# Variation to the NBN Co Special Access Undertaking

## Draft Decision

April 2023

Contents

# Abbreviations and acronyms

| | |
|---|---|
| ABBRR | Annual building block revenue requirement |
| ACCC | Australian Competition and Consumer Commission |
| ADSL | Asymmetric digital subscriber line |
| AER | Australian Energy Regulator |
| AVC | Access virtual circuit |
| BBM | Building block model |
| Capex | Capital expenditure |
| CCA | *Competition and Consumer Act 2010* (Cth) |
| CPI | Consumer Price Index |
| CVC | Connectivity virtual circuit |
| FTTB | Fibre to the building |
| FTTC | Fibre to the curb |
| FTTP | Fibre to the premises |
| FTTN | Fibre to the node |
| HFC | Hybrid fibre coaxial |
| ICRA | Initial cost recovery account |
| LTIE | Long-term interests of end-users |
| Mbps | Megabits per second |
| MRP | Market risk premium |
| MTM | Multi-technology mix |
| NBN | National Broadband Network |
| NBN Co | National Broadband Network Company Limited |
| Opex | Operating expenditure |
| RAB | Regulatory asset base |
| SAU | Special access undertaking |
| SAO | Standard access obligations |
| SIP | Statutory Infrastructure Provider |
| TC-4 | Traffic Class 4 |
| VDSL | Very high-speed digital subscriber line |

| | |
|---|---|
| WACC | Weighted average cost of capital |
| WAPC | Weighted average price control |
| WBA | Wholesale broadband agreement |

# 1. Executive Summary

In this draft decision, we reject the variation that NBN Co proposed to its special access undertaking (SAU) in November 2022, and provide our draft reasons and findings. We will move to a final decision after considering any further information and feedback that we receive in response. The draft reasons and findings may also assist NBN Co to develop a revised SAU variation proposal, should it wish to do so, that could be capable of acceptance.

The SAU establishes a framework for regulating access to the NBN, including rules by which maximum wholesale prices are determined and other measures that have important implications for competition and efficiency. Hence, the SAU can play an important role in maximising the economic and public benefits of the NBN.

The SAU commenced in 2013 and now requires a fundamental update to be effective. For instance, the SAU does not cover services supplied over all the access technologies that have since been incorporated into the NBN, and nor can it provide NBN Co with appropriate incentives to operate prudently and efficiently.

To update the SAU, NBN Co must propose an SAU variation, which the ACCC assesses against the relevant statutory tests, having regard to the submissions that we receive. We can decide to either accept or reject an SAU variation, but we cannot do so conditionally or substitute terms that we consider to be more reasonable than those proposed to us, or more likely to promote the long-term interests of end-users.

The SAU variation proposes a number of important initiatives that NBN Co developed in response to the views that it has received from stakeholders, including at stakeholder forums and working groups and in written submissions provided during consultation on an earlier SAU variation.

These initiatives have the potential to bring significant benefits should they be implemented as part of a robust framework and include:

- adopting a weighted average price control (WAPC), instead of a revenue cap, which aims to strengthen incentives to achieve revenue, cost, and demand targets.
- providing ex-ante and ex-post oversight over the prudency and efficiency of expenditures through a replacement module determination process.
- incorporating a service standards framework, with the aim of allowing better coordination in the regulation of the price and quality of access to the NBN.
- specifying the balance of the initial cost recovery account (ICRA) at $12.5 billion in current nominal terms, well below the amount that would result from a continuation of the current methodology, with the aim of providing additional long-term certainty while allowing a reasonable opportunity for NBN Co to achieve and then maintain a stand-alone investment grade credit rating during the SAU term.
- an initial resetting of prices for residential grade wholesale offers and adopting the 25/5 megabits per second (Mbps) speed tier as the entry level wholesale offer.
- initially limiting increases in the WAPC to no more than the Consumer Price Index (CPI). When NBN Co reaches annual cost recovery, which is currently projected for the 2030 financial year, this price control would transition to a CPI-X basis until FY2032. Price increases for individual wholesale offers would also be capped at a maximum of either CPI or the higher of CPI and 5 percent per annum up until 30 June 2032. From FY2033, the ACCC would have more discretion to specify maximum prices for wholesale offers in its replacement module determinations.

- requiring that NBN Co consult with stakeholders (including representatives of low-income groups) on its expenditure and pricing proposals, and including provisions aimed at increasing accountability when NBN Co is acting other than on a purely commercial basis, with the aim of promoting investment in projects of most value to its customers and to reduce the risk of unnecessary price rises.

These improvements notwithstanding, our draft decision is to reject the November 2022 SAU variation. We have reached this draft decision taking account of certain aspects of the SAU variation, which we consider significantly weaken its effectiveness and has the consequence that the SAU variation does not satisfy the statutory tests for acceptance established by Part XIC of the CCA.

In this regard, we are not satisfied that the proposed variation would result in access terms that promote the long-term interests of consumers over the duration of the SAU. This is due to

- limitations in the proposed process to periodically reset regulated access terms and other regulatory controls which are not reasonable, and which would risk access terms coming into effect by default that would not promote efficiency and competition.
- the principle that would require the ACCC to adjust NBN Co's revenue allowances during the post 2032 regulatory period to give it the opportunity to achieve its credit rating objective not being premised on NBN Co operating and investing efficiently. This would permit NBN Co to be compensated for the additional cost of achieving its credit rating objective that results from inefficiency, and risk price shocks for consumers.

We also found that the measures proposed for the first regulatory cycle following acceptance of the SAU variation (which would operate from 1 July 2023 to 30 June 2026) would be unlikely to efficiently address existing drivers of poor consumer sentiment towards NBN services, remove inefficient costs from the NBN supply chain, and promote retail competition. We consider this would in turn risk retail prices that are above efficient levels, and impact customer satisfaction scores, that would impede efficient use of the NBN in this initial period. We made these draft findings as

- the proposed benchmark service standards would likely be superseded before or soon after the SAU variation would come into effect, and the SAU variation would not commit NBN Co to effective consultation with retailers about measures that could be applied to efficiently address known causes of poor quality over the first regulatory cycle.
- the pricing model proposed in the SAU variation leaves open a very broad range of cost outcomes when using the standard 50 Mbps wholesale offer over this period, and it is unlikely that retailers could efficiently manage the residual cost uncertainty without further support from NBN Co.

We also consider that a revised SAU variation could bring greater clarity over the operation of the proposed Low-income Forum. This would provide additional assurance that the perspectives of low-income and disadvantaged consumers would be properly considered when NBN Co makes decisions of importance to them. In this regard, the SAU variation does not expressly state the scope of consultation and reporting that will be undertaken in connection with the Forum, with these important details left to subordinate documents which could potentially be amended without regulatory oversight.

We have reached draft findings that other aspects of the November SAU variation would not provide grounds to reject the SAU variation. This is because we consider that the approach that is specified in the SAU variation is reasonable and would promote the LTIE in the circumstances, including because we consider that targeted mitigations can safeguard against the risks that stakeholders had identified with what had been proposed.

The matters of most significance to stakeholders relate to the SAU variation's product and pricing proposal. Our draft findings include that it would be reasonable for the AVC price of the standard 50 Mbps wholesale offer to increase by $5 to $50 per month. Further, it would be reasonable for the cost of wholesale offers to progressively increase in nominal terms over the medium term, and for CVC charges to be phased out over the first regulatory cycle as NBN Co has proposed.

We make these draft findings because this approach to pricing access would be necessary for NBN Co to have a reasonable opportunity to recover its efficient forward-looking costs. We note that, as matters stand, NBN Co's revenues are materially below efficient cost levels, and that growth in demand alone could not reasonably be anticipated to make good this shortfall.

In our view it would be better to commence an orderly transition to efficient pricing now, and that this occurs gradually over time so that households and businesses are protected from sharper price increases in later years.

We are also publishing alongside this draft decision a letter that NBN Co has provided to the ACCC in which it outlines changes to aspects of the November SAU variation that it would be willing to make should it come to pass that the ACCC would not accept it. We note that these changes on their face are directed to many of the issues that have led to our draft decision to reject the variation, but certain other potential changes are also discussed in the letter.

The next steps in this consultation are to call for submissions on our draft decision, as well as to canvass views on the potential changes NBN Co has indicated it is considering for a revised SAU. We will then consider the submissions we receive and, unless it is first withdrawn, make a final decision on the November 2022 SAU variation.

We note that, based on NBN Co's letter, there is a likelihood that it will withdraw and lodge a revised SAU variation proposal. In that case, we would intend to quickly publish the revised SAU variation, and NBN Co's submission in support, and call for submissions.

We encourage NBN Co to take two actions before we make a final decision on an SAU variation. The first is to provide assurances that it will quickly resolve the ongoing competition concerns with its network-to-network interface charges, which smaller retailers continue to raise as impediments to expanding their operations over the NBN and competing more directly with incumbents. In its letter, NBN Co's states it is considering options to address these concerns, with a view to providing an update following this draft decision. The other is for NBN Co to publish its initial pricing roadmap and supporting worksheets for the first regulatory cycle.

NBN Co taking these steps would allow the SAU consultation process to focus on the core issues that go to the long-term regulatory framework, and to allow stakeholders to contribute on a more informed basis.

# 2. Introduction

## 2.1. Purpose

The purpose of this draft decision is to provide the findings that we have made on matters arising in connection with the SAU variation that NBN Co provided on 29 November 2022 and to advise stakeholders of the decision that we intend to make on whether to accept or reject that variation. These findings and our proposed decision are provided in draft form subject to any further information or submissions that we receive in response.

We have also included comments in this draft decision on some revisions to the SAU variation that could potentially make it capable of acceptance, which have come from the submissions that we received from stakeholders or from NBN Co in its letter dated 24 March 2023. We have published these submissions and NBN Co's letter. For clarity, we have included these comments to assist NBN Co in considering whether to withdraw and resubmit a revised SAU variation proposal and if so to assist NBN Co in developing this further variation. These comments also provide stakeholders with an opportunity to comment on potential changes that could be made in any revised SAU variation proposal.

## 2.2. The SAU variation and supporting documents

NBN Co's current SAU was accepted by the ACCC in December 2013. It established principles and a framework for regulating access to the National Broadband Network (NBN) until June 2040. It is also included detailed commitments regarding the pricing of wholesale offers during the NBN rollout. An overview of NBN Co's current SAU and the telecommunications access regime is at Annexure A.

The 29 November 2022 SAU variation is published on our website, along with the following materials that NBN Co has provided in support of its acceptance

- a covering letter, which provides additional context for the submission, including a description of each of the documents
- NBN Co's supporting submissions, separated into topics of discussion, to explain the rationale behind NBN Co's proposed changes to the SAU
- expert reports from Frontier Economics, Castalia, Analysys Mason and Roberson and Associates commissioned by NBN Co
- the core services BBM for the 2009-2023 and the 2024-2040 periods to assess essential variables and the effect that the proposed SAU variation would have on NBN Co's revenue constraint (NBN Co also provide a BBM handbook for both time periods)
- a set of forecasts in support of NBN Co's replacement module application. These forecasts include projected revenue, demand, and other metrics for the 2021 to 2026 financial years
- a template WAPC model to assist stakeholders and the ACCC to assess the proposed WAPC model in the SAU
- a cost allocation manual describing the methodology by which NBN Co's costs will be allocated in accordance with the principles of the SAU
- a draft statement of pricing intent.[1]

[1] The SAU variation and supporting materials are available here. They have been published in full save for a small number of redactions to Part F of NBN Co's supporting submission which the ACCC decided not to disclose having assessed NBN Co's claims for confidentiality. In addition, the version of NBN Co's building block model which we have published is the non-confidential version of that model

In broad terms, the SAU variation proposes to broaden the current SAU to cover each of the access technologies it has adopted since the SAU was accepted, along with making fundamental revisions to the regulatory framework with a view to improving its effectiveness. These changes are outlined in Section 3 of this draft decision.

## 2.3. Consultation

Our consultation on the SAU variation is occurring after extensive engagement with NBN Co and other stakeholders in previous regulatory proceedings. This has included stakeholder forums and working groups that we have chaired and via submissions to the SAU variation submitted in March 2022, which was subsequently withdrawn.

An important output of this early engagement was the development of five key outcomes from a varied SAU that could guide NBN Co's development of an SAU variation proposal. These were:

- NBN Co has the opportunity to earn the minimum revenues it needs to meet its legitimate financing objectives, including to transition to a stand-alone investment grade credit rating
- NBN end-users are protected from price shocks and from prices that are higher than necessary in later years
- the regulatory framework provides incentives for NBN Co to operate efficiently and promote efficient use of the NBN
- retailers have greater certainty over the costs that they will face when using the NBN
- there is a clear and robust quality of service framework so retailers and end-users know what to expect from NBN services, including a review mechanism so that service standards remain fit for purpose.

An overview of our stakeholder engagement and consultation prior receiving the current SAU variation proposal is at Annexure B.

We published the SAU variation on 30 November 2022 and then set a date for submissions of 17 February 2023. We published NBN Co's supporting materials as they were received, with most of these materials published in December 2022. We released a consultation paper on 13 January 2023 to further assist stakeholders in preparing submissions. These steps followed extensive consultation with stakeholders in 2021, including a series of industry working groups in the second half of 2021 to consider detailed aspects of the long term regulatory framework for NBN services.

We received submissions from 15 stakeholders in February 2023. The submissions are listed at Annexure D and published on the ACCC website. We have considered each of these submissions.

We additionally met with stakeholders throughout our consideration of the SAU variation to facilitate the making of submissions as part of the public consultation process. We have only considered information and submissions to the extent that they have been provided to us as part of the public consultation process or will be tested publicly.

### Submissions to the draft decision

We seek stakeholder submission on our draft decision within 4 weeks from its publication. This also includes views on the draft findings that we have made and the indicative comments that we have provided on potential changes that could be made in any revised SAU variation proposal to respond to certain issues.

To enable an informed and transparent process, all submissions will be published on the ACCC's website. Submitters are encouraged to provide a public version of their submission that keeps any confidentiality redactions to a minimum. The ACCC's approach to considering confidentiality claims and its approach to publishing information contained in submissions is set out at Annexure D.

### Format for submissions

The ACCC prefers to receive submissions in electronic form, in either PDF or Microsoft Word format which allows the submission text to be searched.

Please email submissions by 5pm on 30 May 2023 to nbn@accc.gov.au and copy to:

Sean Riordan
General Manager, Communications Markets and Advocacy
ACCC
Sean.Riordan@accc.gov.au

Scott Harding
Executive Director, Communications Markets and Advocacy
ACCC
Scott.Harding@accc.gov.au

## 2.4. Timeframe for assessment

The ACCC must decide to either accept or reject a proposed variation within 6 months of receiving it, subject to any permitted extensions. If it does not do so within this period, it is deemed to have accepted the variation.

The ACCC may extend (or further extend) the time for assessment by a period of not more than 3 months in accordance with section 152CBG (9) of the CCA. The ACCC must give written notice to NBN Co explaining why the Commission is unable to decide on the variation within the six-month (or previously extended) period and publish the notice on the ACCC website.[2]

In addition, the ACCC's decision-making period will also be extended by the following:

- the period in which the ACCC is undertaking the first public consultation
- any period during which the ACCC has requested further information from NBN Co under section 152CBH and the request remains unfulfilled.

The ACCC published NBN Co's proposed variation on the ACCC website on 30 November 2022 and set a due date for submissions of 17 February 2023. In addition, the ACCC made a request for information under section 152CBH of the CCA on 31 January 2023, which NBN Co provided its final response to on 26 April 2023. Consequently, by our calculations 8 days of the assessment period had elapsed by the time that the ACCC published this draft decision.

The ACCC intends to make its final decision on whether to accept or reject the SAU variation as soon as it is practicable to do so, taking into account the scale and complexity of the issues that arise in stakeholder submissions on this draft decision.

## 2.5. Assessment framework and our approach to its application

The ACCC must decide to accept or reject a proposed SAU variation after assessing it against the legislative criteria. This includes assessing it in accordance with section 152CBD(2) of the CCA.

---

2 CCA, subsections 152CBG(9) and (10).

The ACCC must not accept a proposed variation unless:

- the terms and conditions specified in the variation in relation to compliance with the category B standard access obligations are consistent with those obligations and are reasonable
- any conduct that is specified in the variation in relation to access referred to in section 152CBA(3B) will promote the LTIE, and the related terms and conditions are reasonable
- any conduct that is specified in the variation in relation to certain matters referred to in section 152CBA(3C) will promote the LTIE.

In determining whether a particular thing promotes the LTIE, the CCA requires the ACCC to consider the extent to which the thing is likely to result in the achievement of the following objectives:

- promoting competition in markets for listed services
- achieving any-to-any connectivity in relation to carriage services that involve communications between end-users
- encouraging the economically efficient use of, and economically efficient investment in the infrastructure by which these services are supplied, and any other infrastructure by which these services are, or are likely to become capable of being supplied.[3]

The ACCC cannot consider any other objectives in assessing the LTIE.

The ACCC must also be satisfied that the undertaking as varied would be consistent with any Ministerial pricing determination. However, no relevant Ministerial pricing determinations are in effect.

The CCA specifies three reasons why the ACCC must not reject a variation. These reasons relate to:

- a fixed principle term or condition[4] that is identical to one in the original SAU in all respects, provided the variation was given during the notional fixed period, and none of the qualifying circumstances exist, for the original fixed principle term or condition.
- price related terms and conditions that are reasonably necessary to achieve uniform national pricing of eligible services provided by NBN Co.
- a refusal by NBN Co to permit interconnection or supply services that is authorised by the CCA because it is reasonably necessary to achieve uniform national pricing of eligible services provided by NBN Co.

Finally, the ACCC must refuse to accept an SAU variation proposal if it provides that a term or condition is a fixed principle term or condition for a notional fixed period, and the ACCC considers that it should not be a fixed principle term or condition, or the notional fixed period or qualifying circumstances for the fixed principle term or condition specified in the variation should not be the notional fixed period or qualifying circumstances.[5]

In applying this assessment framework to the SAU variation, we interpret the LTIE as incorporating the end-users' long term economic interests. These interests include sustainably lower prices, increased quality of service and greater diversity and scope in product offerings. Broadly speaking, this assessment can involve a balancing of costs and

---

3 CCA, section 152AB(2).

4 CCA, section 152CBAA.

5 CCA, subsection 152CBD(4).

benefits to end-users over time and involve a range of potentially competing considerations. The LTIE and reasonableness framework, and our approach to these matters, are discussed in Annexure E.

We do not consider that the SAU variation calls for a reassessment of existing provisions in the SAU. Consistent with its approach to previous SAU variations, we have focused our consideration on the additions, deletions and other changes that have been proposed in the SAU variation. In doing so, we have had regard to the likely effects of these changes, including their interaction with unchanged provisions of the SAU. That is, we have considered the SAU variation in the context of the whole SAU.

## 2.6. Further background information

We provide an outline in Annexure F of the expenditures that NBN has proposed for the first regulatory cycle, for convenience when considering our discussion of these expenditures in chapter 4. We provide in Annexure G an overview of the markets in which NBN services are supplied, including our views on competition in those wholesale and retail markets. This discussion is relevant to our assessment of the implication of the SAU variation for competition and efficiency in those markets.

In addition we have published two expert reports. The first is the draft independent assessment of the capital and operating expenditures that have been proposed for the first regulatory cycle. This is in draft pending the supply of further information from NBN Co.

The second is an independent report on reasonable estimates of the ICRA balance that would provide NBN Co a reasonable opportunity to transition to a stand-alone credit rating based upon the information contained in its building block model. The estimates are based on various assumed scenarios, in each of which NBN Co operates in a prudent and efficient manner to meet the long term forecasts contained in that model. The scenarios differ based on matters such as the WACC value used to calculate the return on the regulated asset base and the rate at which dividends are paid to shareholders, commencing when NBN Co's financial position allows of the payment of such dividends.

## 2.7. Structure of Draft decision

The Draft decision is structured as follows:

- Section 3 provides an overview of NBN Co's SAU variation.
- Section 4 discusses key elements of the SAU variation and includes our findings on matters relevant to whether they are reasonable.
- Section 5 provides the ACCC's assessment of the SAU variation having regard to the legislative criteria.
- Annexure A provides an overview of telecommunications access regime and current NBN Co SAU
- Annexure B outlines ACCC engagement and consultation with stakeholders prior to NBN Co's lodgement of the SAU variation
- Annexure C contains the ACCC's approach to handling information received during this consultation
- Annexure D lists the submissions received by the ACCC in relation to its consultation paper
- Annexure E outlines what is meant by the long-term interests of end-users and reasonableness.

- Annexure F outlines the proposed expenditures relevant to the first regulatory cycle
- Annexure G provides an overview of the markets in which NBN services are supplied, including our views on competition in those wholesale and retail markets.
- Annexure H provides an explanation of the various regulatory periods and regulatory cycles that would occur over the SAU term and the SAU modules relevant to each should the SAU variation come into effect.

# 3. SAU variation

NBN Co's SAU variation proposes the following key changes to the current NBN Co SAU.

- **Regulatory module applications and determinations** – the SAU variation would continue the approach for certain matters to be determined ahead of each regulatory cycle through the replacement module process. NBN Co would submit a replacement module application and the ACCC would make a replacement module determination in response, accepting some or all of what NBN Co proposes, or otherwise determining matters for itself. Under the proposed variation, each regulatory cycle would last between 3 and 5 years, and the assessment process would be streamlined and specified in the SAU itself, rather than this process partially relying on the statutory SAU variation process as is the case today.
- **Post-2032 arrangements** – the SAU variation would split the remaining term into pre-and-post 30 June 2032 periods. Some aspects of the regulatory framework would fall away at the end of the first of these periods. However, although some of these aspects could be included in a determination in the post-2032 period and the ACCC can issue a statement of approach to inform what NBN Co includes in a replacement module application. The replacement module application and determination process would also operate differently. In Module 2 there are more prescriptive rules that bind the potential determinations that can be made by the ACCC, whereas post-2032 determinations would be limited by high-level terms and principles, in particular the principles in Module 3. Notably, these principles would appear to prevent the ACCC from making a regulatory determination that would set the annual regulated revenue amount below an amount necessary to give NBN Co a reasonable opportunity to achieve and maintain, for the duration of the relevant regulatory cycle, a stand-alone investment-grade credit rating, which would potentially require large price increases at the beginning of Module 3. As discussed elsewhere, this proposed limitation could introduce several risks to the effectiveness of regulation during the post-2032 regulatory period.
- **Move to flat rate pricing offers** – the SAU variation would require residential grade 100 Mbps and higher speed tiers to be offered on a flat monthly charge basis from 1 July 2023 or three months from acceptance, with the remaining residential grade speed tiers to transition to flat rate offers by 1 July 2026. The latter would involve the CVC overage charge being reduced each year of the first regulatory cycle from $8/7/6 Mbps/month and then being set to zero. The CVC allowances in the bundled offers would also be adjusted every 6 months over the initial regulatory period, with a view to offsetting around half the change in peak daily CVC usage associated with the relevant speed tiers.
- **Price controls** – the SAU variation would establish new individual product price controls for the flat rate and bundled product offers, along with an overall WAPC covering NBN Co's core product offerings. For the speed tiers that remain subject to CVC charging over the first regulatory cycle, the price controls will apply to the bundled charge amounts as calculated on a weighted average basis across retailers. Hence cost outcomes for retailers may depend on how their usage compares to industry averages.
- **Regulated price path to 30 June 2032** – the SAU variation would result in regulated price paths for the period up until 30 June 2032 that appear largely dependent on the operation of the price controls specified in the SAU, rather than regulatory determinations made at each reset. Until NBN Co reaches the point where its annual revenues align with its regulatory allowances, which it projects to occur in the 2030 financial year, the WAPC would be limited to increases in CPI. From that time the annual change in average price could be either above or below CPI and driven by NBN Co's then regulatory allowances and forecasts of demand. Price changes for speed tier offers would be limited to no more than 5 percent or CPI (whichever the higher), other

than for the entry level data access offer, which would be limited to CPI increases. Where a speed tier increased in price within its individual control by more than CPI, another speed tier offer would need to increase by less than CPI to allow compliance with the WAPC.

- **Other price certainty measures** – the SAU variation would require NBN Co to publish by 1 May of each year a binding tariff list for the forthcoming financial year and roadmap of prices for the next three financial years. Subsequent year tariff list prices would not be able to differ significantly from roadmap prices previously published for that year, due to the operation of a mechanism that would maintain relativities between monthly prices to within $1 per month of the relevant roadmap pricing. NBN Co would also be required to publish a statement of pricing intent for each regulatory period, with a requirement for the tariff list and roadmap prices to be consistent with this statement.
- **Building block model** – the SAU variation would continue the current SAU framework in relation to the composition of the annual building block revenue requirement (ABBRR) and regulatory asset base (RAB) roll-forward, albeit with a more rigorous test for prudency and efficiency of capital expenditure (see below). This includes separate identification of costs attributed to core regulated services, in recognition that NBN Co has entered competitive enterprise markets. NBN Co also proposes to revise the economic lives of some of its asset classes and has updated the model it has submitted to include its recently announced investments in fibre to the premise (FTTP) and fixed wireless networks, which alters each capital cost profile compared to earlier BBMs that it has submitted.
- **Recovery of historical losses** – the SAU variation proposes to specify the balance of the ICRA as $12.5 billion in current nominal terms, significantly below the balance accumulated under the current SAU. This balance would be maintained in real terms, but no further losses could be added to it. The balance would be progressively recovered by adding drawdown amounts to the ABBRR from around the 2030 financial year to give an overall annual regulated revenue allowance. NBN Co considers the recovery of this additional amount is required to provide a reasonable opportunity to achieve and maintain an appropriate investment grade credit rating during the SAU term. The proposed ICRA amount also appears to result in an annual regulated revenue allowance (revenue allowance) that generally aligns with or exceeds the revenues that NBN Co projects for the remaining SAU term from the time that ICRA drawdown would commence.
- **Cost allocation methodology** – the SAU variation proposes to separate cost bases for ‘core’ and ‘non-core’ services using cost allocations. Services that are categorised as being supplied in competitive markets will be allocated to the non-core cost base, and prices for these services would sit outside the SAU controls. Residential grade and all other services would be core services, and their costs would be allocated to the core services cost base and SAU price controls would apply to them. New services would be categorised ahead of each regulatory cycle through the replacement module process.
- **Expenditure criteria** – The forecast expenditures that NBN Co proposes as part of a Regulatory Module Application are to reasonably reflect those that a prudent and efficient operator in NBN Co’s position would incur in achieving the ‘expenditure objectives’, having regard to a number of ‘expenditure factors’. The ACCC would also be required to have regard to the expenditure objectives and expenditure factors in making a regulatory module determination. Similar considerations would apply to the assessment of cost pass-throughs and the assessment of whether capital expenditures ought to be included in the RAB. The forecast expenditures for the first regulatory cycle have been incorporated into a building block model that NBN Co has submitted as part of its supporting submission.

- **Weighted average cost of capital** – the SAU variation would apply a nominal 'vanilla' WACC (that is a weighted average of the pre-tax cost of debt and the post-tax cost of equity) to determine the allowed rate of return on capital, which is based on individual estimates for all key parameters. NBN Co has proposed specific values for WACC parameters for the first regulatory cycle using a detailed methodology that it intends to adopt thereafter. This would result in a higher WACC than applied under the simple methodology that was in effect during Module 1 of the SAU (which applies until 30 June 2023). That said, the ACCC would now have the power to undertake a review of the WACC methodology ahead of each regulatory cycle.
- **Service quality** – the SAU variation would include a framework for specifying benchmark service standards for each regulatory cycle, with these initially tied in large part to the service levels, and associated performance objectives and rebates, applying under WBA4. These could be changed for each regulatory cycle, and mid-regulatory cycle changes could also be made in response to retail regulatory changes, a systemic service standard event or an application lodged by NBN Co. During the post-2032 regulatory period, NBN Co would have the option of nominating benchmark service standards but would be under no obligation to do so unless requested by the ACCC in its statement of approach. Regardless, the ACCC could specify benchmark service standards for a regulatory cycle in a replacement module determination.
- **Expanded scope of SAU to cover other access technologies** – the SAU variation would make services supplied over the fibre to the building/curb/node (FTTB/C/N) and HFC networks subject to the SAU. Some important specifications for these services have been included into the SAU, including peak information rate and committed information rate objectives and service boundary points.
- **Reporting and transparency** – the SAU variation proposes to introduce commitments to report on service levels, operational matters such as network availability, network utilization and corrective action. This proposed reporting mostly mirrors current reporting under WBA4.
- **ACCC functions and powers** – the SAU variation would confer additional functions and powers on the ACCC, including those described above. These are generally confined in their scope, such as to administering a specific regulatory process. The SAU variation does not propose a broad power of direction to address new or systemic issues.

# 4. ACCC assessment of key aspects of the SAU variation

## 4.1. The replacement module framework

**Key points**

- The structure of the proposed replacement module framework is reasonable and would promote the LTIE. This framework establishes the replacement module process through a conferral of power on the ACCC and introduces alternative arrangements for the post 2032 period. It also provides for the expiry of the SAU if NBN Co no longer remains in government ownership, which would allow the ACCC to make access determinations or give scope for a new SAU to be established following privatisation.
- Deemed acceptance of NBN Co's regulatory proposals if the ACCC has not made a determination within specified timeframes is not reasonable and will not promote the LTIE. This proposal will place unreasonable limits on ACCC decision making and would risk unreasonable access terms coming into effect by default, such as where the ACCC is awaiting information from NBN Co that it needs to make its determinations.
- NBN Co's potential changes to the replacement module framework, which it indicates could be included in a future revised SAU variation proposal by NBN Co, could address issues raised by the ACCC and stakeholders on the deemed acceptance of regulatory proposals.

### 4.1.1. Overview of SAU variation proposal

**Changes to the replacement module process**

The SAU variation builds on the modular structure of the current SAU, with different arrangements applying over the SAU period. NBN Co proposes that the term of the SAU be broken into two regulatory periods, namely the subsequent regulatory period which runs from 1 July 2023 to 30 June 2032 and the post-2032 regulatory period, which comprises the remainder of the SAU term.

Both the subsequent regulatory period and the post-2032 regulatory period would contain shorter regulatory cycles of between 3 and 5 years. Other than the first regulatory cycle, for which key terms are specified in Module 4 of the SAU variation proposal, access terms for each regulatory cycle would be determined through the replacement module process.[6]

This process would be self-contained within the SAU through conferring relevant powers on the ACCC under section 152CBA(10A) of the CCA and specifying additional processes relevant to establishing terms for each regulatory cycle.[7] Under this revised process, NBN Co would submit a replacement module application ahead of each regulatory cycle; and then the ACCC would make a replacement module determination. A replacement module determination may adopt NBN Co's application in whole, or in part, or specify alternatives in accordance with the requirements of the SAU.

This compares to the arrangements under the current SAU, where NBN Co must first seek to vary the SAU under section 152CBG of the CCA to establish access terms for a regulatory cycle. The ACCC must than assess that SAU variation under the Part XIC

[6] An explanation of the regulatory periods and regulatory cycles that would occur over the SAU term and the SAU modules relevant to each should the SAU variation come into effect is provided in Annexure H.

[7] NBN Co, *SAU variation, Main Body*, clause 5. NBN Co, *SAU variation Supporting submission, Part D: ACCC roles and powers*, November 2022, Chapter 13, p 6.

process. If the ACCC does not accept the SAU variation, the ACCC may then make a replacement module determination under the SAU to determine an alternative set of access terms for that regulatory cycle.

### Scope of the matters to be assessed for each regulatory cycle

The SAU variation would expand the scope of matters which NBN Co must include in its replacement module applications and which the ACCC must determine in replacement module determinations.[8] For the subsequent regulatory period, NBN Co would include the length of each regulatory cycle, a BBM proposal (which includes the proposed expenditure, WACC, regulatory depreciation and all other necessary inputs under the BBM), an entry level offer proposal and a service standards proposal.

The ACCC would then determine each of these matters as part of its replacement module determination. In making a replacement module determination, the ACCC would have to take into account the matters set out in section 152BCA(1) of the CCA (which specifies the matters the ACCC must take into account when making an access determination) and would need to publish its determination, together with its reasons, on its website.[9]

Under the current SAU variation proposal, if the ACCC does not make a replacement module determination for a regulatory cycle in the prescribed time, a replacement module determination will be taken to be in effect during that regulatory cycle in which the matters required to be determined are as stated in NBN Co's replacement module application. In our January 2023 consultation paper, we expressed concern that this could:

- limit the ACCC's decision-making, and
- pose issues if the ACCC were waiting on relevant information from NBN Co which impacted the ACCC's ability to make a determination on time

in circumstances where the replacement module framework does not require NBN Co to provide all the relevant information at the time of making its application.[10]

### Post-2032 arrangements

The SAU variation proposes a significant change in approach for the post-2032 period. Notably, the SAU variation, in particular Module 3, would specify high level rules and principles that would apply to replacement module applications and determinations after 2032. While the ACCC has more discretion in specifying the access terms to apply, its power to do so is subject to the limiting principles that are specified in Module 3. The post 2032 arrangements are discussed in more detail in section 4.2.

### Additional procedural provisions

Under the SAU variation, the ACCC may publish, by 31 March of the last financial year of each regulatory cycle, a preliminary view on the matters to be determined as part of any ACCC replacement module determination for the next regulatory cycle.[11] Further, the SAU variation would require NBN Co to consider any ACCC preliminary views (should the ACCC publish these) and consult with access seekers and consumer advocacy groups in preparing its replacement module applications.[12] The ACCC could also consult as part of the process.[13]

---

8 NBN Co, *SAU variation, Main Body*, clauses 5.2(e) and 5.9(a) and (b). NBN Co, *SAU variation Supporting submission, Part D: ACCC roles and powers*, November 2022, Chapter 13, pp.7-8.

9 NBN Co, *SAU variation, Main Body*, clause 5.8(b) to (d)

10 ACCC, *Proposed variation to the NBN Co SAU – Consultation paper*, January 2023, sections 5.1, 5.7 and 5.13.

11 NBN Co, *SAU variation, Main Body*, clause 5.11.

12 NBN Co, *SAU variation, Main Body*, clause 5.7.

13 NBN Co, *SAU variation, Main Body,* clause 6.1.

**Expiry of the SAU and proposed change of control clause**

The arrangements described above would apply until the expiry of the SAU. The current SAU variation now proposes that the SAU expire on the earlier of 30 June 2040 or a change of control occurring. This would be triggered either by the Commonwealth government ceasing to hold more than 50 percent of the shares in NBN Co, or 20 business days after the Commonwealth government publishes a change of control notice, stating it intends to take steps to relinquish control over NBN Co.[14] The proposed arrangements would allow the ACCC to make access determinations or give scope for a new SAU to be established following privatisation.

### 4.1.2. Submissions

Submissions that commented on the replacement module process were generally supportive of the proposal to incorporate the process into the SAU, with some considering that this could provide a more straightforward and streamlined process.[15]

However, there were several aspects for which stakeholders considered further changes were necessary if the replacement module framework is to promote the LTIE. These concerned the:

- proposed timeframes for future regulatory module processes, including pre-consultation requirements, and the ‘deemed acceptance’ provisions
- appropriateness of the change in control provisions to terminate the SAU then in operation.

Numerous stakeholders raised concerns with the deemed acceptance of replacement module applications (ACCAN, Aussie Broadband, Commpete, Optus, TPG and Vocus). These stakeholders considered that such provisions limited the ACCC and industry’s power to properly assess the replacement modules. Optus further noted that information asymmetries and a lack of provision of information obligations on NBN Co may allow it to game or delay the process.

Stakeholders considered it preferable and more consistent with standard practice for the existing SAU module to be rolled over until the ACCC makes a decision, instead of being deemed to have made a determination on the same terms proposed by NBN Co. Some stakeholders (Aussie Broadband, Optus) also proposed more explicit information obligations on NBN Co and “stop the clock” provisions where NBN Co has not provided any prescribed information.

Submissions were supportive of the additional requirement for NBN Co to consult with access seekers and consumer groups before submitting a replacement module application, though some either considered that more time was needed to meaningfully engage (ACCAN)[16] or that stronger obligations were needed for NBN Co to:

- share detailed information, including on expenditures and the objectives and underpinning economic analysis for material business cases (ACCAN, Aussie Broadband, Telstra)
- explain how / why it has or has not addressed stakeholders’ concerns when submitting a replacement module application to the ACCC (Optus).

On the change of control provisions, TPG and ACCAN raised concerns that the timeframes and notice periods associated with a change of ownership are inadequate. TPG also queried

---

[14] NBN Co, *SAU variation, Main Body*, clause 3.2(b).

[15] See submissions from ACCAN, Aussie Broadband, Commpete, and Telstra

[16] ACCAN proposed a minimum 90-day consultation period. It also considered that NBN Co should fund resources necessary for best practice consultation ahead of submitting a regulatory cycle proposal (either by funding arrangements like those used in the energy market, or financial penalties for failure to consult adequately).

why a 50 percent threshold was justified, noting that it is currently unknown how the Government may choose to privatise NBN Co in the future.

### 4.1.3. NBN Co's potential revised SAU variation proposal

On 24 March 2023, NBN Co wrote to the ACCC with a potential proposal to address several issues raised by the ACCC and stakeholders that it would be willing to include in any revised SAU variation proposal.

NBN Co has proposed two further potential changes to the provisions around deemed acceptance of replacement module applications if the ACCC has not made a replacement module determination by the start of the relevant regulatory cycle:

- a new clause that makes clear the ACCC can require NBN Co to provide specific information upfront when it lodges a replacement module application
- provision for the ACCC to extend its decision-making timeframe by up to 3 months at a time, up to a maximum of 6 months. If, at the end of this period, the ACCC has still not made a replacement module determination, NBN Co's replacement module application would be taken to have been accepted.

NBN Co submits the proposed changes would ensure NBN Co submits a complete proposal with all information necessary for the ACCC to perform its assessment, and effectively allow the ACCC to extend its decision-making period to up to 24 months after NBN Co lodges a replacement module application.

To account for the extended decision-making period, NBN Co has proposed that interim measures would apply between the start of the regulatory cycle and the time the ACCC makes the replacement module determination (if extended):

- the regulatory cycle would still start from 1 July (as it normally would) and would have a total length as set in the replacement module determination, once made
- benchmark service standards would carry over from the final year of the preceding regulatory cycle
- for the purposes of materiality thresholds for cost pass through applications only, the forecast ABBRR would be as proposed by NBN Co in its replacement module application[17]
- other aspects would not be specified on an interim basis as they do not need to be determined and in place by start of regulatory cycle (for example, WAPC escalation forecasts, WACC, expenditure, ICRA drawdown).

NBN Co has also set out interim measures if there was a delay in making the replacement module determination for the first Regulatory Cycle in the post-2032 period. These include a commitment by NBN Co to publish a tariff list for financial year 2032 by no later than 1 May 2032, and continued application of the WAPC.

### 4.1.4. ACCC assessment

We consider that the general structure of the proposed changes to the regulatory framework in the SAU variation are reasonable in concept. However, we consider that the deemed acceptance of replacement module applications if the ACCC has not made a determination within the specified timeframes places unreasonable limits on our decision making and is not reasonable and further, would not promote the LTIE. However, we consider that the potential

[17] NBN Co indicates that this closes an unlikely gap which may arise if NBN Co needed to determine whether it may or must submit a cost pass-through application for a particular event that occurs in the interim period.

changes NBN Co has indicated it would be willing to make, if included in a revised SAU variation proposal, could address ACCC and stakeholder concerns.

**Proposed structure of SAU regulatory framework is reasonable and would promote the LTIE**

We consider the proposed replacement module application and determination process in the SAU variation is reasonable and would promote the LTIE. The proposed changes would allow the ACCC to assess replacement module applications and make replacement module determinations under a conferral of power on the ACCC under the SAU. This represents a simplification of the replacement module assessment process as the entire process would take place under the SAU framework. This will likely lead to a more streamlined process than current replacement module arrangements, where the replacement module applications are proposed variations to the SAU itself and must be assessed by the ACCC under Part XIC of the CCA.

The introduction of alternative arrangements for the post 2032 period is also reasonable. We consider that the proposed post 2032 framework appropriately has regard to the long term nature of the SAU and the need to balance flexibility to adapt to changing circumstances and market conditions, while also providing a degree of certainty about how key elements of the regulatory framework will be considered in future. We consider that, conceptually, the appropriate use of high-level principles in Module 3, which will apply during the post 2032 period, in conjunction with the replacement module process and the ability for the ACCC to specify additional principles through the statement of approach, achieves this balance.

We consider the additional requirement that NBN Co must consult with its customers and consumer representatives will assist NBN Co to reflect industry and consumer preferences in developing its regulatory proposals. The proposed requirement does not specify a minimum period that NBN Co must consult with customers and consumer representative before it lodges a replacement module application, only that NBN Co must provide a reasonable opportunity for parties to provide input. We consider this requirement is sufficient and that no minimum timeframe for consultation need be specified in the SAU. We expect that the risks raised by ACCAN about compressed timeframes to provide input can be mitigated by ongoing engagement between NBN Co, industry, consumer representatives and the ACCC through the administration of the replacement module process.

Finally, we consider that the proposed provision for the expiry of the SAU upon change of ownership is reasonable. We consider that change of ownership would be an appropriate point for the long-term regulatory arrangements to be reviewed, which would be best facilitated by the expiry of the SAU. We note concerns raised by ACCAN and TPG about the short timeframes between a change of control notice and expiry of the SAU. We consider that the regulatory arrangements to apply to NBN Co after a change of control, which include access determinations or a new SAU, would need to be developed before the SAU expires but work on these arrangements could commence ahead of a change of control notice being given.

**Deemed acceptance of replacement module applications is not reasonable and will not promote the LTIE**

Although we consider the general replacement module framework proposed in the SAU variation is reasonable, it does not consider the provision for the deemed acceptance of replacement module applications to be reasonable.

We consider the proposed deeming of the acceptance of replacement module applications places material limitations on ACCC decision making and creates material risks of regulatory terms being established through the replacement module process that are not reasonable and that will not promote the LTIE. If the ACCC has not made a replacement module determination by the start of the relevant regulatory cycle, the proposed terms as contained in NBN Co's replacement module application would apply, notwithstanding ACCC's views on the reasonableness of those terms or whether they will promote the LTIE. This could create inefficient arrangements, or arrangements with a high risk of inefficient outcomes, being put in place. In the absence of any provision to extend the decision-making period, the we consider there is a material risk of this situation occurring. This would be most likely if the ACCC is awaiting information from NBN Co in order to make its determination. It could also create incentives on NBN Co to withhold information that would be necessary or useful for the ACCC to consider as part of its assessment, both in the information supplied as part of a replacement module application, or in response to requests for information during the replacement module assessment process.

**Potential changes proposed by NBN Co could address concerns about replacement module process**

NBN Co has proposed a range of further potential changes to the replacement module process, that it would be willing to include in a revised SAU variation proposal.[18] We consider that potential changes, if made, could potentially address ACCC and stakeholder concerns about the deemed acceptance of replacement module applications

We consider the ability to extend the timeframe for making a replacement module determination by 3 months, up to a total of 6 months, could strike the right balance between providing flexibility for the ACCC to take additional time to make a determination, while establishing a clear maximum timeframe for completing the process.

We consider the existing assessment timeframes should be sufficient in most cases, and expects the ability to extend the decision-making period would be used on an exceptional basis only. We acknowledge it is preferable for all parties for arrangements to be put in place before a regulatory cycle, and extending the decision-making period would create some regulatory uncertainty. This would be mitigated by the proposed maximum timeframe of 6 months, which should also create incentives for all parties to bring any extended process to a close.

Further, the potential ability for the ACCC to specify the types of information NBN Co must include with its replacement module determinations could reduce risk of delays in the assessment process, as the ACCC could specify upfront the information it requires to assess NBN Co's proposals. The potential provision would not allow the ACCC to request the required information at other points except for the replacement module applications, or require NBN Co to maintain certain records. However, we consider this could be mitigated by existing information gathering powers under proposed clause 6.3 of the SAU variation, or through an RKR. The ACCC will give further consideration to the types of records it may require NBN Co to keep, for example for future assessments of forecast expenditure (see sections 4.7 and 4.8 for further discussion).

Finally, we consider that the interim measures that would apply under the potential changes between the start of a regulatory cycle and the making of a replacement module application could provide sufficient certainty over that interim period. Under the potential revised arrangements, prices for the first year of a regulatory cycle would already be specified, and interim arrangements would apply to benchmark service standards, and materiality thresholds for cost pass through events. We consider these items could cover any gaps during the extended decision-making period. We also agree that values for other items or items for latter years of the regulatory cycle would not need to be specified on an interim basis.

[18] NBN Co letter to ACCC, 24 March 2023.

## 4.2. Post-2032 framework and principles

**Key points**

- The general framework for the post 2032 period appropriately balances flexibility to adapt to changing circumstances and market conditions and provides a degree of certainty about how key elements of the regulatory framework will be considered in future. In these circumstances, we are satisfied that the general framework is reasonable and will promote the LTIE, subject to the comment below.
- We are not satisfied that the proposed credit rating objective principle to apply in the post 2032 period, as set out in the SAU variation, is reasonable or would promote the LTIE. This is because the principle is not premised on NBN Co operating and investing efficiently. As such this would permit NBN Co to be compensated for the additional cost of achieving its credit rating objective that results from inefficiency, and risk price shocks for consumers.
- We consider that the potential changes that NBN Co would be willing to make to the credit rating objective principle could address the concerns raised by the ACCC and stakeholder submissions.
- We are satisfied that the balance of the post-2032 framework and principles that govern the making of replacement module determinations for the period are reasonable and would promote the LTIE.

### 4.2.1. Overview of SAU variation proposal

The SAU variation would introduce a new module, Module 3, into the SAU. Module 3 would operate from 1 July 2032 until the end of the SAU term. The replacement module process would continue in the post 2032 period and replacement module determinations made during the post 2032 period would need to be consistent with Module 3. However, module 3 contains more high level principles for how certain matters are to be determined through the replacement module process, compared to the prescriptive rules contained in module 2.

Under the proposed arrangements, replacement module determinations for the post-2032 period would need to determine certain matters (including the term of the regulatory cycle, annual regulated revenue allowance, forecast nominal ABBRR, and certain values related to ICRA drawdown amounts).[19] Replacement module determinations may also specify other elements, including maximum prices, a framework for controlling maximum prices, rules applicable to NBN Co tariff lists and pricing roadmaps, benchmark service standards and rules applicable to the development and withdrawal of products.[20]

The ACCC would also be able to issue a statement of approach before NBN Co is required to give the ACCC a replacement module application for the post 2032 period. If the ACCC issues a statement of approach, any replacement module application would need to include the relevant proposals and be accompanied by any information requested by the ACCC or specified through the statement of approach. The statement of approach would need to be consistent with the principles set out in Module 3.

A key principle NBN Co has proposed under Module 3 is that revenue allowances must be set to allow NBN Co a reasonable opportunity to achieve and maintain, for the duration of a regulatory cycle, a stand-alone investment grade credit rating with a stable outlook.[21] The

[19] SAU variation clause 5.10 (a)

[20] SAU variation clause 5.10 (b)

[21] SAU variation, Module 3, Schedule 3A.1.2 and 3B.3.1(a) to (c)

ACCC made a number of observations on the proposed credit rating objective principle in its consultation paper on the SAU variation. We observed that the proposed principle could limit the ACCC's ability to make regulatory determinations that encourage NBN Co to invest and operate more efficiently over time or could risk price shocks in the future. Other observations we made were:

- The principle that revenue allowances must be set to allow NBN Co a reasonable opportunity to achieve and maintain a stand-alone investment grade credit rating with a stable outlook does not appear to be qualified by reference to efficient investment and operation of the NBN.
- NBN Co may be permitted under the principle to increase its revenues to pay down its debt over a compressed timeframe at the beginning of Module 3, creating the risk of price shocks or inefficiently high pricing.
- The ACCC could be required to consider factors in determining revenue allowances used by rating agencies that are not typically used for regulatory purposes.
- The complexity of the operation of the proposed principle in in combination with other elements of the Module 3 framework for determining allowable revenues, such as the provisions governing the different elements of the ABBRR and ICRA drawdown, and the interaction with any statement of approach issued by the ACCC.

In addition to the proposed credit rating objective, other elements of the SAU variation that relate to NBN Co's opportunity to transition to a standalone investment grade credit rating (the ICRA and ICRA drawdown arrangements) are discussed in section 4.3.

### 4.2.2. Submissions

**Post 2032 framework**

ACCAN, Aussie Broadband, Optus and Telstra each commented on the balance between flexibility and certainty in the post 2032 period.

ACCAN raised concerns that the proposed arrangements for Module 3 do not currently provide an appropriate balance between providing regulatory certainty and flexibility to determine arrangements that best respond to conditions at the time. Aussie Broadband indicated that Module 3 appears to limit the ACCC's powers in making a replacement module determination.

Optus argued that the modular structure of the SAU should allow a sufficient degree of regulatory certainty for NBN Co while providing flexibility for the SAU to adapt to changes in the market over time. Although it supports the stated intent of enabling the ACCC to reset the regulatory framework to apply post-2032, Optus is concerned about the potential for some of the proposed general principles set out in draft Module 3 to curtail the ACCC's discretion. Similarly, Telstra noted that there must be enough flexibility in the SAU to allow the ACCC to address issues that arise in the post 2032 period.

ACCAN also recommended that the ACCC be required to provide a statement of approach within a minimum of 180 days before NBN Co lodges their replacement module application to allow sufficient time for it to be considered.

***Credit rating objective principle***

Stakeholders generally agreed with the ACCC's concerns about the proposed principle in relation to NBN Co's credit rating objective as specified in the SAU variation.[22]

ACCAN agreed that achieving a stand-alone investment grade credit rating is a worthy policy objective, but recommended that references to the principle be removed as it is not an objective to be considered as part of the LTIE. Commpete also argued the proposed credit rating objective would not satisfy the 'efficient use and investment' objective that forms part of assessing whether something promotes the LTIE test. Optus indicated that the proposed credit rating objective principle would introduce assessment criteria outside the traditional scope of Part XIC of the CCA. Telstra also noted the lack of precedent for adopting a principle based on achieving a credit rating objective in regulatory decisions.

Aussie Broadband also recognised the importance of providing an opportunity to achieve a stable stand-alone investment grade credit rating. However, it recommended the requirement be made conditional on NBN Co investing and operating efficiently. It also highlighted the risks of inefficiently high pricing if the ICRA is drawn down in a compressed timeframe and the lack of incentives for NBN Co to operate efficiently. Optus, Telstra and TPG expressed similar views.

Commpete argued that it is the role of management to achieve the outcomes that its owners require, including maintaining a certain credit rating. It would therefore be a matter for NBN Co's board and management to take necessary actions to address consequences of not meeting the required objective, rather than for the ACCC to reflect the objective in its decisions.

Finally ACCAN and TPG also noted the credit rating principle would only become relevant to the extent that NBN Co does not remain under government ownership.

In its submission, NBN Co indicated it would consider the concerns raised by the ACCC in the consultation paper and would consider options for addressing these concerns.

### 4.2.3. NBN Co's potential revised proposal

In its supplementary submission, NBN Co proposed a range of potential changes to the proposed credit rating objective principle that it would be willing to make to address the concerns raised by the ACCC and stakeholders during consultation. NBN Co indicated it would be willing to incorporate these changes in a revised SAU variation should the ACCC draft decision be to reject the current SAU variation proposal.[23]

NBN Co has proposed making the following two key potential changes to the credit rating objective principle:

- The ACCC would be required to set annual ICRA drawdown amounts to provide NBN Co with a reasonable opportunity to transition to and maintain a standalone investment grade credit rating in the shortest timeframe practicable. This requirement would be subject to avoiding price shocks, and would be assessed by reference to quantitative financial metrics consistent with a stand-alone investment grade credit rating with a stable outlook from one or more established and reputable rating agencies.[24]
- The ACCC, when setting the Forecast Nominal ABBRR, would be required to have regard to the principle that revenues should allow a prudent and efficient operator in

[22] ACCAN, Aussie, Commpete, Optus, Telstra, TPG, NBN

[23] NBN Co letter to ACCC, 24 March 2023, pp. 1-3

[24] Note this change would apply to both Module 2 and Module 3

NBN Co's position (and with benchmark efficient capital structure) a reasonable opportunity to maintain a stand-alone investment grade credit rating with a stable outlook.

NBN Co submits that these potential changes would clarify its intention that it is afforded a reasonable opportunity to recover the Module 3 ICRA amount in a way that enables it to transition to a position in which it can satisfy quantitative financial metrics consistent with achieving and maintaining a standalone investment grade credit rating with a stable outlook.

### 4.2.4. ACCC assessment

**Alternative arrangements for the post 2032 period are reasonable and would promote the LTIE**

We agree with the concept of alternative arrangements for the post 2032 period. Subject to the views discussed below on the credit rating objective principle, we consider the proposed arrangements, appropriately balance flexibility to adapt to changing circumstances and market conditions and provides a degree of certainty about how key elements of the regulatory framework will be considered in the future. Although Module 3 would provide some limits or constraints around ACCC decision making in future, we consider that the proposed arrangement retain sufficient flexibility around ACCC decision making.

**SAU variation credit rating objective principle will likely lead to inefficient outcomes and risk of price shocks**

We consider that the proposed credit rating objective to apply in the post 2032 period, could lead to price shocks and inefficient outcomes and is therefore not reasonable and would not promote the LTIE.

We considers that, conceptually, the opportunity to achieve and maintain a standalone investment grade credit rating is reasonable.[25] However, we consider that the proposed credit rating objective principle, as currently framed, will create significant risks of price shocks and inefficient outcomes for the following reasons:

- The requirement that the ACCC must set allowable regulated revenue allowances to meet the credit rating objective principle appears to override other elements of the framework for determining revenue allowances, namely the ABBRR and ICRA drawdown provisions. These two elements are intended to provide the opportunity for NBN Co to achieve and maintain a standalone investment grade credit rating on a forward looking basis. The proposed principle could operate to require the ACCC to allow NBN Co to recover more than these amounts in the revenue allowance. This could in turn weaken incentives on NBN Co to invest and operate efficiently, and transfer to consumers risks that would otherwise be borne by shareholders
- In addition, the scope for revenue allowances in excess of those otherwise consistent with the ABBRR and ICRA drawdown provisions would not be subject to any requirement that NBN Co has operated or invested efficiently, or is undertaking efficient financing practices. The proposed principle could require additional revenue allowances to compensate NBN Co for the incremental costs of achieving and maintaining an investment grade credit rating that arise from inefficient practices by NBN Co.
- The proposed principle may permit NBN Co to increase its revenues to pay down debt over a compressed timeframe at the beginning of Module 3, depending on its actual

[25] We discuss other elements of the SAU variation that are intended to provide NBN Co with a reasonable opportunity to achieve an investment grade credit rating in section 4.3

financial position at the time. This could create the risk of price shocks or inefficiently high pricing, or at least prices that are higher than would have applied without the principle in place.

- In determining revenue allowances for NBN Co in the post 2032 period, the ACCC could be required to consider factors that, although used by rating agencies for credit rating purposes, are not typically used for regulatory purposes or would be difficult for the ACCC to apply in practice.
- The interaction between the credit rating objective principle and other SAU elements relating to revenue allowances for the post-2032 period (ie, ABBRR, ICRA drawdown provisions and ACCC statement of approach) will create a high degree of complexity and uncertainty about the future application of the various provisions.

**NBN Co's potential revisions to the credit rating objective principle could address concerns about the current proposal**

NBN Co has proposed a range of potential changes to the proposed credit rating objective principle, which could form part of any revised SAU variation proposal. We consider that the proposed changes could address the concerns raised by the ACCC and stakeholders during consultation. We make the following observations on the potential changes proposed by NBN Co in relation to the credit rating objective principle:

- The potential changes would clarify that the credit rating objective principle is to be considered from the perspective of quantitative metrics used by credit rating agencies. This could confine consideration to matters that are typically used by regulators in considering the financeability of regulated firms and related matters.
- The proposed changes would clarify that the ACCC must ensure that the credit rating objective principle is met in relation to ICRA drawdown amounts and would be subject to other provisions relating to the calculation of these amounts. The ACCC considers that this requirement could affect the timing of ICRA drawdown, but would not affect the total amount of ICRA that NBN Co can recover over the SAU period (in real terms). We note that this requirement concerning the total amount of ICRA that NBN Co can recover would apply to ICRA drawdown amounts in the subsequent regulatory period and the post 2032 period.
- The credit rating objective principle would also explicitly be made subject to no price shocks being incurred. 'Price shock' would not be defined explicitly so normal interpretation would apply when the ACCC considers the proposed price impacts of the proposed ICRA drawdown timing before each regulatory cycle. We consider this provision, in combination with other elements of the revised proposal, could significantly reduce the risk of compressing repayment of debt and price shocks.
- In assessing the ABBRR component of allowable revenues, the ACCC would only need to have regard to the credit rating objective. It would then be left to the ACCC to decide how it reflects that consideration, if at all, in its decision on ABBRR. The ACCC would not be required to set the ABBRR to provide NBN Co with a reasonable opportunity to achieve the credit rating objective.
- Further, when having regard to the credit rating objective when considering the ABBRR, the ACCC would consider the objective from the perspective of a benchmark efficient firm. This approach would break any link between NBN Co's actual financial position and the objective of achieving of a stand-alone investment grade credit rating, which would eliminate the risk of inefficient expenditure, investment or financing practices being reflected in the ABBRR. The benchmark efficient firm approach would also be consistent with other provisions in Module 3 outlining the requirements for determining the various

building block elements, which are either based on a benchmark efficient firm approach, or forecasts of prudent and efficient expenditure.

## 4.3. Proposed ICRA amount and drawdown framework

**Key points**

- The proposed opening ICRA balance of $12.5 billion as of 1 July 2023 will be sufficient to provide NBN Co with a reasonable opportunity to achieve and maintain a standalone investment grade credit rating, under various assumed scenarios regarding its cost of capital and dividend policy settings.
- We consider the proposed opening ICRA balance will also provide an opportunity for dividend payments to shareholders in future years.
- NBN Co will not be guaranteed to recover the ICRA, or any minimum portion of the ICRA. Similarly, NBN Co will not be guaranteed to achieve an actual standalone credit rating of investment grade under the proposed arrangements.
- We consider that determining the amount of the ICRA drawdown ahead of each regulatory cycle achieves an appropriate balance between flexibility and certainty about how ICRA will be drawn down over the SAU period.
- We therefore satisfied that the opening ICRA balance, and the rules for recovery of the ICRA in each of the subsequent regulatory period and the post 2032 period are reasonable, and would promote the LTIE.

### 4.3.1. Overview of SAU variation proposal

The SAU variation provides a framework for NBN Co to reach a position where it will earn sufficient revenue to cover its annual building block revenue requirement (ABBRR), and then allow it to recover a portion of the losses it had accumulated to 1 July 2023. NBN Co submits that the proposed framework would provide it with a meaningful opportunity to earn the revenues it requires over the term of the SAU to pay down debt so as to achieve and maintain a standalone investment grade credit rating with a stable outlook.[26]

This proposed framework is specified in clause 2G.3 and 2G.4 of the SAU variation. The SAU variation specifies an opening core services ICRA balance of $12.5 billion (in 2022-23 terms), which NBN Co will seek to recover over the SAU period. NBN Co will seek to recover the $12.5 billion by adding a portion of this amount (the ICRA drawdown amount) to the ABBRR in determining its revenue allowances for certain years over the SAU period.

This ICRA balance proposed in the SAU variation is less than the projected capital-adjusted ICRA balance that is forecast for the end of 2022-23.[27] NBN Co submits that an ICRA balance of $12.5 billion would still be sufficient to achieve its credit rating objective based on two analytical methods. These are the 'benchmark' and 'credit score' methods, which are set out in NBN Co's supporting submission and expert report by Castalia on the economic effects of the ICRA.[28]

---

26 NBN Co, SAU variation, *Supporting submission, Executive summary and key narratives*, November 2022, p.9. NBN Co's proposed approach to the ICRA is discussed in detail in *Supporting submission Part E: Calculation of NBN Co's regulated revenue requirement*, November 2022

27 NBN Co forecasts that under the ICRA rules allowed under the current SAU the ICRA balance would reach around $44b by the end of 2022-23.

28 NBN Co expert report, Castalia, *Economic effects of ICRA*, December 2022

NBN Co would be able to recover $1.1 billion of the ICRA (in 2022-23 terms) over the subsequent regulatory period, which operates until 30 June 2032. NBN Co would only be entitled to recover this amount after it reaches cost recovery, which is expected to occur in 2029-30 based on NBN Co's current projections. NBN Co would not include any new losses incurred over this period in the ICRA or any other deferred recovery mechanism. Any portion of $1.1 billion that NBN Co does not recover by the end of 2031-32 would be extinguished.

NBN Co would then have an opportunity to recover $11.4 billion of the ICRA (in 2022-23 terms) in the post-2032 regulatory period. Any residual amounts from this portion of the ICRA would be extinguished at the end of the SAU period.

Finally, in both the subsequent regulatory period and the post-2032 period, the timing and size of the ICRA drawdown amounts would be determined through the replacement module process.

### 4.3.2. Submissions

ACCAN, Aussie Broadband, Commpete, and Optus welcomed the significant proposed reduction in the ICRA balance compared to current levels.

ACCAN indicated that the reduction would act as constraint on future prices and reduce uncertainty associated with a large ICRA balance and would promote more efficient outcomes. Aussie Broadband indicated that the recovery of the proposed amount would be predictable, constrained and transparent and ensure recovery against past losses is not greater than required to maintain a standalone investment grade credit rating. Commpete commented that the proposed arrangements were a significant improvement on current arrangements and those proposed by NBN Co in the March 2022 SAU variation.

ACCAN also indicated support for determining ICRA drawdown amounts ahead of each regulatory cycle through the replacement module process. Optus, although expressing cautious optimism for the proposed arrangements, suggested that some uncertainty remains around the drawdown of ICRA over the SAU period, making it is difficult to assess the reasonableness of the BBM and pass through of ICRA amounts in future years, and the impact that may have on future prices.

Launtel made the general observation that the lower the ICRA is set, the easier it will be for NBN Co to provide cheap and reliable service to Australian homes and businesses whilst also making a commercial return.

Telstra argued that, although NBN Co has proposed a significant reduction to the ICRA balance, the ICRA will still reflect historically inefficient expenditure. It further submitted that the varied SAU would constrain the ACCC's ability to exclude inefficient costs associated with government policy projects, and prevent the ACCC from ensuring efficient costs are recovered in a way that promotes the LTIE. Telstra also referred to analysis prepared by Incenta, which indicates that NBN Co could achieve a standalone investment grade credit rating with more moderate price increases than those proposed by NBN Co.

### 4.3.3. ACCC assessment

The ACCC supports the position that NBN Co should be provided a reasonable opportunity to achieve and maintain a standalone investment grade credit rating, as this will provide NBN Co access to financial markets on a standalone basis and to receive debt funding on efficient terms. The proposed arrangements under the SAU variation regarding the ICRA valuation and draw down provisions should provide regulatory allowances for NBN Co to have a reasonable opportunity to transition to a point of cost recovery and then pay down debt so that it can reach a standalone investment grade credit rating. We consider that the arrangements appropriately balance this objective with a degree of certainty about how ICRA recovery will be factored into prices, and good incentives on NBN Co to maintain efficient financing practices.

**The opening ICRA balance will provide sufficient opportunity to achieve credit rating objectives and is therefore reasonable and would promote the LTIE.**

We consider the opening ICRA balance of $12.5 billion will be sufficient to provide NBN Co with a reasonable opportunity to achieve and maintain a standalone investment grade credit rating.

In considering this matter, we are of the view that there is unlikely to be a single correct value for the ICRA that NBN Co requires to meet the stated credit rating objective. There are likely to be alternative reasonable approaches for considering this question, and each approach could produce different estimates for the value or range of values of the ICRA required. There is also scope for different interpretations on what is required to provide a reasonable opportunity. Finally, we consider it important to consider the opening ICRA balance in the context of the framework for ICRA recovery and the combined effect of all changes proposed in the SAU variation.

To assist the ACCC in considering the opening ICRA balance, we engaged Sapere Research Group (Sapere) to provide an independent view on the matter. We requested Sapere to advise on the additional revenue NBN Co would require above the ABBRR so as to transition to a standalone investment grade credit rating and what ICRA balance would be required as of 1 July 2023 to allow NBN Co an opportunity to recover those revenues. [29]

In undertaking this analysis, Sapere looked at the revenue that would be required to achieve credit rating objectives from both a benchmark efficient firm perspective and an actual firm perspective. The benchmark efficient firm perspective adopts the benchmark financing assumptions proposed by NBN Co, whereas the actual firm perspective incorporates NBN Co's actual debt levels and projections of debt as contained in NBN Co's integrated operating plan (IOP).

Sapere also examined a range of different scenarios, including sensitivity of the opening ICRA balance to changes to the WACC, and different scenarios regarding future dividend payments to shareholders. Sapere has adopted inputs from the building block model for revenue, expenditure forecasts, the WACC and CPI assumptions.[30] Sapere's modelling also reflects the ICRA drawdown model reflected in the SAU variation.

The key finding of this analysis is that that a minimum ICRA balance of $8.2 billion as of 1 July 2023 would be required to allow NBN Co to recover sufficient revenue above ABBRR over the SAU period to transition to and maintain a standalone investment grade credit rating based on NBN Co's actual financial position and projections. This result assumes any revenues NBN Co earns above ABBRR will be used to pay down debt.

Sapere also examined a number of dividend payment scenarios and their effects on the opening ICRA balance. The key results from these scenarios are as follows:

- A higher ICRA balance will be required if it assumed dividends will be paid to shareholders in future. Sapere first looked at two scenarios where NBN Co would pay fixed amounts of either $100 million or $200 million per year to shareholders from 2029-30, when NBN Co would generate sufficient taxable profits for payment of dividends. These scenarios would lead to higher opening ICRA values of $8.6 billion and $9.0 billion respectively.

[29] Sapere Research Group, *Revenue required for investment grade credit rating*, 1 May 2023

[30] Sapere was not required to provide a view on the reasonableness of these inputs as part of its advice to the ACCC.

- Sapere then examined a scenario where dividends are assumed to grow in a smoothed fashion towards a target pay-out ratio of 50 per cent of net income over the SAU period. Under this scenario, the ICRA balance that would be required under this would be $9.5 billion.
- Finally, Sapere looked at a scenario where dividend payments were assumed to increase more sharply from 2029-30. In this scenario, the dividend payments are assumed to increase quickly toward a target pay-out ratio of 80 per cent of net income. The required ICRA balance under this scenario would be $12.5 billion.

These findings indicate that the proposed opening ICRA balance of $12.5 billion as of 1 July 2023 will be sufficient to provide a reasonable opportunity to achieve and maintain a standalone investment grade credit rating. The findings also indicate there is significant scope for future dividend payments, should they be sought by stakeholders in future.

We acknowledge the proposed ICRA balance of $12.5 billion is higher than the base case scenario calculated by Sapere and all but one of the dividend scenarios considered. However, we consider that, on balance, the proposed ICRA balance is reasonable and appropriate considering other elements of the ICRA recovery framework and the broader context of the SAU variation.

The opening ICRA balance will be locked in and only adjusted in line with the detailed ICRA drawdown provisions specified in the SAU variation. There would be no reconsideration of the ICRA balance and NBN Co is not guaranteed to recover all, or any minimum amount of the ICRA balance (discussed further below), which will provide strong incentives on NBN Co to invest and operate efficiently and engage in efficient financing practices.

We note that the opening ICRA balance will be locked in and only adjusted in line with the detailed ICRA drawdown provisions specified in the SAU variation. There would be no reconsideration of the ICRA balance and NBN Co is not guaranteed to recover all, or any minimum amount of the ICRA balance (discussed further below), which will provide strong incentives on NBN Co to invest and operate efficiently and engage in efficient financing practices.

Further, the baseline scenario that Sapere modelled assumes a continuation of current arrangements, where NBN Co does not pay dividends. We consider it important that the proposed regulatory arrangements leave scope for changes in dividend policy that would allow for reasonable dividends to be paid to shareholders in future.

That is, we consider the proposed opening ICRA balance should allow for a dividend policy within the range that could be expected for an efficient infrastructure firm with a largely sunk and depreciated asset base, and which has not paid a dividend over an extended start up period. In this regard, we note that NBN Co has not yet made any dividend payments since it was established in 2009 and is not expected to do so until financial year 2030.

We consider that each of the dividend scenarios that Sapere has modelled could be reasonable while the SAU is in effect. We note that ultimately the setting of the dividend policy, which could in turn influence the pricing strategy, would be a matter for the government shareholders. We would intend to consider this matter further if the SAU were to cease.

We acknowledge that the proposed ICRA balance reflects previous expenditures or investments that have not been recovered. We have adopted a forward looking approach to assessing the opening ICRA balance and focussed on projected credit ratings, which is reflected in the Sapere analysis. We have therefore not formed a view on the extent to which the ICRA reflects historical inefficiencies or individual cost items that have taken place in the past. It is of the view that it is appropriate to consider the opening ICRA balance from the perspective of the revenue required for the achievement and maintenance of a forward looking investment grade credit rating. That said, we note the proposed ICRA balance is significantly below the balance of the ICRA account that would otherwise result from a continuation of the current arrangements.

**The approach to setting and drawing down ICRA is reasonable and would promote the LTIE**

Under the proposed framework for recovering the ICRA, NBN Co is not guaranteed to achieve or maintain a standalone investment grade credit rating. Similarly, it is not guaranteed to recover all, or any minimum portion of the ICRA, over the SAU period.

NBN Co would need to reach certain milestones in order to meet these objectives. First, NBN Co would only be able to recover the ICRA once it reaches its breakeven point. This is when NBN Co will earn enough revenue to recover its ABBRR, which is expected to occur in 2029-30 based on current projections. If NBN Co is delayed in reaching the breakeven point, through either lower than forecast revenues or higher than expected expenditure, NBN Co will have less opportunity to recover the ICRA over the SAU term.

For example, NBN Co would be able to recover up to $1.1 billion up to 2031-32, but would not be able to carry forward any unrecovered portion of this into the post 2032 period. This means that any delays in reaching the breakeven point of more than a year could result in NBN Co forfeiting this amount. Similarly, if NBN Co does not recover the $11.4 billion in ICRA it is entitled to recover over the post 2032 period, it would also forfeit the amount remaining.

The setting of the opening ICRA balance and rules for ICRA drawdown independent of NBN Co's actual financial arrangements will promote incentives on NBN Co to operate and invest efficiently. If NBN Co operates inefficiently or undertakes inefficient investments, has lower demand or revenues that will impede its ability to drawdown the ICRA, or it otherwise undertakes inefficient financing practices, NBN Co will bear that risk. We therefore consider that the proposed opening ICRA balance and framework for drawing down ICRA are reasonable and would promote the LTIE.

Further, separately to the above, we note that NBN Co has indicated that it would be willing to make potential changes the ICRA draw down rules contained in both Module 2 and module. These changes would make clear that the rate at which NBN Co could draw down the ICRA in the post-2032 period would be subject to a protection against prices shocks, save for the 2040 financial year. These changes would significantly improve the reasonableness of the ICRA draw down provisions.

For completeness we note that NBN Co is not guaranteed achieving its financial objectives by drawing down the full ICRA balance over the SAU period, and this will depend on NBN Co's operating performance and efficiency, and the actual financial arrangements NBN Co puts in place. That is, although the regulatory arrangements can provide an opportunity for these objectives to be achieved in a manner that is reasonable and promotes the LTIE, the responsibility will ultimately rest with NBN Co.

**Determining ICRA drawdown amounts before each regulatory cycle achieves an appropriate balance between flexibility and certainty**

Finally, we consider the process for determining the ICRA drawdown amounts before each regulatory cycle through the replacement module process will achieve an appropriate balance between flexibility and certainty.

This will allow NBN Co to consider current market conditions in preparing its replacement module applications and allow it to propose ICRA drawdown amounts that best reflect these conditions at the time. It would give scope to the ACCC to give similar consideration in making its replacement module determinations.

The ICRA drawdown amounts themselves will be determined consistent with the Module 2 rules during the subsequent regulatory period and the Module 3 rules in the post-2032 period. We note that these draw down rules would not require consideration as to whether the resulting regulatory allowance would lead to price shock. Subject to NBN Co proceeding with its proposal to make the draw down amounts subject to consideration of avoiding price shocks as discussed above, we consider that the proposed process for determining ICRA draw down amounts ahead of each regulatory cycle would be reasonable and promote the LTIE.

## 4.4. Pricing and product constructs

**Key points**

- We consider that the product and pricing arrangements that are contained in the SAU variation are, on balance, reasonable and would encourage efficient and competitive NBN markets, except as follows:
    - There is residual cost uncertainty that retailers would still face when acquiring services for the 50 Mbps wholesale offer during the First Regulatory Cycle (as elaborated in section 4.5)
    - Important specifications for the working of the Low Income and Digital Inclusion Forum are not specified in the SAU variation
    - There is no commitment to effectively address the competition concerns that retailers continue to express over network-to-network interface charges.
- We provide comments on how these matters could be resolved should NBN Co decide to provide a revised SAU variation proposal.
- We consider NBN Co's phased withdrawal of CVC charges over the first regulatory cycle to be otherwise reasonable.
- We are satisfied that the proposed increase in the bundled charge for 50 Mbps wholesale offer would not provide a basis to reject the SAU variation as it is necessary to provide NBN Co a reasonable opportunity to recover its efficient costs. We also note that it is occurring as part of an overall package of price changes that includes reductions in prices for other wholesale offers.

### 4.4.1. Overview of SAU variation

NBN Co proposes the following significant changes to its product and pricing model:

- the introduction within 3 months from acceptance of the SAU variation of a flat monthly charge construct for residential grade 100 Mbps and higher speed offers[31]; and
- the transition of the remaining lower bandwidth residential grade bundled offers of less than 100 Mbps to flat rate offers from 1 July 2026 by reducing the CVC overage

[31] These speed tiers represent less than 20 percent of NBN residential grade services; see ACCC, *NBN wholesale market indicators report*, September 2022.

charge for each intervening financial year from $8/$7/$6 per Mbps per month and then setting this at zero.[32]

NBN Co is also proposing to charge for CVC overage for the bundled offers by utilised, rather than provisioned, CVC capacity, which could reduce exposure to CVC overage on days when some of the provisioned capacity is not used. .[33] There is also provision for the CVC allowances in the bundled offers to be adjusted formulaically every 6 months, with the apparent intention of offsetting around half the expected growth in peak CVC usage over time.[34]

Some notable price differences from the current WBA4 offer[35] are:

- a rise of $5 per month in the minimum charge for 50 Mbps fixed line and Wireless Plus services from $45 to $50
- $3 to $10 per month reductions of the minimum charges of services of 100 Mbps or more
- $11 per month reduction in the minimum charge for 25 Mbps services from $37 to $26 per month
- a $3.10 per month increase in the cost to acquire the 12 Mbps broadband access service[36]
- the availability of a new voice capacity offer priced at $12 per month, which is down by $10.50 per month from the existing commercial offer of $22.50 per month.

NBN Co has also lowered its monthly recurring charges for the ports typically used by smaller retailers to interconnect to the NBN (network-to-network interface) in line with a recent change made to its commercial offer.

Some of the proposed pricing changes also differ to those proposed in the March 2022 SAU variation.[37] These include:

- a reduction in the commencing bundled charge for 12 Mbps broadband speed tier from $26.00 to $24.40
- minor increases in starting CVC inclusions for the 25 and 50 Mbps tiers (by 0.1 Mbps and 0.05 Mbps respectively)
- the progressive reduction in the price of CVC overage[38] and its complete removal from the start of 2026-27 for residential grade wholesale offers
- a $5 to $10 per month reduction in the previously proposed flat rate charges for several 100 Mbps and higher speed offers
- the reduced monthly recurring charges for its lower capacity network-to-network interfaces.

---

32 NBN Co, SAU variation, Module 2, Schedule 2E.2.2(d).

33 NBN Co, SAU variation, Module 2, Attachment E, clause 3.1 (a).

34 NBN Co, SAU variation, Module 2, Schedule 2B.5.1.

35 The commencing prices and CVC inclusions (as applicable) are listed in Attachment E of the SAU variation.

36 The $3.10 cost increase comprises a $1.90 per month increase in the minimum charge from $22.50 to $24.40, and the removal of the CVC inclusion of 0.15 Mbps that increases exposure to CVC overage charges by $1.20 per month.

37 These earlier pricing changes were outlined in the ACCC's May 2022 consultation paper, the key pricing changes from the existing SAU being a flat monthly charge construct for residential grade 100 Mbps and higher products, bundled offers for products less than 100 Mbps with provision for a CVC overage charge of $8 Mbps, close pricing alignment of the 12 Mbps and 25 Mbps broadband offers and a $12 per month voice-only offer.

38 The prices are to be $8 per Mbps in 2023-24, $7 per Mbps in 2024-25 and $6 per Mbps in 2025-26.

The SAU variation does not commit NBN Co to develop a special offer for low income or disadvantaged consumers but does contemplate the potential for NBN Co to introduce discounts that are targeted at such consumers.[39] It does commit NBN Co to establish a low-income forum to identify initiatives to improve access to the NBN for low-income, vulnerable and unconnected consumers.[40] NBN Co would have to have regard to the outcomes of the Forum in changing or setting prices,[41] and would report to Forum members ahead of each meeting, and publish a report each year, on NBN Co's progress in implementing low income initiatives.[42]

In addition to the product offers outlined in the SAU variation, NBN Co has stated in its supporting submission that it will consider introducing offers that would provide suitable support to low use consumers and protect them from more significant price increases if they instead faced the same charges as other consumers when the flat rate pricing model takes effect from the start of the second regulatory cycle.[43] However the SAU variation proposal does not contain a commitment to do so.

The SAU variation confers discrete powers on the ACCC to support the regulatory product and pricing controls remaining fit for purpose over time. These include a power to object to prices of new products for up to two years from introduction (clause 2F.5) and to object to the withdrawal of products (clause 2H.6.3), which is an important regulatory safeguard, as product withdrawals have the potential to reduce choice and competition.

In the post-2032 regulatory period the product and pricing approach described above would not apply. However, a replacement module determination for that period may more directly specify maximum prices and a framework for setting or controlling maximum prices (clause 5.10(b)).

### 4.4.2. Submissions

Submissions addressed various aspects of NBN Co's proposed approach to product and pricing as contained in the SAU variation:

- The phased withdrawal of CVC charges for residential grade services
- The increase in the minimum charge for the 50 Mbps wholesale offer, and potential for the combined charge for this offer to converge with the charge for the 100/20 Mbps wholesale offer
- The increase in the cost of the 50 Mbps wholesale offer without a commensurate increase in service quality or a commitment to rectify underperforming connections
- The likely impact of the product and pricing changes on costs of supply, and on the overall demand and speed tier mix
- The effectiveness of the proposed low-income measures
- The scale effects of network-to-network interface charges

More particularly, submissions raised concerns over the initial $5 increase of the bundled charge for the 50/20 speed tier, and its potential convergence with the 100/20 cost with CVC usage growth. (Telstra, Optus, Vocus, Aussie, Xintegration, IAA, ACCAN). A related concern expressed by several submitters was that end-customers on poorly performing 50/20 speed

---

[39] NBN Co, SAU variation, Module 2, Schedule 2C.4.3(a) (iv)(B).

[40] NBN Co, SAU variation, Module 2, Schedule 2B.7. NBN Co has constituted the Forum, with an initial meeting convened on 22 March 2023.

[41] NBN Co, SAU variation, Module 2, Schedule 2B.2.1(f).

[42] NBN Co, SAU variation, Module 2, Schedule 2B.7

[43] NBN Co, SAU variation *Supporting submission, Part B: Pricing and price controls*, November 2022, p. 12.

tier lines were already paying for speeds the lines cannot deliver and that there should be no increase in price unless accompanied by service quality improvements (Telstra, Optus, ACCAN, Hucklebridge).

Those retailers that have a larger proportion of customers on entry level broadband products submitted that the pricing proposal for these products risk driving customers to consider alternative networks. (TPG, Vocus). Telstra submitted that further changes should be made to the voice only 12 Mbps offer product, including not restricting it to a voice only product (Telstra pp. 16, 41-42). NBN Co in its submission provided additional clarity over its proposed product and pricing proposals for the lower speed tiers, indicating it would continue to support separate pricing outcomes for the 12 Mbps and 25 Mbps wholesale offers. (NBN Co).

Submissions included the following suggestions for alternative product and pricing commitments in the SAU variation:

- Keeping the starting price of the 50 Mbps wholesale offer at $45 (Telstra, Optus, Vocus, Aussie, IAA, ACCAN) and capping the CVC charges payable (Telstra)
- Making price increases for the 50 Mbps and higher speed wholesale offers conditional on quality improvements, particularly for non-performing lines (Telstra, Optus, ACCAN, Hucklebridge)
- Improved entry level pricing offers (TPG, Vocus, Telstra)
- Removal of CVC charging across all residential grade services from the start of the first regulatory cycle (TPG, Optus, Vocus, AGL, Commpete, Xintegration)
- Changing the structure of network-to-network interface charges so that retailers looking to expand their operation are not at a material cost disadvantage to incumbent retailers. (Launtel, Internet Association of Australia)

NBN Co states in its submission (p. 14) that access costs are likely to be less than retailers might expect, and in subsequent correspondence has explained how an effective cost optimisation strategy could lead to better cost outcomes than basing forecasts on current demand and speed tier mix.[44]

Stakeholders expressed differing views about the likely effectiveness of the proposed low income and digital inclusion forum unless further support was provided for it in the SAU (Telstra, AGL, IAA, Xintrergration, ACCAN, Bebbington). Some submissions advocated for more direct measures to support relevant consumers such as introducing wholesale offers targeted to disadvantaged customers (Optus, Vocus, Launtel).

### 4.4.3. ACCC assessment

**The phased withdrawal of CVC charges for residential grade services**

We consider that CVC charges have become a relatively inefficient means to grow revenues and have placed at risk busy-hour service quality for consumers.[45] Further, the potential for CVC charging to improve efficient use of the NBN now appears limited to networks that are subject to hard capacity limits such as satellite. Targeted fair use policies are also available to manage such capacity issues.

---

44 NBN Co letter to ACCC, 24 March 2023, p. 4.

45 For instance, CVC charges are based exclusively on download volumes during the busy hour and so cannot monetise willingness to pay for other usage, including remote working or learning during the day over a home broadband connection; require a high degree of forecasting accuracy so that targeted overage revenues can be realised without congestion of end-user services; and drives higher retail costs in monitoring CVC.

However, we consider that the approach that NBN Co has proposed in its SAU variation to withdrawing CVC charges for residential grade services is, on balance, reasonable and would promote the LTIE. We note that NBN Co has committed to withdraw CVC charges from its high-speed residential grade offers within three months of acceptance of the SAU variation and will exit these charges from the remaining residential grade offers over the course of the first regulatory cycle.

We also note that forecast growth in daily peak CVC utilisation continues to trend down with developments in popular busy hour applications, such as streaming, which if it continues would moderate growth in CVC overage revenues and the extent of cost increases for retailers.

In saying this we acknowledge that CVC charges are a material source of uncertainty and complexity for retailers despite providing the opportunity for greater retail product differentiation, and that removing these charges sooner could bring efficiency and competition gains. Adjustments to CVC inclusions will be more predictable and the per Mbps price of CVC overage will reduce by $1 each year, which could partially alleviate cost uncertainty associated with these charges. We discuss below the residual cost uncertainty from continuing CVC charges over the first regulatory cycle.

Separately, we note that NBN Co has submitted that it is considering the introduction of a flat rate wholesale offer to support low use services on more basic wholesale offers. We acknowledge that having such a wholesale offer in place before removing CVC from the entry level offer could protect consumers with more basic needs from significant price increases. We consider that NBN Co will likely have a commercial incentive to introduce wholesale offers to this effect in order to retain customers on its network and, if adopted, this could reduce concerns that NBN Co chose not to include a commitment to do so in its SAU variation.

**The increase in the minimum charge for the 50 Mbps wholesale offer, and potential for the combined charge for this offer to converge with the charge for the 100/20 Mbps wholesale offer**

We consider that the proposed increase in the minimum charge for the 50 Mbps speed offer to be reasonable given that:

- NBN Co's annual revenues are significantly below its efficient costs as estimated in the building block model (BBM) and higher average revenues would be needed for NBN Co to have a reasonable opportunity to recover its efficient costs; and
- increasing demand for higher yielding wholesale offers or value-added services alone is unlikely to increase average revenues to address the shortfall.

We recognise that NBN Co's pricing was set on a benchmark basis during the rollout. Entry level access offers were benchmarked to ADSL prices, meaning that the price of higher speed offers would be bound by the value consumers placed on them relative to the entry level offer. This was with a view to smoothing the migration and reflected the practical difficulty in ascertaining efficient cost levels during the rollout. With these issues resolving, we consider it is an appropriate time to transition NBN access pricing towards a more cost-reflective basis that will better ensure efficient use of and investment in the network.

We note that the increase in price for the 50 Mbps wholesale offer will be partially offset by reductions in other speed offers. Combined with the increase in the 50 Mbps speed offer, this will narrow the difference in the cost of a 50 Mbps wholesale offer (i.e., the combined AVC and CVC overage charge), and of a residential grade 100 Mbps wholesale offer.

We note the concerns expressed in submissions that a typical service could cost more to acquire under the 50 Mbps wholesale offer than under the 100 Mbps wholesale offer. We share these concerns due to the likely impact of reduced wholesale product differentiation and end customer choice on efficiency and competition arising from the effective withdrawal of the standard wholesale offer.

We note however that NBN Co has stated in its draft indicative statement of pricing intent provided in January 2023 that it intends to price its services to support the ongoing viability of the 50 Mbps wholesale offer. The draft statement noted that, based on NBN Co's best forecasts, its product and pricing model would lead to its 50 Mbps wholesale offer representing 46 percent of all residential grade wholesale access in FY26.[46]

This suggests that, although there is potential for a growing proportion of services acquired under the 50 Mbps wholesale offer to be more economic to acquire under the 100 Mbps wholesale offer over time, the 50 Mbps wholesale offer could remain competitive for most such services.

NBN Co has also indicated that it would be willing to provide for additional reporting to retailers on peak CVC usage in any revised SAU variation proposal, to help in selecting higher using 50 Mbps services to transition to the wholesale 100 Mbps offer.[47] If adopted, this could be a potential means to keep the wholesale 50 Mbps offer economic for retailers. We consider this potential initiative in the price control and transparency discussion in section 4.5 below.

**The likely impact of the product and pricing changes on costs of supply, and on overall demand and speed tier mix**

As compared to current wholesale prices, the proposed tariffs that would apply on commencement of the first regulatory cycle would likely:

- reduce the average cost to serve consumers currently acquiring 25 Mbps and 100 Mbps and higher speed plans, and those that require only a voice service.
- increase the cost to serve consumers currently acquiring 12 Mbps and 50 Mbps broadband plans.
- reduce the use of 12 Mbps wholesale offer (other than for voice only and low use broadband consumers), as the cost to acquire the 25 Mbps wholesale offer to supply consumers (other than voice only and low use broadband consumers) would be roughly the same.[48]

We had previously indicated that the product and pricing model could lead to an effective withdrawal of the 12 Mbps wholesale offer for all broadband use. NBN Co has submitted that this is not the case and that it would continue to be offered and represent a lower cost option for some services.

We note the differing views that have we have received concerning the impact of the proposed product and pricing changes on supply costs and demand within these broad directional changes, with NBN Co basing its forecasts on industry averages whereas retailers are providing forecasts more reflective of their business.[49]

46 See NBN Co, Draft Statement of Pricing Intent, undated, at Table 1, page 4.

47 See NBN Co, letter to ACCC, dated 24 March 2023 at p.4

48 A service would cost the same under a 12 Mbps or 25 Mbps wholesale offer should it on average use 0.2 Mbps of CVC, which is the CVC inclusion of the 25 Mbps wholesale offer. This equates to a theoretical download limit of no more than 180MB in an hour. (90 MB = 0.2 Mbps x 3600 seconds / 8 bits per byte.)

49 NBN Co provides its industry average forecasts In Part of its supporting submission at p.11, which includes an estimate of $50.02 to acquire the 50 Mbps wholesale offer.

We consider that unit cost charges for each retailer would likely be distributed around the estimates that have been provided, with the complexity of the pricing model making precise estimates difficult. The usage profile of a retailer's customer base, the extent to which a retailer has historically provisioned CVC above the level of actual utilisation, and its future take up of cost optimisation strategies would likely make a significant contribution to the effective unit costs that a retailer will incur under this model for each wholesale offer.[50] We discuss the potential for cost optimisation and potential implications for cost outcomes and cost certainty below.

We note that cost outcomes for retailers could also be influenced by the methodology that NBN Co applies in calculating CVC overage or other charges which sit outside the SAU variation.[51]

We consider the divergence in submissions on the likely demand impacts of the pricing model stems from a difference in view on whether price increases would be directed to different classes of consumers and businesses based on their willingness to pay for broadband. If this is not the case, then it is more likely that attempting to realise higher yields would more materially impact demand than NBN Co has forecast.

We recognise that RSPs have advised that some consumers have already churned to less expensive retail plans and note that growth in total NBN access services stalled in the most recent quarter.[52] This is consistent with growing interest from more price sensitive consumers in exploring options for lower cost broadband. We also acknowledge that predominately voice and/or low-capacity broadband services would be more likely to be supported by alternative wireless networks.

We consider NBN Co will continue to have an incentive to attract or retain such households via adjustments to its wholesale offers over time where it is efficient to do so. The adoption of a price cap rather than a revenue cap assists with setting these incentives. In this regard, we note that NBN Co has previously offered targeted discounts to encourage connections to its network, and has proposed in its SAU variation a low cost voice only wholesale offer and resetting the 25 Mbps wholesale offer so that retailers can offer a higher speed inclusion in their entry level broadband plans.

On balance we consider that outside of the continued price uncertainty generated by the retention of CVC for 50 Mbps tier, the likely impact of the pricing changes on the market will be reasonable and in the LTIE.

Relatedly, we note that NBN Co has indicated that should it withdraw and resubmit its SAU variation proposal it would be willing to rebadge the lower priced 12 Mbps wholesale offer so it would support use for voice only and very low use broadband.[53] We consider the ongoing availability of 12 Mbps wholesale offers for low and very low use consumers would assist with retail product diversity and contribute further to the LTIE.

---

[50] NBN Co discusses this cost optimisation strategy in its letter of 24 March 2023.

[51] We note that the methodology to calculate charges is not specified in the SAU variation and is instead a matter to be addressed as part of NBN Co's development of its next commercial offer to retailers.

[52] ACCC, NBN Market Indicators Report for December 2022 Quarter available at www.accc.gov.au

[53] NBN Co proposes renaming this offer the Basic Bundle offer and to allow a retailer to use 0.1 Mbps of CVC capacity without facing higher charges. This would be roughly double the rate of a dial up internet connection, and theoretically support no more than 45 MB of data to be downloaded per hour. See NBN Co letter to ACCC, dated 24 March 2023, at pp. 6-7.

**The increase in the cost of the 50 Mbps wholesale offer without a commensurate increase in service quality or a commitment to rectify underperforming connections**

We recognise that the November SAU variation does not commit NBN to seek out opportunities to materially uplift its service standards, or to make a significant inroad into fixing the drivers of negative consumer sentiment in the near term. These drivers include underperforming copper lines and connections that regularly experience network outages without prior notification.

While we agree that the SAU variation should provide a clearer path to current quality issues being efficiently addressed, we do not consider that it would be reasonable or in the LTIE for the proposed increase in the price for the 50 Mbps wholesale offer to occur only after this has occurred.

We discuss in section 4.12 below the consultation process that is proposed in the November SAU variation for subsequent regulatory cycles, and the additional consultation measures and transparency commitments that NBN has recently indicated it would provide for the initial regulatory cycle in a revised SAU variation.

**The effectiveness of the proposed low-income measures**

We acknowledge that submissions raise equity issues concerning access to affordable broadband and that it would be difficult for potential initiatives to address this to succeed without support of the broadband network operator.

We note that the SAU variation would commit NBN Co to actively consult with representatives of low income and other disadvantaged groups via a forum that it would convene and chair. NBN Co has already established a forum to serve this purpose, and advised that it would intend to convene the forum more regularly than once per year as specified in the SAU variation.[54]

We consider that this forum could make a positive contribution to addressing the equity concerns by working to address impediments that disadvantaged consumers face in accessing online applications and information. This would likely depend on the effectiveness of consultation with Forum members and on the accountability that NBN Co's reporting on the Forum would create.

We note that submissions identified potential weaknesses in the proposed commitments regarding the Forum. We agree that the level of commitment made in the SAU surrounding the operation of the forum could be strengthened to make it in the LTIE.

In this regard, NBN Co should consider including commitments in the SAU variation to respond to the Forum's recommendations in the reports that it provides to Forum members, as well as when reporting to the public on the Forum's work. We note that NBN Co has expressed a willingness to do this and potentially make corresponding commitments in the Forum's terms of reference in its submission to the consultation paper, but not the SAU variation itself.[55] In addition, NBN Co could clarify that it would have regard to the views of the forum before proposing product withdrawals, as the SAU variation would commit NBN Co to do when considering price changes. Further, the SAU variation could clarify that it would undertake effective consultation with Forum members ahead of these price changes and product withdrawals and report to forum members explaining how their views were considered.[56]

---

[54] NBN Co established the low income and digital inclusion forum (LIDIF) and held the first meeting on 22 March 2023

[55] NBN Co submission to ACCC consultation paper, p. 16.

[56] The SAU variation would commit NBN Co to consider the outcomes of the Forum when settling its upcoming tariff statement and pricing roadmap, but is silent on the need to effectively consult with the Forum ahead of these decisions or

We note that other commitments in the SAU variation related to the pricing of entry level offers referred to above could also be of benefit to low income customers even though they are not presented as specific to low income or other disadvantaged consumers.

As one example, the SAU variation also proposes changes to the 25 Mbps wholesale offer so that it would be economic for entry level retail services to migrate from a 12 Mbps speed to a 25 Mbps speed inclusion at little to no additional wholesale cost. This may assist those disadvantaged consumers who choose from lower priced retail plans to gaining access to plans with higher download and upload speed inclusions for the same price that they pay today.

The SAU variation also proposes a low-cost voice-only offer at $12 per month that should help deliver lower priced phone services to some lower income cohorts. NBN Co has recently indicated that it would intend to amend this wholesale offer so it could be used for both voice and very low use broadband. This offer may be relevant to improving digital inclusion by those disadvantaged consumers who have fixed line voice and basic data connectivity needs, but not consumers with standard data connectivity requirements.

**The scale effects of network-to-network interface charges**

We note that network-to-network interface charges continue to be a source of competition concerns notwithstanding changes that NBN Co recently made. These concerns were raised at the stakeholder working groups that we chaired in 2021. They arise from the economies of scale embedded in the NNI price structure which disadvantage smaller retailers when seeking to compete with larger incumbent retailers.

We are concerned that this issue has ongoing potential to impede competition by raising barriers to entry and expansion by smaller operators that could otherwise assist in keeping retail prices and demand at more efficient levels as wholesale charges increase. We are therefore not satisfied that the NNI charges are either reasonable or would promote the LTIE. We note that NBN Co has stated that it is further considering options to address these concerns and intends to provide an update following our draft decision.[57]

## 4.5. Price controls and transparency measures

**Key points**

- We consider that the proposed price controls and transparency measures for the subsequent regulatory period strike an appropriate balance between giving flexibility to price efficiently in the wholesale market and providing the degree of cost certainty that retailers require to offer competitive services to the households and businesses that use the NBN. On balance, we are therefore satisfied that the controls and transparency measures are reasonable and would promote the LTIE.
- We note that stronger commitments over the pricing roadmap could impede efficient wholesale pricing that responds to market conditions and could extend the period required to reach efficient cost recovery.
- We note that the combined AVC and CVC charges for services acquired under the 50 Mbps wholesale offer could fall within a very broad range under the proposed pricing model for the first regulatory cycle. This results in cost uncertainty for

to explain to Forum members how their views were considered in this regard. See section 2B.2.1 and 2B.7 of the SAU variation.

[57] NBN Co letter to ACCC, 24 March 2023, p. 6.

RSPs, and therefore the ACCC is not satisfied that the pricing for the 50Mbps wholesale offer is reasonable or would promote the LTIE.

- We consider the SAU variation should provide an efficient means by which retailers can manage this residual cost uncertainty over the first regulatory cycle in order for the ACCC to be satisfied that he 50 Mbps wholesale offer is reasonable and would promote the LTIE.
- In this regard, if NBN Co were to submit a revised SAU variation, it should assess the respective benefits of applying a billing rule to cap the maximum combined AVC and CVC charge that a service would attract under this wholesale offer and its own proposal of developing additional reporting on CVC utilisation and business to business systems with a view to retailers optimising their wholesale costs by switching services between wholesale offers.
- We note that the price controls are complex and more could be done to demonstrate and explain their operation by NBN Co in order for stakeholders to better assess the operation of the SAU variation. To assist in this respect, NBN Co should consider publishing its proposed pricing roadmap for the first regulatory cycle and accompanying modelling that shows the conformity of its pricing with the WAPC and other price controls before we make a final decision on the SAU variation.

### 4.5.1. Overview of SAU variation

NBN Co's November SAU variation proposes significant changes to the SAU price controls compared to both the current SAU and the March 2022 variation proposal. This includes, for the subsequent regulatory period, the use of a Weighted Average Price Cap (WAPC) in place of a revenue cap. In addition to the WAPC, there are price caps for individual wholesale products or product combinations that apply during this period. These include a CPI cap for the entry level product,[58] and the higher of CPI or 5 percent for other residential grade products.[59]

NBN Co has designated the 25/5 Mbps speed tier as the entry level service for the first regulatory cycle. NBN Co would propose, and the ACCC determine, which wholesale offer is to be designated as the entry level product for each relevant NBN network for an upcoming regulatory cycle within the subsequent regulatory period (other than the first regulatory cycle).[60]

For so long as annual revenue recovery is below the ABBRR, the annual increase in weighted average prices permitted by the WAPC would be set at the annual increase in the CPI.[61] Once this point is reached, an annual ICRA drawdown amount would be included in the annual regulated revenue allowance, and the annual WAPC increase allowance would be determined by an annual CPI-X increase for each subsequent regulatory cycle. Notably, the X in the CPI-X formula could be negative (i.e., so the formula becomes CPI+X) and so real price increases could be possible, where the annual regulated revenue allowance grows faster than CPI.

58 NBN Co, SAU variation, Main body, clauses 5.2(e)(iii), 5.5 and 5.9(a)(ii). Module 2, Schedules 2B.4.1 and 2E.2.1.

59 NBN Co, SAU variation, Module 2, Schedules 2D and 2E. A WAPC sets a global limit over the price movements across all products in 'the cap', whereby the positive and negative price movements for each product are weighted by their demand data and then summed to give an average value. Each product would need to be priced so that the individual cap applying to it is, and the overall WAPC, not be exceeded.

60 NBN Co, SAU variation, Module 4, Schedule 4A.4.

61 The relevant CPI figure for a given financial year would be as published for the 12 months ending on 31 December prior to the financial year.

As discussed above, CVC overage charges for residential grade products would be phased out over the first regulatory cycle and set at $0 for 2026-27 onwards.[62] The required price reductions for CVC overage could be offset commensurately by rises in the price of the bundle of AVC and CVC inclusions under the WAPC and the individual price caps. This is because the individual price caps and the WAPC will be applied to an average combined charge (a combination of the bundle of AVC and CVC overage charges) for each product group on a weighted average basis across retailers, rather than separately to each of the bundled charge and the CVC overcharge charge.[63]

The proposed WAPC and the individual price caps are based on a 'use-it-or lose it' basis that would not permit unutilised historical allowable price increases to be carried over from one year to the next (i.e., the WAPC and individual price caps provide for price increases to prior year actual prices, not prior year maximum allowable prices). This provision would also apply between regulatory cycles such that no-catch up in prices to meet a forecast revenue allowance for a previous regulatory cycle would be permitted.

Product additions and withdrawals are to be accounted for in the WAPC although there would be short delay for new products being added. NBN Co has indicated that products that are first introduced between 1 April and 31 March prior to the commencement of a financial year would be included in the WAPC for the following financial year. This is so data to calculate and weight price movements will be available to inform the tariff list for that year. That said, replaced products would have their demand assigned to the successor product, subject to approval of the ACCC (clause 2D.3). These rules help to drive accuracy in the measures of effective price movements and discourage the inefficient churn of product offers (e.g., to circumvent the price controls on increasing prices for the existing product set).

The SAU variation also proposes transparency measures intended to increase pricing certainty in addition to the price controls. During the subsequent regulatory period, NBN Co would have regard to the specified pricing principles in setting new prices or changing prices,[64] and would publish an up-front statement of pricing intent for each regulatory cycle outlining its financial objectives; the pricing strategies it intends to adopt; any intended changes to its price structures; and areas of likely product innovation and development that are expected to influence price changes. The statement of pricing intent could only be varied in limited circumstances and after consultation.[65]

NBN Co would also publish a binding tariff list by 1 May each year for the forthcoming financial year and a pricing roadmap of prices for that and the subsequent two financial years.[66] The published prices are required to be consistent with the statement of pricing intent for the regulatory cycle.[67]

Subsequent year tariff list prices for individual products could differ from the pricing roadmap that had previously been published for that year, subject to price relativities remaining within $1 of those in the roadmap.[68]

Discounts would not be counted for the purposes of WAPC and individual price cap compliance. This means that changes in the nature or scope of any targeted discounts (such as for certain speed tiers or service locations) could not change the degree of pricing discretion that NBN Co would have when pricing its offers more generally. There are also

---

62 NBN Co, SAU variation, Module 2, Schedule 2E.2.2(d).

63 NBN Co, SAU variation, Module 2, Schedule 2F.4.

64 NBN Co, SAU variation, Module 2, Schedule 2B.2.1.

65 NBN Co, SAU variation, Module 2, Schedule 2B.2.2.

66 NBN Co, SAU variation, Module 2, Schedule 2B.2.3 and cl 2B.2.4.

67 NBN Co, SAU variation, Module 2, Schedule 2B.2.3(b)(iv) and 2B.2.4(c)(iii).

68 NBN Co, SAU variation, Module 2, Schedule 2C.2.

powers for the ACCC to review discount offers (and NBN Co's pricing conduct more generally) where it offers a significant volume of services under temporary discounts or pricing materially departs from the published statement of pricing intent.[69]

NBN Co has also proposed a commitment to only withdraw discount measures in accordance with the terms it announced on their introduction,[70] and to limit the value of discounts on an annual basis such that its otherwise undiscounted revenue is no more than 5 percent above its discounted revenue. Some discounts, such as for low income offers, would be excluded from this analysis.[71] Should NBN Co exceed the threshold, NBN Co would need to convert the amount exceeding the threshold to permanent price reductions in the subsequent year.[72]

In the post-2032 period, the maximum prices and other price certainty measures would be as specified in the replacement module determination that the ACCC makes for a regulatory cycle.[73] That is, there is no requirement that the price control elements specified for the subsequent regulatory period, i.e., Module 2, must carry over into the post-2032 regulatory period under the terms of such a determination.

That said, the ACCC's ability to determine price controls in the post-2032 regulatory period would be subject to the framework and high level principles established under Module 3 of the SAU variation. Section 4.2 above discusses this framework.

### 4.5.2. Submissions

Submissions addressed the following aspects of the proposed approach to the price controls and related measures for the subsequent regulatory period:

- The maximum rate at which prices should be permitted to increase each year
- The causes of price uncertainty and further options to address them
- The complexity of the price controls.

Submissions considered that the specified maximum price movements of CPI, or the higher of CPI and 5 percent, depending on the control, were too generous. Alternative proposals ranged from no increase to half the rate of CPI, or the lesser of CPI and 5 percent. (TPG, Optus, Vocus, Aussie, Launtel, Xintegration)

Submissions pointed to CVC charging as a principal cause of cost uncertainty and made the point that removing these charges from all residential grade products would simplify forecasting access costs. This was in addition to arguments for removal based on avoiding operational complexity and avoiding associated costs. (Telstra, TPG, Optus, Vocus, AGL, Commpete, Xintegration, ACCAN). Submissions also identified the absence of annual limits on ICRA drawdown as a source of cost uncertainty. (Optus)

Submissions generally expressed concern over whether the pricing principles would be applied in a predictable manner or whether the statement of pricing intent would have sufficient detail. This appears to have been based on the indicative draft of the statement of pricing intent that NBN Co made available in January 2023. Submissions also queried the certainty that the roadmap would provide as tariff prices in the second and third years could depart from the roadmap. (Telstra, TPG, Optus, Vocus)

69 NBN Co, SAU variation, Module 2, Schedule 2C.4.2.

70 NBN Co, NBN SAU variation, *Supporting submission Part B: Pricing and price controls*, November 2022, p. 29.

71 NBN Co, SAU variation, Module 2, Schedules 2C.4.1 and 2C.4.3.

72 NBN Co, SAU variation, Module 2, Schedule 2C.4.

73 NBN Co, SAU variation, Main body, clause 5.10(b)(i) to (iii).

Submissions from two retailers raised concern over the complexity of the WAPC and other price control specifications, which makes it difficult to reach a view on their appropriateness and to reliably forecast the values they would generate for a given period. (Telstra, Optus). More specifically, Telstra raised whether the quantity weights that would be used for the WAPC calculations properly accounted for changes in product mix. (Telstra pp. 34-36)

Submissions also raised concerns over the period of notice that retailers could receive of changes in prices or discount arrangements, including the two-month window to adjust its retail offers prior to the next tariff list taking effect (as well as potentially needing to implement the new product and pricing contained in the SAU variation within three months of the SAU acceptance). (Optus)

To address these concerns, submissions suggested the following alternative proposals:

- Capping or completely removing CVC exposure (Telstra, TPG, Optus, Vocus, AGL, Commpete, Xintegration, ACCAN, Hucklebridge)
- Placing a tighter bound on allowed annual price increases (TPG, Vocus, Aussie, Launtel, Xintegration)
- NBN Co providing greater clarity on operation of the WAPC and other controls prior to the variation's acceptance, including populated examples (Telstra, Optus)
- Bolstering of NBN Co's tariff commitment documents (Telstra, TPG, Optus, Vocus) including introducing a firm three-year pricing commitment or tariff list (TPG, Optus, Vocus)
- Extending the implementation timeframe for the price terms and conditions that are specified in the SAU variation, and adopting a longer minimum notice period for withdrawing discounts. (Optus)

In its submission and supporting expert reports, NBN Co argues that the WAPC as proposed has appropriate efficiency properties and provides the appropriate certainty to promote competition.[74] NBN Co further submits that it opposes price controls that would prevent prices increasing at CPI as this would likely delay it reaching efficient cost recovery. NBN Co also submitted that CPI is a driver of some of its costs and reiterated its view that it faces increasing competition, as other reasons not to restrict annual price movements in this way.[75]

### 4.5.3. ACCC assessment

We are satisfied that the price control arrangements and transparency measures are reasonable in the circumstances and would promote the LTIE in the circumstances, save for specific points that are discussed below. We consider that these arrangements would permit NBN Co to transition to efficient cost recovery with suitable protections against price shock and inefficient use of the NBN, and reasonable predictability over future pricing paths for wholesale offers.

**The maximum rate at which prices should be permitted to increase each year**

We consider that CPI would provide a reasonable basis for limiting the annual change in maximum prices under the WAPC until cost recovery is reached. Although NBN Co's costs

74 NBN submission (pp. 19-20), Frontier Economics, *Further assessment of NBN Co's proposed SAU pricing arrangements,* December 2022 and Dr William Taylor, Review of the weighted average price control in nbn's special access undertaking, NERA Economic Consulting, February 2023.

75 NBN Co letter to ACCC, 24 March 2023, p. 5.

are not forecast to increase at this rate[76], the purpose of this control is to allow NBN Co to grow its prices over a reasonable period so that they more closely align with its annual costs while avoiding price shocks for retailers and end customers.

While other reference points could be chosen, the use of CPI based measures should enable price increases to be better understood by consumers relative to a general basket of retail goods and services they acquire, and potentially militate against price increases causing inefficient use of the NBN.

We note that NBN Co has forecast that it can achieve cost recovery by FY2030 with annual price increases of 3.69 percent over the initial regulatory cycle and 2.5 percent thereafter. Should CPI values remain materially above the price increases that NBN Co has modelled, this could provide it an opportunity to reach annual cost recovery sooner, but not to price materially above its efficient costs. From that point, any real price increases would be constrained by annual changes in its efficient cost base.

We consider that annual price increases for the entry level product should be restricted to no more than CPI on equity grounds. This ensures that an entry level service continues to be made available at a reasonable price, which may not be the case under an overall CPI cap on the WAPC. We note that, under the SAU variation, the designated entry level product for the first regulatory cycle would be the 25 Mbps wholesale offer. We consider that this is a more suitable entry level wholesale offer for the first regulatory cycle than the 12 Mbps wholesale offer, given the latter's reducing demand.[77] It is also an offer that could be attractive to some lower use 50 Mbps customers should the price of 50 Mbps services exceed what they are willing to pay, thereby helping to provide for the efficient use of the network.

We note that we could nominate a different wholesale offer as the entry level offer for future cycles, which we consider a necessary safeguard so that the entry level product rules continue to be an effective constraint on pricing.[78]

NBN Co submitted in its March letter that there would be practical difficulties to implementing a change to the entry level product for the first year of a regulatory cycle if we make this decision as part of the replacement module determination. NBN Co has therefore indicated that it would be willing to amend its SAU variation proposal to provide for any change to this entry level product designation being deferred until the second year of a regulatory cycle.[79] While we are open to a SAU variation providing for outcomes that are practicable to implement, if NBN Co were to submit a revised SAU variation proposal, we would encourage NBN Co to consider whether a redesignation could take effect more quickly than the change that NBN Co has recently proposed.

We note that, during the subsequent regulatory period, the SAU variation would permit prices for other wholesale offers (i.e., other than the entry level offer) to increase each year at a maximum of 5 percent or CPI. This would provide NBN Co with flexibility to

---

76 This is consistent with NBN Co having limited direct exposure to costs that inform the CPI, and potential to achieve significant efficiencies over this period.

77 NBN Co has nominated the 25/5 Mbps wholesale offer as the entry level offer. The 25 Mbps tier represented 14 percent of residential grade wholesale market as at Dec 2022, with the 12 Mbps speed tier representing 9 percent of the wholesale market (with some of this supporting predominantly voice services). Retail plans that use the 25 Mbps tier are marketed to households with single (or a small number of) concurrent users, which would cover a material proportion of households. The pricing of this speed tier could also provide a constraint on prices for higher speed tiers (within their individual price caps) such that relative prices reflect the additional value they provide to households and businesses over and above the 25/5 Mbps baseline.

78 Demand for 25 Mbps speed tier (as well as the 12 Mbps speed tier) has reduced over the last two years by around 3 percentage points. Should this trend continue, the entry level product rules may need to be repointed to another speed tier to remain effective.

79 See NBN Co letter to ACCC dated 24 March 2023, Annexure 2, page 9.

progressively rebalance its wholesale offers should this be needed to better meet market conditions while safeguarding against major price shocks. We consider this level of price flexibility to be reasonable, noting the actual price changes would need to satisfy both the proposed price cap for the relevant wholesale offer, and the overall WAPC that is capped at CPI.

**The causes of cost uncertainty and further options to address them**

We acknowledge that cost uncertainty can impede competition and efficiency in retail markets, particularly if the retail price structure does not allow variability in costs to be readily passed on to end customers.[80] Where there is significant risk over future costs, retailers need to hedge this risk by increasing prices or reducing quality. They are also less likely to invest in NBN product development or incur other sunk costs to better differentiate themselves from other retailers.

We also recognise that NBN Co retaining a suitable degree of pricing discretion under the price controls would allow it to price to respond to market conditions more effectively. We also note that there is scope for retailers to reasonably and effectively manage the impact of small differences in wholesale charges for an upcoming financial year (compared to those it had expected) through reasonable updates to its retail offers.

Hence, we consider that the measures proposed in the SAU variation concerning cost certainty should be viewed from the perspective of their effect on the operation of both wholesale and retail markets.

We note that NBN Co has sought to respond to concerns over its pricing discretion over the subsequent regulatory period via the statement of pricing intent, binding tariff statement and indicative pricing roadmap, as well as limiting the use of discounting measures (rather than price reductions to which the price certainty commitments attach). This includes the pricing relativity measure that limits more fundamental changes in wholesale pricing strategy. NBN Co will also provide 2 months' notice of tariffs to apply for the upcoming financial year given its tariff statement must be published by 1 May. We consider that these commitments on their face should provide for a suitable balance between flexibility to respond to changes in wholesale demand and reasonable cost certainty to retailers.

While we acknowledge concerns that the effectiveness of these measures would depend on the approach taken to developing the statements and roadmap, we consider it would be in NBN Co's interest to ensure that this material can serve the purpose it intended when including the relevant commitments in its SAU variation. This was to address the cost uncertainty concerns of retailers.

We note that NBN Co has also sought to respond to the significant cost uncertainty that retaining CVC charges will cause during the first regulatory cycle. This includes a more regimented approach to adjusting CVC inclusions and stepping down the price for CVC overage.

While these measures assist, they do not remove cost uncertainty caused by retaining CVC charges over the first Regulatory Cycle, particularly for the 50 Mbps wholesale offer. We note that NBN Co has recently provided information that suggests that most services could continue to be acquired under the 50 Mbps wholesale offer for around the headline price of $50 per month, i.e., the $50 combined AVC and CVC inclusion charge without incurring CVC overage. However, the cost of services currently acquired under the 50 Mbps wholesale offer that make most use of CVC in the busy hour would be around three times this

---

[80] To the extent that wholesale prices are in excess of the efficient costs of provision, the negative impact in the retail market will be exacerbated.

amount.[81] The potential for such a wide spread of cost outcomes for a wholesale offer demonstrates the nature and scale of the residual cost uncertainty. This residual cost uncertainty means that we cannot be satisfied that the CVC charging for the first regulatory cycle as it pertains to the 50 Mbps wholesale offer is reasonable and would promote the LTIE.

To help address this, NBN Co has advised retailers that it intends to report information to assist them in identifying which of its customers could drive high CVC overage charges. This is with a view to the retailer changing the wholesale offer used to supply them to the flat rate 100 Mbps wholesale offer. Successfully doing so would cap the cost of supplying such customers from around $150 to around $55 per month.[82] [83]

However, we note that to take advantage of these reports retailers would likely need to invest in their own systems and processes (which some may find more difficult to achieve) to efficiently use the reports. In addition, retailers would likely need to repeat their analysis of these reports frequently and incur ongoing costs with changes in their customer base, as well as changes in usage patterns of individual households from week to week.[84]

We consider that an alternative means to provide cost certainty that NBN Co should also consider is to update its billing system to apply a cap on the combined AVC and CVC charge for a service acquired under the 50 Mbps wholesale offer. Such a billing rule could operate so that a service acquired under the 50 Mbps wholesale offer would not exceed the monthly cost of the residential grade 100 Mbps wholesale offer (i.e. initially $55 per month). This billing rule could be implemented in a way that would lead to the same revenue outcomes as if its CVC reporting proposal was to work as intended, but mean that retailers would not need to incur the systems development and ongoing costs that NBN Co’s method would require.

In light of the above, if NBN Co were to resubmit a revised SAU variation, we encourage NBN Co to consider the relative merits of the above approaches to managing residual cost uncertainty and include suitable commitments to effectively address this issue.

**The complexity of the price controls**

We acknowledge that the WAPC formulation proposed in the SAU variation is complex and that there is limited information about its operation beyond the overview that NBN Co has made available in its supporting submission.[85] It would likely be more difficult to predict the range of pricing outcomes that could be permitted following the new product and pricing model coming into operation, given its potential to drive changes in overall demand and speed tier mix, which are factors that influence the operation of the price controls.

---

81 NBN Co letter 24 March 2023 at page 5 notes that shifting the top 2 percent of services by busy hour usage from the 50 Mbps wholesale offer to the 100 Mbps wholesale offer would reduce the average wholesale access cost of services remaining on the 50 Mbps tier by $2 per month. This indicates that the cost of the very high use services is $100 per month (100 = $2 / 0.02) above the cost of the average cost to acquire the other 98 percent of services that use the 50 Mbps wholesale offer. This data also implies that the remaining services would not incur overage and hence incur only the $50 per month charge for the AVC and included CVC allowance.

82 In this regard, under NBN Co’s proposed product and pricing model for the first regulatory cycle it would be more cost effective for a retailer to acquire the 100/20 Mbps speed offer when supplying some of its customers that have chosen a 50 Mbps retail plan. Such a strategy would only be effective, however, where retailers can forecast with a high degree of accuracy which of its customers will be online in the upcoming busy hours and are likely to be making more intensive use of their broadband.

83 See NBN Co letter of 24 March 2023 for further explanation and indicative outcomes from adopting a successful cost optimisation strategy.

84 These are the costs of reviewing recent busy hour download data; successfully identifying services that are likely to regularly download relatively more data in the busy hour; (re)provisioning those services to a flat rate wholesale offer; and, shaping the service on its network to deliver the retail product speed that the consumer has chosen to acquire.

85 See Part B of NBN Co Supporting Submission at pp 20-22.

In these circumstances, we consider that it would be reasonable for NBN Co to publish the roadmap for first regulatory cycle, along with populated worksheets that demonstrate that the proposed prices are expected to meet the various price control arrangements, before we make a final decision on the SAU variation.

We note that NBN Co has indicated that it would be prepared to publish the initial pricing roadmap once it has finalised it as part of its business planning and ahead of any final decision on the SAU variation.[86] We understand that this would include the necessary explanatory material to demonstrate the operation of the price controls and the conformity of the roadmap prices with them.

We also note that submissions queried the use of historic quantity data to weight price movements in the WAPC formula. The SAU variation proposes the use of quantities that are for the period from 1 April to 31 March prior to the commencement of the relevant financial year.[87] We consider, however, that it would be reasonable to use the weights as proposed in the SAU variation to calculate weighted average price movements.

We acknowledge that the use of historic weights can lead to less precision in the calculated price movement than would be the case if more contemporaneous weights had been used. This is more so in a period of transition. This is due to the potential for historic weights to depart materially from those observed over the period when the relevant price changes are occurring.[88]

There can however be practical issues with the use of contemporaneous weights as it makes it more difficult to set tariffs for the upcoming year that will be consistent with the price controls. This is because the tariffs are set when the weights are not yet known. Under the SAU variation tariffs need to be set by no later than 1 May prior to the commencement of the relevant financial year. Further, to promote cost certainty, the tariffs cannot usually be reopened once set.

## 4.6. BBM proposals and NBN Co's approach to the BBM

**Key points**

- We consider that the framework proposed by NBN Co in the SAU variation for the preparation of building block model proposals in the subsequent regulatory period is reasonable and would promote the LTIE.
- We consider the building block model submitted by NBN Co in support of the proposed regulatory asset base for the first regulatory cycle, prepared in accordance with the Schedule 2G of the proposed SAU variation, adopts a reasonable approach to assigning asset lives to asset categories. We note that this approach is consistent with the requirements of the SAU.
- However, if NBN Co were to submit a revised SAU variation proposed, we encourage NBN Co to consider including in Schedule 2G a provision which defines separate asset classes for assets commissioned prior to the 2024 financial year and those commissioned from that time, which could promote economically efficient investment.

86 NBN Co letter to ACCC, 24 March 2023, p. 6.

87 These are referred to as $t_{-1.25}$ weights.

88 We note that the use of contemporaneous weights and prices for each year, i.e., so that previous period weights are used with previous period prices and current period weights are used with current prices, would constitute a revenue cap, which has the undesirable property of transferring the volume risk to retailers and in turn the consumers and business that acquire services over the NBN.

- We expect NBN Co to consider its approach to the treatment of third-party funding and government grants in any subsequent versions of the SAU variation.
- If NBN Co were to submit a revised SAU variation, we would also encourage NBN Co to explore options to improve transparency for stakeholders over the BBM and its explanatory materials.

### 4.6.1. Overview of SAU variation

Clause 5.3 of the SAU variation outlines what a building block module proposal for a regulatory cycle within the subsequent regulatory period must include. Schedule 2G of the SAU variation then sets out the detailed requirements for NBN Co's BBM proposal for the second and subsequent regulatory cycles. Schedule 4B and Attachment J (in Module 4) of the revised SAU variation set out proposed values for various inputs into the BBM for the first regulatory cycle. High-level principles regarding the ABBRR and RAB are included in Module 3 for the post 2032 regulatory period.

NBN Co has proposed to introduce several high-level principles for governing the post-2032 arrangements (discussed in section 4.2).

NBN Co has provided forecasts of the ABBRR and its components for the first regulatory cycle of 3 years commencing 1 July 2023 and included them in the SAU variation in Module 4.

NBN Co has provided public and confidential versions of its BBM in Excel format, as supporting information for the proposed building block model parameters for the first regulatory cycle of the subsequent regulatory period in Attachment J to Module 4. The public BBM does not contain information on the build-up of ABBRR for 'competitive' services. The confidential BBM appears to provide a detailed cost allocation procedure for 'core' and 'competitive' services. Compared with the BBM submitted in March, key changes include:

- changes to asset lives for certain asset classes
- grouping detailed asset classes into a smaller number of aggregated asset classes
- removal of the financeability test.

### 4.6.2. Submissions

We received submissions from stakeholders on the following:

- The treatment of asset lives within the grouping of assets into asset classes.
- The removal of the financeability test.
- The need for further transparency in the public version of the BBM.

**Treatment of asset lives**

NBN Co's SAU variation states that the remaining asset lives for each asset class, calculated in supporting material (that is, the BBM) using the values from the previous regulatory cycle ending in 2023, represent the weighted average asset lives from the individual assets in the roll forward model.

ACCAN submits that it is not reasonably clear whether the asset lives for asset classes reasonably reflect the technical lives of the assets within the classes.[89] Telstra agrees with this sentiment in its submission.[90]

Telstra also observes the approach to determine remaining life in the BBM for the first regulatory cycle is inconsistent with the proposed SAU variation (in Schedule 2G, clause 2G.7.1). Instead of using the weighted average remaining lifetime, the BBM divides the real closing RAB by the real depreciation taken from the roll-forward model.[91] The company considers this approach leads to materially different asset lives, estimating Active Plant has a weighted average remaining life of 3.7 years (rather than the 6.38 years in the BBM).[92]

Aussie Broadband submits there are no major issues with the assumptions provided in the BBM regarding depreciation and useful economic lives of asset.[93]

**Financeability test**

NBN Co's SAU variation removed the financeability test as a feature in the BBM.

ACCAN is seeking for the financeability test to be reintroduced to ensure internal consistency with the BBM.[94]

**Transparency**

NBN Co submits that providing the old and new model are sufficient to achieve transparency.

Telstra considers, except for which costs are allocated to core and non-core services, there is sufficient information to meaningfully engage on key aspects of the BBM.[95] The company suggests a working model could be added to the BBM at least for the First Regulatory Cycle to show how the Forecast Nominal Annual Building Block Revenue Requirement (ABBRR) satisfies the NPV=0 expectation.[96] It observes Asset lives are not included in the SAU, so that there is scope in future to change them if it becomes clear that they are unreasonable.[97]

Optus notes the ACCC will need to play a significant role in overseeing NBN Co's BBM (due to the confidential nature of the material).[98]

**Other issues**

Telstra is seeking for the remediation credit to be recognised in the BBM as payment to NBN Co in each year of each regulatory cycle.[99]

Aussie Broadband is concerned that the end goal from the BBM will be greatly impacted if NBN Co does not achieve its connected premises goal.[100]

---

[89] ACCAN, Submission, February 2023, p. 18.

[90] Telstra, Submission, February 2023, p. 43.

[91] Telstra, Submission, February 2023, p. 43.

[92] Telstra, Submission, February 2023, p. 43.

[93] Aussie Broadband, Submission, February 2023, p. 3.

[94] ACCAN, Submission, February 2023, p. 17.

[95] Telstra, Submission, February 2023, p. 43.

[96] Telstra, Submission, February 2023, p. 40.

[97] Telstra, Submission, February 2023, p. 43.

[98] Optus, Submission, February 2023, p. 24.

[99] Telstra, Submission, February 2023, p. 44.

[100] Aussie Broadband, Submission, February 2023, p. 3.

**NBN Co supplementary submission**

NBN Co has provided a supplementary submission to the ACCC responding to the concerns raised by Telstra about its weighted average remaining lives approach.[101] After considering Telstra's submission it confirmed that its calculation of remaining asset lives for the first regulatory cycle is consistent with the definition of the remaining weighted asset lives in the SAU Variation. It has provided a memo from Frontier Economics which provides worked examples and identifies where this approach has been applied in other regulatory decisions. Frontier Economics notes *"the BBM calculates a remaining life for each asset class by dividing the real closing RAB of each asset class by the sum of annual depreciation in each asset class."*[102]

Frontier Economics points out that the assumptions made in Telstra's calculations assumed a standard asset life of 7 years, which is *"not correct"*.[103] Assets that were included in the Active Plant class did not have a standard asset life of 7 years prior to the 2024 financial year.

### 4.6.3. ACCC assessment

We consider the elements proposed by NBN Co in Schedule 2G.5 of the SAU variation for the preparation of building block model proposals in the subsequent regulatory period are reasonable and would promote the LTIE.

However, for the reasons that follow, if NBN Co were to submit a revised SAU variation, we encourage NBN Co to consider its approach to weighted average asset lives and the treatment of third-party funding and government grants.

**Weighted average asset lives**

We are satisfied that NBN Co's supplementary submission addresses Telstra's concerns.

We note the weighted average asset life is weighted by the depreciation of individual assets within each asset class. This has been clarified in Frontier Economics' note which is referenced in NBN Co's letter. We note this approach has been used in other regulatory decisions, such as by the Australian Energy Regulator for SA Power Networks.[104] However, we note that the proposed approach in the supporting information submitted by NBN Co departs with respect to the treatment of asset classes with respect to regulatory cycles subsequent to the first regulatory cycle

In the context of SA Power Networks, the remaining asset lives has been set in the model for 2009-10 for each of the asset classes. These asset lives remain locked in and treated separately from assets added to the RAB post 2009-10. These asset classes are treated separately and depreciated to a life of zero. SA Power Networks has not modified or amended these assets in future years. This provides certainty to access seekers, which enables efficient investment.

In these circumstances, if NBN Co were to submit a revised SAU variation proposal, we encourage NBN Co to consider including provision in Schedule 2G which defines separate asset classes for assets commissioned prior to the 2024 financial year and those commissioned from that time.

---

[101] NBN Co, Supplementary submission, 24 March 2023, p. 10.

[102] Frontier Economics, nbn's depreciation approach for Module 2, 13 March 2023, p. 3.

[103] Frontier Economics, nbn's depreciation approach for Module 2, 13 March 2023, p. 4.

[104] AER, SA Power Networks - Determination 2020-25 – Attachment 4 – Regulatory depreciation, Accessed 24 March 2023.

In addition, if NBN Co were to submit a revised SAU variation proposal, we would welcome any refinements to the explanatory material around the BBM to improve transparency around the issues identified in submissions. These could include:

- explicitly stating the use of depreciation weights in either the SAU or BBM handbook
- providing numerical examples demonstrating how remaining asset lives are calculated
- providing information on the remaining asset lives in the SAU, and/or
- any other refinements suggested in the submissions.

We propose to engage with NBN Co to explore any opportunities and mechanisms to improve transparency.

**Third-party funding and government grants**

If NBN Co were to submit a revised SAU variation, we would encourage it to include in Schedule 2G a provision to recognise third-party funding (including Telstra's remediation credits) and government grants. This could ensure NBN Co does not over recover costs associated with delivering core services within the SAU.

**Asset lives for the first regulatory cycle**

Our view the treatment of asset lives in the BBM is consistent with the definition contained in clauses 2.G.5.5 (RAB roll forward), 2.G.7.1 (Nominal taxation) of the SAU.

We observe the weighted average remaining lives for each of the asset classes in the first regulatory cycle, from examining the supporting BBM provided by NBN Co, may indirectly include the technical lives of NBN Co assets. The asset classes combine individual assets which have had asset lives previously informed by the tax asset lives. In considering the appropriate asset life, it is important to consider a range of factors including the technical life. For example, the Australian Tax Office notes the effective life of the asset can consider:

- whether the asset is subject to wear and tear at a reasonable rate
- whether the asset is maintained in reasonably good order and condition
- the period within which the asset is likely to be scrapped, sold for no more than scrap value or abandoned.

## 4.7. Expenditure review and criteria

**Key points**

- We consider that the expenditure review process and assessment criteria proposed in the SAU variation for the second and subsequent regulatory cycles in the subsequent regulatory period are reasonable and would promote the LTIE, subject to the comments below.
- We note that the SAU variation partly responds to various concerns raised by stakeholders concerning this aspect of the March 2022 SAU variation. This response includes committing NBN Co to stakeholder consultation prior submitting a replacement module application; narrowing the categories of expenditure that do not require assessment for prudency and efficiency; and streamlining the expenditure objectives and factors. We consider these changes would allow transparency and promote the prudency and efficiency of NBN Co's proposed expenditures, and have assisted us to conclude the expenditure review process

and assessment criteria proposed in the SAU variation are reasonable and would promote the LTIE.

- However, key areas of ongoing stakeholder concern relate to weak obligations on NBN Co to adequately justify proposed expenditures and the opportunity for stakeholders and the ACCC to properly scrutinise and assess such expenditures.
- We note that NBN Co has indicated that should it submit a revised SAU variation proposal it would be willing to confer an additional power on the ACCC to specify the information and documents that NBN Co must provide, together with a replacement module application, to support the assessment of its application. This additional power could provide more assurance that expenditure assessments could be conducted in an efficient and timely manner. However, we encourage NBN Co to craft this new power so that the ACCC has power to require NBN Co to prepare, maintain and share with stakeholders and the ACCC the types of information that would be typically required by regulators for expenditure review processes.
- We consider that NBN Co will need to quickly adapt its decision-making frameworks and information systems as part of implementing the SAU variation. Commitments on information NBN Co would provide to support the ACCC in future expenditure reviews and consultation processes would assist in providing assurance these changes would be made.

### 4.7.1. Overview of SAU variation

The SAU variation includes a number of requirements that, if accepted, would govern the way in which NBN Co's proposed and actual operating and capital expenditures would be determined and recovered from customers of its 'core regulated services' over time.

In relation to the Subsequent Regulatory Period commencing 1 July 2023 (other than the first regulatory cycle of that period), these requirements are set out in Module 2 of the SAU Variation. They would apply, in varying ways, to NBN Co's replacement module applications and the ACCC's replacement module determinations, to NBN Co's expenditures on government-directed projects, to forecasts of its operating and capital expenditures (opex and capex, respectively), as well as to the scope for NBN Co's core services revenue to be adjusted during a regulatory cycle in response to changes in its costs (known as cost pass-through provisions).

In relation to the Post-2032 Regulatory Period, a less prescriptive set of requirements are set out in Module 3 of the SAU Variation. These are discussed in section 4.2. The ACCC's assessment of NBN Co's proposed expenditure forecasts for the first regulatory cycle (1 July 2023 to 30 June 2026) are discussed in section 4.8.

Some aspects of the provisions of NBN Co's proposed SAU variation concerning the expenditure review process and assessment criteria for the second and subsequent regulatory cycles of the subsequent regulatory period reflect changes made in response to feedback provided by stakeholders on the March 2022 SAU variation proposal. In particular:

- **Stakeholder consultation requirement** – Clause 5.7 of the SAU variation introduces a new obligation for NBN Co to consult with access seekers and consumer advocacy groups prior to submission of a replacement module application for a regulatory cycle on the relevant capex and opex that NBN Co proposes to undertake in that regulatory cycle.
- **Deemed prudency of government-directed investment** – Clause 5.9 and Schedule 2G of the SAU variation would effectively deem actual capex incurred and opex forecast to be incurred pursuant to a government policy project notice as 'prudent'. However,

compared to the March 2022 SAU variation proposal, the current SAU variation provides that such deeming will only occur to the extent that those expenditures are incurred in a manner that implements the details of the project or program specified in the notice. Expenditures attributable to service capabilities that go beyond the specified details will not be deemed to be prudent.

- **Definition of 'Regulatory Requirement'** – Attachment C (Dictionary) of Module 0 of the SAU variation narrows the definition of the term "Regulatory Requirement" that was proposed in the March 2022 variation proposal. This narrowing has implications for the scope of permitted opex and capex, as well as the scope of permitted cost pass-through applications (see below).
- **Demand forecasts** – Clause 2G.2.5(b) of the SAU variation now obliges NBN Co to ensure that the demand forecasts upon which its opex and capex forecasts are based are developed using an appropriate forecasting methodology, on reasonable assumptions about key demand drivers, using the best available information, and taking into account current demand and economic conditions. These obligations were all introduced subsequent to the March 2022 SAU variation proposal.
- **Expenditure Objectives and Factors** – Compared to the March 2023 SAU variation proposal, clause 2G.2.5(c) of the SAU variation streamlines both the set of objectives ("Expenditure Objectives") towards which its opex and capex should be directed, as well as the factors ("Expenditure Factors") to which it must have regard when making those forecasts. One of the key additions to the Expenditure Factors since the March 2022 SAU variation proposal is a new reference to expected end-user willingness to pay (as opposed to simply end-user demand) for NBN Co's products and services.

Relatively modest changes were made to the following provisions from the March SAU proposal:

- **Ex post review of capex** – Clause 2G.5.10 of the SAU variation requires the ACCC to review NBN Co's actual capex for prudency and efficiency prior to the end of a regulatory cycle. The ACCC could include a lesser amount of capex in the opening value of NBN Co's RAB for the subsequent cycle than the actual capex NBN Co incurred if the ACCC determined the lesser amount is that which would have been (or would be) incurred prudently and efficiently by NBN Co based on the information and analysis that could reasonably have been considered at the time. In this respect, the key change since the March 2022 SAU variation proposal is a clarification that such a timing restriction on the information and analysis to be taken into account by the ACCC would not apply to future capex likely to be incurred by NBN Co.
- **Cost pass-throughs** – Clauses 2D.4 to 2D.6 of the SAU variation would enable or oblige NBN Co to seek the pass-through of certain changes in its costs to its regulated revenue and prices during a regulatory cycle. In this respect, the key change since the March SAU proposal is the raising of the threshold cost impact of an event required for triggering a cost pass-through from 0.25% of Core Services ABBRR for a financial year to 1%.

### 4.7.2. Submissions

Stakeholder submissions on the expenditure criteria were largely focussed on the theme of minimising the risk that end users will be forced to pay for NBN Co expenditures above prudent and efficient levels. Stakeholder concerns broadly arose from their concerns regarding the risk of a new Regulatory Module Application incorporating NBN Co's forecast expenditures coming into effect without proper assessment.

The key outstanding concerns raised by stakeholders in relation to the expenditure criteria in the SAU variation were:

- A lack of stakeholder engagement, information provision and justification supporting NBN Co's expenditure forecasts for the First Regulatory Cycle (FY24-26) (during which the Expenditure Factors do not apply), leading to inadequate scrutiny of NBN Co's first period expenditures (see section 4.8 below);[105] and
- Weak obligations on NBN Co to justify proposed capex and opex, included in its replacement module applications for the second and subsequent regulatory cycles of the subsequent regulatory period, especially for major planned capex projects. Stakeholders submitted that NBN Co should be required to prepare and publish business cases to enable proper ACCC and stakeholder scrutiny and consultation.[106] Project justification should include the objectives of the proposed expenditure, the incremental costs and benefits, the identity of beneficiaries, NBN Co's prudency and efficiency rationale, and the need for greater accountability of funding expenditures approved under SAU process.[107] Business cases should be provided for capital expenditure over a certain amount and protections are needed against NBN Co disaggregating capital expenditure into smaller categories to avoid providing business cases.[108]
- In response, NBN Co submitted that it will be incentivised to put forward business cases or cost/benefit analysis with an appropriate level of detail to justify its proposed expenditure for an upcoming regulatory cycle, noting it is not necessary or appropriate to require the production (or prescribe the form) of such analysis.[109]

### 4.7.3. ACCC assessment

We consider the expenditure criteria and assessment arrangements for the subsequent regulatory period (other than the first regulatory cycle) included in the proposed SAU are improved compared to the March 2022 Variation and are reasonable and would promote the LTIE, subject to the comments below.

Stakeholders have raised concerns about the adequacy of NBN Co's justification of proposed expenditures and the opportunity for stakeholders and the ACCC to properly scrutinise and assess such expenditures. In particular, there has been a lack of an extensive stakeholder engagement and consultation process on forecast expenditure leading up to NBN Co's lodgement of the SAU variation. We consider that could be addressed by a clear requirement in the SAU specifying what type of information NBN Co is expected to supply as part of the RMA/D process in relation to both stakeholder consultation and ACCC assessment. This should include business case information in support of significant proposed expenditures.

We engaged Grex Consulting (Grex) to provide independent expert advice in relation to the SAU variation. We sought advice firstly on NBN Co's proposed expenditure forecast in relation to the first regulatory period, which is discussed later in this report (see section 4.8).

We also sought advice on arrangements that could be implemented as part of the SAU variation to support the ACCC in assessing the prudency and efficiency of NBN Co's expenditures. For instance, we sought advice on the type and format of information NBN Co

---

[105] ACCAN Submission, February 2023, pp.20-21. Telstra Submission, February 2023, pp.24-25.

[106] ACCAN Submission, February 2023, p.20. Aussie Broadband Submission, February 2023, p.4. Telstra Submission, February 2023, pp.24-25.

[107] Telstra Submission, February 2023, pp.27, 46.

[108] ACCAN Submission, February 2023, p.21.

[109] NBN Co submission, p. 26.

should keep, maintain, and supply, assurance measures and the design of processes for collecting this information.

In response, Grex has made draft findings concerning the information and processes that NBN Co currently uses to develop expenditure proposals and track actual expenditures and realised benefits. These include:

- a formal business analysis, reporting and monitoring process was not developed in connection with the expenditures proposed for the First Regulatory cycle. In this regard, NBN Co documents link expenditures to relevant initiatives and activities but do not link clearly to other information relevant to the process of prudent and efficient expenditure assessment.

- multiple individual (mutually exclusive) reports exist for internal purposes that contain some pertinent and useful data and information (particularly for reporting on capital expenditure progress). However, there do not appear to be clear mechanisms in place for an external party such as the ACCC to track changes and developments from the previous years, and/or to inform the ACCC of any significant changes to existing or future initiatives.
- there does not appear to be a documented process that requires detailed business cases be prepared to establish why the expenditure item was the best option (to support an assessment of prudent expenditure as that which reflects the best course of action, considering available alternatives), and a consistent, tangible, documented process to enable the ACCC to assess that each item of expenditure results in the lowest cost to consumers over the long term (to support an assessment of the efficiency of expenditure, with for example, targeted benefits tracked over time in a consistent way project by project and initiative by initiative).[110]

We consider that addressing these draft findings could have significant implications for the efficiency of NBN markets over the remaining term of the SAU.

Accordingly, a key consideration in assessing the SAU variation is whether its acceptance would likely lead to appropriate systems and processes that encourage efficient and prudent expenditure decisions, and safeguard against consumers facing higher costs due to inappropriate expenditures entering the regulatory cost base.

We note that the SAU variation would commit NBN Co to consult with its customers and consumer advocates when developing its replacement module applications, which would include its expenditure proposals for future regulatory cycles.[111] We consider this can materially assist NBN Co in developing its proposed expenditures so that it can better target the needs of its customers. We note that the effectiveness of this consultation would depend upon the preparation of suitably detailed external facing explanatory material for the significant expenditure programs and expenditure categories.

However, we note that the SAU variation does not confer a clear power on the ACCC to specify the materials that need to accompany a replacement module application. As discussed previously, NBN Co has indicated it would be prepared to propose changes to confer such a power should it submit a further SAU variation for consideration. We note that the materials so specified could also be used to guide pre-lodgement consultation.

We note that this is the first time NBN Co has been involved in a regulatory ex ante expenditure review process, which focuses on the efficiency and prudency of its proposed expenditure. The information limitations that have arisen during the review of this first

[110] Grex Consulting, draft report, Part C, p.107.

[111] See Clause 5.7 of the SAU variation

expenditure proposal are potentially a result of NBN Co's existing systems and processes not being designed with such a review process in mind.

In this regard, NBN Co has multiple information systems which appear to be piecemeal in nature, and so would not be well suited for regulatory purposes. Hence, we consider that NBN Co will need to adapt these systems ahead of any future expenditure assessment.

We note that in its draft report, Grex has outlined the type of materials that should accompany an expenditure proposal, which would include the presentation of consistent business case material for all significant expenditures amongst other things. This documentation would identify the funding requirement, as well as the anticipated benefits and the associated risks, and discuss alternative courses of action that had been considered and the reasons for selecting the recommended option.[112]

Grex has also made a draft recommendation that NBN Co should further develop a consistent, tangible, documented process for its expenditure decisions that would enable the ACCC to assess whether the expenditure proposal would result in the lowest cost to consumers over the long term commensurate with the anticipated benefits. This would include keeping records that track not only expenditures but also the benefits and risks/mitigations applied and refinements in approach as contingencies arise.[113]

We also note that in its draft report, Grex has outlined an information and reporting framework to better enable tracking of the delivery of expenditure programs, which includes the following elements:

- 'Annual review template' which would build upon existing information and reporting systems to provide an overall view of significant expenditures and expenditure categories, including additional metrics and further levels of detail where required
- 'Benefit framework' which would accompany the Annual Review Template to assess individual initiatives for their impact and viability, and would provide a view of projected spend with direct and indirect benefits in absolute terms, as well as against the original forecast
- 'Mechanism for change' which would provide a periodic update on any material changes to proposed expenditures during the regulatory cycle, with significant changes notified within a suitable period following the relevant governance body's approval.

Implementing recommendations of this nature would in our view lead to a renewed focus on prudency and efficiency considerations as and when capital is committed, as well as facilitating future expenditure assessments that the ACCC undertakes.

We consider that the SAU variation as currently proposed could provide a strong impetus on NBN Co to implement each of the type of initiatives that Grex identifies in its draft report. That said, we would engage closely with NBN Co to understand its intentions and to assist it making any necessary changes as soon as practicable.

We consider that if NBN Co were to confer an additional power in any revised SAU variation proposal regarding specification of supporting materials to accompany a replacement module application, that would indirectly provide further assurance that these recommendations would be adopted. We note that the ACCC could potentially issue record keeping rules should further assurance be needed.

---

112 We note that in its draft report, the independent expert recommends that NBN Co develop business cases for expenditure items proposed, working with ACCC to develop a pre-agreed framework for the business case, including any practicable templates. See Part D of the Independent expert draft report at p.13

113 See Part C of the Grex draft report at p.107.

We note that the NBN Co has stated in its letter to the ACCC that it may submit a revised SAU variation that provides the ACCC with a power to request and publish (subject to confidentiality considerations) relevant information required for undertaking future expenditure reviews in the context of the replacement module process.

We consider that such a power would be helpful in addressing residual stakeholder concerns. However, it will be important that NBN Co frames the proposed new power in a way that satisfies us that it would be obliged in the future to prepare, maintain and provide the information and documents that would be typically required by regulators for such processes, so that the ACCC would be enabled to effectively conduct future assessments. For instance, properly framed, this power would give assurance that NBN Co would prepare specified categories of documentation (such as business cases for its material investments and operations).

## 4.8. Forecast expenditure for FY24-26

**Key points**

- NBN Co has not yet provided sufficient information to demonstrate the efficiency and prudency of the proposed expenditure for the first regulatory cycle that would be typically required in a regulatory process.
- Our independent expert (Grex Consulting) will take into account any further information made available by NBN Co in finalising its report.
- While we are unable to reach a conclusive view at this stage about the prudency and efficiency of NBN Co's proposed expenditures in the first regulatory cycle, we do not consider they are likely to have any material bearing on our assessment of the proposed SAU variation against the statutory criteria for acceptance of that variation.

This section discusses the ACCC's assessment of the expenditure forecasts for the first regulatory cycle (1 July 2023 to 30 June 2026) specified in Module 4 of the proposed SAU variation. The rules in the proposed SAU variation governing expenditure proposals by NBN Co and expenditure reviews by the ACCC in the course of the replacement module process for the other regulatory cycles of the subsequent regulatory period are discussed in section 4.7. The requirements for the replacement module process for the post 2032 period are primarily set out in Module 3 of the proposed SAU variation and are discussed in section 4.2.

### 4.8.1. Overview of SAU variation

An element of the SAU variation is the proposed settings for the first regulatory cycle, including its length (FY24-26), expenditure forecasts, other building block model (BBM) parameters and service levels.

Module 4 of the SAU sets out the BBM parameters for the first regulatory cycle, including forecast real and nominal capital and operating expenditure. These forecasts feed into the calculation of the Annual Building Block Revenue Requirement (ABBRR) and rolling forward of the Regulatory Asset Base (RAB) for the first regulatory cycle.

NBN Co provided materials in support of its expenditure forecasts as part of the SAU variation.[114] NBN Co's supporting submission discusses its overall approach and forecast methodology for the proposed expenditure. In particular, NBN Co has based its expenditure forecasts on the Integrated Operational Plan (IOP) that underpins its FY23 Corporate Plan.

[114] NBN Co SAU Variation supporting submission (efficiency of NBN Co's expenditure and demand forecasts), November 2022.

NBN Co noted that the IOP expenditure forecasts are appropriate for use within the SAU's BBM because they account for the progressive transition from building to upgrading and operating the NBN and include only prudent costs, which also factor in future efficiency gains.[115] NBN Co's supporting submission also includes the actual expenditures for FY21-22 and the forecast expenditures for FY23 (which are not part of the first regulatory cycle's settings).

NBN Co has forecast its capital and operating expenditure in the first regulatory cycle to be $13,551 million in real terms (FY14 price level[116]) across its 'core' and 'competitive' services, with the majority of the costs being allocated to 'core' services.[117] Total capital and operating expenditures are forecast to reach $7,016 million and $6,535 million in real terms (FY14 price level) respectively.[118] Table 1 in Annexure F presents NBN Co's annual actual and forecast expenditure in the period of FY24-26.

NBN Co's capital expenditure (capex) is summarised into 5 key categories (see Table 2 in Annexure F), which relate to the purpose of the expenditure.

NBN Co noted that a key focus over first regulatory cycle is the progression and completion of the following 5 major initiatives, which are expected to deliver increased network capability to meet growing end-user demand, better quality of service, and ongoing efficiency gains:

- Network Upgrade Initiative.
- Fixed Wireless Upgrade Program.
- SMB (Small and Medium-sized Businesses) Enablement.
- Regional Co-Investment.
- Enterprise Simplicity.

NBN Co noted that average capex for the first regulatory cycle is forecast to be 9.3 per cent lower in real terms than average capex between FY21 and FY23.[119] In particular, following a significant increase in FY23, which is primarily driven by the FTTN to FTTP Network Upgrade and the Fixed Wireless Upgrade initiative, capital expenditure will decrease over the First Regulatory Cycle.[120]

NBN Co's operating expenditure (opex) is summarised into 6 categories (see Table 3 in Annexure F). Over the first regulatory cycle, operating expenditure is forecast to decrease annually, driven by material reductions in costs across a number of areas.[121]

NBN Co noted that the level and nature of opex activities has not yet reached a steady-state level due to ongoing efficiency initiatives and therefore the detailed activity-by-activity forecasting approach in the IOP process provides more accurate forecasts of required opex than other approaches such as top-down methods.[122]

### 4.8.2. Stakeholder submissions

---

[115] NBN Co SAU Variation supporting submission (efficiency of NBN Co's expenditure and demand forecasts), November 2022., p. 30.

[116] NBN Co's real values in the SAU are expressed at FY14 price level.

[117] NBN Co also provided a breakdown between the two service categories.

[118] NBN Co's supporting submission presents expenditure figures in real terms (as at June 2021).

[119] NBN Co SAU Variation supporting submission (efficiency of NBN Co's expenditure and demand forecasts), November 2022., p. 40.

[120] Grex Consulting, draft report, Part C, p. 16.

[121] Grex Consulting, draft report, Part C, p. 16.

[122] NBN Co SAU Variation supporting submission (efficiency of NBN Co's expenditure and demand forecasts), November 2022., p. 51-52.

Some stakeholders have raised concerns that NBN Co has not provided sufficient information to demonstrate the efficiency of the proposed expenditure for the first regulatory cycle.

ACCAN noted that:[123]

> *There is no commitment that NBN Co will provide explanation as to why it's spending certain amounts regarding its capital and operational expenditure. This limits the ability of Consumer Advocacy Groups to critically examine expenditure proposals. Whilst NBN Co provides some of this detail in the Appendix of Part F of their supporting submission for the first regulatory cycle, the level of detail is not sufficient compared to other essential service sectors.*

Telstra expressed similar views:[124]

> *There has been no exposure to NBN Co's business case or economic analysis to justify its FTTP investment as efficient and prudent. Therefore, it is not possible to determine the efficiency or otherwise of NBN's proposed FTTP spend. Yet it is used as a key justification for raising wholesale prices. Until there is greater transparency of this spend, the benefits, and the efficiency of it, there cannot be confidence that the proposed SAU variation will promote the LTIE.*

We also received submissions on the quantum of the proposed expenditure. In relation to capex, Telstra noted that NBN Co has incorporated strong productivity improvements in its non-FTTP spend, but raised concerns about the proposed increases in FTTP capex. Telstra noted that this results in a capex cost of approximately $1800 per premise ready to connect, which is higher than the NZ Chorus total cost per premise of AU$1500 for FTTP connections.[125] Telstra also considered that NBN Co's efficient nominal opex should decline by 2-3 per cent per annum from FY23, noting that NBN Co's productivity improvements should not be outweighed by upward pressure from inflation.[126]

### 4.8.3. ACCC assessment

We are considering the appropriateness of the expenditure proposal for the first regulatory cycle as part of the overall assessment of the SAU variation. This is because the expenditure proposal for this cycle, along with other BBM parameters, are specified as part of the SAU variation.[127]

**Independent expert review and draft report**

To assist our consideration of NBN Co's expenditure forecasts for the first regulatory cycle, we engaged Grex Consulting (Grex) to provide an independent expert opinion on the appropriateness of the proposed expenditure. Grex has also been asked to provide advice on what arrangements would be required for ongoing monitoring and reporting and future SAU replacement module processes.

Grex has to date attended presentations given by NBN Co, reviewed pre-existing NBN Co documents relating to the processes that it undertook for its FY23 IOP and has assessed further information and documents provided by NBN Co during the review. NBN Co supplied

[123] ACCAN submission, p. 20.

[124] Telstra submission p. 25.

[125] Telstra submission, p. 25.

[126] Telstra submission, p. 24.

[127] See Module 4 of the SAU variation

documents and information in various tranches. [128] The most recent tranche was received on 26 April 2023.

The independent expert's review remains ongoing, with the expert providing a draft report to assist us in preparing this draft decision. In its draft report, Grex includes draft findings based on its review of all information and documentation that had been provided to it by 28 March 2023. That is, Grex will review the additional tranches of information and documents provided after that time in finalising its opinions and advice.

We have released a copy of the draft report of the independent expert along with this draft decision for transparency. We note that the text of the draft report is reasonably complete save for a small number of redactions that NBN Co has requested on confidentiality grounds.

In the draft report, Grex includes its current views on the prudency and efficiency of all material expenditures that form part of the expenditure proposal for the first regulatory cycle. These expenditures are classified into specific capital investments, special work programs and initiatives, or business as usual expenditure categories. Grex has rated the prudency and efficiency of each based on current information reviewed, ranging from expressing a view that the expenditure is or is not prudent, either in absolute or qualified terms. Items for which necessary information was not yet available were rated as inconclusive.

Grex will finalise its report prior to the ACCC's Final Decision in respect of the SAU variation. This will include updating the prudency and efficiency ratings in light of additional information. We will consider the opinions and advice contained in the report in preparing the Final Decision.

**Appropriateness of the proposed expenditures**

Grex has found that some proposed expenditure items for the first regulatory cycle are prudent and efficient based on current information. In some cases, Grex has also found that the expenditure item is not relevant to the review as the expenditure would be allocated to competitive services and so be ringfenced from the pricing of core regulated services under the SAU variation.

However, most of the expenditures by dollar value and number receive only qualified ratings. This includes the most significant capital investment programs being the FTTN to FTTP Network Upgrade and FTTN/C to P Connect programs. These programs account for around 31 and 13 per cent of the total capital expenditure in the first regulatory cycle respectively.[129]

Further, a small number of the expenditure items receive an inconclusive rating in the Grex's draft report. This includes the fixed wireless network upgrade, which accounts for around 10 per cent of the total capital expenditure in the first regulatory cycle.[130]

At this time, we are unable to express a view on the appropriateness of the proposed expenditures for the first regulatory cycle given the qualified or inconclusive opinions that Grex has been able to reach based on the information that was available to it at the time of

[128] On 31 January 2023, the ACCC issued a formal request for information to NBN Co under section 152CBH(2) of the CCA seeking information to be provided by 14 February 2023.

[129] These capital investment programs are intended to enable around 3.5 million premises in the FTTN network footprint, and around 1.5 million premises in the FTTC network footprint, to access FTTP services. These are discussed in Part F of NBN Co's SAU Supporting Submission at Appendix A, section 2.5 – Capability; and at Part C of the independent expert's draft report at p. 65.

[130] This capital investment program aims to enable the supply of higher speed wholesale offers over the fixed wireless network, e.g., of 100/20 and 250/20 Mbps, and indirectly improve satellite end-user experience by allowing 120,000 satellite end users to connect to the fixed wireless network This program is discussed at Part F of NBN Co's SAU Supporting Submission at Appendix A, section 2.5 – Capability; and at Part C of the independent expert's draft report at p.72.

finalising its draft report. Hence, we will revisit this issue for the purpose of our Final Decision, by which time the Grex will have assessed further information including the information tranches that NBN Co recently supplied.

We note that the expenditure proposal for the first regulatory cycle brings reduced risk of inefficient pricing as compared to the expenditure proposals that would be provided in respect of subsequent regulatory cycles were the SAU variation to be accepted.

In this regard, the proposed expenditure for the first regulatory cycle is unlikely to have material pricing impacts. We note that, until NBN Co reaches a point of annual cost recovery, its maximum prices will be linked to inflation rather than depend on changes in its underlying cost base. NBN Co has forecast that in the short to medium term, it is unlikely to fully recover the forecast BBM costs.[131] This is materially different from a typical regulatory reset process (including the resets that would apply to NBN Co once it reaches the point of annual cost recovery) where proposed expenditure will be a key driver for prices in that regulatory cycle and beyond.

In addition, under the proposed SAU variation, NBN Co will likely bear most of the risk for any inefficient expenditure. This is because any unrecovered annual capital expense (depreciation) or operating expenditures will not be carried over to future periods. In addition, the ACCC will have the power to undertake ex-post reviews of capital expenditure which will mitigate the risk of inefficient capex being rolled into the RAB for future recovery.

We also note that actual expenditures incurred in the first regulatory cycle alone might not provide a suitable basis to assess for expenditure proposals that are submitted for future regulatory cycles. This is because NBN Co will still be transitioning over the first regulatory cycle to an operating model that focuses primarily on maintaining and running the network, as opposed to undertaking significant network build. Further, should Grex reach final opinions that some of the proposed expenditures for the first regulatory cycle appear not to be efficient or prudent then this would further diminish the reliability of those expenditure amounts as a reliable benchmark for future expenditure proposals.

While we are unable to reach a conclusive view at this stage about the prudency and efficiency of NBN Co's proposed expenditures in the first regulatory period, we do not consider they are likely to have any material bearing on our assessment of the proposed SAU variation against the statutory criteria for acceptance of that variation.

## 4.9. Cost allocation and accounting separation

**Key points**

- Robust cost allocation and accounting separation measures would encourage more efficient use of NBN Co's regulated services and discourage anti-competitive practices in wholesale markets
- We consider that the cost allocation principles that have been proposed in the SAU variation for the subsequent regulatory period are reasonable and would promote the LTIE, and that the SAU variation specifies a suitable framework by which to develop the cost allocation manual and implement accounting separation measures. This framework includes an approval and oversight role for the ACCC

131 NBN Co's forecast aggregate revenue in the first regulatory period is around 27 per cent lower than its forecast aggregate costs. Further forecast in NBN Co's building block model indicates that it will only begin to fully recovery its costs from around FY30.

- We note that SAU variation would allow for NBN Co to implement the cost allocation and accounting separation measures over the first regulatory cycle, and that this work would commence with the lodgement of a draft cost allocation manual within 30 days of the SAU variation being accepted.

### 4.9.1. Overview of SAU variation

**Cost allocation principles**

The SAU variation sets out the following cost allocation principles that NBN Co will follow to allocate costs between its core and non-core services:

- "costs that are directly attributable to a Core Regulated Service will be allocated to that Core Regulated Service;
- costs that are directly attributable to a Competitive Service will be allocated to that Competitive Service
- shared costs (i.e., costs that are not directly attributable to a Core Regulated Service or Competitive Service) will be allocated to reflect causal relationships between supplying services and incurring costs, unless establishing a causal relationship would require undue cost or effort, in which case an alternative suitable allocator will be used
- all costs will be allocated, and
- no cost should be allocated more than once to any service."[132]

Services supplied by NBN Co in competitive markets are categorised as non-core services, while all other services supplied by NBN Co are initially categorised as core services.[133]

**Cost base and categorisation of core and non-core services**

Under the SAU variation, NBN Co has categorised enterprise ethernet, business satellite and satellite mobility services as non-cores services (unless and until the ACCC subsequently re-categorises them as core services under the SAU). All other services, including all services supplied to residential premises, are initially categorised as core services.

Under the SAU variation, NBN Co will establish separate cost bases for core and non-core services using cost allocations. This provides for the ABBRR, RAB and ICRA to be allocated between the two categories of services.[134] The BBM calculates a Core Services RAB Portion, Core Services ABBRR, and Core Services ICRA, as well as a competitive RAB portion, a competitive ABBRR and a competitive ICRA allocation. The allocation between Core Regulated Services and Competitive Services includes further breakdowns of ABBRR elements including Core Regulated and Competitive capex, depreciation, opex and asset disposals, and a revised tax calculation.[135]

Core services are subject to the SAU's regulatory requirements including maximum regulated prices, price controls, benchmark service standards and product withdrawal restrictions. NBN Co can set prices and other terms for non-core services outside of the SAU framework.

---

132 NBN Co, SAU variation, Module 2, Schedule 2G.6.2.

133 NBN Co, SAU variation, Module 2, Schedule 2G.

134 NBN Co, SAU variation, Module 2, Schedule 2G, Part A & Part B.

135 NBN Co, FY09-FY23 Building Block Model handbook, p.4.

The categorisation of services between core and non-core services and allocation of costs to these services for the subsequent regulatory period will be determined before the start of each regulatory cycle through the replacement module process for that period.[136] As part of that process, NBN Co may propose that a product or service be re-categorised as a core or non-core service.[137] In doing so, NBN Co must propose the ABBRR, RAB and ICRA values that account for the proposed re-categorisation, in accordance with the cost allocation principles and the cost allocation manual.[138] The ACCC will have the power to re-categorise a product or service as a non-core or core service through a determination under the replacement module process for the subsequent regulatory period.[139]

### Cost allocation manual

The SAU variation requires NBN Co to submit to the ACCC, within 30 days of the variation being accepted, a proposed cost allocation manual.[140] This manual describes the methodology NBN Co will use to allocate costs between core and non-core services.[141] The ACCC has the power to approve a proposed cost allocation manual in either the form it is submitted or a form that incorporates reasonable changes made by the ACCC.[142] The ACCC can, at any time after the SAU variation is accepted, direct NBN Co to submit a revised cost allocation manual to the ACCC.[143]

NBN Co's March 2022 SAU variation proposal did not include a role for the ACCC to formally consider and approve a cost allocation manual or initiate changes to it.

### Accounting separation record keeping, reporting and assurance

The SAU variation requires NBN Co to establish and maintain consolidated and separate accounts for core and non-core services.[144]

NBN Co will also be required to establish an accounting separation record keeping, reporting and assurance framework under the SAU. The SAU variation requires NBN Co to submit to the ACCC, by 31 March 2024, a document setting out the procedures and methodology for establishing and maintaining consolidated and separate accounts for key products and services supplied under the SAU, and associated reporting and external assurance arrangements.[145] The ACCC may direct NBN Co to propose changes to the accounting procedures for approval or amendment by the ACCC.[146]

NBN Co's March 2022 SAU variation proposal did not include an accounting separation record keeping, assurance and reporting framework.

---

136 NBN Co, SAU variation, Module 2, Schedule 2G.6.4(c) to (f). Alternatively, pursuant to clause 2G.6.4(b), if NBN Co proposes to introduce a new product or service or vary an existing one, and that product or service, if so introduced or varied, would fall within the scope of a product or service that has already been categorised, then the relevant product or service will be categorised in the same way as the existing one.

137 NBN Co, SAU variation, Module 2, Schedule 2G.6.4(c).

138 NBN Co, SAU variation, Module 2, Schedule 2G.6.4(c) and (d).

139 NBN Co, SAU variation, Module 2, Schedule 2G.6.4(e) and (f).

140 NBN Co submitted a public version of an initial (not yet approved) cost allocation manual with its SAU variation proposal.

141 NBN Co, SAU variation, Module 2, Schedule 2G.6.3.

142 Pursuant to Module 2, Schedule 2G.6.3(c), if the ACCC does not notify NBN Co of its decision in 3 months (or such longer period for notification of the ACCC's decision as a result of the ACCC extending time), the applicable cost allocation manual will be the proposed manual submitted by NBN Co.

143 NBN Co, SAU variation, Module 2, Schedule 2G.6.3(e).

144 NBN Co, SAU variation, Module 2, Schedule 2I.6.3 & 2I.6.4.

145 NBN Co, SAU variation, Module 2, Schedule 2I.6.

146 NBN Co, SAU variation, Module 2, Schedule 2I.6.5.

### 4.9.2. Submissions

The key theme in submissions regarding cost allocation and accounting separation was the extent to which the proposed arrangements would mitigate the risk of NBN Co inappropriately cross subsidising its non-core (i.e., competitive) services from its core services.

A number of submitters were concerned that NBN Co could potentially have an unfair advantage over other network providers operating in competitive markets (e.g., business service markets). That is, were NBN Co to shift the costs of providing its services in competitive markets to its core services thereby reducing its commercial risk of operating in these markets.[147] Submitters considered that such an outcome would be detrimental to investment by other network providers in competitive markets, the degree of competition and consumer interests in the long term.

Although submitters did not claim that NBN Co was currently (or previously) cross subsidising the cost of supplying its non-core services from its core services, submitters emphasised the need for appropriate safeguards to address this potential risk through a cost allocation framework. This would encompass accepted cost allocation principles and a transparent cost allocation manual supported by ongoing assurance and monitoring arrangements to ensure costs are being allocated appropriately.

Several concerns were raised by submitters regarding the initial cost allocation manual NBN Co submitted with its SAU variation proposal.[148] Submitters considered that the manual lodged by NBN Co had insufficient detail such that the proposed approach to allocation of costs across core and non-core services lacked transparency.[149] Submitters considered this could provide NBN Co with the opportunity to shift costs from non-core to core services, noting in particular the risk of inappropriate allocation of capital and operational costs shared across these services. Among other issues, submitters questioned the proposed approach to allocation of operational costs between core and non-core services.[150] The approach proposed is based on the respective proportions of revenue received from core and non-core services and does not incorporate allocators based on causal relationships between the supply of services and related costs incurred.

Overall, submitters considered that further consultation with stakeholders on NBN Co’s cost allocation manual is required.[151] NBN Co’s submission recognised this noting that it has provided an initial cost allocation manual to enable RSPs to provide feedback and that the manual is subject to change.[152]

Several submitters queried whether recovery of the ICRA would be allocated across core and non-core services and considered that the allocation should be based on the cost allocation framework.[153]

Submitters did not raise concerns about the cost allocation principles proposed in the SAU variation or its obligations for NBN Co to establish and maintain consolidated and separate core and non-core services accounts and to develop associated reporting to the ACCC and external assurance arrangements.

---

147 Telstra submission p.28. TPG submission p.16. Optus submission pp. 24-25. Aussie Broadband submission p.4.

148 Telstra submission p.29. Optus submission p.45. Commpete submission pp. 7-8. ACCAN submission p.26.

149 Telstra submission p.28 & p.47. Optus submission pp. 24-25.

150 Optus submission p.45. Commpete submission pp.7-8. ACCAN submission p.26.

151 Optus submission p45. ACCAN submission p.26.

152 NBN Co submission p.36.

153 Telstra submission p.29 & p.47. Optus submission p.46. ACCAN submission p.6 & p.25.

### 4.9.3. ACCC assessment

Appropriate allocation of costs between NBN Co's core and non-core services is important to ensure access seekers are not paying inefficiently high prices for core regulated services and NBN Co cannot obtain an unfair competitive advantage though cross subsidy from its core services when supplying non-core services. In that context the cost allocation framework is a key component for safeguarding against the risks from any unfair cost advantage NBN Co may have in the supply of competitive services. Appropriate cost allocation is an important check for whether core regulated services are recovering only efficient costs, including costs justifiably shared across core and non-core services, and are not funding losses incurred in competitive markets.

Correct implementation of appropriate cost allocation principles through a cost allocation manual, accounting separation and record keeping, external assurance and regulatory reporting arrangements, are critical to guarding against these risks and the potentially harmful outcomes for efficiency and competition. Also, a robust cost allocation framework is an important deterrent against anti-competitive conduct and can inform compliance initiatives if such conduct arises.[154]

We consider that the proposed cost allocation principles for the subsequent regulatory period in the SAU variation provide a sound basis for the cost allocation framework set out in the variation and are reasonable and would promote the LTIE. Also, we consider that the overall framework proposed for the subsequent regulatory period, to separately cost and categorise core and non-core services in the building block model, and the obligations on NBN Co to establish and maintain consolidated and separate accounts for core and non-core services, will enable transparent cost allocation if implemented correctly and is reasonable and would promote the LTIE.

Regarding the issue of whether recovery of the ICRA will be allocated across NBN Co's core and non-core services, we note that the BBM calculates a core services ICRA and a competitive ICRA allocation, as described in NBN Co's FY09-FY23 Building Block Model handbook.[155]

Several concerns were raised by submitters regarding the initial cost allocation manual NBN Co submitted with its SAU variation proposal. We agree there is significant scope for improvements to the cost allocation manual submitted. Based on our initial assessment, the manual's level of detail and the transparency of the proposed approach, the proposed method for allocation of operational costs, and the rationale for cost allocators proposed, require consideration by NBN Co and further stakeholder consultation. We note that submitters raised several other issues for NBN Co to consider regarding the initial manual submitted.

As set out above, the SAU variation requires NBN Co to submit to the ACCC, within 30 days of the variation being accepted, a proposed cost allocation manual. The ACCC has three months to consider the manual (and can extend this timeframe) and the power to approve it in either the form it is submitted or a form that incorporates reasonable changes.

Subject to our acceptance of the SAU variation, we will consult stakeholders when NBN Co submits its cost allocation manual for our consideration and assess the proposed manual separately at that time. We intend to also seek external expert advice to assist our consideration of whether the cost allocation manual submitted is fit for purpose or whether further changes are required.

---

154 Part XIB of the CCA includes a range of compliance measures available to the ACCC to address anti-competitive conduct in the telecommunications industry.

155 NBN Co, FY09-FY23 Building Block Model handbook, p.4.

The SAU variation requires NBN Co to submit to the ACCC a document setting out the procedures and methodology for establishing and maintaining consolidated and separate accounts and associated reporting to the ACCC and external assurance arrangements.[156] NBN Co must consult with the ACCC in developing the proposed accounting procedures and the ACCC can direct NBN Co to incorporate reasonable changes. Further, we note that the ACCC can at any time after it determines the approved accounting procedures, direct NBN Co to submit changes to the procedures including changes to account for matters which the ACCC considers warrant a change.[157]

In the circumstances outlined above, we consider that the cost allocation framework proposed under the SAU variation for the subsequent regulatory period provides a good foundation for ongoing regulatory oversight and monitoring by the ACCC of NBN Co's implementation of cost allocation and accounting separation arrangements and is reasonable and would promote the LTIE. We note that we can make changes to these arrangements as circumstances change and where issues arise, given the ACCC's ongoing oversight of the cost allocation manual and accounting separation in the subsequent regulatory period.

## 4.10. Weighted average cost of capital

**Key points**

- We consider that the principles proposed for the weighted average cost of capital (WACC) give sufficient flexibility for the ACCC in making its replacement module applications. Although the ACCC would need to have regard to the principles specified under the SAU variation, the proposed principles do not preclude the ACCC from having regard to other factors or preclude the ACCC from making decisions consistent with factors including the LTIE. The ACCC would therefore have sufficient flexibility in assessing the WACC in future regulatory cycles.
- The proposed WACC values for the first regulatory cycle are unlikely to have any substantial impact on outcomes for both the first regulatory cycle or future regulatory cycles in the SAU period. On this basis, we consider the proposed WACC values for the first regulatory cycle are reasonable and would promote the LTIE.
- If NBN Co submits a revised SAU variation proposal, it would be desirable that it update the WACC values to reflect the more current information now available.

### 4.10.1. Overview of SAU variation

Schedule 2G.2.4(d) of the SAU variation sets out a requirement, for the subsequent regulatory period, to use a nominal vanilla WACC commensurate with the efficient financing costs of a benchmark efficient entity with a similar degree of risk as that which applies to NBN Co in providing the NBN Access Service, Ancillary Services and Facilities Access Service, having regard to:

A. The objective of producing reliable estimates of the market cost of capital in a wide range of plausible market conditions;

B. The objective of promoting stability in the rate of return over time; and

C. Calculated in accordance with the following formula:

[156] NBN Co, SAU variation, Module 2, Schedule 2I.6.

[157] NBN Co, SAU variation, Module 2, Schedule 2I.6.5.

$$R_t^{nominal} = Re \times (1-G) + Rd_t \times G$$

Where:

> $R_t^{nominal}$ is the nominal rate of return for each Financial Year (t) of the Regulatory Cycle;
>
> $Re$ is the expected return on equity for the Regulatory Cycle;
>
> $Rd_t$ is the expected return on debt for each Financial Year (t) of the Regulatory Cycle; and
>
> $G$ is the benchmark proportion of debt in total financing (i.e. the benchmark gearing ratio) for the Regulatory Cycle.

Schedule 3B.3.2 sets out a requirement as above, excluding the specification of the formula, to be applied in the post 2032 period. Schedule 2G.7.4 of the SAU variation sets out the overall approach to gamma for the subsequent regulatory period.

Schedule 4B proposes values for each element of the nominal vanilla WACC and for gamma, to be used for each year of the first regulatory cycle (2023-24, 2024-25 and 2025-26). Frontier's report[158] indicates that NBN would update these values closer to the commencement of the regulatory cycle to reflect the latest available data relating to risk free rates, market risk premiums, inflation forecasts and the cost of debt.

### 4.10.2. Submissions

We received submissions from stakeholders on the following:

- *Inclusion of objectives other than LTIE* – Telstra questioned why objectives (the set out in cl 2G.2.4(d) and outlined above) other than LTIE are specified in the SAU variation, while ACCAN noted that promoting stability in the rate of return over time does not necessarily work towards achieving an efficient WACC (although it sees merit in reducing volatility and price shocks). [159] [160]
- *Proposed WACC values* – Telstra submitted that the proposed WACC values have very little impact in the first regulatory cycle and that the benchmark WACC for the first regulatory cycle is overstated, though likely only to be relevant to the second regulatory cycle. They support the ACCC having the power to determine the WACC methodology and values for the second and subsequent regulatory cycles, without regard to the WACC values specified in the SAU variation for the first regulatory cycle (or the methodology used by NBN Co to calculate them).161
- *Proposed sample of benchmark firms* – Telstra submitted that NBN Co's position in the Australian telecommunications market is In fundamentally different to most telecommunications companies overseas and that these differences affect the systematic risks faced by investors. It was submitted that while a benchmark approach to the WACC is broadly appropriate, much care must be given to what the right benchmarks are. Although it is unlikely to have an effect in the first regulatory cycle, it will be important that no precedent is taken from the first regulatory cycle that

158 Frontier Economics Return on capital and inflation. 7 December 2022, pp 7, 8, 53.

159 Telstra Submission in relation to NBN's proposed SAU variation. Public version. 17 February 2023, p 48.

160 ACCAN Submission to ACCC consultation paper. February 2023, p 26.

161 Telstra Submission in relation to NBN's proposed SAU variation. Public version. 17 February 2023, p 48.

constrains a thorough analysis of an appropriate WACC for the second regulatory cycle. 162

NBN Co's submission[163] to the ACCC consultation paper noted sections of its supporting submission and reports by Frontier and CEG. On its proposed WACC values and proposed sample of benchmark firms NBN Co submits that:

> *As observed by the ACCC in its Consultation Paper, the WACC for the First Regulatory Cycle is unlikely to have a material impact on nbn's prices because, for the duration of that cycle, the WAPC will be capped at CPI rather than being subject to the outputs of the BBM.*[164]

### 4.10.3. ACCC assessment

Under the replacement module process (see section 4.1.1) NBN Co would submit a replacement module application ahead of each regulatory cycle; and then the ACCC would make a replacement module determination. A replacement module determination may adopt NBN Co's application in whole, or in part, or specify alternatives in accordance with the requirements of the SAU. Replacement module determinations provide an opportunity for the ACCC to determine the WACC values for a regulatory cycle by reference to the WACC methodology (including the sample of benchmark firms in future) of its choice, subject to the requirements of the SAU.

One of the requirements under the SAU variation is that the ACCC must have regard to the objectives prescribed in cl 2G.2.4(d). NBN Co has noted that the ACCC may make a determination on the rate of return that is not consistent with these objectives, as long as it has had regard to them when making its decision.[165] In this regard, the SAU Variation would not preclude the ACCC from having regard to the other mandatory factors when making regulatory module determinations and giving a weighting that it considers appropriate to each or act to impede the ACCC developing a WACC methodology that would promote the LTIE.

The WACC for the first regulatory cycle is unlikely to have a material impact on prices due to the likelihood that NBN Co will not be recovering its ABBRR over this regulatory cycle and any revenue shortfalls relative to the ABBRR will not be carried forward for future recovery. In other words, the WACC values specified in the SAU variation for the first regulatory cycle will not lead to any substantive impact on pricing, either for the first regulatory cycle or later regulatory cycles in the SAU period. For these reasons, we are satisfied that the provisions of the SAU variation specifying WACC values for the first regulatory cycle and governing the determination of WACC values for the subsequent regulatory cycles of the SAU term are reasonable.

In future regulatory cycles it will be important for the ACCC to closely consider NBN Co's WACC proposals through the replacement module process to ensure the proposals reflect the practices of a benchmark efficient firm and will promote efficient outcomes. This will be particularly important for regulatory cycles after NBN Co has reached the point of cost recovery, when the WACC will have a direct impact on prices. We will look closely at all aspects of NBN Co's proposals, including the appropriate sample of comparison firms used to determine benchmark parameters. In this regard, we note that NBN Co has developed a broad based sample for the First Regulatory Period which appears to include some firms

---

162 Telstra Submission in relation to NBN's proposed SAU variation. Public version. 17 February 2023, p 48.

163 NBN Co Submission to ACCC consultation paper. February 2023, p 37.

164 NBN Co Submission to ACCC consultation paper. February 2023, p 37.

165 24 March 2023 Letter from NBN Co to ACCC; NBN Co Response to issues raised in ACCC Consultation Paper on the variation to nbn's Special Access Undertaking (SAU), page 9.

that would be a poor proxy for NBN Co, while potentially omitting others that may be suitable for inclusion.

However, updating the WACC values for the first regulatory cycle specified in Module 4 of the SAU variation closer to the commencement of the regulatory cycle so as to reflect more current information, as foreshadowed by Frontier's report, would be desirable, if NBN Co elects to submit a revised SAU variation. We note that this would require further changes to module 4 of the SAU variation, which could be implemented through a revised SAU variation proposal, should NBN Co decide to do so.

## 4.11. Provisions for incorporating other access technologies

**Key points**

- We consider that in principle the SAU should be extended to cover services supplied over additional access technologies, as proposed in the SAU variation, and the we are satisfied that the provisions incorporating the further access technologies are reasonable and would promote the LTIE.
- We consider that the proposed service specifications relating to the additional access technologies are reasonable and would promote the LTIE.
- We note that NBN Co commits in the SAU variation to maintaining the network connection device that it supplies for installation on the end-customer side of the network boundary, with the result that we are satisfied of the reasonableness of the boundary point proposed for the fibre to the curb service.

### 4.11.1. Overview of SAU variation

The current SAU only covers the FTTP, fixed wireless and satellite networks. This means that the multi-technology mix (MTM) is not covered. The MTM consists of the FTTN, FTTB, FTTC and HFC networks, which together equal almost 75% of services in operation.

The SAU variation would include new service descriptions in the SAU for each of the new connection types. These descriptions have been developed through WBA negotiations. The proposed SAU variation lists the network boundary points for each service type. It adds terms for each service's installation,[166] implementation[167] and regulatory needs.[168] Additionally, the variation includes appropriate terms and performance objectives for the co-existence period.[169] The co-existence period refers to when FTTB/N/C connections coexist with ADSL services and other non-fibre services.

We sought views on whether the terms that would be added by the proposed SAU variation to incorporate the MTM technologies into the SAU are reasonable and would promote the LTIE. In particular, we sought views on whether the network boundary points for each technology are reasonable and would promote the LTIE. The network boundary point is an important consideration as it is the point where NBN Co's responsibility for the network ends and the customer's responsibility begins.

---

166 NBN Co, SAU variation, Module 1, Schedule 1C and Annexures 3, 4, 5 and 6.

167 NBN Co, SAU variation, Module 1, Schedule 1A.

168 NBN Co, SAU variation, Main Body, Attachment C.

169 NBN Co, SAU variation, Main Body, Attachment C; Module 4, Attachment I and Module 1, Schedule 1A.4.

### 4.11.2. Submissions

Many stakeholders did not remark specifically on the inclusion of the MTM in the SAU. However, Telstra noted issues with the subsequent installation terms for the FTTB/N/C technologies.[170]

ACCAN submitted that NBN Co should change the network boundary point for some FTTC services, to include the Network Connection Device.[171] This is because the proposed FTTC boundary appears to leave the NCD and a portion of the wiring that connects it to the NBN and provides power to the FTTC network outside of NBN Co's responsibility. ACCAN added that the varied SAU should empower NBN Co to repair the wiring when this would promote public safety.[172] NBN Co submitted that the responsibility for the maintenance of the NCD sits within the service boundary outlined within the SAU and therefore remains a responsibility of NBN Co as part of its extended service boundary.[173]

### 4.11.3. ACCC assessment

We support incorporating the MTM into the SAU as we consider that this would give greater certainty to access seekers and end-users and consides that the proposed SAU variation in this respect is reasonable and would promote the LTIE. This is in the long-term interests of end-users and provides regulatory certainty to NBN Co's residential services. This is because there will now be a single regulatory framework under the SAU, reduced complexity and a minimised scope for different network technologies being subject to different regulatory treatments. We consider the new service descriptions for the MTM technologies are appropriate, reasonable and provide clear definitions.

We consider that further changing the network boundary for FTTC services is not necessary. This is because NBN Co has committed in the proposed SAU variation to maintain the NCD. This commitment arises from the definition of 'access component reactivation' and other operative terms of the SAU. [174]

## 4.12. Service quality

**Key points**

- The SAU variation includes benchmark wholesale service standards for the first regulatory cycle and a framework by which the benchmark service standards could be updated at specified times or in specified circumstances during the SAU term.
- We are satisfied that the framework for setting and reviewing benchmark service standards during the subsequent regulatory period, including the mid-cycle review processes, are generally reasonable and would promote the LTIE except in relation to the first regulatory cycle.
- We are concerned that certain aspects of the proposed benchmark standards for the first regulatory cycle would likely be superseded by the time the SAU variation would come into effect or shortly thereafter.

170 Telstra, *Submission in relation to NBN's proposed SAU variation,* 17 February 2023, p.52

171 ACCAN, *Submission to ACCC Consultation Paper*, 17th February 2023, p. 27.

172 ACCAN, *Submission to ACCC Consultation Paper*, 17th February 2023, p. 27.

173 NBN Co, *SAU supporting submission Part C: Non-price terms*, November 2022, p.8.

174 NBN Co, SAU variation, Main Body, Attachment E, table 8.1; see together with Attachment C (under the definitions of 'Access Component', 'Access Component Reactivation' and 'UNI)' and Schedule 1 clause 1A.3.1(a) and (b)(v).

- We note that reasonable and targeted investments in NBN Co's networks, products, and systems could enable material improvements to the benchmark service standards over the first regulatory cycle, including improvements that address issues that drive negative sentiment regarding NBN services.
- We are not satisfied that the framework for improving service standards over the first regulatory cycle would be effective during the first regulatory cycle as NBN did not consult with stakeholders in preparing the proposed benchmark service standards as it would do for future regulatory cycles, and there is no commitment in the SAU variation for NBN Co to consult with stakeholders about measures that could be applied to efficiently address known causes of poor quality.
- Accordingly, we are not satisfied that the benchmark service standards for the first regulatory cycle specified in the SAU variation, or the framework for changing benchmark service standards over the first regulatory cycle are reasonable or would promote the LTIE.
- We consider that this could potentially be addressed by changes to the SAU variation to include:
    - a commitment to update the benchmark service standards proximate to any acceptance of the SAU variation and to inform the ACCC and other stakeholders whether the updated benchmark services standards will be part of a future cost pass-through application.
    - a commitment to periodically consult stakeholders over the measures that NBN Co should prioritise over the first regulatory cycle, and update the benchmark service standards to incorporate improvements that are identified in this way. We note that NBN Co would consult stakeholders on these matters ahead of making regulatory module applications to apply in subsequent regulatory cycles should the SAU variation be accepted.
- We note that NBN Co has recently indicated that it would be willing to make potential changes in any revised SAU variation in relation to additional consultation and reporting. With further development, including these additional commitments in a revised SAU variation, this initiative could result in a reasonable set of service quality commitments for the subsequent regulatory period.
- We are satisfied that the framework for regulating NBN Co's service level commitments in the post 2032 period is reasonable and would promote the LTIE.

### 4.12.1. Overview of SAU variation

The SAU variation proposal includes benchmark service standards for the first regulatory cycle and incorporates a framework for specifying benchmark service standards for subsequent regulatory cycles of the subsequent regulatory period.[175] NBN Co must meet or exceed these benchmark service standards when supplying services to RSPs.[176]

Benchmark service standards for the first regulatory cycle are specified in the SAU variation and include most WBA4 service levels, and associated performance objectives and rebates.[177]

The SAU variation confers a power on the ACCC to specify benchmark services standards in a replacement module determination made in respect of other regulatory cycles in the

175 NBN Co, SAU variation, Main Body, clause 5.2(e)(iv).

176 NBN Co, SAU variation, Main Body, clause 5.6.

177 NBN Co, SAU variation, Module 4, Attachment I.

subsequent regulatory period and in the post-2032 period.[178] The SAU variation also allows for a review of benchmark service standards during a regulatory cycle in certain circumstances.[179] That is, the ACCC may initiate a review of benchmark service standards if a systemic service standard event occurs or if a change to retail service standard regulation is made or varied during a regulatory cycle.

NBN Co must include a service standard proposal as part of its replacement module applications during the subsequent regulatory period and consult stakeholders ahead of lodging these applications.[180] Under the arrangements that would apply from 2032, the ACCC would have greater flexibility over how it regulates service quality issues. From that time NBN Co would have the option of including proposed benchmark service standards in a replacement module application but would be under no obligation to do so unless requested by the ACCC.

### 4.12.2. Submissions

There was support from RSPs for the inclusion of benchmark service standards for each regulatory cycle. NBN Co considered that commercially agreed service standards, with ACCC powers to set additional or alternate service standards, should provide the market with confidence that service level commitments would reflect performance expectations.[181]

Other stakeholders expressed concerns about potential suboptimal outcomes for consumers and potential weaknesses in both the benchmarks service standards for the first regulatory cycle and the framework for setting and reviewing benchmark service standards for the balance of the SAU term. These concerns related to the framework for consultation with stakeholders; the mid-cycle review process; and specificity on how service quality is treated in Module 3. Stakeholders sought immediate improvements on certain benchmark service standards and stronger incentives for NBN Co to deliver on service quality commitments.

#### Regulatory framework for setting and reviewing benchmark service standards

ACCAN considered the mid-regulatory cycle review processes in Module 2 would ensure sufficient flexibility during a regulatory cycle of the subsequent regulatory period to respond to unforeseen events. However, ACCAN was unsure if the ACCC could initiate a mid-regulatory cycle review of benchmark service standards post-2032 and recommended that the SAU be amended to clarify that it could.[182]

Telstra and Optus viewed the mid-regulatory cycle review process as too narrow and considered that it may result in poor consumer outcomes and poor ACCC decision-making. They both submitted that the definition for a systemic service standard event that triggers an ACCC initiated review of benchmark service standards should refer to the impact on end-users and not just access seekers. Aussie Broadband considered that regulatory oversight should be flexible to respond to unforeseen events.[183]

Optus was also concerned about the complexity in the provisions and the number of qualifications regarding the ACCC's discretion, noting that restricting ACCC decision-making was unlikely to support decisions that promote efficient investment in the NBN.[184] Optus

---

178 NBN Co, SAU variation, Main Body, clauses 5.2(f)(iv) and 5.10(b)(iv).

179 NBN Co, SAU variation, Module 2, Schedule 2I.2.

180 NBN Co, *Submission to ACCC consultation paper*, 17 February 2023, p. 23.

181 NBN Co, *Submission to ACCC consultation paper*, 17 February 2023, p. 23.

182 ACCAN, *Submission to ACCC consultation paper*, 17 February 2023, p. 28.

183 Aussie Broadband, *Submission in response to ACCC consultation paper*, 17 February 2023, p.4.

184 Optus, *Submission in response to ACCC consultation pape*r, 23 February 2023, p. 47.

considered that the ACCC should have the ability to stop the clock for all outstanding requests for information to support the LTIE objectives.[185]

Telstra submitted that benchmark service standards should be dependent on a high level of consultation and transparency.[186] NBN Co was of the view that proposed safeguards in the SAU variation provided flexibility to respond to unforeseen events during a regulatory cycle of the subsequent regulatory period.[187]

Telstra and Vocus considered that further changes to the SAU variation would need to be made in respect of the benchmark service standards, and the incentives to deliver them and ongoing improvements.[188] NBN Co submitted that including service standards would provide certainty for each regulatory cycle and a meaningful price/quality link that would be subject to regular review.[189]

### Benchmark service standards in the first regulatory cycle

NBN Co submitted that the purpose of including benchmark service standards in the SAU was to establish a price-quality link to ensure that there is not an incentive to reduce service standards to increase margins.[190]

However, several RSPs and ACCAN described the proposed benchmark service standards for the first regulatory cycle as backward-looking, noting that the benchmark service standards did not address known issues for end-users.[191] XIntegration considered that a justification for increased cost to consumers would be providing a better quality service.[192] Telstra and Commpete were concerned that negotiations for WBA4 service standards occurred two years ago, and that basing benchmarks on those negotiations is not reflective of any improvements that may have occurred in the interim.[193] In their view it is reasonable to expect substantial improvements in NBN Co's service standards over the first regulatory cycle. RSPs and other stakeholders raised concerns about dropouts, outage notifications and speed assurance. Optus described the benchmark service standards as not capable of being accepted by the ACCC.[194]

Mr Bebbington raised concerns in relation to satellite services. He noted that there are no proposed speed upgrades from those established over 10 years ago and data limits have not grown with demand. Mr Bebbington also commented that there are only poor or non-existent service standards with no improvement planned.[195]

ACCAN commented that poor service outcomes are a driver of lower consumer expenditure on NBN services, with end-users being reluctant to spend on higher-speed tiers due to

---

185 Optus, *Submission in response to ACCC consultation pape*r, 23 February 2023, pp.38-39.

186 Telstra, *Submission in relation to NBN's proposed SAU variation*, 17 February 2023, p. 49.

187 NBN Co, *Submission to ACCC consultation paper*, 17 February 2023, p. 22.

188 Telstra, *Submission in relation to NBN's proposed SAU variation,* 17 February 2023, p.7; Vocus, *Response to ACCC consultation paper*, February 2023, p.8

189 NBN Co, *Submission to ACCC Consultation Paper*, 17 February 2023, p. 23.

190 NBN Co, *Submission to ACCC consultation paper*, 17 February 2023, p. 23.

191 Vocus, *Response to ACCC consultation paper*, February 2023, p.8; Telstra, *Submission in relation to NBN's proposed SAU variation*, 17 February 2023, p. 8; Optus, *Submission in response to ACCC consultation pape*r, 23 February 2023, pp.31-32; ACCAN, *Submission to ACCC consultation paper*, 17 February 2023, p. 28.

192 XIntegration, *Submission in response to ACCC consultation paper*, 17 February 2023, p.4

193 Commpete, *Submission in response to the revised proposed variation to the NBN Co SAU*, 17 February 2023, p.8; Telstra, *Submission in relation to NBN's proposed SAU variation*, 17 February 2023, p. 8.

194 ACCAN, *Submission to ACCC consultation paper*, 17 February 2023, pp.28-30; Optus, *Submission in response to ACCC consultation pape*r, 23 February 2023, p.28; Telstra, *Submission in relation to NBN's proposed SAU variation,* 17 February 2023, p.8

195 Mr Bebbington, *Submission re NBN proposed SAU,* 19 February 2023, p.9.

underperformance.[196] ACCAN proposed penalties (in the form of a write-down of the ICRA) where NBN Co fails to meet its benchmark service standards.[197]

NBN Co's submission acknowledged RSPs' advocacy for enhanced service standards (relative to WBA4). NBN Co submitted that enhanced service level commitments should be assessed with regard to their impact on its ability to upgrade and maintain the network. NBN Co considered it important that higher service standards are not introduced for access technologies that are to be upgraded. That is, if enhanced service level commitments were to divert capital expenditure more efficiently spent on upgrading the network or would have a negative impact on NBN Co's ability to maintain the network.[198]

### 4.12.3. NBN Co's potential revised SAU variation proposal

In its supplementary submission, NBN Co outlined potential changes to the SAU variation that it would be willing to make, that could respond to concerns expressed by stakeholders in their submissions. The first of these would be to bolster the mechanism by which benchmark service standards could be improved during a regulatory cycle to make clear that a recurring event that impacts end-users can trigger such a review, rather than only those that impact retailers.

The second potential change would be to implement a new transparency and reporting mechanism over how NBN Co would work to uplift service performance over the first regulatory cycle. This would entail NBN Co preparing an annual service improvement plan and reporting on an annual service performance review during that time.

The service improvement plan would summarise NBN Co's key initiatives that underpin its planned expenditures for uplifting customer experience and service performance for the regulatory cycle. As well as describing the initiatives themselves, the plan would detail their intended benefits, provide intended timeframes for their delivery and give details of the capex/opex that had been allocated. The service improvement plan would not be binding on NBN Co in that there would not be direct consequences under the SAU variation for a failure to deliver the improvements that had been outlined. The plan would be updated each year and provided to the ACCC, with a public version made available on NBN Co's website.

The proposed service performance review would be conducted before the end of FY24 and FY25. It would focus on the effectiveness and relevance of the existing service levels as specified in the WBA. At the end of each review, NBN Co would prepare a report in which it would outline performance over the last 12 months, explain material differences between actual and target performance and consider how its service improvement initiatives have contributed to changes in performance. The report would also specify what changes NBN Co is considering for the service standards that are contained in its WBA or the Benchmark Service Standards or to its processes. NBN Co has stated it will consult with retailers in the course of the review and outline any feedback that it receives from them in its report.

### 4.12.4. ACCC assessment

We recognise that service quality has been a contentious issue over an extended period. We consider that incorporating a service quality framework into the SAU would assist in efficiently improving service quality over time. This would also better support commercial resolution of service quality issues given NBN Co's underlying market power. Where however this would not lead to an appropriate resolution, the regulatory mechanisms that are specified in the SAU variation could then be used to do this more directly.

---

196 ACCAN, *Submission to ACCC Consultation Paper*, 17 February 2023, p. 29.

197 ACCAN, *Submission to ACCC Consultation Paper*, 17 February 2023, p. 29.

198 NBN Co, *Submission to ACCC Consultation Paper*, 17 February 2023, p. 21.

During the subsequent regulatory period (i.e., when Module 2 of the SAU applies), the ACCC would have a power to step in at each regulatory reset, or during a regulatory cycle where a systemic issue has arisen. The ACCC would have further discretion over how it regulates service quality during the post 2032 regulatory period.

We are satisfied that the framework for regulating NBN Co's service level commitments in the post 2032 period is reasonable and would promote the LTIE.

We are also satisfied that the framework for setting and reviewing benchmark service standards during the subsequent regulatory period, including the mid-cycle review processes, is reasonable and would promote the LTIE, except in relation to the first regulatory cycle.

We note that the benchmark service standards for the first regulatory cycle were developed prior to the latest round of commercial discussions over the next WBA. We understand that NBN Co has proposed improvements for a small number of service standards as part of those discussions, however it is not clear how these would be incorporated into the benchmark service standards.

We also note that NBN Co has not yet consulted stakeholders over the improvements that it could make to the benchmark service standards during the first regulatory cycle, as it would do for future regulatory cycles should the SAU variation come into effect. We consider that effective consultation is important to ensure efficient use of the NBN and to promote efficient network investment to address key service quality concerns. In this regard, consulting with stakeholders could better allow NBN Co to identify, and where necessary to reprioritise its budgeted expenditures, to implement additional measures that would uplift performance to benefit retailers and their customers. Similarly, further consultation could allow more efficient implementation of these initiatives.

For these reasons, we are not satisfied that the benchmark service standards for the first regulatory cycle specified in the SAU variation, or the framework for setting and reviewing benchmark service standards in the first regulatory cycle, are reasonable or would promote the LTIE.

We also note that NBN Co has indicated that it would be willing to make clearer that the ACCC could step in mid-regulatory cycle to address systemic issues that impact consumers and businesses that use the NBN, even where the issues might not the impact the retailer directly. This potential change to the SAU variation could help address retailer concerns over the intended scope of the mid cycle review mechanism.

We consider that changes to the SAU variation to incorporate into benchmark service standards for the first regulatory cycle those changes to service standards agreed for the next WBA, so they are an up to date reflection of the standards that are being applied in practice, could assist to address concerns in relation to the benchmark service standards specified in the SAU variation for the first regulatory cycle.

We acknowledge that NBN Co is also considering whether to incorporate additional transparency mechanisms into a revised SAU variation proposal should it proceed to submit such a proposal. These mechanisms would apply for the first regulatory cycle and would include NBN Co undertaking some further consultation with stakeholders.

In our view it appears reasonable for such measures to apply during the first regulatory cycle, with the consultation mechanism already proposed in the SAU variation to apply to future regulatory cycles. We also consider that this approach to providing further transparency and consultation to be conceptually sound. We consider this approach will help drive efficient development and delivery of service quality improvements, and it would be more likely that, when combined with existing rebate and rectification obligations and public reporting on service quality pursuant to a record keeping and reporting rule, this approach could result in material quality improvements without resort to other regulatory processes.

That said, we consider it would be important for NBN Co to develop its proposal so that the intended benefits are more likely to be realised. In this regard, the proposed mechanisms for inclusion in a revised SAU variation could make clear that stakeholders would have the opportunity to provide views on the service performance issues that should be prioritised for action and to share their perspectives on how this could be done in a timely and effective way.

It would also appear beneficial for NBN Co to report on the effectiveness of the initiatives it has implemented. This could require specific metrics to be developed for those initiatives where effectiveness could not be clearly demonstrated by reference to more general WBA metrics.

Further, the proposal could benefit from further consideration as to appropriate sequencing so that the views of stakeholders can be promptly considered by the relevant governance committee.

We note that under the SAU variation, cost pass through applications would be limited to service improvement initiatives that cannot be funded from within the expenditure amounts specified for the regulatory cycle. Hence, NBN Co could commit to clarifying with stakeholders which initiatives would be funded from within its budgeted expenditures, such as via a reprioritisation of existing budgets, and which (if any) would likely be subject to a pass-through application.

We note that NBN Co's expenditure proposal for the first regulatory cycle includes significant initiatives that have the potential to uplift service performance over time. For example, NBN Co is proposing to make FTTP connections available in additional areas currently served by copper connections and to offer Fixed Wireless connections to some premises currently serviceable only by satellite. These investments could potentially provide a pathway for a significant proportion of consumers on underperforming copper connections to access more reliable services and for service restrictions on satellite services to be lifted. That said, it will take time to build these networks, and then to migrate the relevant copper and satellite services to the new networks.

We acknowledge that NBN Co has stated that its current financial circumstances limit the scale of investment it can make in addressing service quality issues in the first regulatory cycle. While we accept that this has informed NBN Co's overall approach to the SAU variation, we note that it has still forecast incurring material expenditures that appear directed towards improving its products, systems and processes.

A commitment to meaningful engagement with retailers and stakeholders over the first regulatory cycle as discussed above concerning how this funding is to be prioritised across projects would assist in bringing forward efficient solutions to known and future service quality issues. In addition to better supporting consumers, we consider that successfully resolving issues that cause negative sentiment towards NBN services can also lead to more efficient use of the NBN and efficient cost recovery. This is because it can avoid situations where consumers could be more likely to disconnect or downgrade their service.[199]

---

[199] For instance, NBN Co has offered discounted pricing to attract disconnected households back onto the network.

## 4.13. Reporting

**Key points**

- NBN Co's SAU variation includes performance and operational reporting commitments that largely mirror those set out in WBA4 and monthly and quarterly network utilisation reporting. We consider what is proposed to be reasonable and that this would promote the LTIE.
- Stakeholders are seeking a comprehensive reporting and transparency framework that can adapt to changes in service standards and stakeholder expectations over time. Stakeholders also support implementation of service quality record keeping rules by the ACCC and NBN Co continuing public reporting.
- Separately, we note the ACCC intends to develop a record keeping rule for NBN Co on service levels and encourages NBN Co to continue public reporting and ongoing improvements to operational reporting to RSPs regarding service quality, faults and reliability issues impacting end-users.

### 4.13.1. Overview of SAU variation

Module 4 of the SAU variation sets out NBN Co's proposed reporting commitments for the first regulatory cycle for service quality and network performance. These reporting commitments largely mirror those set out in WBA4. NBN Co has also committed to providing monthly network utilisation reports where certain network resources exceed the proposed new utilisation threshold[200] and quarterly reports where NBN Co undertook to increase available capacity.[201]

NBN Co has submitted that additional operational and process reporting should be addressed through the WBA arrangements, rather than the SAU, given expected ongoing changes to reporting processes and potential delays to such changes if implementation processes are embedded in the SAU.[202]

The November 2022 SAU variation does not include reporting commitments previously included in NBN Co's March 2022 variation proposal, which included provision of 6-monthly reports to the ACCC on network capability, outages and recurring faults. The March 2022 variation also provided for monthly reports on congestion, network availability, and connection and assurance performance to retailers and on its website. NBN Co removed these commitments on the expectation that such service quality metrics would be subject to reporting through an ACCC record keeping rule.[203]

### 4.13.2. Submissions

A key theme from submissions was the need for comprehensive service quality reporting and greater transparency of service quality performance. In addition, there was support for a reporting framework that can adapt to changes in service standards and stakeholder expectations over time.[204]

---

200 NBN Co, SAU variation, Module 4, Attachment I, clause 16.4(a).

201 NBN Co, SAU variation, Module 4, Attachment I, clause 16.4(b).

202 NBN Co, SAU variation, *Supporting submission Part C: Non-Price Terms*, November 2022, p 18 & 19

203 NBN Co, SAU variation, *Supporting submission Part C: Non-Price Terms*, November 2022, p 30

204 Telstra submission p.51, Optus submission p. 48, Aussie Broadband submission p. 5, ACCAN submission p. 30.

Several submitters strongly supported the ACCC's development of a record keeping rule for NBN service quality and network performance. Submissions also supported increased transparency through the publication of this information.[205] Submitters supported NBN Co's voluntary public reporting through its monthly progress reports dashboard. Submitters also supported improvements in NBN Co's operational reporting to RSPs to enable providers to better assist end-users.[206] Telstra submitted that, due to the industry consultation necessary for ongoing operational reporting improvements, these arrangements could be progressed outside of the SAU variation process.[207]

NBN Co's submission recognised the support for a record keeping rule, public reporting and improved operational reporting, and committed to working with the ACCC and RSPs on these issues.[208] NBN Co submitted that it had removed certain network performance metrics from its current SAU variation proposal given its understanding that similar reporting metrics may be included in the ACCC's record keeping rule.[209]

### 4.13.3. ACCC assessment

We are satisfied that the reporting obligations proposed in the SAU variation are reasonable and would promote the LTIE.

We recognise that the SAU variation includes performance and operational reporting that RSPs currently receive under WBA4. We support the additional reporting commitments proposed by NBN Co relating to network utilisation.

We consider that additional reporting obligations are best implemented through WBA consultation and/or record-keeping rules, as they will likely need to be revisited from time to time and these mechanisms provide flexibility to respond to changing circumstances.

In this respect, we consider that future improvements in operational reporting should reflect ongoing WBA consultation between NBN Co and RSPs and can be addressed through this process.

We will also continue its development of a service quality and network performance record keeping rule for NBN Co and intends to improve future public reporting on NBN service levels through these arrangements.[210]

---

[205] Telstra submission p. 51, Aussie Broadband submission p. 5, ACCAN submission p. 30 & 31.

[206] Telstra submission p. 15, Optus submission p. 48, Aussie Broadband submission, p. 5, Launtel submission p. 12.

[207] Telstra submission p. 15.

[208] NBN Co submission p. 24.

[209] NBN Co submission p. 23 & 24.

[210] In December 2022 the ACCC published a consultation paper, and we are currently assessing public submissions.

# 5. Draft assessment of SAU variation

This section provides our current draft assessment of the proposed SAU variation against the statutory framework the ACCC is required to apply when considering proposed variations to a special access undertaking.

This draft assessment relates to all additions and deletions NBN Co has proposed to make to the SAU through the SAU variation considered on a wholistic basis. This assessment complements, and should be read in conjunction with, the draft assessment of key aspects of the SAU variation as discussed in section 4.

The timeframe over which we have undertaken this draft assessment is from 1 July 2023 to 30 June 2040, which is the period over which the proposed SAU variation would apply.

Although the ACCC has identified certain terms of the SAU variation that it considers are reasonable and/or specify conduct that will promote the long-term interests of end-users, the ACCC's current draft decision is to reject the SAU variation. This section focuses on the reasons for the ACCC's draft decision to reject the SAU variation.

The legislative assessment framework that we have applied is set out in full in section 2.5 above and Appendix E. Amongst other things, the ACCC must not accept an SAU variation unless it is satisfied that:

- the stipulated terms and conditions upon which NBN Co would comply with its standard access obligations are (amongst other things) reasonable; and
- the conduct of NBN Co that the SAU variation specifies in relation to access to the service would be in the long-term interests of end-users and the terms and conditions on which NBN Co would engage in that conduct that are specified in the variation are reasonable.

We have considered the proposed variation to the SAU against each of these statutory criteria. Having regard to the matters discussed below, and on the basis of the information currently available to us and the analysis undertaken to date we are not currently satisfied of each of the statutory criteria.

We observe that our assessment of the SAU variation is ongoing and further analysis of the currently available information will be undertaken. Due to temporal constraints, the advice provided to date by our independent experts does not take account of certain recently provided information. This further analysis will be undertaken, together with a consideration of any further information and submissions provided, prior to the making of our final decision.

## 5.1. Long-term interests of end-users

In assessing whether:

- the conduct of NBN Co specified by the proposed SAU variation in relation to access to the service; and
- the terms and conditions on which NBN Co would engage in that conduct or comply with its standard access obligations specified in the variation (for the purpose of assessing their reasonableness)

will promote the LTIE, the ACCC must consider the likely effect they will have on the promotion of competition in relevant markets, the achievement of any-to-any connectivity and the encouragement of the economically efficient use of, and investment in, relevant infrastructure.

**Efficient use of and investment in infrastructure**

We consider that the likely effect of the matters specified in the SAU variation described above on efficient investment and use of infrastructure is that they are more likely to impede efficient use of, and investment in, infrastructure rather than to promote it.

The terms and conditions of the proposed SAU variation on which NBN Co would engage in conduct in relation to access specified in the variation or comply with its standard access obligations provide for mechanisms and principles to govern the making of regulatory module determinations that give rise to a material risk that those determinations will contain terms and conditions of access and specify conduct in relation to access that would impede efficient investment and use of infrastructure or will be precluded from including terms and conditions, and specifying conduct, that would promote efficiency. Specifically:

- The proposed replacement module process creates a material risk that regulated terms will be established for a regulatory cycle that would not promote efficient use of or investment in infrastructure. We are not satisfied the proposed process will ensure the ACCC can make regulatory determinations that will promote efficient use and investment, both in the short term and over the duration of the SAU. We are not satisfied the proposed SAU variation contains sufficient powers for the ACCC to request information as part of the replacement module process to mitigate this risk.
- The proposed credit rating objective principle used to determine annual regulated revenue allowances after 2032 is unlikely to promote efficient use and investment in infrastructure. The proposed objective would create a material risk that higher costs associated with inefficient expenditure or investments are passed on to NBN Co's customers and end-users in the form of higher access prices. This would diminish incentives for NBN Co to pursue efficient investments. Further, these higher prices would lead to inefficient use by end-users. The proposed credit rating objective would also create a material risk of price shocks after 2032. This is likely to create a material degree of cost uncertainty for RSPs and create difficulties for RSPs in developing retail offerings that best meet consumer needs and preferences, which would not be consistent with the efficient use of infrastructure.
- The cost uncertainty for RSPs associated with the 50/20 Mbps product, would likely impact on efficient use and investment in a similar way. We consider more efficient use of the network would be encouraged by NNI charges that do no create a barrier to entry and expansion by smaller retailers, as well as via greater reporting and accountability in relation to low income measures.

**Promoting competition**

We consider that the likely effect of the matters specified in the SAU variation described above on competition is that they are more likely to impede downstream competition rather than to promote it.

This is firstly because the SAU variation proposes mechanisms and principles to govern the making of regulatory module determinations that give rise to a material risk that those determinations will contain terms and conditions of access and specify conduct in relation to access that would impede competition, or conversely will be precluded from including terms and conditions, and specifying conduct, that would promote competition.

In this regard, we consider that

- the proposed mechanism for making regulatory determinations during the subsequent regulatory period could enshrine the terms and conditions that NBN Co proposes in its regulatory module application for the regulatory cycle due to informational limitations or rushed timeframes for decision making. Further, there is a likelihood that the terms and conditions that are proposed in these applications would not reflect sufficient consideration of their possible competition effects.

- the SAU variation would require the ACCC to apply principles when making regulatory module determinations during the post 2032 regulatory period that are likely to result in inefficiently high regulatory allowances and access prices. This would make it more difficult for retail service providers to supply retail services at reasonable prices and would negatively affect competition in the retail market.

We generally accept that most of the arrangements contained in the SAU variation that are intended to allow NBN Co to better align its allowable access revenues with its efficient costs over time would, in and of themselves, be likely to promote competition, provided these arrangements are implemented within an appropriate regulatory framework.

This is because we consider that progressively aligning allowable access revenues with efficient costs will better allow retailers to compete efficiently. We note that these arrangements include safeguards that any price increases for wholesale offers would be spread over time within reasonable annual limits, and pursuant to a set of transparency measures that are intended to give reasonable assurance over the trajectory of future price and cost outcomes for retailers.

That said, we consider that certain of the terms and conditions of access that the SAU variation proposes for the first regulatory cycle are likely to impede competition. These are that:

- the proposed price related terms and conditions of access leave open a very broad range of cost outcomes under the standard wholesale offer (which is the wholesale 50 Mbps offer) that would be difficult for retailers to efficiently manage without suitable assistance and support from NBN Co, which the SAU variation does not commit NBN Co to provide.
- the proposed benchmark service standards are likely to be quickly superseded by changes to its service standards that NBN Co has indicated it intends to implement that go beyond its benchmark service standards offer.
- the SAU variation does not commit NBN Co to consult with retailers about how it could prioritise its investments to resolve current service quality issues and improve the benchmark service standards, noting that NBN Co has not done this for the purpose of developing its SAU variation proposal.

We consider that each of the above matters would likely impede competition over the first regulatory cycle by giving rise to material cost uncertainty, raising supply costs or giving less certainty that service standards will not deteriorate to inefficient levels in future. These in turn are likely to raise barriers to entry and reduce the range of product differentiation possible in the retail market.

**Any-to-any connectivity**

The proposed SAU variation is unlikely to have any material or direct impacts on realising any-to-any connectivity.

## 5.2. The legitimate business interests of NBN Co, and NBN Co's investment in facilities used to supply the services concerned

We consider that the terms and conditions of the proposed SAU variation on which NBN Co would engage in conduct in relation to access specified in the variation or comply with its standard access obligations are not consistent with the legitimate business interests of NBN Co.

The proposed replacement module process will favour NBN Co, as its replacement module applications will be taken to have been accepted if the ACCC has not made a determination within specified timeframes. However, we do not consider provision for the deemed acceptance of a regulatory proposal on a procedural or timing related occurrence, particularly if caused by a lack of provision, or withholding of information by NBN Co, to be a legitimate business interest of NBN Co.

Similarly, the setting of annual regulated revenue allowances after 2032 to meet credit rating objectives does not represent a legitimate business interest. We do not consider setting revenue allowances to meet a credit rating objective notwithstanding price shocks or efficiency outcomes to be a legitimate business interest.

## 5.3. The interests of persons who have the right to use the services concerned

We consider that the terms and conditions of the proposed SAU variation on which NBN Co would engage in conduct in relation to access specified in the variation or comply with its standard access obligations are not consistent with the interests of persons who have the right to use NBN services.

The proposed replacement module process and credit rating objective do not have sufficient regard to the interests of persons who have the right to use NBN Co services, namely NBN Co's customers and end-users. This is because NBN Co's customers and end users face a material risk they could face outcomes including price shocks, inefficient outcomes, prices that are higher than necessary, and the establishment of regulated terms that are not reasonable and/or do not promote the LTIE.

The proposed pricing arrangements for the 50/20 Mbps product will create a material risk of cost uncertainty for retailers. Currently we are concerned that this proposed pricing does not have sufficient regard to the interests of NBN Co's wholesale customers and end users and are not convinced that NBN Co's proposed rectification in the form of enhanced reporting on CVC usage is sufficient to address this.

We consider that the publication by NBN Co of more detailed information for retailers in support of the SAU variation about the operation of the price controls and how the proposed pricing conforms with them during the first regulatory cycle may assist us to conclude that the proposed pricing arrangements for the 50/20 Mbps product are consistent with the interests of persons who have the rights to use the service concerned.

## 5.4. The direct costs of providing access to the services concerned

We consider the terms and conditions of the proposed SAU variation on which NBN Co would engage in conduct in relation to access specified in the variation or comply with its standard access obligation would create a material risk of increases in the direct costs to NBN Co of providing its services due to the scope for inefficient expenditure to be recoverable from RSPs under the proposed arrangements.

Although many elements of the proposed SAU variation are directed at aligning regulated revenues and efficient costs, we are not satisfied these will be sufficient to ensure NBN Co's direct costs are efficient. This is due to risks of inefficient expenditure being accepted under the proposed replacement module process and the proposed credit rating objective operating to require that regulated revenues are set to achieve a certain credit rating regardless of the efficiency of direct costs.

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

The terms and conditions of the proposed SAU variation on which NBN Co would engage in conduct in relation to access specified in the variation or comply with its standard access obligations are unlikely to have a direct or indirect effect that would compromise the safe or reliable operation of the NBN.

## 5.6. The economically efficient operation of a carriage service, telecommunications network or facility.

We consider that the terms and conditions of the proposed SAU variation on which NBN Co would engage in conduct in relation to access specified in the variation or comply with its standard access obligations would be likely to impede the economically efficient operation of the NBN.

Although many elements of the proposed SAU variation are directed at aligning regulated revenues and efficient costs, we are not satisfied these will be sufficient to ensure the economically efficient operation of the NBN. This is due to risks of inefficient operating expenditure being accepted under the proposed replacement module process and the proposed credit rating objective operating to require that regulated revenues are set to achieve a certain credit rating regardless of the efficiency of the operation of the NBN.

# Annexure A: Overview of telecommunications access regime and current NBN Co SAU

## Telecommunications access regime

### *Object of the telecommunications access regime*

Part XIC of the CCA sets out the telecommunications access regime. The object of the telecommunications access regime is to promote the LTIE of carriage services and services provided by means of carriage services.

### *Regulation of access to NBN services*

NBN Co must only supply services that have been declared under Part XIC of the CCA. Services that are, or are capable of being, supplied by NBN Co may become declared services can become declared in the following three ways:

- NBN Co can provide the ACCC with an SAU in relation to a service or proposed service
- NBN Co can publish a standard form of access agreement that relates to access to a service
- the ACCC can declare an NBN service following a public inquiry.

The NBN access service was declared when the current SAU was accepted by the ACCC in December 2013, along with Ancillary Services and, to the extent required for interconnection, the Facilities Access Service.

Declaration of an NBN service is significant as this requires NBN Co to comply with the category B standard access obligations (SAOs) specified in the CCA. These include obligations to supply the declared service if requested by a service provider and to permit interconnection of facilities.

### *Setting regulated terms and conditions of access to NBN services*

While the SAU forms an important part of the regulatory framework for the NBN, the terms and conditions of access and on which NBN Co is required to comply with the category B SAOs may be specified in one or a combination of different instruments. These include:

- access agreements - commercial contracts between the access provider and an access seeker which set out negotiated terms and conditions of supply
- special access undertakings accepted by the ACCC - documents given by the access provider agreeing to be bound by the relevant SAOs and proposing the terms and conditions on which it will offer access to its services
- binding rules of conduct - written rules made by the ACCC where there is an urgent need to make such rules, specifying any or all the terms and conditions for compliance with any or all the SAOs, or requiring compliance with any or all of the SAOs as specified in the rules
- access determinations - written determinations made by the ACCC relating to access to a declared service after conducting a public inquiry, specifying any or all the terms and conditions for compliance with any or all of the SAOs.

Part XIC of the CCA establishes a hierarchy to allow parties to identify which terms and conditions are to apply, particularly in the event of inconsistency between the various instruments that may be in effect.

Essentially, terms and conditions about a particular matter in an instrument that is higher in the above list will prevail over inconsistent terms and conditions about the same matter specified in an instrument that is lower in the list. For instance, commercially negotiated and agreed terms and conditions (set out in an access agreement) between NBN Co and retailers will prevail over regulated terms in a varied SAU, binding rules of conduct and access determinations that are made by the ACCC, to the extent of any inconsistency between these terms. In other words, a varied SAU, binding rule of conduct and an access determination would have no effect to the extent of any inconsistency with the access agreement.

The ACCC assessment of the SAU variation is important in the context of the legislative hierarchy. Once the ACCC accepts a variation proposal, there is no provision under Part XIC of the CCA for the ACCC to vary or set aside the terms of the resulting SAU. Any binding rules of conduct or access determination made by the ACCC in respect of access to the NBN and compliance by NBN Co with the Category B SAOs will have no effect to the extent of any inconsistency with the SAU as varied for so long as the SAU remains in effect.

Part XIC also provides for NBN Co to formulate and publish standing offers, known as a standard form of access agreement. A standard form access agreement is not itself an access agreement and does not form part of the Part XIC legislative hierarchy. Rather, retailers can request NBN Co to enter into an access agreement on the terms of a standard form access agreement. WBA4 is the current standard form access agreement. NBN Co has entered into access agreements based on it.

For completeness, other forms of regulation can potentially affect the terms of access to an NBN service. The Statutory Infrastructure Provider (SIP) regime established by Part 19 of the *Telecommunications Act 1997* commenced on 1 July 2020. Under that regime, the Minister may determine minimum service standards, benchmarks, and performance standards for nominated SIPs. NBN Co has been designated as the default SIP.

The terms contained in any such SIP instrument would prevail over all other terms in the regulatory hierarchy, including terms in commercially negotiated access agreements from the time that those agreements are next varied or new agreements entered. While no such SIP instrument has yet been made, a consultation draft proposed setting a baseline that would not limit a SIP from offering better service standards.

## NBN Co's current SAU

NBN Co's current SAU was accepted by the ACCC in December 2013. The SAU sets out principles for the regulation of wholesale access to the NBN until June 2040. It was intended to act as the overarching regulatory framework through which NBN Co would supply its services to telecommunications companies, including wholesale and retailers. The SAU was varied in April 2021 to extend the application of three non-price provisions,[211] which were originally set to expire after 5 years.

The current SAU contains regulated terms for wholesale access to NBN Co services. It only applies to FTTP, fixed wireless and satellite services, which are the technologies that were included in the initial NBN rollout. As such, MTM services are not covered by the current SAU. The SAU specifies price and non-price terms and conditions for Layer 2 bitstream services provided by NBN Co. These terms and conditions offer a baseline for commercially negotiated access agreements.

[211] NBN Co's SAU variation and the ACCC final decision on the variation are available on the ACCC website.

The SAU has a modular structure which ‘locks in’ matters for different periods of time. This structure provides a degree of flexibility, allowing for some changes to the regulatory settings over the term of the SAU. The current SAU contains three modules numbered from 0 to 2.

Module 0 applies for the whole term of the SAU and provides the overarching structure and context for the SAU. Specifically, Module 0 describes the services the SAU covers and establishes the requirements to publish and maintain standard form access agreements, which can form the basis of the commercially negotiated WBAs. Module 0 also contains fixed principles terms and conditions for NBN Co’s long-term cost recovery.

Module 1 contains comprehensive terms and conditions that have applied during the initial regulatory period, which covers the period from the start of the SAU through to 30 June 2023. Module 1 includes the commitment to supply initial NBN offers, initial prices for NBN offers and methods for changing prices over time, the long-term revenue constraint methodology, non-price terms and conditions and product development and withdrawal provisions.

In the absence of a revised SAU, Module 2 would start on 1 July 2023 and sets out long-term arrangements for determining NBN Co’s required revenue for the remainder of the SAU, which runs until 2040. The mechanism for assessing NBN Co’s required revenue changes will be based on forecast costs rather than the actual costs (as in Module 1). Additionally, Module 2 contains the mechanism for NBN Co to submit ‘replacement module applications’, which seek to vary the SAU to incorporate replacement modules that will operate for 3-5 years. Replacement module applications are subject to ACCC acceptance. Replacement modules will include forecasts of NBN Co’s expenditure and other detailed terms and conditions proposed by NBN Co. Module 2 also contains some other provisions that are similar to Module 1 of the SAU. These include the commitment to supply NBN offers, the annual price cap on price increases and the ability to rebalance prices. Also included are product development and withdrawal provisions.

Under both Module 1 and Module 2, there is no contemporaneous link between the Long-Term Revenue Constraint Methodology and prices so long as there are historical losses that NBN Co is yet to recover, as reflected in the ICRA.

## Annexure B: ACCC engagement and consultation with stakeholders

### Initial stakeholder engagement

The ACCC engaged extensively with NBN Co, access seekers and other stakeholders during 2021 on potential changes to the NBN regulatory framework under the SAU.

In June 2021, the ACCC hosted an industry roundtable with NBN Co, broadband retailers, industry groups, consumer bodies and government to canvass views to assist NBN Co in developing an SAU variation proposal.[212] NBN Co had also notified the ACCC that it intended to lodge a proposed variation to its SAU within the 12 months.

The ACCC then chaired a series of industry working groups to discuss aspects of the NBN regulatory framework. The key issues discussed by the working groups included NBN products and pricing, NBN Co's BBM and the regulatory framework and approach. The ACCC published a report summarising matters arising in the working groups in December 2021.[213]

An important output of this engagement was the development of five key outcomes from a varied SAU that could guide NBN Co's development of an SAU variation proposal. These were:

- NBN Co has the opportunity to earn the minimum revenues it needs to meet its legitimate financing objectives, including to transition to a stand-alone investment grade credit rating
- NBN end-users are protected from price shocks and from prices that are higher than necessary in later years
- the regulatory framework provides incentives for NBN Co to operate efficiently and promote efficient use of the NBN
- retailers have greater certainty over the costs that they will face when using the NBN
- there is a clear and robust quality of service framework so retailers and end-users know what to expect from NBN services, including a review mechanism so that service standards remain fit for purpose.

### March 2022 proposal to vary the special access undertaking

On 29 March 2022, NBN Co lodged an SAU variation proposal with the ACCC. The March SAU variation sought to incorporate into the SAU the hybrid fibre coaxial (HFC), fibre-to-the-node (FTTN) and other copper-based technologies that it had adopted since 2013. It also proposed significant changes to the SAU framework itself. The ACCC published the variation and consultation paper on 23 May 2022, after working with NBN Co to resolve extensive confidentiality claims that would have compromised effective public consultation if the ACCC had accepted them in full.

The response submissions raised a series of concerns with this SAU variation proposal and in addition the Minister for Communications wrote to the ACCC on 22 July 2022 expressing support for NBN Co to withdraw it and submit a revised proposal that would provide pricing certainty to retailers and other changes needed so that it was capable of acceptance. On 27 July 2022 NBN Co notified the ACCC of its decision to withdraw the SAU variation proposal with a view to making a revised proposal.[214]

---

212 A summary of the industry roundtable is available on the ACCC website.

213 A summary of working group meetings is available on the ACCC website.

214 A copy of the Minister's letter and NBN Co's letter of withdrawal are available on the ACCC website.

## Development of a revised proposal

NBN Co published a consultation paper on the changes that it was considering for a revised SAU variation proposal and the ACCC held a further forum on 18 and 19 of August 2022 to discuss these and other potential changes for inclusion in a revised SAU variation, as well as interim arrangements given the delay stemming from the withdrawn March 2022 variation proposal. The forum was attended by NBN Co, retailers and other stakeholders. The forum agenda and public summary of discussion are available on the ACCC website.[215]

Following the forum, NBN Co continued to engage with the ACCC, retailers and its other stakeholders as it developed its revised SAU variation proposal.

[215] The forum agenda and public summary are available here.

# Annexure C: Approach to handling information received during the consultation on NBN Co's SAU variation

The ACCC/AER Information Policy[216] sets out the general policy of the ACCC on the collection, use and disclosure of information.

The ACCC considers that a public and transparent consultation process is necessary to discharge the ACCC's procedural obligations and allow the ACCC to effectively assess the SAU variation proposal in accordance with the legislative framework and given the significance of the proposed changes to the SAU and their potential long-term consequences for Australian consumers and businesses. Hence, the ACCC will only agree not to disclose information that is the subject of a confidentiality claim in limited circumstances.

In these circumstances, the ACCC has also formed the view that making information available to third parties only through limited individual non-disclosure agreements would not be an appropriate means to manage confidentiality claims in this consultation. Hence in this consultation it does not intend to apply the ACCC's confidentiality guideline for submitting confidential material to ACCC communications inquiries.[217]

The ACCC has published the SAU variation in full and has published NBN Co's supporting material with only minimal redactions. The ACCC notes that the redactions are confined to supporting documents and are limited in scope. Therefore, the ACCC does not intend to publish any further information from NBN Co's supporting material at this time.

The ACCC will continue to consider what further information is required for, or of significance to the consultation and should therefore be published, in full or in part.

## Disclosure of information

The ACCC will assess any confidentiality claims on a case-by-case basis and in doing so will consider whether it is required to publish information having regard to its statutory and common law duties and functions in each instance and in accordance with section 155AAA of the *Competition and Consumer Act 2010* (Cth) (CCA).[218]

In assessing confidentiality claims, the ACCC will consider whether publication of the information is required to enable effective public consultation and allow it to perform its statutory function of assessing the SAU variation in accordance with the statutory framework. The ACCC will assess whether this requirement outweighs any significant commercial harm a party submits may result from publication. The ACCC will afford procedural fairness in reaching these views.

## Process for claiming confidentiality

If a party wishes to make a claim of confidentiality over material provided during this consultation, it should follow the process below:

1. Please submit two versions of the submission:
    a) a **public** submission that can be published on the ACCC's website, in which all confidential material has been removed and replaced with 'c-i-c'. Please ensure that redacted information is not searchable or otherwise able to be viewed.

---

216 The ACCC/AER Information Policy is available on the ACCC website.

217 The Confidentiality guideline is available on the ACCC website.

218 The ACCC notes in this regard paragraph 3.1 of the ACCC-AER Information Policy.

b) a **confidential** version that clearly identifies the information over which confidentiality is claimed by bookending the confidential material with a marking of ‘c-i-c’. Please also highlight for ease of reference the material over which confidentiality is claimed.

2. Information over which a party claims confidentiality must kept to a minimum so that consultation on all relevant material is not unnecessarily impeded.
3. Please provide a supporting submission that specifically substantiates the confidentiality claim for each item of information over which confidentiality is claimed. Confidentiality claims need to detail why the information is competitively sensitive or otherwise confidential, and why disclosure of the information would be likely to cause significant harm to the person to whom the information is confidential. ‘Blanket’ claims of confidentiality will not be accepted. The ACCC will notify parties of any additional information required to assess a confidentiality claim.
4. Where the ACCC proposes to publish information the subject of a confidentiality claim, it will provide a right to be heard and to amend or withdraw the information before proceeding to publication with redactions removed.
5. Where the ACCC proposes to not publish information the subject of a confidentiality claim and publishes a redacted submission, it may reconsider that claim at a future date if it becomes evident that publication of the redacted information is required to enable effective public consultation and to allow the ACCC to perform its statutory function of assessing the SAU variation in accordance with the statutory framework. The ACCC will notify with the relevant party and engage with them in relation to how this information can be disclosed.

## Annexure D: Submissions to the ACCC consultation paper on NBN Co's SAU variation

Public submissions to the SAU variation consultation paper are available on the ACCC website. The following is a list of the submissions received by the ACCC:

| **Submission** | **Date Received** |
|---|---|
| NBN Co | 17 February 2023 |
| NBN Co - Expert report | 17 February 2023 |
| Chris Hucklebridge | 16 January 2023 |
| David Lapans | 4 February 2023 |
| Commpete | 16 February 2023 |
| Vocus | 16 February 2023 |
| ACCAN | 17 February 2023 |
| AGL | 17 February 2023 |
| Telstra | 17 February 2023 |
| Telstra (Confidential) | 17 February 2023 |
| X Integration | 17 February 2023 |
| Launtel | 19 February 2023 |
| Aussie Broadband | 20 February 2023 |
| Bruce Bebbington | 20 February 2023 |
| Optus | 20 February 2023 |
| Optus (Confidential) | 20 February 2023 |
| TPG | 20 February 2023 |
| TPG (Confidential) | 20 February 2023 |
| Internet Association of Australia | 21 February 2023 |

In addition to stakeholder submissions, we have also considered the following materials provided by NBN Co with the proposed SAU variation:

- Supporting submission – sections A to H
- The Building Block Model for core services
- The Building Block Model handbook
- The Cost allocation manual
- Five supporting expert reports from Analysys Mason, Castalia, Frontier and RaA

- The Weighted average price cap model
- Forecasts in support of the SAU variation
- A Draft statement of pricing intent

## Annexure E: The long-term interests of end-users and reasonableness

In determining whether a particular thing promotes the LTIE, the CCA requires the ACCC to consider the extent to which the thing is likely to result in the achievement of the following objectives:

- promoting competition in markets for listed services
- achieving any-to-any connectivity in relation to carriage services that involve communications between end-users
- encouraging the economically efficient use of, and economically efficient investment in the infrastructure by which these services are supplied, and any other infrastructure by which these services are, or are likely to become capable of being supplied[219]

The ACCC cannot consider any other objectives in assessing the LTIE.

The CCA further provides that:

- in determining whether a thing is likely to result in the achievement of the objective of promoting competition in markets for listed services, the ACCC must have regard to the extent to which the thing will remove obstacles to end-users of listed services gaining access to those services, but may also have regard to other matters
- in determining whether a thing is likely to result in the achievement of the objective of encouraging the economically efficient use of, and economically efficient investment in the infrastructure, the ACCC must have regard to the following matters, but may also have regard to other matters:
    - whether it is technically feasible for the services to be supplied and charged for having regard to matters such as available technology, the cost involved in supplying the service and the likely effect on the operation or performance of telecommunications networks
    - the legitimate commercial interests of the supplier, including its ability to exploit economies of scale or scope
    - incentives for investment in the infrastructure by which the services are supplied
- the objective of any-to-any connectivity is achieved if and only if each end user is able to communicate with each other end-user who is supplied the same or a similar service, whether or not they are connected to the same telecommunications network.

In determining whether terms and conditions are reasonable, the CCA requires the ACCC to have regard to the following matters:[220]

- whether the variation promotes the LTIE
- the legitimate business interests of NBN Co, and NBN Co’s investment in facilities used to supply the services concerned
- the interests of persons who have the right to use the services concerned
- the direct costs of providing access to the services concerned
- the operational and technical requirements necessary for the safe and reliable operation of a carriage service, telecommunications network or facility

[219] CCA, s. 152AB(2).

[220] CCA, s 152AH.

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

However, the requirement to have regard to these matters does not, by implication, limit the matters to which the ACCC may have regard.

In relation to the objective of encouraging economically efficient use of, and investment in, infrastructure, the ACCC will examine efficiency from an economic perspective consistent with its long-standing approach. The economic concept of efficiency consists of three components:

- **Productive efficiency** refers to the efficient use of resources within each firm to produce goods and services using the least cost combination of inputs.
- **Allocative efficiency** refers to the allocation of goods and services across the economy in a way that is most valued by consumers. It can also refer to the allocation of production across firms within an industry in a way that minimises industry-wide costs.
- **Dynamic efficiency** refers to the efficiencies flowing from innovation leading to the development of new services or improvements in production techniques. It also refers to the efficient deployment of resources between present and future uses so that the welfare of society is maximised over time.

## Annexure F: NBN Co's proposed expenditure and cost categories

The table below shows the actual and forecast capital and operating expenditure forecast in real term (FY14 price level) for the period of FY24-26.

Table 1. NBN Co capital and operating expenditure forecast

| $ 000 (real) | FY24 | FY25 | FY26 |
|---|---|---|---|
| Capital expenditure | | | |
| Core | 2,547,302 | 2,030,385 | 2,164,026 |
| Total | 2,645,187 | 2,120,264 | 2,250,802 |
| Operating expenditure | | | |
| Core | 2,178,873 | 2,103,028 | 2,064,304 |
| Total | 2,234,905 | 2,168,509 | 2,131,712 |

Source: NBN Co SAU variation

NBN Co's capital expenditure is summarised into 5 key categories, which relate to the purpose of the expenditure:

- Expansion: capex required to expand the coverage of the NBN as the population of Australia continues to expand into new developments,
- Take-up & Usage: capex required to connect individual premises on demand (in brownfield and greenfield areas) to the NBN and to provide incremental capacity as usage per end-user grows,
- Maintaining: capex required to maintain the existing capability of the NBN,
- Capability: capex required to increase the capability of the NBN through the Network Upgrade Initiative, Fixed Wireless Upgrade Program, SMB Enablement Initiative and Regional Co-Investment Initiative, and
- Other: capex required across several other categories, including IT (Software Engineering). expansion, take-up & usage, capability.[221]

The table below shows NBN Co's IOP capital expenditure by categories in real terms (June 2021 price level) in the period of FY21-26. FY21 and FY22 figures are actuals and the figures for FY23 to FY26 are forecasts.

Table 2. NBN Co IOP capital expenditure by categories

| $ million (real) | FY21 | FY22 | FY23 | FY24 | FY25 | FY26 |
|---|---|---|---|---|---|---|
| Expansion | 660 | 286 | 245 | 215 | 191 | 201 |
| Take up & usage | 1,041 | 669 | 606 | 503 | 426 | 424 |
| Maintaining | 95 | 80 | 126 | 92 | 55 | 33 |

[221] NBN Co SAU Variation supporting submission (efficiency of NBN Co's expenditure and demand forecasts), November 2022., p. 37.

| | | | | | | |
|---|---|---|---|---|---|---|
| Capability | 501 | 981 | 1,698 | 1,643 | 1,364 | 1,353 |
| Other | 468 | 334 | 450 | 402 | 300 | 276 |
| Total | 2,764 | 2,351 | 3,127 | 2,855 | 2,335 | 2,289 |

Source: NBN Co

NBN Co's operating expenditure (opex) is summarised into 6 categories:

- Infrastructure payments
- Direct operating costs
- Labour costs
- Other operating costs
- Service level rebates
- Subscriber payments

The table below shows NBN Co's IOP operating expenditure by categories in real terms (June 2021 price level) in the period of FY21 to FY26. FY21 and FY22 figures are actuals and the figures for FY23 to FY26 are forecasts.

Table 3. NBN Co IOP operating expenditure by categories

| $million (real) | FY21 | FY22 | FY23 | FY24 | FY25 | FY26 |
|---|---|---|---|---|---|---|
| Infrastructure payment | 794 | 851 | ***CiC*** | ***CiC*** | ***CiC*** | ***CiC*** |
| Direct Operating Costs | 731 | 751 | 649 | 595 | 562 | 560 |
| Labour Costs | 831 | 665 | ***CiC*** | ***CiC*** | ***CiC*** | ***CiC*** |
| Other Operating Costs | 606 | 503 | ***CiC*** | ***CiC*** | ***CiC*** | ***CiC*** |
| Service Level Rebates | 20 | 24 | 11 | 9 | 7 | 7 |
| Subscriber Payments | 1,214 | 168 | 15 | - | - | - |
| Total | 4,195 | 2,963 | 2,631 | 2,507 | 2,433 | 2,391 |

Source: NBN Co

## Annexure G: Market overview

Assessing an SAU variation calls for consideration of its consequences for competition and economic efficiency for the markets in which NBN services are supplied. In other words, the likely implications of the SAU variation should be determined in the context of the current and anticipated conditions of the wholesale market in which NBN services are acquired and the retail market in which retailers supply services over the NBN.

### Wholesale markets

NBN Co states in its supporting submission that it is constrained by competitive pressure arising from (actual or potential) alternative networks that are available to retailers, and so should not be considered as a traditional infrastructure monopoly provider.[222]

In support of this position NBN Co points firstly to alternative direct fibre networks as a source of significant and increasing competition for business services.[223] NBN Co anticipates growing its share of this market, having entered the wholesale market for these services relatively recently.

NBN Co also notes that it competes with other fibre network operators for the right to build fixed line broadband access networks in new developments, also known as greenfields, where networks can typically be constructed more quickly and at less cost.

Further, NBN notes that wireless networks are available across a broad geographic footprint. NBN Co claims 2.9 million of the premises within its network footprint are not using the NBN for broadband and are instead connected to a competing broadband network.[224] That said, NBN Co notes that this competitive pressure may potentially moderate over time as the communication needs of households and businesses outgrow the capacity of alternative wireless networks.

Telstra provided a different perspective in its submission regarding the use of wireless (4G, 5G, fixed wireless and satellite) networks as substitutes for a NBN connection. In its view the potential for such use is presently very limited.[225]

We note that NBN Co is the dominant provider of wholesale telecommunication access services in Australia with around 82% of Australian households connected to the Internet via the NBN.[226] We note that 8.7 million Australian premises use an NBN connection to access telecommunication services.[227] Some of these connections are used for the supply of voice only services[228], but the majority are used either for broadband services, either with or without a voice service.

We note that direct fibre connections have traditionally been used to supply high yielding services to enterprise or government customers within central business districts or other high-density geographies. These networks are not ubiquitous and are not used to supply mass market services due to the high costs to connect premises to direct fibre. We consider that this market segment will become increasingly competitive with NBN Co's entry,

---

222 NBN Co, *Supporting submission Part A: Executive summary and key narratives*, November 2022, p.25.

223 Telstra and Optus are restricted under commercial agreements with NBN Co from using their historic customer access networks to supply services following the rollout of the NBN but they (or other network operators) are not restricted from using direct fibre connections to supply services where it would be efficient to do so.

224 NBN Co, *Supporting submission Part A: Executive summary and key narratives*, November 2022, p.26.

225 Telstra, *Submission to consultation paper*, 17 February 2022, pp.55-58.

226 ACMA, *How we use the internet: Executive summary and key findings*, December 2022, p.3.

227 ACCC, NBN wholesale market indicators report: December 2022, 3 March 2023.

228 Voice only services are likely a subset of services supplied using an NBN entry level wholesale offer, which themselves are less than 10 percent of total NBN wholesale services.

particularly in existing or adjacent localities with incumbent network operators, but that it will continue to represent only a small proportion of the wholesale market.[229]

The main alternative operator in new developments is Uniti Group via its wholesale network arm Opticomm Networks, although there are other smaller network operators active in this segment.[230] We note that Uniti states that its network is available to around 565,000 premises (at 30 June 2021), with this number growing as it completes its build of contracted networks in additional developments.[231] We note that as of April 2023, NBN Co can connect 1.25 million premises to the access networks that it has built in new developments.[232]

Alternative fixed line and wireless networks could be available to households and businesses depending upon their location. We note that TPG Group operates the most significant alternative fixed line network outside of new developments, via its wholesale arm Vision Network. TPG Telecom states that it supplies around 135,000 fixed line customers out of the 400,000 premises within its network footprint.[233]

Our most recent ACCC internet activity reported there were a total of 345,000 premises connected to wireless broadband at June 2022.[234] Singtel Optus has stated that it was supplying 209,000 fixed wireless services as at 30 September 2022 (down from 211,000 a year earlier)[235] and the TPG Group 171,000 at December 2022 (up from 80,000 at December 2021).[236] Telstra does not publish data on connections for its fixed wireless offering but states that the extent to which 4G, 5G, fixed wireless and satellite networks are substitutes is very limited.[237]

We consider that whether the services that are available over alternative networks are likely to be substitutable for NBN services will depend upon their price and quality relative to the needs of the customers. We note that many of the substitute products are not market-wide alternatives and in many cases will require further and ongoing investment to be directly comparable in terms of service quality or availability.

Consequently, we consider that wholesale competition will remain dependent on NBN Co's wholesale offers, notably the pricing of certain plans and their service quality, along with continuing investments by alternative networks.

In this regard, we consider that mobile networks will continue to provide alternatives to many households and businesses that only require a voice service, or which have basic data connectivity needs. We also note that there is potential for competition at the margins over higher quality services should mobile operators continue to offer higher capacity and usage plans over 5G networks. We consider it to be rational for mobile network operators to offer such services while networks have spare capacity but would expect them to preference higher yielding mobile services over time as the networks again approach high levels of utilisation.

---

229 The supply of direct fibre services is proposed to be designated as competitive for the purposes of the SAU, and ringfenced from the regulation of mass market ("core") services.

230 Many of these are listed on the Statutory Infrastructure Provider (SIP) register. See https://www.acma.gov.au/sip-register

231 Uniti Group, Annual Report 2021, p. 7.

232 NBN Co, *NBN Co Weekly Progress Report,* 12 April 2023.

233 TPG Telecom, *Annual Report 2022*, p. 8 and Vision Network, *Customer On-Boarding Guide*, 29t August 2022, p. 4

234 ACCC, *Internet activity report June 2022*, p. 5.

235 Singapore Telecommunications Limited and Subsidiary Companies*, Management Discussion and Analysis of Financial Condition, Results of Operations and Cash Flows for the Half Year Ended 30 September 2022,* p. 40.

236 TPG Telecom, *Annual Report 2022,* p. 8.

237 Telstra, *Submission to consultation paper*, 17 February 2022, pp. 55-58.

## Retail markets

The retail market for broadband is significantly more competitive than the wholesale market.

As noted above, around 8.7 million mass market broadband services are supplied over the NBN with around 800,000 services supplied over alternative networks.[238]

That said, the four incumbent service providers of Telstra, TPG Telecom, Optus and Vocus have a combined market share of around 85% of wholesale services supplied over the NBN.[239] The share of newer entrant retailers is around 15%, up from around 11% a year ago.[240] Many of the emerging retailers have brought new and innovative retail offers, and so serve as an important source of retail product differentiation and competition.

A different mix of retailers supply over alternative networks. The share of retail services supplied over these alternative networks tend to skew towards the retail brands of the network operator, and the larger incumbent retail operators on the NBN tend not to supply services over networks except those that they themselves operate.

Consequently, we consider that it will be important that NBN Co's wholesale product and pricing offers do not constitute barriers to entry and expansion by retailers. This will better support more diversity in retailers and retail offers that enable retailers to better compete with other retailers operating over the NBN, or over alternative networks where these are available.

---

238 The latter figure is derived from ACCC, *Internet activity report*, June 2022 and includes non-NBN fixed line, home wireless and satellite services.

239 ACCC, NBN wholesale market indicators report: December 2022, 3 March 2023.

240 ACCC, NBN wholesale market indicators report: December 2022, 3 March 2023.

## Annexure H: Overview of regulatory periods and SAU modules

| Financial year | 2013 - 2023 | 2024 - 2026 | 2026 - 2032 | 2032 - 2040 |
|---|---|---|---|---|
| Regulatory period | Initial regulatory period | Subsequent regulatory period | | Post 2032 regulatory period |
| Regulatory cycle | | 1st cycle | | |
| Module | Module 0 | | | |
| | Module 1 | Module 2 | | Module 3 |
| | | Module 4 | | |

The SAU term is divided into regulatory periods. The SAU variation would build upon this structure by defining additional regulatory periods, with each such period to be further broken into regulatory cycles.

The SAU is also made up of various Modules each containing provisions to apply during specified regulatory periods or regulatory cycles.

Module 0 sets out terms to operate over the duration of the SAU and includes provisions relation to service descriptions, the dictionary, and the initial products.

Module 1 sets out the commitments made in connection with the provision of access to the NBN access service, etc, to apply during the initial regulatory period. The initial regulatory period will end on 30 June 2023 but may have some ongoing relevance to the extent that it contains definitions for terms that are also used in subsequent modules.

Module 2 sets out the commitments for the subsequent regulatory period which runs from Financial Years 2024 to 2032. It contains the pricing framework, pricing certainty measures, the ABBRR and WAPC revenue requirement, benchmark service standards framework and other terms and conditions amongst other things.

Module 3 sets out terms that will govern the provision of access during the post-2032 regulatory period. It contains the principles applying in the post-2023 regulatory period. Compared to Module 2, Module 3 contains broader principles rather than the more specific and prescriptive terms in Module 2.

Module 4 sets out terms specific to the first regulatory cycle including the Benchmark Service Standards and Building Block Model parameters for this regulatory cycle.

Unlike the regulatory periods, the regulatory cycles do not have fixed timespans. The timeframe for each would be determined ahead of the expiry of the current regulatory cycle.

At the end of the SAU term, the provisions of the SAU would cease to have effect. From that time, regulated access terms for the NBN will be determined under Part XIC of the CCA via access determinations and/or another SAU.