



Australian  
Competition &  
Consumer  
Commission

# Telstra's compliance with the price control arrangements

1 July 2009 to 30 June 2010



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Report to the Minister for Broadband,  
Communications and the Digital Economy

Australian Competition and Consumer Commission  
23 Marcus Clarke Street, Canberra, Australian Capital Territory 2601

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# 1. Background and executive summary

Under s. 151CM(1)(b) of the *Competition and Consumer Act 2010*, the Australian Competition and Consumer Commission (ACCC) must report to the Minister for Broadband, Communications and the Digital Economy on the adequacy of Telstra's compliance with the price control arrangements that apply to it.

These price control arrangements are set by the minister. The current arrangements are contained in Telstra Carrier Charge—Price Control Arrangements, Notification and Disallowance Determination No.1 of 2005 (the determination) as amended.

This report relates to the fourth reporting period under the current arrangements—the 12-month period from 1 July 2009 to 30 June 2010.

The ACCC considers Telstra has adequately complied with these price control arrangements. This view is based on the ACCC's review of an independently audited compliance report that Telstra provided.

## 1.1 Summary of the price control arrangements

The central framework of Telstra's retail price control arrangements consists of a series of price caps that apply to specified 'baskets of services'.

The first basket of services consists of local calls, trunk (national long-distance and fixed-to-mobile) calls, international calls and line rentals. This basket is subject to a price cap of Consumer Price Index (CPI)—CPI per cent. This means that Telstra is entitled to change the individual prices of the services within the basket as it wishes, but the aggregate price of all services in the basket must not increase in nominal terms.

The second basket consists of Telstra's most basic line rental product offered to residential customers. In the current reporting period, this basket was subject to a price cap of CPI–0 per cent.

The third basket consists of Telstra's most basic line rental product supplied to business customers and charity customers. This basket is also subject to an annual price cap of CPI–0 per cent.

The fourth basket consists of connection services and is subject to an annual price cap of CPI–0 per cent.

All public switched telephone network (PSTN) services, except those supplied to large business customers on individual contracts, are subject to the price caps.

Each price cap is an independent price cap and is not subject to any overall price cap. That is, price movements for each basket will be reported separately and are not required to be averaged to an overall price movement for all services.

Telstra is able to claim credits for investing to improve the quality of the services within the baskets, which are offset against actual price movements. Also, if Telstra prices below the maximum level permissible, the difference may be carried forward as a credit into the next price cap period.

The determination also provides for a number of other price controls.

- The price for untimed local calls is not to increase above 22 cents (GST inclusive) for each call (other than a local call made from a public payphone, or a local call made using a calling card), except in the case of discount plans when a customer may be required to pay more than 22 cents per local call.
- Local calls, and Telstra's most basic line rental product, supplied in non-metropolitan areas must be offered at the same or a lower price and on the same price-related terms as in metropolitan areas.
- Telstra must offer a line rental to schools at a price at or below the standard line rental offered to residential customers.
- Increases in line rentals charged at residential rates must be notified to the ACCC, and are subject to the ACCC being satisfied that Telstra has in place a low-income package, and that Telstra consulted with the Low Income Measures Assessment Committee before making any changes to that package.
- The price of each call to an internet service provider using a data network access service number starting with the numerals 0198 is not to exceed 22 cents (GST inclusive).
- Telstra must notify the minister in advance if it intends to alter charges for directory assistance services, with the minister able to disallow the proposed changes if they are considered not to be in the public interest.

Telstra is required to report to the ACCC on its compliance with the price control arrangements, within three months of the end of a price cap period.

## 2. Methodology for determining revenue-weighted price movements

Under clause 13(5) of the determination, the value of a price movement for a basket of services may be determined in accordance with a methodology developed by the ACCC in writing.

Following consultations with Telstra, in January 2007 the methodology for administration of the Telstra carrier charges price control arrangements (the methodology) was established for the period from January 2006 to June 2009. This methodology was later extended to cover the 2009–10 financial year.

The methodology defines the price movement for a component service within a basket of services as a percentage change between the following:

- yield calculated from post-discounted revenue and usage (demand) for the price cap period
- yield calculated from post-discounted revenue and demand for the financial year immediately preceding the price cap period.

The price movement for a basket of services is calculated by weighting the price movement for each component service and summing the weighted price movements.

## **3. Auditing of Telstra's price control report**

### **3.1 Audit process and requirements**

The methodology requires Telstra to provide a final, independently audited report to the ACCC, providing full details of its compliance with the price cap requirements, within three months of the end of the price cap period.

The aim of the audit is to determine whether:

- Telstra has complied with the price cap requirements specified in the determination and the methodology
- Telstra has complied with the procedural requirements specified in the determination and the methodology
- Telstra has exercised consistency in applying the methodology specifications to its data capture systems
- Telstra has in place internal procedures and information management systems to efficiently monitor and report on its compliance with its obligations under the determination and the methodology, including any change to these procedures or systems that may have a material effect on its monitoring and reporting.

The methodology states that the independent auditor will be appointed by the ACCC, so that it may be directly involved in the planning of and approach to the audit as well as having direct access to the auditor's independent advice. In consultation with Telstra, Ernst & Young was appointed as auditor for the 1 July 2009 to 30 June 2010 price control compliance report.

### **3.2 Audit opinion**

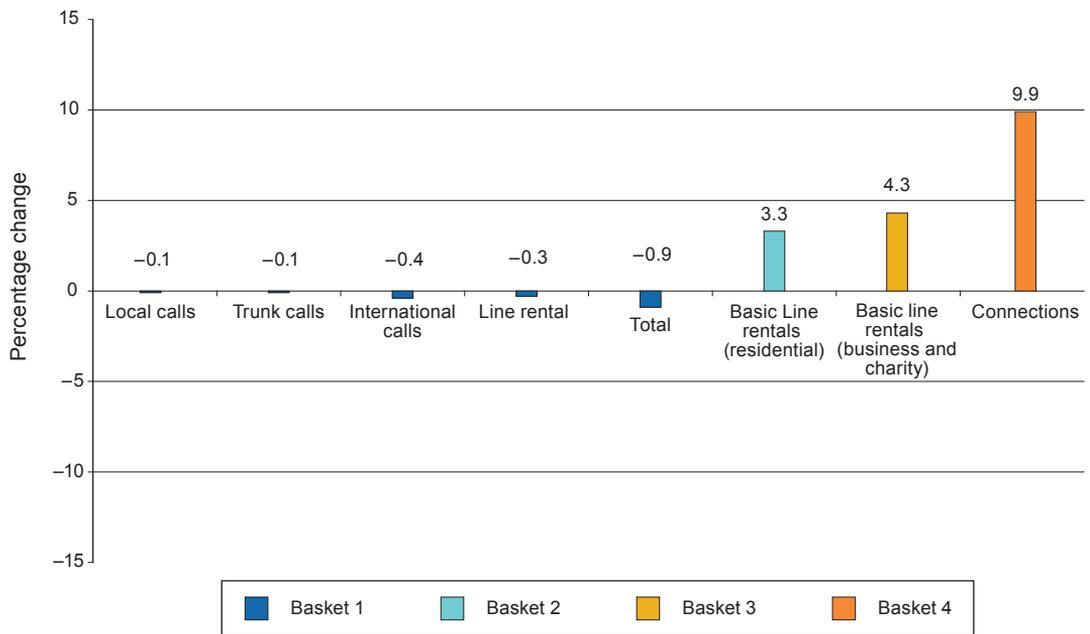
The auditor has expressed the opinion that Telstra has in all material respects fairly presented its compliance report to the ACCC in complying with the determination and methodology as it relates to the aims of the audit as described above.

## 4. Telstra’s compliance with the price control arrangements – 1 July 2009 to 30 June 2010

### 4.1 An overview of the revenue-weighted price movements for Telstra’s services

Figure 1 shows the revenue-weighted price movements for each of the Telstra services subject to the price control arrangements during the period 1 July 2009 to 30 June 2010.

**Figure 1: Telstra’s revenue-weighted price movements for 1 July 2009 to 30 June 2010**



### 4.2 Deemed price reduction for quality improvement

To calculate Telstra’s compliance with the price control arrangements, the determination states that Telstra can be credited with deemed price reductions where it increases the quality of its services. During the current reporting period, no quality improvement related credits were claimed.

## 4.3 Telstra's compliance with the price caps

Table 1 below assesses the weighted price movements against the price cap for each of the four baskets of services during the current reporting period.

For instance, table 1 shows that the first basket of services consists of local calls, trunk calls, international calls and line rentals. (Trunk calls consist of national long-distance calls and fixed-to-mobile calls). For each component service the table sets out the:

- reported price movement
- revenue weight
- weighted price movement.

The table then lists the:

- overall price movement
- CPI value used
- cap (in this case CPI–CPI)
- carry-in credit from 2008–09.

The table then records the reported surplus of 3.7 per cent.

Accordingly, Telstra could have charged a price for the first basket that was 3.7 per cent greater than it actually charged and met the price cap. This is also the carry-in credit that Telstra will be entitled to claim for 2010–11.<sup>1</sup> The reported surplus of 3.7 per cent largely reflects the carry-in (2.9 per cent) from the previous reporting period. Telstra reported a 0.9 per cent decrease in the weighted average prices of services in the first basket during the reporting period.

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<sup>1</sup> The retail price controls methodology has changed for 2010–11: carry-in credits from the 2009–10 price cap period are to be calculated by Telstra using the average number of Services In Operation (SIOs), rather than the method outlined in the previous methodology. The carry-in credit may differ slightly using this different method of calculation.

**Table 1: Telstra's weighted price movements in relation to all four baskets of services during 1 July 2009 to 30 June 2010**

	<b>Service</b>	<b>Price movement (%)</b>	<b>Revenue weight</b>	<b>Weighted price movement (%)</b>
<b>Basket 1</b>	Local calls	-0.8	0.107	-0.1
	Trunk calls	-0.1	0.369	-0.1
	International calls	-10.1	0.037	-0.4
	Line rentals	-0.7	0.487	-0.3
	Overall		1.000	-0.9
	CPI			+3.1
	Cap (CPI-CPI)			+0.0
	Carry-in from 2008-09			+2.9
		<b>Surplus (%)</b>		
<b>Basket 2</b>	Basic residential line rentals	+3.3	1.000	+3.3
	CPI			+3.1
	Cap (CPI-0)			+3.1
	Carry-in from 2008-09			+0.6
		<b>Surplus (%)</b>		
<b>Basket 3</b>	Basic business and charity line rentals	+4.3	1.000	+4.3
	CPI			+3.1
	Cap (CPI-0)			+3.1
	Carry-in from 2008-09			+1.5
		<b>Surplus (%)</b>		
<b>Basket 4</b>	New connections	+4.6	0.467	+2.1
	In-place connections	+14.5	0.533	+7.7
	Overall		1.000	+9.9
	CPI			+3.1
	Cap (CPI-0)			+3.1
	Carry-in from 2008-09			+18.4
		<b>Surplus (%)</b>		

\* Figures do not add up because of rounding.

The specified CPI measure represents the aggregate price movement in the 'all groups' basket for the weighted average of the eight Australian capital cities, as published by the Australian Bureau of Statistics, for the financial year *immediately preceding the financial year in which the relevant price control is to apply*. From June 2009 to June 2010 the CPI increase was 3.1 per cent.

## 4.4 Telstra's compliance with maximum prices for untimed local calls and calls for extended zones

The determination requires that Telstra charge a price of not more than 22 cents (GST inclusive) for each untimed local call, other than an untimed local call made from a public payphone, which is capped at not more than 50 cents (GST inclusive).

It also requires that Telstra charge for calls between customers within an extended zone<sup>2</sup> and between a customer in an extended zone and a customer in an adjacent extended zone at an untimed local call rate. Moreover, Telstra must not charge for preferential calls at a rate of more than the untimed local call rate specified in clause 16 of the determination.

The maximum prices charged for each of these calls as reported by Telstra are set out in table 2.

**Table 2: Maximum prices for untimed local calls and calls in extended zones**

Call type	Maximum charged (\$ including GST)
Extended zone call	0.22
Preferential call	Untimed local call rate
Call to Telstra's BigPond internet service	0.22
Local call from payphone	0.50
Local call	0.22
Dial-up internet call (0198)	0.22

## 4.5 Telstra's compliance with the metropolitan/non-metropolitan 'pricing parity'

The determination requires that Telstra offer untimed local calls, extended zone calls and dial-up internet calls in metropolitan areas at the same or lower price per call and on the same price-related terms as those charged to its customers in non-metropolitan areas.

The rationale for this price control arrangement is to ensure that price reductions in areas where competition has developed also become available to customers in areas where competition may not yet have developed.

Similarly, Telstra is obliged to offer its most basic line rental products<sup>3</sup> on the same, or better, price terms in non-metropolitan areas. Only a small proportion of customers are acquiring these particular line rentals. Should other more popular line rentals increase significantly in price, however, the basic line rental products could act as a safety net, and the parity arrangement will ensure that the safety net is equally available in metropolitan and non-metropolitan areas.

Telstra certified that there were no instances where it did not comply with the pricing parity requirements during the period 1 July 2009 to 30 June 2010.

<sup>2</sup> In general terms, extended zones are areas that fall outside Telstra's standard local call charging zones. They are defined by telephone number ranges and are not always linked directly to a geographic boundary.

<sup>3</sup> During the reporting period, Telstra's most basic line rental products were HomeLine Part and BusinessLine Part.

Telstra reported that its standard offers do not differ between customers in metropolitan areas and those in non-metropolitan areas.

Telstra also reported that it may negotiate non-standard contracts with some customers, meaning that certain offers are not available in all areas. Telstra stated, however, that its preparedness to negotiate non-standard contracts with customers does not vary between metropolitan and non-metropolitan areas.

## **4.6 Telstra’s compliance with requirements to offer standard line rental for residential/charity customers and schools**

Under clauses 18 and 19A of the determination, Telstra is required to offer a standard line rental for residential/charity customers.

The standard line rental is the most popular line rental charged at residential rates. During the price cap period, the standard line rental was HomeLine Plus and the price was \$29.95 (GST inclusive) per month.

Should Telstra supply a residential/charity customer with line rental at a price below that charged for a standard line rental, Telstra is allowed to charge that customer for untimed local calls in excess of the maximum untimed local call price set out in the determination—that is, more than 22 cents per call.

During the reporting period, Telstra offered one such arrangement to residential customers, namely:

- HomeLine Budget—on which Telstra charged a line rental of \$20.95 (GST inclusive) and 30 cents per local call (GST inclusive).

Under clause 19 of the determination, Telstra is required to offer schools a line rental at or below the standard line rental it offers to residential and charity customers.

Telstra reported that it had satisfied this obligation by noting within its standard customer terms that schools are eligible to receive the line rental prices that Telstra offers to non-profit organisations, namely:

- BusinessLine Complete (non-profit organisation)—on which Telstra charged a line rental of \$17.73 (GST exclusive) per month.

## **4.7 Telstra’s compliance with the requirement to notify the ACCC of increases in line rental charged at residential rates**

Under the determination, line rentals charged at residential rates must not be increased unless Telstra has notified the price increase and the ACCC is satisfied that Telstra has complied with clause 22 of the Carrier Licence Conditions (Telstra Corporation Limited) Declaration 1997 (the declaration). The ACCC cannot refuse to consent to a proposed line rental increase on any other basis.

Clause 22 of the declaration requires Telstra to have measures in place to ensure that low-income customers have access to basic telephony services. Specifically, clause 22 requires Telstra to:

- have a low-income package in place that has been endorsed by low-income consumer advocacy groups and specified in writing to the Australian Communications and Media Authority
- have a marketing plan in place for the package, approved by the Low Income Measures Assessment Committee
- obtain and consider the views of the Low Income Measures Assessment Committee on proposed changes to the package.

The ACCC is satisfied that Telstra complied with these requirements in the period 1 July 2009 to 30 June 2010.

Telstra notified the ACCC on 15 September 2009 of an increase in residential line rental charges for both existing and new customers of its HomeLine Part product from \$34.45 (GST inclusive) to \$34.95 (GST inclusive) effective from 1 November 2009.

# ACCC contacts

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Callers who are deaf or have a hearing or speech impairment can contact the ACCC through the National Relay Service [www.relayservice.com.au](http://www.relayservice.com.au).

Voice-only (speak and listen) users—phone 1300 555 727 and ask for 1300 302 502.

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