Vocus response to ACCC consultation paper

Proposed variation to the NBN Co Special Access Undertaking

February 2023

Vocus welcomes the opportunity to provide a response to the ACCC's consultation paper issued on 13 January 2023 on the proposed variation to the NBN Co Special Access Undertaking (SAU).

Vocus serves residential consumers and small businesses through its retail brands Dodo, iPrimus and Commander (Vocus Retail). Vocus also provides wholesale NBN services to other RSPs.

Vocus' response focuses on NBN Co's proposals concerning pricing. Vocus understands the market segment looking for value and affordable broadband, with nearly 90% of our retail residential customers on speed tiers at 50 Mbps or below.

Vocus maintains that the pricing and product construct put forward by NBN Co is not in the long-term interests of end users (LTIE) and will result in consumer detriment. NBN Co has failed to address the issues of affordability and value in its proposed pricing constructs for the 25 Mbps and 50 Mbps speed tiers.

Pricing and product construct

Wholesale price increases will lead to consumer detriment and inefficient utilisation of the NBN

NBN Co's wholesale prices should be set to promote competition and encourage efficient use of the NBN. However, NBN Co proposes to significantly raise the cost of the 50 Mbps plan, the most popular NBN product in the market today. If the ACCC accepts NBN Co's SAU variation, this will result in material price increases for consumers at a time when many are facing significant cost of living pressures. This outcome is not in the LTIE.

To promote competition, NBN Co's pricing must support RSPs operating at acceptable profit margins and being able to provide a product to our customers that provides value, by being priced appropriately for the experience they receive. In contrast to these objectives, NBN Co has proposed an immediate price increase from $45 plus overage to $50 + overage.

The 50 Mbps plan will become materially more expensive for RSPs to supply to their customers - in addition to the $5 increase in minimum access cost, there will be a cost increase of $1.20 due to the 6% reduction in the CVC inclusion (2.65 to 2.5 Mbps). The existing CVC inclusion is already too low, with Vocus already purchasing additional CVC beyond today's inclusion of 2.65Mbps. In addition, Vocus will lose the benefit of economies of scale, as the current, more generous CVC inclusions on higher-speed tiers will no longer be available to be pooled across all AVCs – meaning the overage charge for a 50 Mbps plan will be higher still. These costs are illustrated in the chart below:

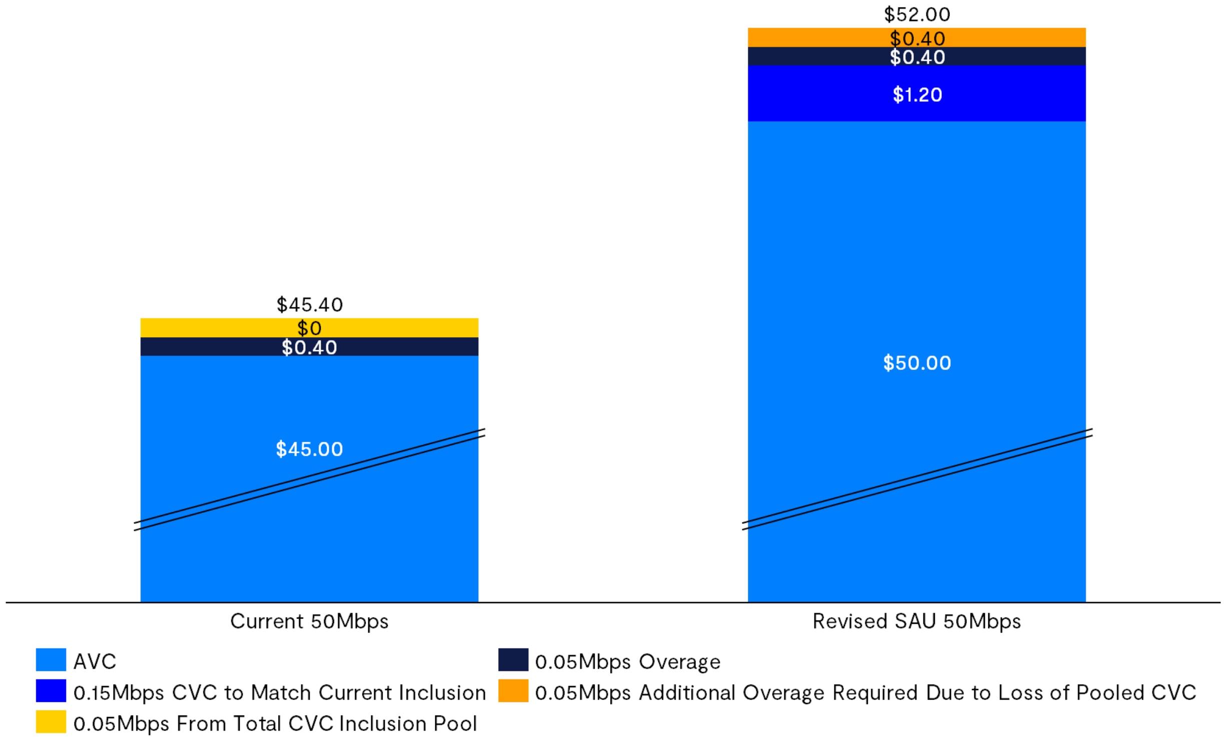

Chart illustrating current vs proposed wholesale input costs on a 50Mbps service (note: CVC overage is for illustrative purposes only and is not indicative of real-world provisioning)

In its supporting submission on pricing and pricing controls, NBN Co states that "it has many end-users with high data usage who subscribe to low-speed plans. These users could be expected to have high willingness to pay for broadband services ...". Vocus does not agree with NBN Co's assertions about consumers' higher willingness to pay. This assertion overlooks the role of price as a major guiding factor in customer choice. Dodo customers are traditionally those who require significant data (and therefore consume significant bandwidth) but seek to do so at the lowest available cost. Our experience has shown that many of our Dodo customers are not willing to pay more to obtain higher speeds. The 50 Mbps plan continues to be the predominant product our customers choose today despite changes in consumer behaviour such as increased working from home and the consistent growth of video streaming services

Lower wholesale prices, not increased wholesale prices, are needed to encourage utilisation of the NBN. In the context of current cost of living pressures, we have already seen customers choosing to downgrade broadband speed tiers to save $5 or $10 per month. As evidenced in the below diagram, Vocus Retail saw a doubling in monthly downgrade requests between March and June 2022, as the Reserve Bank increased the cash rate and banks followed with interest rate rises. Of the users who chose to downgrade over this period, the majority downgraded from a $75 50 Mbps plan to a $65 25 Mbps plan (30% of total downgrades) or $55 15 Mbps plan (22% of total downgrades). Close to a third downgraded from a 100 Mbps plan to a 50, 25 or 15 Mbps plan.

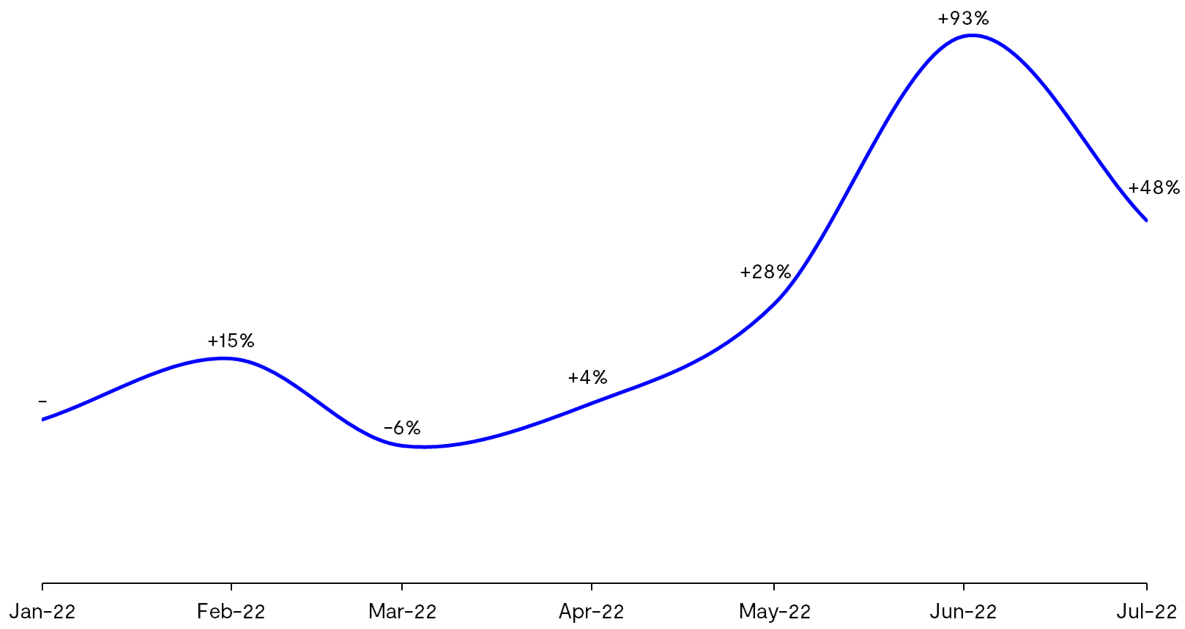

Chart showing a significant uptick in consumers downgrading speed tiers, coinciding with Reserve Bank cash rate increases occurring since May 2022

We maintain that the proposed price increase for 50 Mbps speed tier is likely to lead to further inefficient, under-utilisation of the NBN network. Our experience suggests that price sensitive consumers are likely to downgrade their service or seek alternatives. Neither of these outcomes promote the LTIE and are therefore not reasonable.

Greater use of the 25 Mbps speed tier will also undermine cost certainty for RSPs given the variable CVC component will be a large proportion of the wholesale cost for at least a further three years. NBN Co's proposed pricing of the 25 Mbps and 50 Mbps speed tier will amplify the bypassing of the NBN network. More consumers will be priced out of the market and miss out on the social and economic benefits of NBN connectivity. There are already more than 1 million inactive premises where consumers have connected, disconnected, and not reconnected to an NBN service. RSPs – particularly those that are also Mobile Network Operators – will continue to seek better margins and price certainty than available in reselling NBN. In its July 2022 submission to the ACCC's consultation on NBN's earlier SAU Variation, TPG Telecom noted that "the reality is operators such as TPG Telecom are incentivised to offer fixed wireless services because NBN Co does not want to serve price sensitive customers… the ultimate consequence of end-users bypassing the NBN is everyone else (including present and future users of the NBN) will have to pay more for their NBN access." We highlight that pricing for fixed wireless access services is currently sitting in exactly the part of the consumer market that pays for the 50 Mbps speed tier on the NBN network.

RSPs will also not be able to deliver price stability to price sensitive consumers given NBN Co's permissible annual price increases, which may further reduce demand for the NBN.

NBN Co's permissible price increases are not linked to changes in NBN Co's costs. The proposed pricing increases remain substantial. NBN Co has proposed annual CPI increases on the entry level offer and annual pricing increases that are the higher of CPI or 5 percent for other residential grade products. Vocus submits that NBN Co's annual price increases should beno more than 50 per cent of

CPI. These permissible price increases will exacerbate the consumer detriment flowing from the immediate price increase to the 50 Mbps speed tier, particularly given the price increases are not accompanied by any corresponding uplift in service quality. This outcome does not promote the LTIE. NBN Co should not be able to automatically increase its prices every year for the same service. Doing so will make NBN services progressively less competitive with alternatives.

Encouraging uptake of higher speed tiers should be driven by consumer need

The ACCC has asked if stakeholders are supportive of the proposed approach to encourage uptake of wholesale services at higher speed tiers, including migrating 12 Mbps broadband access towards a 25 Mbps speed tier and more-intensively used 50/20 Mbps services to the 100/20 Mbps tier.

Vocus has progressively migrated customers from NBN Co's entry level 12 Mbps services to 25 Mbps services as their needs have increased. We currently offer an entry level plan at 15 Mbps based on a scaled back version of the 25 Mbps speed tier. While uptake on this product and similar 12 Mbps plans is generally low, it does represent an affordable entry point for light users.

From a consumer perspective, customers do inform us if their service is not meeting their needs and we attempt to "right-plan" them onto a more suitable product. There will also be customers that are heavier users on 50 Mbps services and may have a declining experience but have a low willingness to pay more for a higher speed tier. In both cases, NBN Co's pricing should enable RSPs to provide consumers with a range of products to suit their needs and align with their willingness to spend. 50 Mbps speed tier services have become the most popular plan in the market as they represent the mid-point of willingness to spend and an experience that meets most users' requirements.

In order to maintain price certainty on services that will continue to attract CVC overage, Vocus envisages it will need to separate AVCs that attract overage from AVCs that do not attract overage, which will require ongoing reconciliation activity at an individual service level to determine if incremental usage warrants an AVC shift regardless of the retail pricing and plan speed offered to the customer. We will need to build a solution to assist in forecasting which services require migration, which will be a manual process initially and will result in a small outage to end customer services as they are moved between CVCs. If individual AVC management is scaled to a market level for NBN Co and RSPs to manage, this would require greater investment in real-time reporting and automated management tools necessitating more integrations between NBN Co and RSP systems so that individual user services would not be disrupted by multiple AVC shifts aligned to usage shifts.

Further, there will continue to be cases where Vocus will not be able to migrate customers to 100 Mbps speed tier services as their lines will be unable to support these speeds.

Vocus submits NBN Co's pricing model should be simple, allowing an RSP to purchase a product and resell it at an appropriate margin, on a sustainable basis. Every speed tier should be a viable, sustainable product that is valuable to and easily understood by consumers. Specifically, the reduction in the price of the 100/20 product in NBN Co's proposed wholesale pricing construct should not be at the expense of those consumers with either lower willingness to pay, lower speed requirements or on lines not capable of providing 100 Mbps speeds.

Lack of affordable pricing will not promote the take up of the NBN

NBN Co's Statement of Expectations issued on 19 December 2022 highlights that "NBN Co will offer products and pricing which promote the take up and utilisation of the NBN, and support Retail Service Providers to meet consumer needs at affordable prices."

We understand the price-sensitive market segment well and submit that the construct for the proposed new entry-level product, the 25 Mbps service, does not promote take up or retention of NBN services. The product construct does not appropriately support RSPs to meet consumer needs at affordable prices.

In its SAU supporting submission, NBN Co states that its "proposed pricing significantly reduces the average price for its 12 Mbps and 25 Mbps speed tiers, designed to offer a choice to consumers between basic connectivity (voice-only 12/1) and entry level broadband (25/5, 25/10) offers." NBN Co also stated in this submission that "some RSPs highlighted concerns with the proposed price increase on NBN's 50Mbps offer. These concerns do not appropriately consider that the change to the 50 Mbps offer is part of a broader price rebalancing across NBN's services, in which the prices for all other major speed tiers have been reduced. This overall price re-balance seeks to encourage take-up of the network by making entry level services more affordable."

Vocus' view is that this price "rebalancing" will not encourage take up of the network. Entry level broadband services are not more affordable. The 25 Mbps plan construct is not "more affordable" as it will operate in practice as a price increase. While NBN Co has proposed a lower monthly charge of $26, the offer only includes 0.2 Mbps of CVC capacity. This is an approximately 88% decrease on the current CVC inclusion. Further, if the bundled CVC allowances are exceeded in aggregate, a CVC overage charge of $8 Mbps/month will apply. The outcome of NBN Co's "give and take" approach to the pricing construct, is that to provide the same experience to our customers as we do today, we will need to spend $0.20 more than the current monthly bundled charge of $37 even before adding any variable overage charges as user demand continues to grow. This CVC inclusion is clearly inadequate and fails to promote the LTIE.

To promote competition, NBN Co's pricing and constructs should support RSPs in supplying products at prices and quality that are attractive to consumers and meet their needs. While NBN Co's proposal to only include 0.1 Mbps of included CVC capacity in its 25 Mbps offer may be designed to encourage RSPs to offer a product with data usage caps, these are plans that the industry has moved away from in recent years, it is outdated complexity

Consumers now expect and value the simplicity of plans with no shaping, data caps or excess usage fees. Nor does offering NBN plans with caps on data usage meaningfully address affordability concerns or reduce the likelihood of consumers seeking alternatives. Customers seeking affordable broadband are not necessarily low-usage customers. Vocus wants to sell products that meet our customers' needs enabling them to access the internet, video and streaming services in an unconstrained way.

The ACCC has noted the effectiveness of low-income measures could depend on a high level of engagement from low-income representatives, and NBN Co having a strong incentive to respond efficiently to their recommendations. Vocus highlights that specific NBN Co programs targeted to meet the needs of unconnected households, vulnerable and low-income consumers have historically been complex for RSPs to operationalise and have seen low levels of take-up. In this context, Vocus submits that the current needs of low-income users would be better addressed by the availability of more affordable plans.

To promote greater uptake and usage of the NBN network, the wholesale price of the 25/5 Mbps speed tier should allow for a $50 retail price point. As highlighted above, the proposed approach of NBN Co in reducing the CVC inclusion of this product to a mere 0.2 Mbps of CVC capacity will not encourage greater uptake.

Reduced consumer choice and impaired competition

The ACCC has rightly observed that the gap in minimum access costs between the 50 Mbps and 100 Mbps services is relatively small, and narrows further once the cost of CVC overage is factored in.

Vocus' view is that the proposed wholesale pricing model is not suitably calibrated so that both the 50 Mbps and 100 Mbps wholesale speed tiers support retail product and price differentiation.

The gap between the minimum access costs between the 50 Mbps and 100 Mbps speed tier will not enable RSPs to provide options which meet the needs of different consumer segments, leading to more homogenous wholesale inputs and undifferentiated retail products. NBN Co's model pushes users onto higher speeds by making lower tiers uncompetitive and thereby reduces RSPs' ability to offer innovative pricing and choice for consumers. Retaining CVC on the 50 Mbps tier will likely have a market-distorting effect. The construct will operate as a commercial incentive for some RSPs to push consumers on to higher-priced speed tiers that they do not necessarily want or need. This will not represent fair value and efficient use of the network for those consumers.

NBN Co's dual approach to pricing could also be damaging to the level of retail competition. The impact of NBN Co's proposal to retain CVC charges for speed tiers below 100 Mbps and offer flat monthly charges for 100 Mbps and higher offers will not be equally shared across RSPs. RSPs that over-index in the price-sensitive market will continue to wrestle with higher risk and complex variable usage charges. These pricing pressures will constrain their ability to compete and may push some RSPs out of the market. In contrast, NBN Co's proposals will deliver more price certainty for those RSPs that target high usage high speed customers or customers with a greater ability to pay. High and increasing 25 Mbps and 50 Mbps wholesale prices will also challenge the sustainability of smaller retailers who purchase NBN services from wholesale providers such as Vocus. This is not in the long-term interests of consumers given the role these retailers play in driving competition.

Price and cost uncertainty and operational complexity remains

NBN Co has submitted that "overall, the proposed pricing is designed to promote greater take-up and efficient use of NBN's network through improved price and cost certainty, and simplification, for RSPs."

However, the continuation of CVC charging on the most popular speed tiers to 1 July 2026, means RSPs will continue to bear cost risk of CVC charges due to their mismatch with the prevailing retail price structure until they are fully withdrawn. Moreover, the CVC charge whether at $8, $7 or $6 is well over NBN Co's incremental cost of capacity.

It is also not reasonable that NBN Co is only proposing to increase the CVC inclusions associated with the 25 Mbps and 50 Mbps speed tiers at 6-monthly intervals at 50 per cent of the usage change. This approach is yet another a way of increasing prices for low-speed NBN plans. To meaningfully mitigate cost uncertainty for RSPs and protect consumers, CVC inclusions must, at a minimum, be increased in line with end user demand.

NBN Co's choice to implement a phased reduction of CVC charges rather than removing this complex wholesale price structure puts in place a two-tier approach that will drive operational and technical complexity.

Despite the welcome move to charging for CVC utilisation, Vocus is concerned about the internal overhead costs that will flow from this change. Vocus will still be required to actively manage CVC on the network in line with advertised typical peak-time speeds to control commercial outcomes, with less flexibility than previously available. We will need to carefully manage this commercial risk as Vocus is over-indexed in plans that are 50 Mbps speed tiers and below.

Vocus does not see how it could operate TC-4 Bundled Offers and TC4 AVC-only offers on the same CVC. A mechanism to control the amount of overage used on TC-4 bundled offers (in line with typical peak time speed claims), is not practical when traffic is blended between TC-4 bundled and AVC-only services. In the same CVC model, a RSP is subject to a variable charge from NBN each month based purely on usage in what is assumed to be the peak hour of the day. This usage may exceed the advertised typical peak time speed and therefore provides no certainty in controlling costs for the RSP. Consequently, NBN Co's proposed construct with a mix of TC-4 bundled offers and AVC-only flat rate offers will not provide the asserted simplicity in network operations or promote competition. We will need to develop new end-to-end reconciliation processes, which will drive further costs. NBN Co will need to provide transparency and reporting concerning flat rate and bundled services to aid reconciliation.

Vocus has already experienced the operational challenges of dealing with dual pricing constructs when Dimension Based Discounting and bundles co-existed. We submit that NBN Co's proposed split pricing construct would again create another scale and transition challenge for RSPs, as TC-4 bundle services reduce over time. RSPs must provision minimum bandwidths to the separated CVCs that support TC-4 bundle services to maintain advertised speeds in excess of the per SIO averages required with scale. At this point, there will be a cost decision to move the services to a higher speed tier on the NBN supply side and provide the end user with the speed of service acceptable to their needs being a lower tier. Managing CVC capacity will continue to create unnecessary complexity and inefficiencies for RSPs, adding to pricing pressures. From Vocus' perspective, CVCs will need to be split so we can control usage in line with advertised offers and reduce exposure to variable customer demand for TC-4 bundled offers. Vocus will still need to invest in staff and systems to manage traffic given the retention of the CVC pricing construct. These inefficiencies further contribute to pricing pressures that are not in the interests of consumers. Vocus would prefer to be able to focus on innovation and delivering a good customer experience.

Vocus maintains that NBN Co should remove the CVC construct across all speed tiers to simplify both pricing and network management.

Vocus also submits that NBN Co's proposals on price certainty do not go far enough to meaningfully assist RSPs in business planning. To better promote the long-term interests of consumers, NBN Co's should provide a binding tariff list that applies for the next three financial years, and not one limited only to the forthcoming financial year.

Service quality

NBN Co's core commitments on service quality remain unchanged from those set out in its wholesale broadband agreement (WBA4) published in December 2020. Nevertheless, NBN Co proposes for its prices to continue to increase. To ensure issues currently faced by consumers are addressed, NBN Co needs to commit to service standards that go beyond those set out in WBA4 and are accompanied by penalties for failure to meet those standards.

One area NBN Co needs to improve is in how it deals with modify orders. Operational support for exceptions is inadequate and relies on continued escalation, leading to poor customer experience. The movement of services likely to result from NBN Co's proposed change to the pricing and product construct will exacerbate these existing issues. NBN Co will need to be able to support a significant increase in modify orders which will flow from RSPs managing customer experience and costs.

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