

Public

RG 021203
29 February 2012

Grahame O'Leary
Josh Davies
Communications Group
Australian Competition and Consumer Commission

By email

accessdeterminations@acc.gov.au
grahame.oleary@acc.gov.au
joshua.davies@acc.gov.au

Draft Final Access Determination for the Domestic Transmission Capacity Service

Macquarie Telecom Pty Limited ("**Macquarie**") welcomes the opportunity to make this submission to the Australian Competition and Consumer Commission ("**ACCC**"). This submission is in response to the ACCC's draft final access determination for the domestic transmission capacity service ("**DTCS**") and its accompanying pricing model and explanatory statement.¹ Macquarie appreciates the progress that the ACCC has made toward the objective of achieving fair cost-based pricing of the DTCS. However, while the Draft FAD is a welcome development, the final DTCS pricing objective has not yet been reached.

Against this background, this submission sets out relevant background to the Draft FAD, various concerns that Macquarie has with the Draft FAD and Macquarie's suggested way forward.

Background to the Draft FAD

Australia's communications sector is undergoing significant regulatory reform through the implementation of the Australian Government's national broadband network ("**NBN**") policy agenda. At the same time, the Government recognises that competition in the provision of services which use legacy copper networks must be protected in order to underpin the success of competition in the emerging NBN environment. An essential part of this recognition is the ACCC's work in setting cost-based prices for wholesale network services which are essentially supplied by Telstra to competing carriers. With the ACCC having set cost-based prices for a range of fixed access services in 2011, including ULL and WLR services, the setting of cost-oriented prices for the DTCS remains an outstanding item on the ACCC's agenda.

Macquarie recognises the difficult task facing the ACCC in the pricing of the DTCS. The ACCC has adopted a domestic benchmark DTCS pricing methodology by which the

¹ ACCC, Draft final access determination for the domestic transmission capacity service (DTCS), December 2011, ("**Draft FAD**") and Draft final access determination for the domestic transmission capacity service (DTCS), Explanatory Statement, December 2011, ("**Explanatory Statement**")



Public

regulated prices are derived from observations of prices of transmission services which are supplied in competitive markets. The ACCC's work on DTCS pricing over the previous year has involved *inter alia*:

- promulgating an interim access determination (“**IAD**”) for the DTCS in April 2011;²
- promulgating a draft regression model in July 2011;³
- conducting an industry forum in August 2011; and
- promulgating a further DTCS pricing model, the Draft FAD and the Explanatory Statement in December 2011.

The industry is now faced with the Draft FAD which, if the ACCC decides to make final, will lock-in a pricing methodology which will apply for the period until 31 December 2014.

Macquarie's Concern with the Draft FAD

Macquarie appreciates the progress that the ACCC has made on DTCS pricing through the promulgation of the Draft FAD. The pricing approach which underlies the Draft FAD results in much improved price outcomes compared with the ACCC's earlier IAD. Save for some pricing anomalies, the Draft FAD pricing model produces DTCS prices which are generally lower than Telstra's existing DTCS prices. This outcome is in line with the expectations of industry that the prices observed in competitive markets will be *ceteris paribus* lower than the prices voluntarily set by Telstra in non-competitive markets.

While the Draft FAD provides an improved pricing outcome, Macquarie remains concerned with various aspects of the Draft FAD as follows:

- DTCS pricing anomalies;
- three year lock-in of the DTCS pricing model; and
- unclear DTCS pricing evolution.

DTCS Pricing Anomalies

The DTCS pricing model if adopted would result in lower overall DTCS charges across the suite of DTCS acquired by Macquarie. This result is, however, a net outcome of various price increases offset by various price decreases for specific services. In particular, the pricing of 2 Mbps services in regional routes, especially the longer distance routes, would result in price reductions of 50 *per cent* or more. Such price decreases are offset by increases in the pricing of 2 Mbps services on short distance (0-10kms) metropolitan routes of 20-50 *per cent*. Macquarie understands that a 2 Mbps, short distance, metropolitan route is the “standard” DTCS sought by access seekers which accounts for the clear majority of the services provided in the market.

Some examples of the price increase for the standard DTCS that result from the ACCC's pricing model compared to Telstra's existing prices are shown in the following table.

² ACCC, Interim Access Determination No. 7 of 2011, (DTCS), 18 April 2011.

³ ACCC, Domestic Transmission Capacity Service (DTCS), Draft regression model for consideration in the public inquiry into a final access determination for the DTCS, July 2011.

Public

Standard DTCS: Existing Prices vs ACCC Prices

Service	Existing Telstra Price per Month \$	ACCC Price per Month \$	Price Increase \$ (%)
2 Mb, 0-5 km, Metropolitan Example routes include: - Haymarket to Pyrmont - West Ryde to Gladesville - Sth Melb to Collins St MEL	[cic]	421	[cic]
2 Mb, 6-10 km, Metropolitan Example routes include: - Clarence St SYD to Rosbery - Clarence St SYD to Hillsdale - Flinders St MEL to Footscray	[cic]	482	[cic]

Macquarie is concerned that the Draft FAD would result in prices which are higher than those voluntarily set by Telstra for the standard DTCS. Given that there is no price constraint on services supplied in “monopoly” areas and that Telstra would not supply such services at below-cost prices, a further rise in prices through the Draft FAD would be a perverse outcome. Such an outcome (which would occur if the ACCC were to accept the Draft FAD) would be fundamentally detrimental to competition and would be contrary to the interests of end-users. Accordingly, Macquarie urges the ACCC to revisit the proposed pricing of these services.

Three Year Lock-in of the DTCS Pricing Model

Macquarie notes that a key input to the DTCS pricing model is pricing data which is essentially 12 -18 months old. At the same time, it is evident that the prices of transmission services are generally falling in line with long-term competitive and technology driven trends. Macquarie is strongly of the view that it is not appropriate to lock-in DTCS prices for three years when prices are generally anticipated to fall. The lock-in of DTCS prices will be detrimental to the interests of end-users as they will be denied the benefits of price reductions. Moreover, the lock-in would be detrimental to competition.

Macquarie acknowledges that the lock-in of DTCS prices for three years would be consistent with the objective of providing regulatory certainty. While Macquarie generally welcomes regulatory certainty, this must be balanced with the interests of end-users and the need to protect and promote competition. Accordingly, Macquarie cautions against a three year price lock-in for the DTCS.

Unclear DTCS Pricing Evolution

It would appear to Macquarie that the ACCC may have a tendency to view the DTCS pricing in the Draft FAD on a “set and forget” basis. That is, that the methodology of pricing the DTCS has now been set and need not be revisited until 31 December 2014 approaches. Macquarie is strongly of the view that the ACCC’s oversight of the pricing of the DTCS must continue on its evolution informed by a cost-based methodology. Otherwise, Telstra will continue to reap excessive prices, competition will be constrained and the interests of end-users will be harmed. Accordingly, Macquarie contends that such an outcome is untenable.



Public

Way Forward

Macquarie welcomes the Draft FAD as a positive step towards the effective regulation of the DTCS. However, in the light of Macquarie's concerns with the Draft FAD as discussed above, Macquarie believes that the ACCC, in the process of finalising the Draft FAD, must commit to the following actions:

- a refinement of the DTCS pricing model with a view to eliminating or reducing the impact of pricing anomalies particularly in the case of the standard DTCS, i.e., 2 Mbps, short distance, metropolitan routes;
- undertaking a further review of DTCS prices which would have effect from a date no later than 1 July 2013; and
- on-going collaboration with industry to develop a cost-based approach to the pricing of the DTCS.

The first of these actions is intended to make immediate and minor adjustments to the DTCS pricing model as are necessary to overcome existing pricing anomalies particularly in respect of the standard DTCS. This may, for example, involve a review of the integrity of the ACCC's data set or a change in the relative weighting that the model applies to particular pricing inputs.

The second action is intended to work within the construct of the DTCS pricing model together with those adjustments arising from the previous action. The key feature of this action is to reassess DTCS prices on the basis of an updated competitive pricing data set. That is, it is not intended that the ACCC would develop a new DTCS pricing model *per se*. Such a pricing review is intended to ensure that access seekers (and ultimately end-users) are not precluded from the benefits arising from the anticipated price reductions in the DTCS which would occur in line with market trends.

A further aspect of this second action is for the ACCC to review its DTCS model prices against Telstra Economic Model ("**TEM**") data provided by Telstra to the ACCC in accordance with its structural separation undertaking. Such data should provide a sound basis on which to assess the appropriateness of the ACCC's DTCS model prices.

The third action recognises that the benchmark DTCS pricing model is a proxy for a cost-based model and that efforts should continue towards achieving the cost-based pricing of the DTCS. While the development of a cost model is a major exercise, it may become more manageable if, for example, the cost model focused on the standard DTCS, i.e., 2 Mbps, short distance, metropolitan routes.

Public

Closing

Macquarie appreciates the progress that the ACCC has made on DTCS pricing over the past year. This submission sets out various concerns that Macquarie has with the Draft FAD and Macquarie's suggested way forward to overcome these concerns. Should you have any queries regarding this submission please feel free to contact me.

Yours sincerely



Chris Zull
Senior Manager - Regulatory & Government

T 03 9206 6848
E czull@macquarietelecom.com