

Proposed change to the pricing of AGVC/VLAN and implications for the prices of other fixed services

Purpose

The ACCC is seeking stakeholder comment on a proposal to re-calibrate how the AGVC/VLAN charge for the wholesale ADSL service is determined within the Fixed Line Services Model (FLSM) for the purposes of the forthcoming fixed line services FADs. This also has implications for wholesale ADSL port charges and the prices of other declared fixed line services.

In particular the ACCC has considered whether:

- the draft decision to apply a uniform price change gave rise to unanticipated consequences in the case of the wholesale ADSL service
- the rapid take-up of video streaming services has implications for the current FAD inquiry.

It is not proposed that this consultation will alter the ACCC's timing for the release of the final decision on the FAD for the fixed line services.

Background and Issues

This consultation is undertaken in the context of the ACCC's draft decision to apply a uniform price change to the declared fixed line services and submissions received from stakeholders in response to the draft decision.

The March 2015 draft decision proposed a uniform price change for the fixed line services. An outcome of this position is that individual service prices and revenues recovered would no longer be determined on the basis of costs allocated to each service within the FLSM. Under this position the most significant departure of prices and revenue from allocated costs occurs for the wholesale ADSL service.

In addition, the proposal for a uniform price change means that the share of the wholesale ADSL revenue recovered through the AGVC/VLAN charge would be [c-i-c start] [REDACTED] [c-i-c end] per cent, much higher than the share of [c-i-c start] [REDACTED] [c-i-c end] per cent that was accepted for the 2013 wholesale ADSL FAD and which was based on an attribution of the revenue to the two pricing components determined by Telstra.¹

The March 2015 draft decision supported the uniform price change as best achieving the objective of price stability:

The ACCC considers that applying a uniform price change to all declared services and maintaining price relativities will minimise any undesirable consequences of setting prices for individual services using the current approach. The ACCC considers that the uniform price change will provide stability to the industry in the transition to the NBN. This will minimise incentives for access seekers to change the way they provide services to end users and allow for continued efficient use of infrastructure already in use, which will in turn promote efficient use of declared services. It will also avoid any adverse impacts on competition from changing price relativities.

In July 2015 the ACCC sought information from Telstra and access seekers through information requests to assist it to form a view on the price terms for the AGVC/VLAN charge.

¹ ACCC, *Public inquiry to make a final access determination for the Wholesale ADSL service*, Final Report, Public Version, May 2013, p. 49.

The information obtained in responses indicates to the ACCC that:

- Some access seekers are currently operating at very high AGVC/VLAN utilisation levels per SIO for the wholesale ADSL service and that further requirements for increased bandwidth at the proposed price for the AGVC/VLAN charge in the further draft decision could render the service uneconomic to purchase.
- Some access seekers are finding it necessary to acquire substantially more AGVC/VLAN capacity as a direct consequence of markedly increased consumption of video and streaming content in recent months.

- [c-i-c start] [REDACTED] [c-i-c end]

The ACCC's revised pricing proposal

The ACCC considers that the departure from prices that just recover the costs allocated to each service in the FLSM under the draft decision to apply a uniform price change will disproportionately impact acquirers of the wholesale ADSL service. The reason is that, under the proposed uniform price change, it is the wholesale ADSL service for which the revenues diverge most from the allocated cost, much more in dollar terms than for any other service. In addition, there is recent evidence that access seekers are acquiring higher levels of AGVC/VLAN capacity to meet increased demand from the uptake of video streaming services and an expectation that this will continue. The concern with the uniform price change is that it results in an AGVC/VLAN charge significantly higher than would result if the price was based on the costs of the wholesale ADSL service alone.

The ACCC considers that, in the case of the AGVC/VLAN component of the wholesale ADSL service, the departure from strictly cost reflective prices gives rise to specific disadvantages that outweigh the advantages of the uniform price change noted in the March 2015 draft decision and reproduced above. In particular, the combination of stronger than anticipated demand combined with the AGVC/VLAN price proposed under the uniform price change approach could result in over-recovery by Telstra and distort competition. This is because RSPs rely on this service to compete outside their own infrastructure footprint and competition in these regions may be impeded during the transition to the NBN by the AGVC/VLAN charge resulting from the uniform change proposal. Therefore, the uniform price change is likely to result in an AGVC/VLAN charge that is not in the long term interests of end users (LTIE). Accordingly, reducing this charge to address the significant adverse impacts that may occur under the uniform pricing proposal is likely to encourage efficient use of, and investment in, infrastructure and to promote competition.

The ACCC's proposal involves the removal of the AGVC/VLAN capacity charge from the uniform price change applied to the declared services and setting it independently. To achieve this, the AGVC/VLAN charge is set at a level to recover [c-i-c start] [REDACTED] [c-i-c end] of the wholesale ADSL share of the total fixed line revenue requirement calculated under the uniform price reduction proposal. This AGVC/VLAN share of the wholesale ADSL revenue to be recovered under the uniform price change approach is the same as the share established for the 2013 wholesale ADSL FAD. The AGVC/VLAN charge is therefore determined via a method more consistent with previously established practice.

The ACCC draft modelling indicates that the revised AGVC/VLAN price would be \$17.90 per Mbps per month, which represents a fall of 45 per cent compared to its currently regulated level. The remainder of the charges, including the wholesale ADSL port charges, are then

determined by applying the uniform price change approach. This is done by subtracting the revenue to be recovered through the AGVC/VLAN charge (\$17.90 multiplied by forecast AGVC/VLAN demand) from the total revenue requirement to be recovered through the regulated fixed line services. The resultant uniform price fall for all services other than the AGVC/VLAN charges is 5.8 per cent.² This is based on all other aspects of the pricing determination being unchanged from the June 2015 further draft decision. If, as the ACCC finalises its view on the multiple factors that contribute to modelling the price outcome, there is any change that would alter the 9.6 per cent uniform price change estimated for the further draft decision, such changes could also impact both the draft \$17.90 AGVC/VLAN charge and the uniform price change for the other services.

The ACCC notes that its revised proposal on the charges for the wholesale ADSL service has some similarity with the proposal [c-i-c start]

[c-i-c end] the ACCC's proposal is that the revenue reduction is absorbed by a lesser fall in the prices of all fixed services (including the port charges) than would occur with the uniform price reduction of 9.6 per cent proposed in the further draft decision.

The ACCC reiterates that the revised proposal on primary price terms is made with reference to its June 2015 further draft decision. The ACCC's proposal does not alter the overall revenue requirement determined in the FLSM, which is still 9.6 per cent lower than would be realised assuming currently regulated prices. However, it does mean that the costs of the AGVC/VLAN to access seekers—and also the possibility of over-recovery by Telstra—will be lower than would have been the case under the further draft decision uniform price reduction proposal. It also means that the costs to access seekers of the other fixed services, including the wholesale ADSL port charges, will be greater than in the further draft decision proposal.

The ACCC invites comments on the above proposal by **COB Friday 21 August 2015**. Responses should be sent via e-mail to fixedservices@acc.gov.au.

Queries can be directed to Jane Goldwater on (03) 9290 1493 or jane.goldwater@acc.gov.au.

² This price modelling was done in FLSM v.2.1 used for the June further draft decision.