Submission

Discussion Paper on the WIK Mobile
Network and Cost Model
to inform the
MTAS Pricing Principles Determination
1 July 2007 to 30 June 2009

Rosemary Sinclair

Managing Director

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Introductory Comments

Mobile termination access service pricing has been a key issue for ATUG for a number of years. ATUG's submission to the ACCC Mobile Services Review 2003 included a focus on the need for regulatory intervention to reduce mobile termination rates to cost-based prices given the lack of competitive pressure in this area of the mobile market.

ATUG's comments on the Draft Decision on MTAS in March 2004 presented information indicating that market based mechanisms were not bringing MTAS prices in line with costs. ATUG reported (using Telstra Annual Report data) that the average retail price for a fixed to mobile call was 40 cents per minute in 2000 and had only reduced to 38 cents per minute in 2003.

ATUG also referred to work in other jurisdictions addressing the same issue which resulted in regulators mandating price reductions for MTAS.

ATUG supported the ACCC decision to continue declaration of mobile termination access services and to move away from the retail benchmark pricing principle towards a "target" price, ahead of a more detailed bottom-up cost analysis. This has now been provided by the WIK Consult group.

ATUG accepted the glide path approach to reductions (although we suggested an earlier timeframe of January 2006) and agreed that the end point of 12 cents per minute at January 2007 was at the upper end of the cost range. Research among ATUG members for the 2004 submission suggested 8 cents per minute for the initial end point.

Current price change data (again based on Telstra's Annual Report as at June 2006) suggests very slow flow through to retail of mandated price reductions. Average prices paid for fixed to mobile calls for 2006 were 33 cents per minute compared to 38 cents per minute in 2003. Relevant extracts are attached to this submission.

If mobile carriers had implemented the mandated pricing, ATUG would have expected to see greater reductions in prices at retail, particularly given the power of the corporate customer to secure better than average price reductions.

ATUG is not aware that the ACCC Annual Report on Changes in Prices Paid for 2005-2006 has been released but the 2004-2005 report suggests very slow reductions in retail prices by comparison with other call services, as below:

Prices paid by PSTN consumers, on average, for basic access increased in 2004–05 by 5.2 per cent—the smallest increase since carriers began changing the price structure of PSTN services by increasing the fixed price of basic access while decreasing the price of per-call services or 'rebalancing'. Basic access charges in the overall PSTN index have increased by 43 per cent since 2000–01 and 79.4 per cent since 1997–98. Figure 4.2 further shows that the process of rebalancing and restructuring PSTN charges has resulted in the share of consumers' total expenditure on PSTN services spent on basic access doubling from 19 per cent in 1997–98 to 40 per cent in 2004–05.

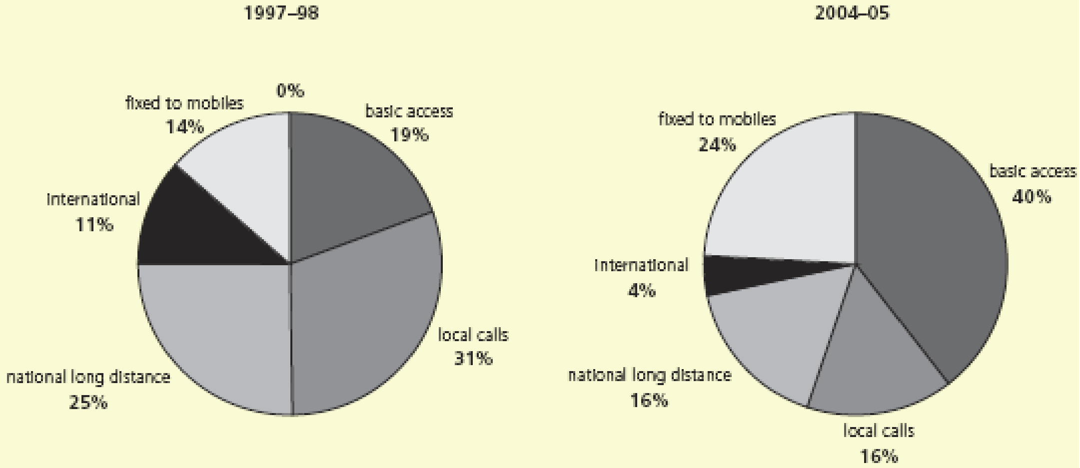
Table 4.1 Percentage change in the PSTN services index by service type from 2000–01 to 2004–05

	2000–01	2001–02	2002–03	2003–04	2004–05
Basic access	15.2	13.2	12.4	6.8	**5.2**
Local calls	–17.9	–11.7	–3.8	–3.3	**–7.7**
National long-distance	–6.3	–8.7	–4.7	–1.9	**–3.1**
International	–17.2	–15.3	–5.8	–5.9	**–4.4**
Fixed-to-mobile	–6.2	–3.2	–2.4	–2.2	**–3.8**
PSTN services index	–5.8	–2.6	1.0	0.2	**–1.2**

Source: data supplied by Telstra, AAPT, Primus, Optus (except 2001–02 data, which was excluded from the index) and (until 2000–01) One.Tel.

The price of local calls fell by 7.7 per cent in 2004–05, 24.3 per cent since 2000–01 and 43.9 per cent since 1997–98. Figure 4.2 shows that between 1997 and 2004–05 the proportion of consumer total expenditure on local calls halved from 31 per cent to 16 per cent again due to carriers rebalancing call and access charges.

Figure 4.2 Comparison of share of total consumer PSTN expenditure by service 1997–98 and 2004–05



Source: data supplied by Telstra, AAPT, Primus, Optus (except 2001–02 data, which was excluded from the index) and (until 2000–01) One.Tel.

The report also shows the increasing component that fixed to mobiles calls are of total consumer expenditure, hence the continuing interest by ATUG and our members in this issue.

Comments on the WIK Model

ATUG supports the use of the WIK bottom-up engineering-economics TSLRIC model for determining the appropriate pricing principles for the proposed timeframe of two years up to 30 June 2009.

ATUG welcomes the comments of the consultants at page 6:

"It should not be the aim …to sacrifice the efficiency merits of bottom-up modelling by inflating and/or averaging cost model results to the cost 'realities' of specific carriers, particularly if these realities reflect inefficiencies."

ATUG accepts the WIK model approach at page 25 that "..the WIK MNCM takes great care to ensure that all relevant costs, but no more, are taken into account and are appropriately allocated to the various services."

End users understand that operators need to be covering costs appropriately to ensure the right incentives remain for innovation and investment. ATUG's view is that allowing over-recovery of costs works against these incentives.

ATUG accepts the findings of the WIK cost model assessment, noting that at various decision points the WIK model takes a conservative position allowing higher costs for operators than an alternative view would support. Examples include Cost of spectrum (3.5), Working Capital (3.6), Fixed-mobile integration (3.7), Integration 2G and 3G (3.8), exclusion of Government subsidies (3.10), site sharing assumptions (5.3.4), current replacement values for equipment (5.3.6), Telstra wholesale leased line price averages (5.3.7.), and 10% mark-up for common organisational costs (5.3.10).

ATUG supports the use of international modelling for reference purposes to benchmark outcomes for the WIK model Australian market data.

Comments on Scenarios

The scenarios reflected in Table 6-4 suggest model costs of around 6 cents per minute would mitigate various risks and uncertainties, using the 25% market share assumption.

A higher market share of 31% drives higher traffic and lower costs of 5.3 cents per minute. Market share of 44% drives costs down to 5 cents per minute. Integrated operators have lower costs also at 5.5 cents per minute.

International Benchmarks

The subject of termination rates remains under discussion in Europe in the context of international roaming (rather than fixed to mobile) prices.

A report by the European Consumers' Organisation BEUC in February 2007 addresses many of the same issues concerning ATUG in the context of fixed to mobile prices.

One point of particular concern is the comment that wholesale reductions are not being passed onto consumers. ATUG understands that this is a separate issue from modelling the level of costs. However, if modelling costs and mandating reductions does not flow through to consumers, the economic benefits at which the intervention is directed will not be achieved.

It is for this reason the discussion in the EU has shifted to retail price measures.

The BEUC report includes January 2006 data on mobile termination rates showing average 10 Eurocents for France, 11 Eurocents for Germany, and 8 pence for UK – Table on page 8/48.

The report is attached to the submission as a separate pdf.

Conclusions

ATUG's view in 2004 was that initial glide end point should be 8 cents per minute. Given the detailed analysis of the model some 3 years down the track, a figure around 6 cents per minute suggested by the WIK model is a reasonable assessment of costs and should be introduced immediately.

On the problem of "pass through", the lack of recent price information from the ACCC Annual Report on Changes to Prices Paid 2005-2006 means it is not possible to get an industry –wide view of flow through to consumers. As outlined above the Telstra results (used as an example) suggest that retail prices are not reflecting the termination rate reductions in full.