averaged or de-averaged charges. Primus considers the charges should be de-averaged. [Primus, 4/5, pp.15-18] Telstra and Request consider averaged charges would be appropriate. [Request, 4/5, p.32] [Telstra, 4/5, Part 3, p.13]

The Commission has had regard to the LSS pricing principles in determining the LSS 'single' connection and disconnection charges. Under those principles, LSS connection and disconnection charges should comprise the forward-looking efficient costs of connecting and disconnecting the LSS.

Further, in principle, prices should be geographically de-averaged, however, averaged prices can be justified where their distortionary effect is not significant.

In this instance, using averaged charges would not lead to a materially different charge.

4.2.5 Technical advice

Introduction

The Commission has received a number of reports (some of a draft or interim nature) concerning the connection or disconnection of the LSS. The report that is relevant to an assessment of the efficient costs of LSS 'single' connection and disconnection costs is Consultel, *Analysis of ULLS and LSS undertakings and subsequent submissions – final report*, February 2006.

The Commission proposed to the parties that these reports should be considered, and further that Dr Brooks' views should be sought on relevant points raised in the parties' submissions. The Commission sought the parties' views on this approach.

Parties' submissions

Telstra submits that the Commission should not have regard to the Consultel reports. Telstra's main criticism is that Consultel is not qualified to advise on salary costs. Telstra also questions whether Dr Paul Brooks, the author of the reports, is impartial. [Telstra, 14/5, Response to Request, Part 3, p.1]

Request submits that the Consultel reports should be taken into account. Request advises that it considers the conclusions reached in the Consultel reports to be reasonable and in line with its experience. Request also notes that the position put by Consultel falls within the range advocated by Telstra and access seekers. [Request, 4/5, p.30]

Primus submits that regard should be had to the views expressed by Gibson Quai in a report prepared for Primus and other access seekers. In the alternative, Primus submits that where Consultel provides a range of estimates, the Commission should adopt the midpoint of the range. [Primus, 4/5, pp.8-15]

Commission's views

Dr Brooks and Consultel are qualified to provide advice to the Commission regarding the systems and processes that are used to make 'single' LSS connections and disconnections. The Commission considers that Dr Brooks and Consultel are impartial, and does not consider that they could reasonably be perceived to be otherwise.

Accordingly, the Commission has had regard to the Consultel reports in reaching its decision, and referred relevant matters raised in submissions to Dr Brooks for his assessment.

4.2.6 Assessment of efficient costs

Introduction

There are a number of distinct cost categories that are relevant to LSS connections and disconnections.

- 'Back-of-house' costs
- Jumpering, travel and vehicle and tool costs
- Indirect costs
- Materials (coper pairs)

In practice, Telstra currently uses a mix of third party contractors and its own staff to perform the exchange-based work necessary to connect and disconnect the LSS. Telstra staff and systems perform back-of-house tasks.

'Back of house' costs

Introduction

Costs associated with the following Telstra workgroups and processes are considered within this category:

- Wholesale customer service group (WCSG)
- Data activation centre (DAC)
- Integrated deployment solution centre (IDS)

However, costs associated with Telstra's wholesale customer front of house activities are recovered through LSS annual charges.

Relevant costs are those incurred by Telstra in providing manual service qualifications, validating point of interconnection (POI) data and responding to faults in POI cables, in respect of connecting or disconnecting the LSS.

The Commission proposed that, for back-of-house costs, to generally adopt the approach discussed in ACCC, *Assessment of Telstra's LSS undertaking relating to connection and disconnection charges – final decision*, April 2006, pp. 37-43. These costs were also discussed in Consultel, *Analysis of ULLS and LSS undertakings and subsequent submissions – final report*, February 2006, pp. 30-38 and pp 56-57.

This approach results in an allowance of around [c-i-c] for back-of-house costs associated with LSS 'single' connections, and around [c-i-c] for LSS 'single' disconnections.

The Commission sought the parties' views.

Parties' submissions

Telstra did not object to the Commission's proposed allowance for back-of-house costs. In Telstra's view, however, the costs for wholesale customer front of house activities should be recognised in connection charges, and to this end, Telstra excluded such costs from its most recent cost claim for LSS annual charges. [Telstra, 4/5, Part 3, pp.2, 12-13]

Request does not dispute the back-of-house allowances the Commission proposed. [Request, 4/5, p.31]

Primus submits that wholesale front-of-house costs should be excluded to avoid double-recovery of them. Primus also submits that certain allowances are too high. In particular, Primus considers its staff costs would be a more suitable benchmark for assessing efficient back-of-house costs, and DAC costs for investigating and rectifying incomplete cable records should be disallowed. [Primus, 4/5, pp.12-14]

Telstra disputes that access seeker rates of pay and uplift for salary on-costs should be used in assessing efficient back-of-house costs. Telstra considers it unlikely that access seeker staff would have the skill sets necessary to perform the relevant tasks. Telstra also disputes that an efficient operator would have complete cable records, or that it would be efficient to check and update records ahead of an order being received on the line. Telstra notes this issue affects both retail and wholesale orders. [Telstra, 14/5, Response to Primus, Part 2, pp.5-6]

Commission's views

The Commission has determined to maintain its estimates of efficient back-of-house costs that were proposed to the parties.

The Commission has not made an allowance for wholesale front-of-house costs, as these costs have been recognised in the cost pool to be recovered through LSS annual charges.

As a result, the allowance for categories included in back-of house costs have been calculated as follows:

- Efficient DAC related costs are derived by applying an hourly salary cost of [c-i-c] to the upper bound of the range of average times ([c-i-c] minutes) an efficient operator would require to perform the DAC tasks per LSS connection. (Consultel, *Analysis of ULLS and LSS undertakings and subsequent submissions – final report*, February 2006, pp. 34-35)
- Efficient IDS related costs are derived by estimating the quantum of IDS staff costs that would be avoided if the IDS did not perform tasks relating to LSS tickets of work (TOW) i.e. LSS connections or disconnections. Avoided IDS staff costs are estimated by, firstly, multiplying (the percentage of LSS TOWs to total TOWs considered by IDS group) by total IDS staff numbers [c-i-c]. This gives the number of IDS staff positions [c-i-c] that would not be required if the IDS group did not consider LSS TOWs. Secondly, the annual associated staff cost is calculated by applying to this number of staff positions an annual salary cost of $[c-i-c]. Finally, IDS cost per LSS TOW is calculated by dividing by annual LSS TOWs [c-i-c]. (Consultel, Consultel, *Analysis of ULLS and LSS undertakings and subsequent submissions – final report*, February 2006, pp 34-35)

Adopting the position advocated by Primus would have reduced the allowance for back-of-house costs below these levels. The Commission has assessed its proposed approach and that advocated by Primus against the section 152CR(1) criteria.

In terms of the promotion of competition, Primus's position would be preferable if this better reflects the forward-looking, efficient cost of performing these tasks.

However, the Commission is not satisfied that using the access seeker's salary costs would be a suitable benchmark for efficient forward-looking costs, given the potential for the work performed by each workforce to differ. Also, on the information before it, the Commission is not satisfied that an efficient access provider would have complete cable records in all cases, or that incomplete cable records could be rectified more efficiently.

Further, the information before the Commission suggests that similar back-of-house systems and processes are used for both LSS and downstream DSL connections, and hence LSS access seekers and Telstra would currently face a similar cost base.

In these circumstances, the Commission did not consider that the efficient, forward-looking cost base would be in line with Primus's submissions.

The Commission did not revise down time estimates to reflect mid-points as opposed to upper bounds, as it considers on balance that it should take a conservative approach to estimating the efficient, forward-looking level for these cost categories. In any event, the differences in charges that would result from the values used by the Commission and midpoint values are not significant.

For similar reasons, the Commission considers that adopting Primus's position would not better encourage more efficient use of and investment in infrastructure, the efficient supply of the LSS and downstream services, or is necessary to satisfy access seeker's interests in competing on their merits. On the other hand, adopting this approach would tend to compromise Telstra's legitimate interests, including its ability to recover direct costs, to the extent that

Telstra could not attain salary and on costs, and cable records, at the levels advocated by Primus.

Jumpering, travel, vehicle and tool costs; Materials costs; Mark-up for indirect costs

The Commission proposed to the parties that it should assess efficient jumpering, travel, vehicle and tool costs based upon the charges of Telstra's contractors that connect ADSL services. The Commission proposed that this assessment should not be based upon cost measures that Telstra has modelled where it uses own staff.

The Commission proposed to adopt the materials cost (i.e., the cost of copper pairs used to connect points on the MDF) that Telstra modelled in previous proceedings. No allowance was made for materials in disconnection costs, as no cable is required. The costs proposed were, for CBD areas, [c-i-c], and for other areas [c-i-c].

The Commission proposed a mark-up of 10 percent on third party contractor rates to cover indirect costs such as contract management costs, in preference to Telstra's previously claimed mark-up of [c-i-c] percent. This reflected the view that when using third party contractors, Telstra will avoid the indirect cost categories that comprise its claimed mark-up. Further, efficiently incurred contract management costs would not represent a significant component of per LSS connection costs.

The Commission sought the parties' views.

– *Jumpering etc*

Telstra submits that the Commission's proposed approach could be adopted for connections and disconnections that contractors perform. However, a mix of own staff and contracted-labour is used to connect services across Telstra's fixed-line network. Telstra submits that LSS 'single' connection and disconnection charges should be based upon the cost of this 'blended' workforce. In Telstra's view, the cost associated with a contractor-made connection is much less than the cost for a Telstra-made connection, and as a result 'blending' results in a higher charge. [Telstra, 4/5, Part 3, pp.4-5]

Telstra submits that LSS 'single' connection and disconnection charges should vary over time in line with significant changes in its cost base. The significant change relates to the introduction of contractors to make LSS 'single' connections and disconnections.

Until July 2006, Telstra advises that contractors were rarely used to make LSS connections. Since that time, contractors have made around [c-i-c] per cent of all connections on Telstra's fixed-line network. Telstra advises that it uses contractors where possible, but that contractors cannot perform all connections within relevant time limits. Further, in Telstra's view, there are practical reasons why contractors will not be able to be used for all exchange-based work. [Telstra, 4/5, Part 3, pp.5-7]

Telstra supplies details of the relevant costs it faces when contractors perform LSS or DSL connections (which are below the rates used in preparing the draft determination). Included are details of a 'jumper-over charge', for connections that involve running a jumper between a second main distribution frame. The average rate at which charges increase each financial year under the agreements with contractors is also provided. [Telstra, 4/5, Part 3, pp.8-9]

Primus and Request submit that contractor charges should be used as the measure of the efficient level for these cost categories. In their view, this benchmark should be applied to all connections, including those performed by

Telstra staff. Primus submits that the costs Telstra claims for connecting the service itself are inefficient, as they exceed the charges at which contractors will perform that work. [Primus, 14/5, Part 3, p.3] Request considers the distinction between connections that Telstra make and those contractors make should be irrelevant to determining the efficient forward-looking cost of connections. In Request's view, the efficient, forward-looking cost of each connection should be the same. [Request, 21/5, p.9]

Primus questions whether contractors' charges may have too high an allowance for travel. In Primus's view, a relatively high number of connections can be batched, and for some CBD exchanges, no travel may be necessary. [Primus, 4/5, pp.8,11] Primus considers that the high number of connections that Telstra reports across its fixed-line network demonstrates significant potential for batching of jobs. [Primus, 14/5, Part 3, p.3]

Telstra advises there is little potential for further batching to occur above that already reflected in costings, and manned exchanges may not always have the requisite skills on hand to avoid a travel component. [Telstra, 14/5, Response to Primus, Part 2, pp.3-4]

– Materials

Primus questions whether Telstra, or contractors, meet the costs of materials. [Primus, 4/5, p.15]

Telstra advises that when contractors make the connection, they supply their own materials. Telstra incurs the cost of materials when Telstra staff makes the connection. [Telstra, 14/5, Response to Primus, Part 2, p.7] Telstra advises that cost of materials has increased, and a higher allowance beyond what the Commission proposed would be appropriate from 1 July 2007 (for when Telstra incurs materials costs). [Telstra, 4/5, Part 3, pp.3-4,13]

– Mark-up for indirect costs

Telstra submits that the proposed 10 per cent mark-up for indirect costs would be appropriate for the purpose of the final determination. [Telstra, 4/5, pp.3-4]

Commission's views

A number of the principles for setting LSS connection and disconnection charges are not controversial. It is not disputed, for instance, that the charge for connections and disconnections that are performed for Telstra by contractors should be based upon the contractors' charges (together with a mark up of 10 per cent for indirect costs).

Telstra has sought, however, an increment to the connection charges to reflect a higher claimed cost when Telstra staff does the exchange-based work. This claimed increment results from 'blending' of discrete cost measures associated with (i) Telstra connected services; and (ii) contractor connected services. It is of a more significant magnitude for the period up to 30 June 2006, as in this period the claimed increment is calculated on the basis that Telstra connected all services.

The possible approaches open to the Commission are (i) to base the allowances for cost of exchange-based work that are included within LSS 'single' connection and disconnection charges on the cost of contractor-connected services, or (ii) to include an increment of the type that Telstra seeks. The Commission has assessed these two possible approaches against the section 152CR(1) criteria.

The first of these criteria concerns the promotion of the long-term interests of end-users (LTIE) of carriage services or of services supplied by means of carriage services. The Commission is directed to a number of subsidiary matters. The Commission has considered, in particular, the likely effect of each approach on:

- competition in markets for carriage services, and in particular broadband/DSL services;
- efficient use of and investment in infrastructure by which services are supplied (including the access network, and DSLAMs) or by which services are capable of being supplied (including a FTTN); and,
- the legitimate commercial interests of the supplier of the service.

The Commission considers that, to the extent that allowing Telstra's increment would result in the charges faced by access seekers exceeding the costs faced by Telstra when line sharing, then the approach would lessen competition in markets for downstream services.

Here, Telstra had in place Installation and Maintenance contracts, and had used contractors to connect downstream DSL services, earlier than 1 July 2006. Telstra was not prevented from using contractors for LSS connections at that time, but generally chose not to use contractors for LSS connections. As a result, contractors connected, at lesser cost than Telstra claims for LSS, Telstra services that LSS access seekers compete with in downstream markets.

Another circumstance in which recognising the increment would fail to promote competition is where it would lead to access seekers facing charges that exceed the forward-looking efficient cost of connecting the LSS. In this case, access seekers would face charges based on costs that Telstra could avoid in the long run, resulting in access seekers facing a higher cost base to Telstra's. This would discourage efficient entry and exit in downstream DSL markets.

A key consideration, then, is whether contractor charges are an appropriate benchmark for the efficient, forward-looking level of the cost categories that underlie those charges. This in turn calls for consideration of whether there are impediments in the long run to both:

- Telstra using contractors exclusively for exchange based work for the LSS and internal line sharing; and,
- Telstra being as efficient as that implied by the contractor charges when connecting services itself.

If so, then recognising an increment of the type Telstra seeks may be less likely to harm competition, provided that Telstra and access seekers would each face an equivalent cost base for connections going forward. However, unless both these conditions are met, then recognising the increment would impede competition.

While there are currently insufficient contractors to perform all LSS and downstream connections, it is reasonable to expect that over time Telstra would be able to use contractors to a greater extent. For instance, as competing service providers complete network migrations to LSS and/or ULLS platforms, existing contractor capacity will be able to be directed towards a greater number of 'single' connections.

On the second of these points, the Commission considers the level of cost Telstra incurs when connecting services will closely approach the levels implied by the contractor charges. Given that contractors are recovering their incremental costs (such as labour, travel and materials) and a contribution towards overheads and profit from their charges, it is not apparent why Telstra could not also achieve this level of costs when connecting the LSS and downstream services.

Turning to efficient investment in and use of infrastructure, the Commission firstly considers efficient use of and investment in infrastructure used to supply the LSS. The Commission also considers consequences for efficient use, and investment in, the DSL access multiplexer (DSLAM) infrastructure used to supply downstream DSL services.

The Commission considers that efficient use and investment will be encouraged where Telstra is able to recover the efficient, forward-looking costs in making LSS connections, including a normal commercial return on capital employed. Connection charges above this level for LSS access seekers would, however, have the effect of discouraging efficient investment in and use of infrastructure used to supply the LSS. Use and investment in downstream services would also likely be below efficient levels as a result.

Also relevant here is the preceding discussion of whether, in the long run, there are impediments to Telstra meeting the efficiency benchmark implied by contractor charges across all LSS and 'downstream' connections. As discussed above, it is unclear whether such impediments currently exist, but if they do, the Commission considers that they will not persist. Accordingly, the Commission considers that contractor charges provide an efficient benchmark for underlying cost categories for all LSS connections, and not just those performed by contractors. If follows that including an increment as sought by Telstra would discourage efficient use and investment.

The Commission notes Telstra's claims regarding investment in other broadband infrastructure, such as a FTTN, but does not consider on the information before it that LSS 'single' connection and disconnection charges will materially influence these investment decisions.

Telstra's legitimate commercial interests include its ability to recover its costs and make a normal commercial return on capital employed.

The Commission does not consider that these interests require that LSS access seekers pay connection charges for the period up to 1 July 2006 on the basis that Telstra made all their connections. This is because Telstra has used a mix of contractors and own staff to make connections over this period, and recovered associated costs across connection charges for retail and wholesale services. It is not necessary for LSS access seekers to bear a higher proportion of costs to ensure that they are recovered.

On the other hand, setting LSS connection charges on contractor charges without an increment as Telstra has sought could be contrary to Telstra's legitimate interests should it prevent Telstra from recovering its costs. This will be more so where Telstra is not able to attain a cost base for all LSS and 'downstream' connections at the levels commensurate with those charges, or it takes longer to achieve that level of costs.

The next criterion concerns the legitimate business interests of the access provider, and the carrier's or provider's investment in facilities used to supply the declared service. The Commission's views on the effect of this decision on these matters are discussed as part of the first criterion.

The third criterion is the interests of all persons who have the right to use the service. The Commission considers that access seekers' interests lie in being able to compete for the custom of end-users on the basis of their relative merits.

It is in the interest of LSS access seekers to pay charges that reflect the efficient, forward-looking cost of connecting services. Paying connection charges on the basis that Telstra, rather than contractors, makes all LSS connections, or on the basis of Telstra's actual cost base, is contrary to this interest. In this case, access seekers would be required to pay connection charges that are higher than the costs Telstra incurs, or will incur in future, for connecting downstream services. This would put access seekers at a disadvantage to Telstra in downstream markets.

The fourth criterion is the direct cost of providing access to the declared service. Included here are LSS incremental costs and a contribution to 'indirect' costs. It calls for consideration to be given to Telstra's ability to recover these costs.

The Commission considers that Telstra will likely recover the direct cost of providing LSS connections in the long run regardless of the approach taken to this issue. This will be the case provided that Telstra is able to reduce its cost base to the level implied by contractor charges, such as by increasing its use of contractors for LSS 'single' connections and disconnections. Any restriction on Telstra's ability to recover its actual costs incurred in connecting the LSS would not be expected to persist.

The next two criteria are the value to a party of extensions, or enhancement of capability, whose cost is borne by someone else; and the operational and technical requirements necessary for the safe and reliable operation of a carriage service, or a telecommunications network or a facility. The cost of extensions to Telstra's ordering systems necessary to supply the LSS (or the ULLS) have been taken into account in other charges. The Commission does not consider that the 'operational and technical requirements' criterion materially contributes to this decision.

The last criterion is the economically efficient operation of a carriage service, a telecommunications network or a facility.

As noted previously, the Commission considers that should an approach result in LSS connection charges that are above efficient forward-looking levels, this would impede competition in the provision of downstream (DSL) services. In these circumstances, Telstra would be able to set above-cost prices for its downstream services, leading to a reduction in the consumption of these services below efficient levels, and consequential allocative inefficiencies.

It follows from the above analysis that, firstly, LSS 'single' connection and disconnection charges for the period up to 1 July 2006 should not be set on the basis that Telstra connected all these services without using contractors. Secondly, whether these charges should be based solely on costs incurred when contractors connect the service, or include an increment as sought by Telstra, calls for a weighing of competing criteria.

On the one hand, not including this increment may be contrary to Telstra's commercial and legitimate business interests to recover the costs it currently incurs, including its direct costs of making LSS and downstream connections. Any such impediment that may exist will, however, reduce as Telstra realises a more efficient cost base for making connections.

Turning to the remaining criteria, the long term interests of end-users (including the promotion of competition, and efficiency in use and investment), and the interests of persons with rights to use the declared service, will be promoted by not including the claimed increment to connection charges.

Similarly, efficiency in use of carriage services and facilities used to provide them will also be encouraged by this approach, as it provides stronger incentives for Telstra to seek out and adopt the more efficient processes that have been employed to date by contractors. This could be by replicating the contractors' business model, or using contractors more.

Having regard to these matters, the Commission considers that LSS 'single' connection and disconnection charges should not include the increment as sought by Telstra. This is because those factors that could support the inclusion of the increment would not persist, while including the increment would discourage efficiency and impede competition over the long term.

In terms of the contractor charges to apply, the Commission has, for the proportion of connections that were made by contractors, adopted the weighted-average contractor charges for LSS (‘ADSL simplex’) connections that Telstra supplied in its submission to the joint hearing for (i) the period up to 30 June 2006, and (ii) for 2006-07. The Commission has added to these weighted–average charges an allowance to reflect the ‘jumper-over extra charge’. For 2007-08, the 2006-07 charge was indexed at [c-i-c]%, being the average rate that charges are to increase across all I&M contracts.

For the remainder of connections (those currently performed by Telstra technicians), the Commission has again applied the contractor charge data that Telstra supplied in its submission to the joint hearing. The Telstra-reported weighted average contractor charge is used as a proxy for contractor charges in metropolitan (bands one and two) areas. The Telstra-reported ‘country’ charge is used for connections in band 3.

As actual distribution of these connections between bands is not known, the Commission has weighted the ‘metro’ and ‘country’ charge by the distribution of lines in bands 1, 2 and 3 in order to calculate an average charge. Band 4 lines are not used, as the derived charges do not apply in band 4. There is some potential for this approach to over-weight the higher ‘country’ charge. As Band 3 exchange areas are larger, and LSS/ADSL services are only available within a limited distance from the exchange, a greater proportion of lines in band 3 (as compared to other bands) may not support LSS/ADSL services. And so, LSS/ADSL services would be expected to be more concentrated in metropolitan areas than the distribution of lines would suggest.

Disconnection costs are calculated on a similar basis to connection charges, except here an allowance for DAC group costs is not included. The above discussion regarding connection charges is otherwise applicable to disconnection charges.

Conclusion on LSS ‘single’ connection and disconnection charges

This approach to back-of-house costs, and the jumpering and related cost categories, results in a LSS ‘single’ connection charge of:

- $38.70 for the period ending 30 June 2006,
- $39.30 for 2006-07, and
- $40.90 for the period from 1 July 2007 to 31 December 2007.

Resulting LSS ‘single’ disconnection charges are:

- $34.70 for the period ending 30 June 2006,
- $35.10 for 2006-07, and
- $36.70 for the period from 1 July 2007 to 31 December 2007.

Circumstances in which LSS ‘single’ disconnection charges are to apply

Introduction

Where a LSS disconnection request is made as a result of an end-user churning the downstream DSL service to another service provider, there is the potential for the removal of the existing jumpers being combined with installing the new jumpers on the relevant line. Where this work is combined, then overall costs can be significantly reduced, and costs of removing redundant jumpers recovered within the relevant connection charge.

Reflecting this, the Commission proposed to the parties that a disconnection charge should not be imposed in respect of disconnections made, after 15 November 2006, as a result of churn.

It was proposed that churns be identified by whether an order on the same line is received within 30 days of the disconnection request. A 30 day period was nominated as this appeared a reasonable period to provide for the gaining service provider to submit its order. Telstra previously nominated 15 November 2006 as the date by when Telstra considered it could make any necessary arrangements to implement a churn process.

The Commission sought the parties' views on this approach.

Parties' submissions

Telstra advises that it has introduced a churn process that includes the LSS. This process allows services to be churned from one service provider to another upon gaining service provider submitting an order. Participating service providers give a standing authority to transfer services they lose. The process is unavailable unless both the gaining service provider and losing service provider have agreed to participate. Where this process is used to transfer the service, Telstra does not apply a disconnection charge. [Telstra, 4/5, Part 3, pp.9-10]

Telstra advises that for a churn process to have value, the arrangements need to support all, or a significant proportion, of churn requests that could be made. [Telstra, 4/5, Part 3, p.10] In Telstra's view, this requires the process being agreed to by at least all significant ISP's, and ratified in an industry code. [Telstra, 4/5, Part 3, p.12]

In Telstra's view, it is otherwise impracticable to implement a churn arrangement. Telstra points, firstly, to limitations in its current ordering systems that mean churn processes could not be supported without a standing authority from losing service providers. [Telstra, 4/5, Part 3, pp.9-11]

Telstra also submits that any lag between service cancellation and disconnection should be kept as short as possible. Telstra points to possible reductions in service quality for the period that a continuing service remains connected to the losing service provider's DSLAM, and to the associated inability for the losing service provider to re-use the port. [Telstra, 4/5, Part 3, pp.10-11]

Telstra states that the costs of any systems changes to support a different churn process should be taken into account. [Telstra, 4/5, Part 3, pp.11-12]

Primus supports the proposed approach to LSS disconnection charges, and wants it also applied to disconnection requests made prior to 15 November 2006. Primus considers an associated notice obligation should apply so it can check when a LSS disconnection charge is applicable. [Primus, 4/5, p.19]

Primus disputes Telstra's claims that jumpers should be removed as soon as a disconnection request has been made. Primus points to the high demand for jumpering work, and the inability of contractors to meet this demand. In Primus's view, this makes the efficiencies offered by combining the removal of jumpers with new connections more compelling.

Primus is sceptical of whether Telstra's proposed LSS churn process would ever be effective if industry agreement is first required. Primus refers to reported statements attributed to Telstra Bigpond that it will not participate in the Telstra LSS churn process.

Lastly, Primus disputes that systems changes to support churn would involve significant cost. [Primus, 14/5, Part 3, pp.3-5]

Request submits that it is considering Telstra's proposed LSS churn process, following the arrangements being recently raised with it, but that this should not interfere with the making of a final determination. Request also submits that Dr Brooks' views on churn and associated disconnection costs should be preferred to those of Evans & Peck. [Request 21/4, pp.9-10]

Commission's views

The parties accept that a LSS churn process should be implemented. Further, where disconnection costs can be avoided by such a process, disconnection charges should not be payable. Telstra has, after a long lead-time, introduced a churn process that includes the LSS. Telstra has noted the benefits of effective customer churn processes when introducing an earlier (2003) churn process for DSL services.

Efficiency improvements and cost savings to Telstra are significant; more so given the current limits Telstra reports on use of efficient contractor labour for exchange-based work. Access seekers benefit by being better able to compete on an equal footing in downstream markets. End-users benefit directly, as it removes an obstacle to end-users gaining access to services offered by other service providers, and promotes competition, by reducing time and expense associated with switching service provider.

In previously considering this issue, it was proposed that Telstra should not be able to charge for LSS disconnections that occur as a result of the end-user churning their DSL service. This reflected that (i) Telstra did not have a churn process that included the LSS; (ii) Telstra could avoid almost all costs of disconnecting a churned LSS if it had an effective churn process; and (iii) access seekers should not pay for costs that could be avoided.

The Telstra LSS churn process has potential to provide an effective means by which to churn a LSS (either to or from another LSS, or a DSL service), and would allow exchange work to be aligned, and unnecessary cost avoided. It also appears consistent with the DSL churn process, which has gained acceptance from a number of service providers; and represents a least cost option by which to introduce a churn process for LSS, given it avoids reconfiguration of Telstra's ordering systems.

Accordingly, the Commission considers that it should harmonise its approach to LSS disconnection charges with the implemented Telstra churn process. The Commission has revised its 'churn' definition to encompass only service transfers processed within the Telstra LSS churn process.

The Commission is concerned, though, as to whether the Telstra LSS churn process will be fully effective in ensuring that LSS access seekers do not pay avoidable costs. Primus has provided a media article in which Telstra (Bigpond) is reported as not intending to participate in the Telstra LSS churn process. The most recent listing that Telstra has published concerning participants in its broadband churn processes (May 2007) confirms that Telstra (Bigpond) was participating in the DSL churn process, but not the LSS churn process. It is possible this position may have since changed, but for the purposes of this discussion, the Commission has proceeded on the basis that Telstra (Bigpond) is not a participant in the LSS churn process.

The Telstra LSS churn process is available only where the gaining and losing service providers are participants, and it appears that Bigpond (which has the largest share of DSL services) is not a participant. And so, a number of churns could attract a disconnection charge, even though Telstra could avoid the underlying costs.

Accordingly, the Commission has considered whether LSS disconnection charges should also be avoided where the Telstra LSS churn process could be unavailable due to Bigpond's non-participation. The two options considered by the Commission against the section 152CR(1) criteria are: (i) allowing disconnection charges on all LSS disconnections that are not processed via the Telstra LSS churn process; and (ii) disallowing LSS disconnection charges otherwise payable under option (1) where the LSS access seeker is a participant in the Telstra LSS churn process, but Telstra (Bigpond) is not.

Option (2) will not emulate all outcomes expected if both the losing service provider and Telstra (Bigpond) were participants in the Telstra LSS churn process, as there is the potential for additional disconnection charges being disallowed under this option. However, there would be practical difficulties in use of a more precise test, and this option provides slightly stronger incentives on Telstra (Bigpond) to participate. Bigpond currently has relatively weak incentives to participate. Unlike other service providers, Bigpond does not itself face these disconnection charges, and has a larger share of the retail market.

In applying the section 152CR(1) criteria, the Commission first considered the long term interests of end-users, and within this criterion, the promotion of competition.

Effective churn processes promote competition by removing obstacles to end-users gaining access to services provided by other service providers.

While Telstra (Bigpond) does not participate, if Telstra gains the customer, then the losing LSS access seeker may be required to pay disconnection charges simply as a result of Telstra's decision not to participate. This will be the case where the losing service provider has provided a standing authority that would permit its services being cancelled and disconnected.

A gaining service provider that is participating in the Telstra DSL and LSS churn processes could use a two-stage process to churn a Telstra (Bigpond) end-user customer to a wholesale DSL service, and then to a LSS-based service, should Bigpond not participate in the Telstra LSS churn process. However, this will require more time and expense.

Accordingly, the Commission considers that Bigpond's participation would lead to a more effective churn process, and thereby promote competition. As option (2) will encourage Bigpond to participate in the Telstra LSS churn process, the Commission considers this option will better promote competition.

Economic efficiency in use of and investment in infrastructure used to provide listed services requires consideration of Telstra's infrastructure as well as the infrastructure of LSS access seekers. Obstacles to acquiring end-users customers, such as would exist in the absence of an effective churn process, would tend to discourage otherwise efficient use of and investment in infrastructure used to provide the LSS and downstream DSL services. This is because those restrictions would discourage take up of the LSS, and use of Telstra's LSS ordering systems, as well as discourage efficient investment in access seeker's DSLAMs. Again, option (2) would be preferable.

Telstra's legitimate business and commercial interests, including the recovery of direct costs, are satisfied under all options. Telstra's interest in recovering necessary capital costs to augment ordering and associated systems, or operating expenses, is satisfied through the approach to setting cost-based LSS annual charges. Further, by encouraging efficiency in connecting churned services, more efficient contractors can complete a greater proportion of Telstra's exchange work, including connection of Telstra retail services. This will reduce Telstra's cost base, making it more likely that Telstra's direct costs will be able to be recovered. To the extent that option (2) could mean that Telstra would not recover disconnection costs it incurs, Telstra can avoid this outcome by deciding to participate in the Telstra LSS churn process.

Access seekers' interests lie in being able to compete on their relative merits without being impeded in acquiring end-user customers or incurring unnecessary cost. These interests are promoted by arrangements that provide better access to effective churn processes, and not incurring disconnection costs that could be avoided by such processes. The Commission considers that option (2) would best meet these interests. Option (1) would be less likely to lead to an effective churn process, as little incentive is provided to Telstra (Bigpond) to participate.

As noted above, the direct costs of any system enhancements will be able to be recovered, including through LSS annual charges (subject to Telstra being able to demonstrate they were efficiently incurred). All service providers, including Telstra, will be able to share in the value of extensions to system capability that an effective churn process represents. All parties would similarly share in the recovery of associated cost, with LSS access seekers contributing through cost-based approach to setting of the LSS annual charge.

Each option is consistent with Telstra's current systems, and hence would be able to be implemented without potential for compromising operational quality or reliability of services. And so, they would not lead to the problems Telstra envisaged as arising from a more-encompassing LSS churn process.

The last criterion calls for consideration to be given to the economically efficient operation of a carriage service, network or facility, of either Telstra or other service providers. It calls for consideration to be given to the effectiveness of the churn process that would be likely to result from each approach, and the resulting effect on competition. This is because dynamic efficiencies caused by competition in downstream services provide the best discipline on all service providers to operate in an economically efficient manner. It also calls for consideration to be given to productive and allocative efficiency.

Option (2) is preferred here as dynamic efficiencies are more strongly encouraged as more downstream services will be likely to fall within the ambit of the Telstra LSS churn process. This will reduce obstacles to a wide class of end-users gaining access to competing services, thereby promoting competition.

Productive efficiency (caused by processing churns as a single ticket of work) will increase as further encouragement is given to service providers, including Telstra (Bigpond), to participate in the LSS churn process. Allocative efficiency will also increase as more service providers participate, and service providers pay for costs that they cause.

For these reasons, the Commission considers that option (2) should be adopted. These arrangements will apply from the time the final determination takes effect until 31 December 2007. Other arrangements will apply before this time.

Until 15 November 2006, charges will be payable on all LSS disconnections, as the Commission considers that it was likely to have been reasonable for a LSS churn process not to be implemented before this time. For the period between 15 November 2006 until the time the final determination takes effect, no disconnection charges will be payable. This maintains the position taken at the interim determination stage in the absence of a Telstra LSS churn process, and Telstra's advice that in practice those arrangements did not support Telstra applying charges for any LSS disconnections.

It may be that some refinements in approach may be appropriate in future. For instance, further consideration may become necessary if a significant number of services remain outside the ambit of the LSS churn process, or any problems or limitations in the process that could be identified in the process in future are not able to be resolved.

Miscellaneous matters

The Commission raised with the parties a number of further issues that have a bearing on LSS ‘single’ connection and disconnection terms. Some of these have been discussed already. The Commission’s views on these matters are as follows:

Discounts for unmanaged bulk connections

The Commission does not consider it appropriate to determine connection charges for unmanaged bulk connections, but rather considers that the charge for LSS ‘single’ connections should apply in those circumstances.

Costs for 2006-07 and 2007-08

Costs for 2006-07 and 2007-08 were measured by indexing 2005-06 costs where appropriate. For jumpering and associated costs, the Commission adopted the average escalation rate provided in the contractor agreements, as provided by Telstra. For back-of-house costs, these were indexed by *ABS 6345 Labour Price Index ‘Ordinary time hourly rates of pay excluding bonuses; Australia; Communication services; Private; All occupations’.*

As it eventuated that materials costs are reflected in contractor charges, it is unnecessary to derive discrete cost allowances for this cost category. Annual changes in these costs are reflected in the escalation permitted under the contracts.

Cost model

A simple cost model that adopts the Commission’s views is attached to these reasons. It is based on the same structure as the previous model. The contents of this cost model are to be treated as [c-i-c] and subject to the confidentiality undertakings given and directions made, as it reproduces information that is confidential to the parties.

Averaged or de-averaged charges

As noted previously, the Commission decided to specify averaged LSS ‘single’ connection and disconnection charges.

Bands 1, 2, 3

The Commission did not specify charges to apply to LSS ‘single’ connections or disconnections in band 4, as there is little if any demand for the LSS in this band.

Transfers from the ULLS to LSS

The Commission did not specify charges to apply for the transfer of services from the ULLS to the LSS.

4.2.8 Commencement date, expiry date and interest

The Commission has backdated the LSS ‘single’ connection and disconnection terms. These charges are to apply until 31 December 2007. Interest is payable on any over-payment that has occurred. The term of backdating, and reasons for this approach, are discussed previously.

4.2.9 Changes to draft final determination

Some of the terms specified in the final determination differ to some extent to those proposed at the draft determination stage. These changes reflect revised cost data, or approach to when disconnection charges can be applied and backdating. Reasons for these changes are discussed previously.

4.3 LSS Managed Network Migration ('MNM') terms and conditions

4.3.1 Background

A Managed Network Migration is a transfer or migration of services that is achieved by the project management by Telstra of a coordinated cancellation and connection of services.

MNM terms include charges payable for connections, disconnections, or order cancellations; preconditions to ordering a MNM; and forecasting timeframes and migration plan amendment terms.

There are potentially a number of different types of network migrations that could be requested. In these proceedings, consideration was given to migration from a wholesale DSL platform to the LSS; and migration from a LSS platform to a ULLS platform.

Telstra, Chime and Primus participated in the joint hearing on all the MNM related terms that were disputed. Request participated only on the price-related terms and the pre-requisites to ordering a LSS MNM.

4.3.2 Current terms and conditions

Chime, Primus and Request are each in dispute with Telstra over LSS MNM terms and conditions. These terms and conditions are addressed in agreements between the parties, e.g., Customer Relationship Agreement 192 (which in some cases incorporates terms specified in Customer Relationship Agreement 191), or separate agreements.

The MNM connection, disconnection and cancellation charges, and (in the case of the arbitrations involving Chime and Request) pre-requisites to MNMs, currently applying are specified in interim determinations.

4.3.3 Prior consideration

LSS MNM terms and conditions have been considered by the Commission in each of these arbitrations. ACCC, *Statement of reasons relating to an interim determination*, 12 July 2006 (Primus dispute); *Reasons for interim determination*, 2 November 2006 (Request dispute); *Reasons for interim determination*, 2 November 2006, and *Reasons for interim determination*, 21 December 2006, (Chime dispute).

The Commission has published an extract from each of the decisions to make an interim determination in the Telstra / Request LSS arbitration and Telstra / Chime LSS arbitration concerning LSS MNM charges. (www.accc.gov.au)

4.3.4 Principles to apply

The Commission proposed to the parties that the price-related terms for LSS MNMs should be determined having regard to the LSS pricing principles. The parties' submissions regarding the use of these principles are discussed previously.

The parties are generally supportive of the use of the LSS pricing principles. Some parties questioned whether MNM charges should be averaged, as had been proposed, while others where supportive of averaging. [Primus, 4/5, p.20] [Chime, 18/5, pp.14, 17] [Request, 4/5, p.39] [Telstra, 4/5, Part 4, p.8]

The Commission has had regard to the LSS pricing principles in determining the price-related terms for LSS MNMs. Under those principles, these charges should comprise the forward-looking efficient costs of connecting and disconnecting the LSS as part of a MNM.

Further, in principle, these charges should be geographically de-averaged. However, averaged prices can be justified where the distortionary effect of an averaged charge is not significant. As a result of the approach adopted in these proceedings to the cost of materials, the same costs apply to LSS MNMs across different bands. Hence, using averaged charges does not lead to a different charge.

4.3.5 Technical advice

Introduction

The Commission has received a number of reports (some of a draft or interim nature) concerning the connection or disconnection of the LSS. The reports that are relevant to an assessment of the efficient costs of LSS MNM costs are:

- Consultel, *Analysis relating to Primus / Telstra LSS Dispute interim report*, February 2006
- Consultel, *Small Scale MNMs between wholesale ADSL, ULLS and LSS – Interim report*, March 2007

The Commission proposed to the parties that these reports should be considered, and further that Dr Brooks' views should be sought on relevant points raised in the parties' submissions. The Commission sought the parties' views on this approach.

Parties' submissions

Telstra submits that the Commission should not have regard to the Consultel reports. Telstra's main criticism is that Consultel is not qualified to advise on salary costs. Telstra also questions whether Dr Paul Brooks, the author of the reports, is impartial. [Telstra, 4/5, Part 4, p.2] [Telstra, 14/5, Response to Request, Part 4, p.1]

Request submits that the Consultel reports should be taken into account. Request advises that it considers the conclusions reached in the Consultel reports to be reasonable and in line with its experience. Request also notes that the position put by Consultel falls within the range advocated by Telstra and access seekers. [Request, 4/5, p.36]

Primus bases its submissions on views expressed by Gibson Quai in a report prepared for Primus and other access seekers, and also the Consultel reports. [Primus, 14/5, Part 4, p.1]

Commission's views

Dr Brooks and Consultel are qualified to provide advice to the Commission regarding the systems and processes that are used to make LSS MNMs. The Commission considers that Dr Brooks and Consultel are impartial, and does not consider that they could reasonably be perceived to be otherwise.

Accordingly, the Commission has had regard to the Consultel reports in reaching its decision, and referred relevant matters raised in submissions to Dr Brooks for his assessment.

4.3.6 Assessment of efficient costs

Introduction

There are a number of distinct cost categories that are relevant to LSS connections and disconnections.

- 'Back-of-house' costs
- Jumpering, travel and vehicle and tool costs
- Indirect costs
- Materials (coper pairs)

Telstra uses third party contractors to perform the exchange-based work necessary to connect and disconnect the LSS as part of a MNM. Telstra staff and systems perform back-of-house tasks.

'Back of house' costs

Introduction

Costs associated with the following Telstra workgroups and processes are considered within this category:

- Wholesale customer service group (WCSG)
- Wholesale Product Delivery (WPD), which includes the data activation centre (DAC)
- Integrated deployment solution centre (IDS)

However, costs associated with Telstra's wholesale customer front of house activities (WCSG and WPD) are recovered through LSS annual charges.

These work groups have periodically been reorganised. Now, some of these functions are performed by the Wholesale Broadband Infrastructure and Operations (WBI&O) group and the Product Delivery Co-ordination (PDC) team.

The Commission proposed to include an allowance for IDS group costs within LSS MNM connection charges, and to base this allowance on advice previously provided by Consultel concerning the efficient cost associated with IDS group tasks. The relevant costs are those incurred by Telstra in coordinating LSS MNMs and scheduling contractors to perform them.

Parties' submissions

Telstra considers that the *[c-i-c redaction]* proposed hourly labour rate *[end c-i-c redaction]* for IDS group staff is quite low, although it was not in a position to provide an estimate of what it considers the efficient forward-looking labour cost for the IDS group would be. In Telstra's view, this would vary from team to team within the IDS group, depending upon tasks performed.

Telstra would not object to the proposed allowance for IDS group costs, provided that an allowance was made for costs associated with the WCSG and WPD work groups. Telstra submits that if this is done, then the total allowance for these work groups would align with efficient cost measures for all 'back-and-front-of-house' functions that are derived from Telstra's accounts. [Telstra, 4/5, Part 4, p.7]

Telstra disputes that it would be appropriate to base efficient labour cost of its IDS group on salaries paid by access seekers to their administrative staff. [Telstra, 14/5, Response to Chime, Part 3, p.1]

Telstra submits that WCSG and WPD group costs should be recovered in LSS MNM charges, and to this end has excluded costs associated with these groups from the cost claim it has made in these proceedings in respect of LSS annual charges. Telstra provides estimates of the costs associated with these work groups, including how these costs have changed over time as manual tasks have been automated. [Telstra, 4/5, Part 4, pp.3-7, Annexure A, Annexure B]

Chime submits that *[c-i-c redaction]* the proposed hourly rate *[end c-i-c redaction]* for IDS group staff is too high, and that a rate derived from the salaries of Chime's administrative staff would provide a more reasonable measure. [Chime, 4/5, p.17] Chime and Primus are concerned by the potential for double recovery of WCSG and WPD group costs, and consider that the better approach is to leave these costs in the LSS annual charges cost pool. They also submit that only efficient, automated, processes should be costed. [Chime, 18/5, p.14] [Primus, 14/5, Part 4, pp.1-2]

Primus also questions whether the costs of IDS functions are already recovered through the mark-up for indirect costs allowed in the LSS annual charges cost pool. [Primus, 14/5, Part 4, p.2]

Commission's views

The Commission has determined to maintain its estimates of efficient back-of-house costs that were proposed to the parties.

The Commission's view is to include in LSS MNM connection charges an allowance for efficiently incurred IDS group costs. The measure of efficient IDS related costs are derived by multiplying (i) an hourly labour cost, by (ii) the amount of time it would take an efficient operator to perform IDS functions in relation to a LSS MNM (as claimed by Telstra).

The efficient hourly labour cost used for the period up to 30 June 2006 is $[c-i-c], with an annual indexing used to derived a *[c-i-c redaction]* per hour rate for 2006-07 and 2007-08. *[end c-i-c redaction]* This is considered to result in a reasonable measure of the cost that will be incurred by the IDS group on an efficient and forward-looking basis, and falls between the rates advocated by the parties in these proceedings.

The Commission does not consider that the costs associated with the tasks performed by the IDS group would already be recovered within LSS annual charges. The mark-up for indirect costs there is to cover additional cost categories, such as costs of managing contracts and billing.

Adopting the position advocated by Chime would have reduced the allowance for back-of-house costs below these levels. The Commission has assessed its proposed approach and that advocated by Chime against the section 152CR(1) criteria.

In terms of the promotion of competition, Chime's position would be preferable if this better reflects the forward-looking, efficient cost of performing the IDS group tasks.

However, the Commission is not satisfied that using the access seeker's salary costs would be a suitable benchmark for efficient forward-looking costs of the IDS group, given the potential for the work performed by each workforce to differ.

For similar reasons, the Commission considers that adopting Chime's position would not better encourage more efficient use of and investment in infrastructure, or the efficient supply of the LSS and downstream services, or is necessary to satisfy access seeker's interests in competing on their merits. On the other hand, adopting this approach would tend to compromise Telstra's legitimate interests, including its ability to recover direct costs, to the extent that Telstra could not attain salary and on costs, at the levels advocated by Chime.

The Commission has not included in LSS MNM connection charges an allowance for WCSC and WPD costs. The costs of these work groups are fully reflected in the cost pool that the Commission has recognised for the purposes of setting LSS annual charges.

This approach results in an allowance for back-of-house costs of between $126.00, for the period ending 30 June 2006, and $134.50, for the period commencing 1 July 2007 (per LSS MNM).

Jumpering, travel, vehicle and tool costs; Materials costs; Mark-up for indirect costs

The Commission proposed to base the efficient costs for jumpering, travel, vehicle and tool cost categories for MNMs involving 50 or more services on third party contractor rates Telstra obtained in 2005 for substantial network migrations in Adelaide and Perth. Details of these contractor charges were provided by

Telstra in August 2005. (Telstra, *Primus LSS access dispute – Telstra's submission*, August 2005, Annexure A) The Commission modelled the efficient cost estimate on the scenario where MNMs were performed in two stages: a pre-jumpering stage, and a cutover stage.

For smaller scale MNMs (involving between 20 to 49 services), the Commission proposed to base the efficient costs for these categories on third party contractor rates that Telstra obtained in 2005 for 'single' connections at the one exchange or at exchanges in close proximity. Details of these contractor charges were provided by Telstra in August 2005. (Telstra, *Primus LSS access dispute – Telstra's submission*, August 2005, Annexure B)

The Commission proposed to adopt the materials cost (i.e., the cost of copper pairs used to connect points on the MDF) that Telstra modelled in previous proceedings. No allowance was made for materials in disconnection costs, as no cable is required. The costs proposed were, for CBD areas, [c-i-c], and for other areas [c-i-c]. This was on the understanding that these costs weren't already included in third party contractor charges.

The Commission proposed a mark-up of 10 percent on third party contractor rates to cover indirect costs such as contract management costs, in preference to Telstra's previously claimed mark-up of [c-i-c] percent. This reflected the view that when using third party contractors, Telstra will avoid the indirect cost categories that comprise its claimed mark-up. Further, efficiently incurred contract management costs would not represent a significant component of per LSS connection costs.

The Commission sought the parties' views.

Parties' submissions

Telstra confirms that the contractor charges for MNMs used in preparing the draft determination are correct, and these charges have applied from April 2005 to now. Telstra advises that the charges to apply in future are being negotiated, and as a result they may increase. [Telstra 4/5, Part 4, p.5] Telstra subsequently provided revised rates agreed with contractors to apply from I June 2007. These rates are for LSS MNM connections made, by way of pre-jumpering and cut-over, either in the one visit or in two visits to the exchange. [Telstra, 10/7] Telstra does not object to a 10 per cent mark-up for indirect costs. [Telstra 4/5, Part 4, p.5]

Telstra considers that efficient costs should be modelled upon the scenario where pre-jumpering and cutover activities are done on separate days. In Telstra's view, this maximises the number of services that can be cutover on the day. [Telstra 14/5, Response to Primus, Part 3, p.3]

Telstra confirms that the contractor charges include the cost of materials. [Telstra, 14/5, Response to Chime, Part 3, p.1]

Primus submits that the efficient cost for larger scale MNMs should be modelled on the scenario where the service is cutover in a single step. In its view, pre-jumpering is unnecessary, and only serves to increase associated costs, especially where the service order is cancelled after pre-jumpering. [Primus, 4/5, pp.20-21]

Primus and Chime also question whether contractors charge Telstra on the basis of a two-stage process, even where such a process is adopted. [Primus 14/5, Part 4, pp.4-5] [Chime 18/5, pp.15-16]

Primus submits that the cost allowances for MNMs should be revised down, in line with revised contractor charges that apply to LSS 'single' connections at the one exchange or at exchanges in close proximity. [Primus, 14/5, Part 4, p.3]

Commission's views

The Commission had proposed different per connection costs for these categories to apply to larger-scale and smaller-scale MNMs, on the understanding that contractor charges would differ materially in each case.

The Commission has revised this approach following Telstra's further advice in its submission to the joint hearing of 4 May 2007 concerning contractor charges that apply to 'single' connections at the one exchange. The average of these charges is now below the charges that apply to MNM connections.

In these circumstances, it is unlikely that a contractor would require a premium above the agreed per connection charge in order to conduct a smaller scale MNM. And so, the agreed MNM rate has been applied as an efficient benchmark for the jumpering costs for all MNMs.

Contractor rates for LSS 'single' connections are pegged to rates for 'ADSL simplex' connections; but LSS MNMs are performed for access seekers alone. Telstra may not have as compelling an incentive to seek the most efficient connection costs for LSS MNMs, given these flow through to LSS access seekers only.

As contractors have agreed to perform LSS 'single' (ADSL simplex) connections on average more cheaply than the agreed rate for LSS MNM connections, there could be scope to reduce the allowance for jumpering costs for MNM connections. At this time, the Commission has not done so. However, further consideration could be given to this option should LSS MNM connection rates remain above LSS 'single' connection rates.

As contractors incur the cost of materials, they are already reflected in contractors' charges and the Commission has not included a further and discrete allowance for materials costs.

The Commission notes that a 10% mark-up for indirect costs is not controversial.

The remaining issue is whether efficient cost should be modelled on a single process or two-stage process. Further, if a two-stage process is used, whether the associated costs have been correctly estimated.

Adopting the position put by Primus would reduce the allowance for these cost categories by around $3. The Commission is satisfied that the contractor charges that Telstra has reported for MNM connections done in two stages or single stage have been correctly reported, given Telstra's express confirmation of them. It considers it is reasonable that the 'two-stage charge' would be higher than the charge for 'cancellation following pre-jumpering', as more work would be involved in connecting the jumpers than in simply removing the pre-jumper on a cancelled order.

Here, the approaches that the Commission could adopt would be (i) to model jumpering and related costs on a single process; or (ii) to model efficient jumpering and related costs on a two-stage process. The Commission has assessed these options against the section 152CR(1) criteria.

On the first criterion and the promotion of competition, a single process would be preferable if this better reflects the forward-looking, efficient cost of performing MNM connections. If so, this would better facilitate efficient entry and exit by suppliers in the supply of downstream DSL services. The effect on competition would be most pronounced in marginal exchanges, where higher MNM charges may preclude entry by LSS-based suppliers.

The information before the Commission does not clearly establish whether, looking forward, one or other approach would be more efficient in a particular instance. The fact that Telstra has negotiated rates for each eventuality suggests that a single stage process could be more efficient for some MNMs at least. The Commission anticipates that the least cost approach could vary between MNMs, depending upon whether, e.g., pre-jumpering would increase or decrease the number of technician days required for that MNM. It will also be influenced by access seeker preference. However, it could be that, at least in the longer term, contractors may be unwilling to perform ‘single stage’ MNMs at the lesser charge unless this represented the least cost option to them.

Next, efficient use and investment will be encouraged where Telstra is able to recover efficiently-incurred costs of MNMs, including a normal commercial return on capital employed. MNM charges above this level for LSS-based competitors would have the effect of discouraging efficient investment in and use of infrastructure used to supply the LSS. Use and investment in downstream services would likely be below efficient levels as a result.

Following on from the discussion regarding the promotion of competition, the Commission considers that the efficient, forward-looking level of these cost categories would likely fall somewhere in between the contractor charges that apply to the single stage and two-stage process. This is on the basis that some MNMs will use a single process, and others follow a two-stage process. At this time, the Commission does not have information to allow it to estimate where in this range the efficient cost measure would most likely fall.

Telstra’s legitimate and commercial interests, including its interest in recovering its direct costs would be satisfied by modelling these costs on the basis that a two-stage process is always required. The alternative approach would prevent full cost recovery except for those MNMs where a single stage process is adopted.

For MNMs performed to date, Telstra consulted at least some access seekers and it was their preference for a two-stage process to be adopted. This approach represents a higher quality service, in that it minimises necessary disruptions to end-user service provision. It would be contrary to Telstra’s legitimate interests to now model costs on the lesser-quality single-stage approach.

The next criterion concerns the legitimate business interests of the access provider, and the carrier’s or provider’s investment in facilities used to supply the declared service. The Commission’s views on the effect of this decision on these matters are discussed as part of the first criterion. These would be better met by basing MNM charges on a two-stage process, especially for MNMs previously performed.

Looking ahead, access seekers’ interests could tend to be compromised by basing MNM charges on only the charges associated with a two-stage process when they do not require the increased quality associated with the two-stage process. This could impede their ability to compete on their merits to the extent that it allowed costs to exceed the actual charges paid to contractors, or the increased costs could not be justified in terms of the associated increase in quality.

Telstra’s ability to recover the direct costs of MNMs (including a contribution to overheads) will be better ensured by basing MNM charges on a two-stage process. However, this approach may exceed to a small extent what is required to recover direct costs going forward, in those cases where an access seeker requests a single-stage process.

The Commission does not consider that the next two criteria are particularly relevant here. There is no information to suggest that the adopting one or other approach would lead to unsafe practices being used, for instance.

The last criterion concerns the economically efficient operation of a carriage service, a telecommunications network or a facility. As noted above, the Commission considers that should an approach result in MNM charges that are above efficient forward-looking levels, then this would impede competition. If so, Telstra would be able to set above-cost prices for its services, leading to a reduction in the consumption of these services below efficient levels, and consequential allocative inefficiencies.

Weighing these considerations is a matter of judgment. In these proceedings, the Commission accepts a two-stage MNM process as the approach more consistent with the statutory criteria, especially for MNMs that have already occurred. Accordingly, it has modelled MNM connection charges on this basis. That said, should an access seeker prefer that a single-stage process be adopted for future MNMs, it can negotiate on this basis.

Costs for 2006-07 and 2007-08

The Commission indexed the back-of-house costs for 2006-07 and 2007-08. The Commission used *ABS 6345 Labour Price Index 'Ordinary time hourly rates of pay excluding bonuses; Australia; Communication services; Private; All occupations'.*

The Commission has not indexed contractor charges, but has used the rates as negotiated for each period.

In specifying a charge for the period from 1 June 2007, the Commission has adopted the agreed rate with the first contractor for a two-visit LSS MNM (as per Telstra's advice on 10 July 2007). The Commission considers that specifying the LSS MNM charge on this basis is reasonable, as it will reasonably align with the costs Telstra is likely to incur.

The actual LSS MNM connection cost Telstra faces may, in some instances, be *[c-i-c redaction]* a little higher or lower depending upon, e.g., whether the MNM requires one or two visits. *[end c-i-c redaction]* And so, the actual cost faced by Telstra will depend upon the distribution of LSS MNM connections between the four price points that Telstra has supplied. However, it is not possible to estimate on the available information the precise cost, as the likely distribution of LSS MNM connections is not known.

Cost model

A simple cost model that adopts the Commission's views is attached to these reasons. This model is further simplified from the model distributed at the draft determination stage. The contents of this cost model are to be treated as [c-i-c] and subject to the confidentiality undertakings given and directions made, as it reproduces information that is confidential to the parties.

Averaged or de-averaged charges

As noted previously, the Commission decided to base MNM charges on a geographically averaged estimate of the efficient costs of providing these MNMs. As a result of the approach taken to materials costs, the costs of MNMs do not differ significantly between geographic bands.

Bands 1, 2, 3

The Commission did not specify charges to apply to LSS MNMs in Band 4, due to there being little if any demand for these connections.

4.3.7 MNM connection charges

Introduction

The Commission proposed different schedules of charges to apply to larger-scale and smaller-scale MNMs.

Parties' submissions

Telstra objected to this approach, as it considered that the resulting rate table was too complicated and too difficult to implement within an automated billing system. [Telstra, 4/5, Part 4, p.4] Access seekers considered the difficulties of implementation were overstated. [Chime, 18/5, p.14] [Primus, 14/5, Part 4, p.2]

Commission's views

As discussed above, as a result of revised information provided in respect of jumpering and related costs, the fixed and variable costs associated with smaller and larger scale MNMs are, in fact, similar. In these circumstances, a simple two part tariff for MNM connections can align with costs. Accordingly, the Commission has been able to simplify the MNM connection charges, with a single schedule of charges to apply to all MNMs.

MNM disconnection charges

The Commission proposed not to allow LSS disconnection charges where the LSS is disconnected as part of a MNM. This reflected the view that any associated costs would be taken into account in setting connection charges for that MNM type. The migration type to which this is potentially of more relevance is a migration from the LSS to ULLS. The parties did not object to this approach being adopted. [Telstra, 4/5, Part 4, p.8]

4.3.8 Forecasting timeframes and MNM plan amendment terms

Introduction

Chime and Primus (but not Request) each seek final determinations that address MNM forecasting timeframes and MNM plan amendment terms.

These terms have required that, for each MNM, the access seeker is to advise Telstra of the exchange and the number of services to be migrated, and the week in which the cutover is to occur. This 'forecast' must be made at least 84 calendar days before the requested cutover date. The forecast is confirmed, or updated, 56 calendar days before the cutover date. The access seeker confirms, and provides details of the full national number of the services to be cutover, 20 business days before the cutover date. There are limits on an access seeker's ability to alter the number of services to be cutover as part of a MNM within 56 calendar days of the cutover. Limits also apply to the number of MNMs an access seeker can request for a given day.

The Commission has not considered these terms previously. For the purposes of the draft determination the Commission adopted the terms specified in the current customer relationship agreements, and sought the parties' views.

Parties' submissions

Telstra provides details of tasks performed during the MNM forecast period. These tasks are performed by the wholesale front of house (WCSG) and IDS/PDC workgroups. Some of these are done soon after the MNM request is initially submitted; others are performed when the MNM request is confirmed; and some are performed when the full national numbers of the services to be cutover have been provided.

Telstra considers that these forecasting timeframes are appropriate to ensure the smooth operation of MNMs, and permit contractors to be arranged to perform exchange-based work. The notice periods are also designed to protect Telstra from incurring unnecessary costs arising from cancellations. Telstra notes that when forecast demand is not reached at a particular exchange, the *per-connection* cost to Telstra increases. [Telstra, 4/5, Part 4, pp.8-9; Annexure A & B] [Telstra, Reply to Primus, 14/5, Part 3, p.4]

Telstra submits that variations to MNMs arise primarily from inaccurate forecasting by access seekers, which are circumstances beyond Telstra's control. Telstra also advises that the limitation of one MNM per state per day allows

Telstra to meet its obligations to all access seekers. First, there is a limit to the number of technicians that can work at an exchange at once. Second, a limit of one MNM per state per day per access seeker ensures a level of equivalence for all access seekers. [Telstra, Reply to Primus, 14/5, Part 3, p.10]

Telstra submits that the Commission's proposal of only permitting cancellation charges in respect of cancellations that occur within 20 business days of the scheduled date of a LSS MNM would prevent Telstra from recovering costs that are reasonably incurred earlier in the process. Telstra claims a significant proportion of the work and cost associated with the effective execution of a MNM occurs between 84 days and 56 days prior to the scheduled week of a MNM. [Telstra, 4/5, Part 4, p.10]

Chime objects to an 84-day forecast period, and considers that a 56-day forecast timeframe is more than sufficient to allow Telstra to allocate staff or arrange contractors for a MNM. Chime states that this is supported by the Commission's approach to date in regards to MNM cancellation charges, in that an efficient operator would not incur costs for MNM cancellations before 20 days prior to the proposed cutover date.

Chime also considers that it is unreasonable that Telstra should be able to amend a migration plan without Chime's consent and without the same right being given to Chime. Chime considers that it should be allowed to vary forecast figures 20 percent in both directions prior to 42 days from the cutover date, and 10 percent in both directions up to 14 days before the cutover date. [Chime, 4/5, p.18]

Primus states that the existing MNM forecasting timeframes are unnecessarily slow, cumbersome and inflexible. In its view, a 56 day forecast timeframe is sufficient to allow Telstra to allocate staff or arrange contractors for a MNM. Furthermore, Primus considers that a single confirmation date at 20 days prior to the cut over sufficiently protects Telstra's interests in efficiently allocating staff and contractors.

Primus considers that there is no reasonable explanation that it is restricted to a daily limit of one MNM in each State. In Primus's opinion, a lead-time of 56 days provides Telstra with sufficient time to allocate staff or arrange contractors without this restriction. [Primus, 4/5, pp.22-23]

Primus also notes that it is unreasonable that Telstra should be able to amend a migration plan without Primus's consent without the same right being given to Primus. [Primus, 4/5, p.24]

Commission's views

In considering these terms, the Commission has sought to remove unnecessary delays to MNMs being completed, while not compromising Telstra's ability to efficiently manage MNM processes. This calls for a weighing of potential benefits from additional flexibility in the MNM process, against possible detriments to MNMs generally if forecast accuracy and lead times are insufficient to properly manage MNM processes.

The Commission has considered against the section 152CR(1) criteria three possible approaches to these terms: (1) Maintaining the current arrangements as advocated by Telstra; (2) Providing the additional flexibility as sought by access seekers; and, (3) Providing some additional flexibility, but not all changes that access seeker's sought, and providing measures that seek to promote accuracy in the forecasts and some flexibility in the actual cutover date.

More particularly, the third approach that the Commission considered was to reduce the forecast period to 56 calendar days, and allowing modest fluctuations in forecast volumes. This option does not remove the daily limits on MNMs per state. This option also provides for cancellation charges to apply in all cases where MNMs are forecast for an exchange, and then completely withdrawn.

On the information before the Commission, an 84 day forecast period is unnecessary to perform the project management tasks associated with a particular MNM. The work done within the 84 to 56 day range would not take a substantial amount of time and can be easily accommodated within the 56-day period.

The longer forecast period could potentially be supported if it is reasonably necessary to the efficient conduct of all MNMs; where, e.g., it was necessary to efficiently manage contractors. However, the information before the Commission indicates that the 84-day forecasts would contribute little to this goal. The 84-day forecasts were not passed on to contractors, and Telstra's submissions suggest the volumes forecast at this time were not in any event reliable.

On the information before the Commission, unlimited variations to the forecasts once submitted would tend to compromise Telstra's ability to effectively manage its contractors. This is because large fluctuations in individual forecasts will mean that either too many or too few contractor resources will have been allocated to that MNM. However, the same could not be said for small variations in volumes, where the same level of resourcing would remain appropriate.

Further, it is likely that the number of wholesale ADSL services supplied to the access seeker in the relevant exchange will vary within the eight week forecasts period. This will be due to, e.g., end-user churn, rather than a lack of care when submitting the initial forecast.

To this end, the Commission considers that Telstra should not unreasonably refuse variations that are submitted by the access seeker. This reflects an approach that has been adopted in practice between the parties.

What is unreasonable would depend upon the particular circumstances. However, as general guidance, the Commission would consider that it is likely to be unreasonable to refuse a variation of up to 10 per cent (either above or below the original forecast volume). Further, there could be scope to reasonably accommodate higher order variations the earlier that the request for variation is notified.

Departures from forecast data will not impede cost recovery, as MNM connection charges (including minimum charges) will fully recover project management costs for MNMs that proceed; and cancellation charges will apply for all MNMs that are cancelled following inclusion in a 56 day forecast. This will promote reliability in 56-day forecasts.

Where Telstra cannot reasonably commence a MNM cutover on the agreed cutover date, then, as provided by the Customer Relationship Agreement, Telstra is to commence the cutover as soon as reasonably practicable following the agreed cutover date. This provides leeway where a particular agreed cutover date cannot be met within the 56-day forecast period.

The Commission considers that arguments in favour of ongoing limits to the number of MNMs an access seeker can forecast per day per state are relatively weak. However, at this time, the Commission considers it is generally unlikely that the current arrangements would materially delay finalisation of a network migration program.

This conclusion would hold unless the access seeker has forecast migrations in a significant number of exchanges in a particular state. At present, access seekers have typically restricted forecasts to metropolitan exchanges within each state. Should this change, so that a larger number of exchanges could be involved in

MNMs, then further consideration could be given to the reasonableness of the restriction remaining.

For general guidance, the Commission notes that if rationing mechanisms are necessary, these should be applied only until relevant capacity can be increased. Further, they should respond to the constraint. Where, e.g., available space restricts the number of MNMs that can be performed at the exchange at the one time, the rationing measure should deny access to that exchange to the additional MNMs until the following day. On their face Telstra's restrictions act to deny access to exchanges on the basis of possible constraints, regardless of whether capacity is actually constrained.

In applying the section 152CR(1) criteria, the Commission first considered the long term interests of end-users, and within this criterion, the promotion of competition. The Commission considers that current arrangements impede competition, as they prevent or delay the migration of services at least cost. Additional time and uncertainty associated with migrating services present obstacles to competition, as they tend to discourage access seekers from entering and competing by use of own DSLAMS. This will ultimately be to the detriment of the long term interests of end users.

Reducing delays between forecasts and cutover, and providing a reasonable degree of flexibility to vary forecasts, will tend to alleviate these competition concerns. The access seeker's proposals for further flexibility may further promote competition in the short term, but risks reducing competition in the longer term if it were to compromise the efficacy of MNM processes.

Economic efficiency in use of and investment in infrastructure used to provide listed services requires consideration of Telstra's infrastructure as well as the infrastructure of LSS access seekers. MNM restrictions would tend to discourage otherwise efficient use of and investment in infrastructure used to provide the LSS and downstream DSL services. This is because those restrictions would delay MNMs completing or prevent existing services being migrated to the LSS at least cost. Uncertainty or delay will discourage take up of the LSS, and use of Telstra's LSS ordering systems, as well as discourage efficient investment in access seeker's DSLAMs.

Telstra's legitimate business and commercial interests, including the recovery of direct costs, are satisfied under the third proposed approach. Telstra's interest in recovering project management costs is satisfied, as well as Telstra's interest in the efficient management of resources used to deliver the MNM program more generally. The Commission notes that a 56-day forecast timeframe has been used for LSS MNMs, and on occasions MNM forecast volumes have been able to be amended within limits without adverse consequence. Measures to encourage greater reliability in forecasts will further support Telstra in efficiently managing contractors.

In contrast, maintaining the current approach would not be necessary to ensure these interests are met; while moving to the position advocated by access seekers could compromise these interests, should they prevent Telstra from effectively managing resources used to make MNMs.

The Commission considers that LSS access seekers' interests lie in being able to compete on their relative merits without being unnecessarily delayed, or being denied access to more efficient (least cost) MNM connection processes. These interests are promoted by arrangements that provide more timely access to MNMs, and avoid additional costs that would be incurred if MNMs were not able to be used. The Commission considers that the third proposed approach would meet these interests. The arrangements that access seekers would prefer may go further than what is necessary to achieve these interests, or may not be sustainable if they were to compromise the efficacy of MNMs more generally. However, maintaining the current approach would be contrary to these interests.

The Commission's approach to MNM minimum charges, MNM connection charges, and cancellation charges, means that in all eventualities, the efficient cost associated with a MNM will be borne by the LSS access seeker.

The Commission considers the third proposed approach will provide Telstra with reasonably reliable forecast data that may be necessary to ensure the safe and reliable operation of the facilities it uses in providing MNMs. For instance, sufficient time will be available to ensure safe access to facilities.

Similarly, the Commission considers that the third proposed approach will encourage the efficient operation of carriage services and associated networks and facilities by both Telstra and LSS access seekers. Were the current arrangements to remain, competition in downstream services will suffer as LSS access seekers will be delayed in accessing efficient MNMs, and thereby discouraged from making additional investment in DSLAM infrastructure. A lessening of competition would have significant adverse consequences for the efficient supply of downstream services.

In comparison, the access seekers' proposed approach could compromise the efficient operation of facilities used to provide the LSS, should it compromise Telstra's ability to effectively manage contractors' access to those facilities.

The Commission considers the third option it has proposed balances the interests of Telstra and LSS access seekers, and better ensures that the economically efficient operation of both Telstra's and access seekers' carriage services and facilities will be encouraged.

After applying these criteria to the three identified approaches, the Commission considers that the third option should be preferred, as it is more consistent with each of the criteria than the other approaches.

In implementing this approach, the Commission has retained the existing structure of the Customer Relationship Agreement. Hence the requirement to provide an initial forecast (now at least 56 days before cutover) and a separate 56 day plan remains. However, there is scope for this documentation to be combined, or else the timing of the plan to be brought closer to cutover date. This is something the parties can resolve between themselves.

Cancellation charges

Introduction

The Commission proposed that cancellation charges are to be paid where a MNM is cancelled, or the number of services to be connected as part of a MNM is reduced, 20 business days or less from the cutover date. This reflected the view that cancellation charges would be necessary in each of these instances to enable efficiently incurred costs to be recovered.

The proposed charges were a charge of 50 cents per service, plus an additional charge of $18 where the cancellation follows pre-jumpering.

Parties' submissions

Telstra considers the proposed charges are too low to enable it to recover costs associated with cancellations. It considers that the 50 cent per service allowance is too low to recover back-of-house costs, and should reflect the total back-of-house costs associated with a MNM. Further, the contractor charge for cancelled orders after pre-jumpering is *[c-i-c redaction]* more than the proposed allowance of $18. *[end c-i-c redaction]* [Telstra, 4/5, Part 4, pp.10-11] Telstra considers that significant project management tasks are performed between ordering and

20 days from the cutover date, and these costs should be able to be recovered in all cases. [Telstra, 14/5, Response to Chime, Part 3, p.4]

Primus objects to paying for pre-jumpering. In its view, pre-jumpering is done at the election of Telstra. [Primus, 4/5, pp.21-24] Primus considers cancellation charges are unnecessary where the cancellation occurs more than 20 business days from the cutover date, as no significant costs would be incurred by an efficient operator before this time. [Primus, 14/5, Part 4, p.2] Chime and Request support the proposed approach to cancellation charges. [Chime, 4/5, p.18] [Request, 4/5, p.40]

Commission's views

The Commission has varied its approach to cancellation charges following the parties' submissions. The changes are to better ensure that back-of-house costs will be recovered in the case of cancelled MNMs, and that contractor-related costs will be recovered in the case of cancelled services following pre-jumpering. They are also intended to promote more reliable MNM forecasting, to compliment the other initiatives discussed above.

To achieve this, the Commission has removed the '20 business days or less' condition for 'standard' cancellation charges to apply, and increased the allowance for back-of-house costs for 'MNM cancellations' within the 'standard' cancellation charge. A 'MNM cancellation' is where an access seeker cancels the entire MNM, as opposed to simply reducing the number of services to connect.

The Commission has also increased the allowance for cancellations following pre-jumpering to reflect the charges contractors impose in this instance. The Commission's views on whether 'two-stage' (pre-jumpering followed by cutover) or 'single-stage' MNM processes should be adopted as the efficient MNM process are provided previously. However, these charges are only able to be imposed where the cancellation occurs not less than 20 business days from the cutover date as it would not be necessary for an access provider to pre-jumper earlier than this.

This approach leads to a (entire) MNM cancellation charge of $126 in 2005-06 (indexed for later years), and a 'cancel following pre-jumpering charge' of $23.60 per relevant service for 2005-06 and following years. Telstra's letter of 10 July 2007 did not expressly update the cost data concerning 'pre-jumpering' for the period from 1 June 2007; or provide contractor charges for a combined LSS MNM process, which appear to have operated as a basis for setting the contractor's charge. The information provided in this letter for LSS pre-jumpering and cutover on the same visit suggests that it is reasonable to retain the $23.60 charge for 2007-08. This is because these cost data suggest that, at least in some instances, Telstra will face a lesser cost, should the relevant contractor charge continue to be aligned with 'LSS combined' rates.

On the other hand, the Commission has not specified a 'standard' cancellation charge to recover back-of-house costs for MNMs that proceed with a reduced number of services. This is because the back-of-house costs will still be fully recovered in the MNM charge, including the minimum MNM charge, under the two part tariff that has been specified for those charges.

Further, the possibility of a MNM being deferred as a result of too great a variance between original forecasts and actual cutovers provides an appropriate degree of encouragement for accurate forecasts. And so, an additional 'penalty' type charge is not needed for this purpose.

4.3.10 Pre-requisites to ordering a MNM and minimum MNM connection charges

Introduction

The Commission proposed to the parties that there should be a minimum charge payable for all MNMs, and that this should be based upon the cost of a MNM involving 20 services. However, the Commission proposed that there should be no minimum number of services to be connected before a MNM process could be requested. This reflected the view that access seekers are best placed to determine on the basis of the time and cost associated with a MNM process whether it would be preferable to request a MNM.

Parties' submissions

Telstra submits that it would be unreasonable not to specify a minimum number of services as a pre-requisite to requesting a MNM. Telstra submits that it incurs significant fixed costs in relation to a MNM, and not imposing a minimum number of services would be inconsistent with this. [Telstra, 4/5, Part 4, p.4,11]

Telstra submits that it could accept a 30 service MNM, but would need time to change its systems and processes. [Telstra, 4/5, Part 4, pp.4-5]

Chime, Request and Primus support basing the minimum charge on a 20 service MNM. Primus considers that basing the minimum charge on a higher number of services could make an exchange service area unviable for LSS-based supply. [Primus, 14/5, Part 4, p.2] Chime also supports the approach of not specifying a minimum number of services as a pre-requisite for a MNM. [Chime, 4/5, p.18] Request notes that it typically uses a MNM process when connecting between 20 and 49 services at an exchange to the LSS. [Request, 4/5, pp.38, 40]

Commission's views

The Commission has determined to maintain the position proposed to the parties.

The Commission considers that 20 services is an appropriate scale for MNMs to be requested, as the connection of this number of services can be performed at less cost when done as part of a MNM. This is demonstrated by comparing the cost of 20 connections (as per the cost model for LSS MNMs) ($752.50) to the costs associated with making 20 LSS 'single' connections.

This is not to say that access seekers will always request a MNM for this number of connections at an exchange. They may prefer the shorter connection timeframes offered by 'single' connection processes.

The Commission has not specified a minimum number of connections to qualify for a MNM. The Commission considers that access seekers should have flexibility to request a MNM even if there are fewer then 20 services to connect if this is the approach that they consider preferable. However, Access seekers will still pay for the MNM as though they were connecting 20 services given the specification of the minimum charge.

The approach taken to setting MNM connection charges means that Telstra's 'largely-fixed' back-of-house costs will be recovered in all instances. This is because of the inclusion of a fixed amount within MNM connection charges, including the minimum MNM charge, to recover this fixed cost component.

The final determination will take effect 21 days after the date it is made. As Telstra has previously supplied MNMs comprising 20 services, the Commission does not consider that there is a need to provide additional time for systems changes in order for these arrangements to be implemented.

In terms of the section 152CR(1) criteria, the Commission considers that this approach promotes competition, by removing obstacles to service providers migrating services to the LSS, and migrating services at the efficient, forward-looking cost. LSS-based supply will allow service providers greater ability to differentiate the price and quality of downstream DSL services they offer to end-users.

Economic efficiency in use of and investment in infrastructure used to provide listed services requires consideration of Telstra's infrastructure as well as the infrastructure of LSS access seekers. Restricting MNM processes to larger scale migrations, when MNM processes can result in more efficient outcomes for smaller scale migrations, would tend to discourage otherwise efficient use of and investment in infrastructure used to provide the LSS and downstream DSL services.

This is because those restrictions would delay MNMs completing (until sufficient demand is accumulated within the exchange) or prevent existing services being migrated to the LSS at least cost. Uncertainty or delay will discourage take up of the LSS, and use of Telstra's LSS ordering systems, as well as discourage efficient investment in access seeker's DSLAMs.

This approach satisfies Telstra's legitimate business and commercial interests, including its interest in recovering direct costs, as the minimum MNM charges, and MNM connection charges, permit Telstra to recoup the costs associated with MNMs. It also is consistent with access seekers' interests in being able to compete in downstream markets on the basis of the price and quality of the services they can offer.

The Commission does not consider that higher minimum MNM charges, or a minimum number of services as a MNM pre-requisite, are necessary to promote safe and reliable operation of the network or facilities, or to ensure the recovery of costs Telstra has incurred in making any enhancements that MNM processes may represent.

The Commission considers that the economically efficient operation of carriage services and associated networks and facilities of the access provider and access seekers will be encouraged by smaller-scale migrations utilising MNM processes. This is because it will promote competition in downstream services by removing obstacles to connecting the LSS, while ensuring that efficient costs of connecting the LSS is able to be recovered. Greater competition in the supply of downstream DSL services will encourage efficiency in the supply of those services.

4.3.11 Commencement date, expiry date and interest

The Commission has backdated the LSS MNM connection charges. The balance of the terms that the Commission has specified in relation to LSS MNMs will commence when the final determination comes into effect. These terms are to apply until 31 December 2007. Interest is payable on any over-payment that has occurred. The term of backdating, and reasons for this approach, are discussed previously.

4.3.12 Changes to draft final determination

A number of the terms specified in the final determination differ to some extent to those proposed at the draft determination stage. These changes reflect revised cost data, or approach to cancellation charges, forecasting timeframes and migration plan amendments and backdating for the MNM connection charges. Reasons for these changes are discussed previously.

Further, the decision not to backdate certain of the charges has meant that it is not necessary to specify charges to apply for 2004-05, 2005-06 and 2006-07 for all charges. Any 'obsolete' charges have been deleted.

Minor drafting changes were made to make clear that parties can override the operation of the final determination terms by subsequent agreement, and that, like the MNM connection charges, the MNM minimum charge is not to apply to Band 4 MNMs.

5. TERMS AND CONDITIONS ADDRESSED IN SEPARATE HEARING

5.1 LSS service qualification related charges.

'Service qualification' is the process of checking whether a particular line is capable of supporting a service.

5.1.1 Current charges

Tables CRA191.2 and CRA191.3 specify charges to apply to LSS service qualifications. A charge is payable on the making of a service qualification inquiry, and a separate charge is payable where the service qualification inquiry is not followed by an order. *[c-i-c redaction]* Different arrangements apply depending on whether or not the service qualification inquiry is submitted via LOLO/LOLIG. *[end c-i-c redaction]*

5.1.2 Prior consideration

The Commission has not considered these charges previously.

5.1.3 Principles to apply

The Commission proposed that, consistent with the LSS pricing principles, the LSS service qualification charges should reflect the TSLRIC+ of providing these service qualifications. However, the Commission noted that the relatively small scale of current LSS service qualification charges may mean that a full TSLRIC+ analysis may not be justified, and that it may be appropriate for any TSLRIC+ estimate to be made from higher level data or observations.

5.1.4 Terms to apply

Introduction

The Commission proposed to the parties that the current arrangements should continue, and sought the parties' views.

Parties' submissions

Telstra considers that there is not a dispute, or if there is, it is not a dispute relevant to a standard access obligation that Telstra owes, as service qualifications occur prior to any ordering or provisioning of the LSS. [Telstra, 4/5, Part 6, p.1]

[c-i-c redaction] Telstra further submits that if there is a dispute, it is not of a material consequence to Primus. *[end c-i-c redaction]* [Telstra, 14/5, Response to Primus, Part 4, p.1]

Primus submits that manual service qualifications are inconsistent with an efficient access provider, which would be able to provide automated service qualifications in all cases. Primus also considers that the costs of the staff that perform manual service qualifications are included in the cost pool for LSS connection charges. And so, LSS service qualification charges risk double recovery of underlying costs. [Primus, 4/5, supplementary submission, p.2]. Primus submits that the Commission has jurisdiction to deal with LSS service qualifications, as it is a matter relating to access to the LSS. Primus also submits that there is an ongoing dispute. [Primus, 14/5, Part 6, p.1]

Primus does not consider that it should pay a second charge for service qualifications not followed by an order. In its view, no additional cost is caused by the decision not to follow the service qualification with an order. [Primus, 4/5, supplementary submission, p.2].

Commission's views

The Commission has jurisdiction to deal with this issue, as there is a dispute and the dispute relates to Primus's access to the LSS for the purpose of supplying carriage and/or content services to end-users. The Commission is able to deal with all matters relating to access to the LSS. [Section 152CP]

Service qualification provides information to a service provider as to whether a service could be supplied on a particular line, and comprises an early step taken within the ordering and provisioning of a service.

Hence there is a direct nexus between LSS service qualifications and a service provider accessing the LSS. Further, the terms applicable to LSS service qualifications will form part of the terms on which Telstra satisfies its standard access obligation to provide ordering and provisioning of the declared service.

That such a nexus exists is supported by the contractual terms that have applied between the parties concerning Telstra's supply of the LSS to Primus.

The Commission notes that it need not address each and every aspect of access that may be disputed, should the subject matter of a dispute be trivial, misconceived or lacking in substance. [Section 152CS] However, the Commission does not consider that the dispute is of such a nature.

In March 2005, the Commission advised the parties that it was then not satisfied it should deal with service qualification charges. The Commission has since been informed that Primus could be liable to service qualification charges in around [c-i-c] percent of occasions it seeks to qualify a LSS (i.e., whenever automated service qualifications cannot be performed).

The information before the Commission does not indicate that an efficient service provider would not need to conduct any manual service qualifications, or conduct them less frequently than Telstra. Hence, the Commission considers that the forward-looking, efficient cost associated with LSS service qualifications would include an amount for manual intervention on those occasions when the automated system fails.

The costs associated with providing manual service qualifications that are followed by an LSS order have been included in the cost base allowed for LSS connection charges, and/or annual charges. LSS connection costs include an allowance for manual service qualification work undertaken by the DAC. [Consultel, *Analysis of ULLS and LSS undertakings and subsequent submissions – final report*, February 2006, pp. 34-35] Further an allowance for relevant WSCG costs is included in LSS annual charges. As these charges are paid in respect of all LSS that are connected, it would be inappropriate for Telstra to impose an additional 'LSS service qualification' charge for manual service qualifications that result in a LSS order being submitted.

The information before the Commission does not establish that the charges for manual service qualifications that are not followed by an order are above the costs of efficiently conducting those service qualifications. Nor is it clear that relevant costs are already being recovered through other charges. Accordingly, the Commission has not sought to vary the charges to apply in this instance in the final determination.

5.1.4 Commencement date, expiry date and interest

Neither party sought backdating of these terms. These terms are to apply from the commencement of the final determination until 31 December 2007.