Proposed NBN Co cost allocation manual: Consultation paper

ACCC

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Public submission

Submission

TPG Telecom welcomes the ACCC's consultation on NBN Co's proposed cost allocation manual (**November 2023**).

TPG Telecom acknowledges NBN Co's improvements to the cost allocation manual will mean the allocation of costs between NBN Co's core and competitive services will be clearer.

However, TPG Telecom encourages the ACCC to scrutinise actual figures from NBN Co showing a breakdown of how costs will be separated in practice, particularly for shared capital and operating expenditure.

This would enable the ACCC to test whether the proposed cost allocation manual sufficiently mitigates the cross-subsidisation risk. This safeguard is important, given NBN Co can obtain uncapped profits from its enterprise business.

For example, if the allocation of a shared cost group under NBN Co's proposal means 99% of costs are allocated to core services, the ACCC should assess whether the proposed allocation is appropriate. Ideally, this exercise should be completed before the ACCC issues a final decision in relation to the proposed cost allocation manual.

TPG Telecom believes this would be a valuable exercise, considering the shortcomings of the Farrier Swier Consulting report provided by NBN Co (dated 16 November 2023). Notably, the report states Farrier Swier Consulting has "*not undertaken a detailed review of the data available to nbn when identifying directly attributable costs and causal allocators*." Rather, Farrier Swier Consulting have merely, "*relied on information and representations provided to us by nbn that the process it has followed is sufficient to ensure that these were identified appropriately"* (page v).

Conducting this exercise would provide greater certainty to the ACCC and industry the proposed cost allocation manual will be meaningful and effective in mitigating the cross-subsidisation risk.

At a minimum, NBN Co should provide an estimated percentage of how costs would be split between core and competitive services for each shared cost group under each allocator in the proposed cost allocation model.

The cost allocation manual should also explicitly state records will be maintained by NBN Co to allow attributions and allocations to be audited by the ACCC and otherwise reviewed by a third-party independent auditor appointed by the ACCC, as opposed to one appointed by NBN Co.

Comments regarding specific cost allocators

TPG Telecom makes the following observations regarding specific cost allocators in the proposed cost allocation manual:

- **Use of 'estimated' network data traffic**: The proposed cost allocation manual does not explain why NBN Co prefers to use 'estimated' network data traffic as an allocator, rather than actual network data traffic. If 'estimated' network data traffic is used, NBN Co should provide more detail regarding the methodology used to derive the estimate, such as the timeframe NBN Co will reference to develop the estimate. There should also be a mechanism to enable an audit or true up to reconcile estimates with actual data traffic.

- **Use of average estimated network data traffic as a cost allocator for the Local & Distribution Network:** Each Enterprise Ethernet and FTTP customer has a dedicated fibre pair to the aggregation equipment at the Fibre Access Node site. As such, average network data traffic may be an inappropriate cost allocator for such equipment, given the incurred cost is not related to the average data traffic. Peak network data traffic would more accurately reflect the cost incurred in the provision of both services.

- **Use of 'active' premises and revenue:** In previous submissions to the ACCC, TPG Telecom raised concerns regarding the use of revenue as an allocator for shared expenditure. This is relevant, for example, during the build or growth phase of any new service, where revenue is not being generated, but resources are needed to manage these processes. NBN Co's proposal to calculate the average of 'active' premises and telecommunications revenue does not sufficiently address this concern, given 'active' premises does not factor in the future benefit gained from the expenditure.

- **Allocating marketing and product costs:** The shortcomings associated with the use of active premises and revenue as an allocator is evident when applied to marketing and product costs. The proposed cost allocation manual states the causality relationship for marketing and product costs includes to 'drive increased activations and/or revenue'. However, using the average of active premises and telecommunications revenue as an allocator does not reflect this causality. For example, it would not be fair for NBN Co to spend 90% of its marketing budget to drive increased activations for Enterprise Ethernet and have part of that cost be underwritten by residential consumers. Costs should therefore be allocated to reflect the service benefitting from the marketing spend. This could be achieved, for example, by greater specificity regarding whether costs for a marketing campaign are directed at increasing take-up of a core service or competitive service and allocating the cost accordingly.

- **Enterprise Ethernet connections:** The cost allocation manual states "*fibre cable assets constructed to deliver an EE service are considered shared capital expenditure and treated as a shared cost because they will also be utilised for Core Regulated Services in the future".* If NBN Co were to install new fibre for an Enterprise Ethernet service in an existing-FTTN area, NBN Co could subsequently roll out FTTP (using the cable installed ostensibly to deliver the Enterprise Ethernet service) under the auspices of its 'Fibre Connect' program, to justify sharing cable costs between its regulated and competitive businesses.

In comparison, TPG Telecom must cover the cost of expanding fibre coverage to a corporate customer not served by existing fibre via revenue from that customer alone. Neither TPG Telecom, nor any other carrier, can cross-subsidise build costs in the same manner as NBN Co. This makes it difficult to compete with NBN Co in the supply of competitive services as some of the build costs of NBN Co providing competitive services are cross-subsidised by its regulated services.

- **Fibre network assets and civil infrastructure assets (excluding customer connections):** The capital expenditure to build/construct assets should be separated from expenditure required to upgrade assets to meet growing capacity demand. Where expenditure is incurred to build assets, the allocator used should reflect the potential future benefit of the asset. For example, consider a scenario where NBN Co builds a new duct, and the duct initially contains one conduit for the supply of core services only. Adopting the average estimated network data traffic allocator, NBN Co would estimate 100% of the network data traffic in the relevant financial year will be used for core services, meaning 100% of the costs to build the duct would be allocated to core services. A few years later, the same duct is upgraded to add another conduit to enable NBN Co to run a fibre optic cable to supply an Enterprise Ethernet service. In that scenario, NBN Co could be advantaged because:

  (a) 100% of the cost to initially build the duct has already been allocated to core services (despite the duct now being capable of supplying both core and competitive services); and

  (b) the cost to build a second conduit could be split between core and competitive services based on average estimated network data traffic, despite the purpose of the conduit being for Enterprise Ethernet services; and

  (c) if an Enterprise Ethernet customer does not take up the service in the same financial year the duct is upgraded, it appears NBN Co can allocate 100% of the build cost to core services.

TPG Telecom believes any costs remotely attributable to NBN Co providing competitive services should be allocated as such. Addressing the matters raised above will ensure the proposed cost allocation manual moves closer to this principle, enabling the regulatory regime to work as intended.