

TELSTRA CORPORATION LIMITED

Response to the Commission's Discussion Paper into whether wholesale ADSL services should be declared under Part XIC of the *Competition and Consumer Act 2010*

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01 EXECUTIVE SUMMARY

1. Telstra welcomes the opportunity to respond to the Australian Competition and Consumer Commission's (**Commission's**) Discussion Paper into whether wholesale ADSL services should be declared under Part XIC of the *Competition and Consumer Act 2010* (**Discussion Paper**).
2. Telstra has argued previously, and maintains, that declaration of wholesale ADSL is unwarranted. Such declaration would neither promote competition nor encourage efficient investment in infrastructure, and would not be in the long term interests of end users (**LTIE**).

1.1. Declaration of the wholesale ADSL service is unnecessary and would not promote the LTIE

3. The broadband market is already highly competitive. There is substantial facilities-based competition, particularly in CBD and metropolitan areas. Telstra's competitors actively and aggressively compete with Telstra on a national basis using alternative technologies (including the Unconditional Local Loop Service (**ULLS**) and Line Sharing Service (**LSS**), both of which are declared, as well as wireless technology) and offer the same retail products as Telstra does across a broad geographic footprint. Declaration of the wholesale ADSL service would only serve to limit the incentives for access seekers to invest in DSLAMs and other alternative infrastructure. For these reasons, the Commission does not have a sufficient evidentiary basis to conclude that the jurisdictional threshold for declaration under s 152AL of the *Competition and Consumer Act 2010* (**CCA**) – promotion of the LTIE – is satisfied. On the contrary, declaration would harm the LTIE by dulling incentives for investment by all parties, including Telstra.
4. In April 2011, the Commission advised industry that it did not intend to conduct a wholesale ADSL declaration inquiry at that time, but would adopt a "wait and see" approach. Telstra has since sought to address concerns raised by access seekers by making a number of commitments in relation to the wholesale ADSL service in its Structural Separation Undertaking (**SSU**) (which was submitted to the Commission on 9 December 2011). The wholesale ADSL provisions contained within the SSU – together with the Overarching Equivalence Commitment set out in section 9 of the SSU – impose obligations which are equivalent to the Standard Access Obligations (**SAOs**), and commit Telstra to publishing a reference price in line with RMRC principles set out in the SSU. The SSU also contains additional transparency measures around the disclosure of wholesale ADSL service agreements which mirror the contract disclosure requirements applicable to declared services under Part XIC of the CCA. In light of these SSU commitments, Telstra considers that declaration of the wholesale ADSL service is unnecessary.
5. With the Commission having said that it would "wait and see", the Discussion Paper does not raise anything new which warrants the step of declaration. If the reason is Telstra's SSU,¹ the Commission's acceptance of Telstra's SSU is not predicated upon, and does not require, the declaration of wholesale ADSL. The Commission has itself noted that, although both inquiries (being the inquiry into whether or not to accept Telstra's SSU and the inquiry into whether or

¹ See the Commission's press release entitled "ACCC receives revised structural separation undertaking from Telstra", dated 9 December 2011.



not to declare wholesale ADSL) are concurrent, they are discrete.² The Commission would be in error if it declared wholesale ADSL merely because of the SSU inquiry process. The content of the SSU is reason not to declare wholesale ADSL at all.

6. Telstra strongly rejects any suggestion that the pricing of its wholesale ADSL service, and the terms and conditions upon which it supplies the service, are anti-competitive. Telstra negotiates with its wholesale customers in relation to the pricing of wholesale ADSL. It does not force customers to acquire resale services from Telstra, or to refrain from investing in their own ULLS/LSS-based infrastructure, and nor could it. [c-i-c commences] [c-i-c] [c-i-c ends]. Instead, customers negotiate wholesale ADSL prices with Telstra in the context of a competitive market and the relative efficiency of the wholesale customer pursuing alternative supply opportunities. This is a competitive market at work. It is both commercially rational and economically efficient.
7. Further, Telstra is not “leveraging” its position in the market by imposing pricing policies aimed at discouraging its competitors from investing in infrastructure where it is efficient to do so. The fact that there has been substantial DSLAM rollout is proof that this is not the case.

1.2. If the wholesale ADSL service is to be declared, the Commission should carefully consider the scope of the declaration and the wording of the service description

8. If, notwithstanding the lack of a proper basis, the Commission is minded to declare the wholesale ADSL service, careful consideration should be given to the scope of the declaration. While Telstra agrees with the Commission that the relevant market is national in scope, it does not consider that declaration is warranted (or would be in the LTIE) in areas within that market where there has been, or could be, competitive DSLAM rollout. Telstra submits that, as a minimum, the declaration should not apply to ESAs which meet (a modified form of) the competitive criteria established by the Australian Competition Tribunal (**Tribunal**) in relation to the WLR, LCS and PSTN OA exemptions *and* which have at least three major providers of wholesale DSL services. There are currently 285 ESAs which satisfy this threshold.
9. Furthermore, if the wholesale ADSL service is declared, it is critical that the service description is appropriate. In this regard, Telstra has proposed a number of amendments to the draft service description in the Discussion Paper. These amendments will ensure that the service is described in a manner which provides sufficient clarity and aligns more closely with the Minister's *Telecommunications (Regulated Services) Determination (No. 1) 2011*, which defines the service for the purposes of the SSU.

1.3. If the wholesale ADSL service is declared, the declaration should expire on 31 July 2014

10. If the Commission proceeds to declare the wholesale ADSL service, Telstra considers that the declaration should align with the declaration of the fixed line services and expire on 31 July 2014. This would provide an opportunity for both the Commission and industry to assess whether continued declaration of the service is necessary, particularly in the context of the continued roll out of the NBN.

² Commission, *Telstra's Structural Separation Undertaking - Discussion Paper*, December 2011, p. 11.



1.4. The Commission should employ a pricing methodology appropriate to the circumstances

11. The Commission states that if it were to declare the wholesale ADSL service, it would initially set prices in an Interim Access Determination (**IAD**) using a RMRC methodology. Telstra agrees that, in the context of a competitive broadband market and nationally consistent retail pricing, a RMRC methodology would be the most effective and fastest methodology to implement in an IAD. This approach – which has already been subject to public consultation – was the approach adopted by Telstra in the SSU. Telstra's RMRC methodology could easily be implemented in an IAD by cross-referring to the schedules of the SSU.
12. The price points calculated by Telstra's RMRC methodology are:
 - a. wholesale ADSL port prices of \$30 and \$37 per service per month in Zone1 and Zones 2/3 respectively; and
 - b. AGVC pricing of \$55 per Mbps per month.
13. These price points deliver considerable savings for the majority of wholesale customers.

02 STRUCTURE OF THIS SUBMISSION

14. This submission is divided into the following parts:
- a. Part 3 of the submission explains why declaration of the wholesale ADSL service is unnecessary, in light of:
 - i. the state of competition in the relevant market;
 - ii. ongoing facilities-based investment by access seekers; and
 - iii. the commitments given by Telstra in the SSU;
 - b. Part 4 of the submission sets out Telstra's position in relation to the geographic scope of the proposed declared service;
 - c. Part 5 of the submission examines Telstra's suggested amendments to the Commission's proposed service description for wholesale ADSL;
 - d. Part 6 of the submission addresses the appropriate duration of a declaration of the wholesale ADSL service;
 - e. Part 7 of the submission deals with the appropriate pricing methodology to employ in an IAA;
 - f. Annexure A to this submission contains Telstra's responses to the Commission's questions in the Discussion Paper;
 - g. Annexure B to this submission contains data on the "285 ESAs"; and
 - h. Annexure C to this submission contains the confidential expert report of [c-i-c] **commences** [c-i-c] [c-i-c ends], dated January 2012.
15. Where this submission does not address or respond to a particular conclusion proposed by the Commission in its Discussion Paper, this does not mean that Telstra agrees with that conclusion.

03 DECLARATION OF WHOLESALE ADSL IS UNNECESSARY

3.1. The wholesale ADSL service should not be declared

16. Telstra considers that the declaration of wholesale ADSL is not in the LTIE.³ This is because such declaration would not promote competition or encourage economically efficient use of, or investment in, infrastructure.
17. There is insufficient evidence before the Commission to support a conclusion that intervention in the market for wholesale ADSL (via declaration of the service) is warranted. Recent market data suggests that the national market is highly competitive and access to wholesale ADSL services is being successfully negotiated on commercial terms. Declaration of wholesale ADSL would risk compromising or reversing these positive market developments and, in so doing, would harm the LTIE.
18. In addition, in light of the commitments given by Telstra in the SSU, declaration of the wholesale ADSL service is an unnecessary regulatory step. To the extent access seekers' complaints regarding Telstra's supply (and pricing) of wholesale ADSL services are valid (which Telstra disputes), these complaints are adequately addressed via the SSU, or under Part XIB of the CCA.
19. Following a consultation in 2010-11, the Commission concluded that it was unnecessary to commence an inquiry into the declaration of wholesale ADSL.⁴ All of the issues now raised by the Commission in its Discussion Paper were known by the Commission at that time. Since then, the exemptions in respect of WLR, PSTN OA and LCS have been revoked, providing for a significant reduction in the price of the LSS/voice bundles for wholesale customers. In light of these developments (and for the reasons set out below), and consistent with the Commission's previous position, the Commission should not declare wholesale ADSL.

3.2. There is insufficient evidence to support the declaration of wholesale ADSL

20. Declaration of a service is a significant intervention in any market. In assessing whether declaration of a service is appropriate (and would promote the LTIE, as required by s 153AL(3)(d) of the CCA), the Commission must consider (and weigh up) all available market evidence.
21. Telstra considers that, based on the available market evidence, it is untenable for the Commission to conclude that declaration of wholesale ADSL would advance the LTIE. Data on Telstra's current market share and Access Seeker complaints regarding Telstra's alleged price discrimination and leveraging form an insufficient evidentiary basis to support a conclusion that declaration of wholesale ADSL is in the LTIE. On the contrary, all available data (including the data set out in sections 3.3 and 3.4 of this submission) suggests that the market for wholesale ADSL services is, in fact, highly competitive. Consistent with the Commission's intention to adopt a more commercial (and less theoretical) approach to competition issues,⁵

³ Contrary to s 152AL(3)(d) of the CCA.

⁴ See the Commission's letter dated 18 April 2011.

⁵ Patrick Durkin, "ASCC vovs to get real on corporate deals", *Australian Financial Review*, 16 January 2012.

the Commission should conclude that intervention in the market (via declaration of wholesale ADSL) is unnecessary and may stifle the incentives for investment that have driven positive competitive outcomes to date.

22. In addition, the Commission's acceptance of the SSU does not require or depend upon its declaration of wholesale ADSL. As the Commission has acknowledged, its respective decisions in relation to the declaration of wholesale ADSL and acceptance of the SSU are discrete.⁶ If the Commission concludes that declaration of wholesale ADSL is not in the LTIE (as Telstra submits), its decision with respect to the SSU would not be affected. In fact, a decision to accept the SSU would be reason not to declare wholesale ADSL.

3.3. Competition in the relevant markets is effective

23. Telstra does not agree with the Commission that there are competition concerns in the national broadband market that require the wholesale ADSL service be declared.
24. Telstra agrees with the Commission that the relevant market to be considered in the context of this inquiry is national. Telstra competes nationally in supplying broadband services to end users, including by offering nationally consistent retail prices. However, contrary to the conclusion reached by the Commission in the Discussion Paper, the relevant (national) broadband market is already highly competitive. This view is supported by the market data presented below, together with the submissions set out below.
25. Telstra is effectively constrained in its supply of wholesale services by other providers' supply of broadband internet services using a range of alternative methods and technologies. Competitors are able to effectively compete – and are competing – with Telstra via the following means:
- a. through alternative fixed networks (including fibre and HFC networks) owned by providers other than Telstra;
 - b. through the use of ULLS and LSS (both of which are declared). For each of these services, price and some non-price terms and conditions are set by Final Access Determinations;
 - c. by acquiring wholesale ADSL from Telstra on commercial terms. As outlined below, Telstra has made a number of commitments in relation to the provision of wholesale ADSL in the SSU;
 - d. by acquiring wholesale ADSL from Telstra's competitors, which either own fixed networks or supply services through the use of LSS and ULLS; and/or
 - e. through non-Telstra owned wireless networks (which are highly competitive both within and outside CBD/metropolitan areas). The use of wireless technology is continuing to grow as a competitive threat to fixed network technology, particularly with the increasing popularity of end user devices such as the iPhone, iPad and competing products.

⁶ Commission, *Telstra's Structural Separation Undertaking - Discussion Paper*, December 2011, p. 11.

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26. The competitiveness of these alternative supply methods is demonstrated by the following data:
- a. throughout CBD, metropolitan and some regional areas, access seekers have installed DSLAM infrastructure enabling them to provide broadband and other services via the ULLS and LSS. To date, access seekers have deployed DSLAM-based infrastructure in around 580 ESAs (an increase from 478 in September 2007);
 - b. in the CBD and inner-metropolitan areas of Australia's major capital cities, several companies have deployed point-to-point fibre networks and fibre loops, which are able to provide a full suite of broadband, voice and video services to end users without recourse to the Telstra CAN. In greenfield estates, several of Telstra's competitors (such as Opticomm) have deployed their own fibre to home networks for the provision of broadband and other services to end users within those estates;
 - c. throughout Sydney, Melbourne and Brisbane, Optus has deployed a HFC network capable of providing broadband services of up to 100Mbps (well in excess of the speeds able to be provided via ADSL2+ services), covering more than 1.2 million premises. A similar HFC network is operated by TransACT (now owned by iiNet) in parts of regional Victoria and Canberra; and
 - d. in addition to these fixed line alternatives, Telstra, Optus and Vodafone Hutchison Australia (VHA) have deployed mobile wireless networks capable of providing broadband speeds to more than 96 per cent of Australia's population (with Telstra recently launching LTE-based services capable of providing speeds in excess of those provided over ADSL2+ services). Vividwireless has deployed a fixed wireless, WiMAX-based network in Perth, Sydney and Melbourne, which is also capable of providing broadband services to end users.
27. The intense competition in CBD and metropolitan areas (driven by the factors described above) has the effect of forcing the national price of Telstra's retail ADSL downwards. By virtue of Telstra's national pricing policy, the benefits of vigorous competition in CBD and metropolitan areas are experienced across Australia nationally. Regional customers are offered the same, competitive prices as are available in the CBD (notwithstanding the fact that the costs associated with providing services in regional areas are substantially higher).
28. Notably, as the relevant market encapsulates both actual and potential competitors, the current absence of facilities-based competition in any particular area is not indicative of a lack of competition more broadly.

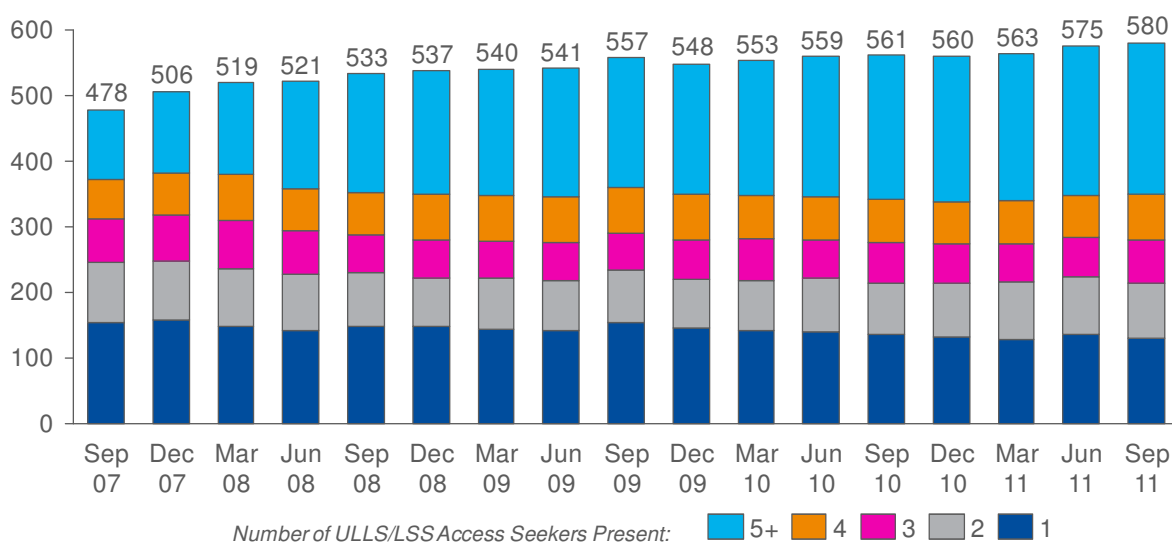
3.4. Facilities based competition is economically efficient and is in the LTIE

29. Telstra considers that declaration of wholesale ADSL would not promote efficient investment in infrastructure.
30. On many occasions, the Commission has expressed the view that facilities-based competition (where feasible) is preferable to resale-based competition. Contrary to this approach (and as the Commission acknowledges on page 23 of the Discussion Paper), declaration of wholesale

ADSL may cause access seekers to reconsider planned deployment of DSLAM infrastructure. More broadly, such declaration would stifle the incentives for competitors to invest in DSLAMs in regional and rural areas (which have previously been limited by de-averaged ULLS pricing) by discouraging existing facilities-based competitors from building, and continuing to invest in, their own networks. Declaration of wholesale ADSL would also reduce incentives to invest in alternate infrastructure to deliver retail broadband services, such as wireless technology.

31. Further, all available evidence suggests that facilities based competition continues to increase. In September 2011, access seekers had a DSLAM presence in 580 ESAs. This is a substantial increase from the 478 ESAs in which access seekers had a DSLAM presence in 2007.

Expansion and deepening of ULLS and LSS based entry across the CAN



32. Particularly (but not only) in CBD and metropolitan areas, Telstra is constrained in its supply of wholesale ADSL by the aggressive offers of its competitors, which are supported by the regulated pricing of ULLS and LSS. In addition, the construction of new NextGen networks in rural and regional areas (sponsored by the provision of Government grants) is already facilitating further competition in these areas. Telstra is aware of competitive builds which have either been completed or are underway in 16 exchanges passed by the Regional Backhaul Blackspot Program. This number could increase further.
33. Further, it is through facilities-based competition that industry is delivering services such as carrier-grade VoIP, Naked DSL, Annex-M (high speed upload), IP-TV and other services. Access seekers' investment in DSLAMs and related infrastructure (in conjunction with the ULLS and LSS) enables them to provide more features and varied services, as well as increase the quality of those services, as compared with services provided over wholesale ADSL. This ability to offer differentiated and innovative services (as well as controlling and operating a greater proportion of the service value chain) has led many service providers to shift from predominantly resale-based offerings to offering services over unbundled lines (ULLS and LSS). It is not possible to offer a comparable range of services (or the same range of pricing options and offers) over wholesale ADSL.

[c-i-c commences] [c-i-c] [c-i-c ends]

34. Access seekers' continuing shift to ULLS and LSS is confirmed by Ericsson Australia's broadband strategy manager, Colin Goodwin, who has indicated that:

"Research revealed [last year's record DSL line sales] was due to many of our ISP customers aggressively moving subscribers off wholesale DSL services and onto their own DSLAMs. By doing so they are able to offer differentiated products, together with more advanced and profitable retail services. Today this includes IPTV services alongside internet access and telephony".⁷

35. It is similarly confirmed by data illustrating (for example) a steady increase in the number of VoIP lines supplied by access seekers. iiNet's VoIP lines have more than tripled since June 2007, to a total of 178,000 lines.⁸
36. Further, recent analysis undertaken by Telstra comparing the voice and broadband plans available in the market in September 2007 and now reveals that the number of players offering voice and bundled services through the ULLS has increased, with TPG, iiNet, and Internode entering the market since September 2007. In particular, the number of data offerings has increased exponentially, with the median data allowance included in bundled plans increasing 2,627% from 5.5 GB to 150GB.
37. In addition to greater competition at the retail layer, DSLAM-based infrastructure has also led to greater competition – and expanded service offerings – at the wholesale layer. For example, Optus and iiNet supply naked DSL resale services to wholesale customers.

3.5. Deployment of the NBN does not significantly change the environment

38. Despite the impending deployment of the NBN, the continued promotion of efficient investment in infrastructure remains important. Irrespective of the Commission's views regarding the costs of DSLAM investment (and the time frames for recovery of those costs), it is patently clear that, given the rollout of the NBN is not expected to be completed until at least 2018, any investment in DSLAM-based infrastructure would be recovered well before that time.
39. The Commission's suggestion that the NBN "may lessen incentives for investment in DSLAM infrastructure"⁹ is contradicted by both market data¹⁰ and public statements which access seekers have made. Progress in the deployment of the NBN appears to be reinvigorating access seeker investment in fixed line services, particularly with respect to core network infrastructure and systems to support IP-based voice, data and IP-TV services. For example, on 25 October 2011, Optus' then Director of Government and Corporate Affairs, Mr Maha Krishnapillai, addressed the Senate's Joint Committee on the NBN as follows:

⁷ *Communications Day* Issue 4012 (30 June 2011).

⁸ This is consistent with iiNet's stated strategy to offer voice, broadband and other services of its DSLAM infrastructure, as outlined by iiNet's Managing Director, Michael Malone, in February 2010 (cited in *Communications Day*, 22 February 2011, p. 2).

⁹ Discussion Paper, p. 16.

¹⁰ As set out in section 4 of this submission.

CHAIR: *From a commercial entities point of view, how are you dealing with a decade-long build in a fairly uncertain policy environment based on the politics of the day? How do you risk-manage that in a commercial sense?*

MR KRISHNAPILLAI: *We are certainly not stopping - to return to the senator's point earlier - investing in HFC networks or ULL networks. We are continuing to invest in and continuing to offer those services to our customers..."*

40. Similarly, at the iiNet Open Day in Perth in October 2011, iiNet's NBN Product Manager, Gary Chappell, suggested that despite the planned NBN rollout, DSLAM infrastructure will remain relevant for several years to come. He indicated that iiNet would continue to build more DSLAMs based on customer demand for ADSL2+ services, stating:

"It's going to take a while to get everybody off the DSLAM and we're not planning to move everybody off on day one... We look at every site individually and if we have customer growth there we will need to upgrade the DSLAM there... It's business as usual for us."¹¹

41. While the impending rollout of the NBN may be causing incremental change to the *nature* of access seekers' investment decisions, it is clear that it is not arresting investment altogether. Whilst access seekers have no incentive to invest (and are no longer investing) in analogue voice services (as this is now "old technology"), their investment in digital alternatives which are compatible with the NBN – particularly carrier-grade VoIP – is accelerating. Importantly, investments in core network technologies will not be stranded when access seekers look to transition their customers to NBN-based access. This is why ULLS-based investment is promoted, rather than hindered, by the NBN.
42. In addition, the supply of bundled voice and broadband services continues to be a viable and efficient commercial supply option, including in the lead up to the NBN rollout. This was acknowledged by the Commission in its Final Report on the Exemptions Variation Inquiry (dated 16 December 2011).¹²
43. Given this, it does not appear to Telstra that the roll-out of the NBN raises sufficient concerns for the Commission to justify the declaration of wholesale ADSL.

3.6. Telstra's commercial pricing of wholesale ADSL does not reflect leveraging conduct

44. In the Discussion Paper, the Commission has expressed particular concern regarding the potential for price discrimination:
- via the imposition of minimum spend or volume commitments; or
 - against access seekers which use their own infrastructure, or which source supply from an alternative access provider.

¹¹ Spandas Lui, "iiNet to continue ADSL2+ investment despite NBN", *ARN*, 25 October 2011; see also Clancy Yeates, "Turnbull's NBN claim rejected", *Sydney Morning Herald - Business Day*, 25 May 2011, which reports that iiNET is investing in DSLAM infrastructure at Geraldton in Western Australia (an NBN test site).

¹² Discussion Paper, p. 35.

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45. Telstra's pricing of wholesale ADSL reflects the outcomes of complex bilateral negotiations with its wholesale customers. [c-i-c commences] [c-i-c].
46. [c-i-c] [c-i-c ends]. Additionally, some customers have a greater propensity to competitively bypass Telstra altogether, because they may themselves be more efficient, and so bring a greater bargaining position to the negotiations. [c-i-c commences] [c-i-c] [c-i-c ends].
47. However, differences in the individual price terms and conditions upon which wholesale customers purchase ADSL from Telstra should not be viewed as problematic from a competitive perspective. Such differences simply reflect the varying requirements of Telstra's respective customers and/or the specific circumstances that arise from a particular supply. This was recognised by the New Zealand Commerce Commission (NZCC) when it said that "different treatment does not of itself amount to discrimination"¹³ and "something more than a mere difference"¹⁴ is required. The NZCC has further suggested that pricing, quality, technical means of access, physical means of access and delays in the provision of access are all areas in which differences might legitimately arise.¹⁵
48. The Commission's concerns are discussed further below.

3.6.1. There is no systematic wholesale ADSL price discrimination on the basis of volume or build

49. [c-i-c commences] [c-i-c] [c-i-c ends].

3.7. Even if there was a systematic discrimination, Telstra's proposed SSU price points would eliminate it

50. [c-i-c commences] [c-i-c] [c-i-c ends].

3.8. To the extent that wholesale ADSL price discrimination occurs, it is likely to be pro-competitive

51. The Commission's concern appears to be that Telstra is discounting to resellers relative to builders to prevent those resellers from becoming builders. Even if such conduct was occurring, it would more than likely be pro-competitive.
52. To the extent that there are examples of wholesale ADSL price discounting, the additional competition that arises as a result of an instance of discounting would most likely be greater than any additional competition that might arise absent the discounting. Indeed, preventing discounting might reduce competition.
53. Assume that discounting wholesale ADSL prices discouraged an individual reseller from building a ULLS/LSS network. Unless the firm is acting irrationally, it would have a lower cost base with discounted wholesale ADSL prices than it would have if it built its own ULLS/LSS

¹³ New Zealand Commerce Commission, *Consultation on draft guidance on Telecom's non-discrimination obligations under the Telecom Separation Undertakings*, December 2009, p. 5.

¹⁴ New Zealand Commerce Commission, *Overview of Telecom Non Discrimination Obligations*, 24 March 2011, p. 1.

¹⁵ New Zealand Commerce Commission, 2009, op cit, p. 8.

network. With a lower cost base the firm would be able to compete more intensely for retail ADSL customers and apply greater retail price pressure on other competitors.

54. Now assume the counterfactual, whereby the firm is not offered a wholesale ADSL discount and, instead, decides to build a ULLS/LSS network. The firm would face a higher cost base and greater risk (given the capital outlays required). It would also most likely be building ULLS/LSS networks in ESAs where there are already multiple ULLS and LSS builders.¹⁶ In this context, it is hard to believe that such a firm would impose any greater competitive pressure on ULLS/LSS incumbents in the market relative to the case where the firm faced a lower (discounted wholesale ADSL) cost base.
55. Further, any remedy that would prevent such discounting would likely be inconsistent with the legislative criteria relevant for declaration. Wholesale customers have different business models, different customer profiles, make different technology choices and have different cost bases. Different wholesale prices reflect these different circumstances.
56. In addition, some wholesale customers are more efficient than others. In negotiating the wholesale ADSL price, more efficient wholesale customers tend to pose a greater threat of bypassing Telstra's wholesale ADSL supply by building a ULLS/LSS network. The fact that Telstra has to respond to such a threat is a strong sign of the competitiveness of the market. More efficient firms are rewarded for their efficiency. Should all firms face the same rewards, regardless of their efficiency, then there would be little incentive for those wholesale customers to compete for additional efficiencies and little chance of the additional efficiencies being passed on to end users in the form of lower prices and better services.

3.9. Early termination charges

57. The Commission questions whether early termination charges (**ETCs**) are likely to prevent wholesale customers from moving to alternative networks. Currently, Telstra charges an ETC if an End User Access is disconnected by the wholesale customer within 6 months of activation.¹⁷ If a wholesale customer decides to shift customers over to an alternative network, only those end users who have been connected within the last six months would attract an ETC. This is likely to be a very low proportion of the base of any wholesale customer's end users. Even so, the process of switching to an alternative network is likely to be undertaken over a period longer than six months. Accordingly, to the extent that wholesale customers sign up new end users prior to switching their wholesale ADSL customer to an alternative network, they can avoid the ETC by shifting the new customers directly on to the alternative network rather than using wholesale ADSL services for a period of less than 6 months and then shifting them to the alternative network.

3.10. The SSU will address the Commission's concerns

58. Even if the concerns raised by the Commission in relation to Telstra's supply (and pricing) of wholesale ADSL services (addressed above) were valid, Telstra considers that those concerns are misconceived in light of the commitments it has given in the SSU. Under clause 9 of the

¹⁶ Refer to the figure below paragraph 31, above, entitled "*Expansion and deepening of ULLS and LSS based entry across the CAN*".

¹⁷ Except where the End User Access is migrated to become a Telstra Wholesale Fibre Access Broadband Layer 2 Internet Grade Service.

SSU, Telstra provides an “overarching equivalence commitment” pursuant to which it undertakes to provide technical, operational, information and pricing equivalence to access seekers. In addition, clause 18 of the SSU (which deals with price equivalence and transparency) provides for the following:

- a. Telstra will supply wholesale ADSL if requested to do so by a wholesale customer;¹⁸
- b. Telstra will publish and maintain a Reference Card with Reference Prices, which will be calculated and updated using RMRC principles as set out in schedule 8 of the SSU, and will supply wholesale ADSL at the Reference Prices to wholesale customers;¹⁹
- c. Telstra will provide transparency for internal and external wholesale prices on fully allocated internal costs and revenues for wholesale ADSL;²⁰ and
- d. Telstra will provide agreements in relation to wholesale ADSL to the Commission.²¹

59. Further, Telstra has agreed to use equivalent order management to process all ADSL service orders, irrespective of whether the order comes from a retail business unit or a wholesale customer, so that service activation and provisioning (as well as fault rectification) for all ADSL services occurs in an equivalent manner.²² If Telstra develops a DSL upgrade, it will develop an equivalent upgrade to the relevant comparable wholesale DSL service.²³

60. These provisions of the SSU (which apply to Telstra’s supply of wholesale ADSL services) create a regime which is equivalent to the SAOs applicable to an active declared service under Part XIC of the CCA. For this reason, declaration of wholesale ADSL is unnecessary.

3.11. A complaint about leveraging conduct does not warrant declaration of wholesale ADSL

61. If the Commission receives complaints about the level of Telstra’s wholesale prices relative to its retail prices, those complaints should be investigated and dealt with in accordance with Part XIB of the CCA (as the Commission has done).

¹⁸ Clause 18.1(a).

¹⁹ Clause 18.3.

²⁰ Clause 18.4.

²¹ Clause 18.8.

²² Clause 11.3 of the SSU.

²³ Clause 15 of the SSU.



04 GEOGRAPHIC SCOPE OF SERVICE DECLARATION

62. If the Commission does decide to declare wholesale ADSL, then Telstra strongly believes that the declaration should be restricted to areas in which there has not been, or is unlikely to be, competitive DSLAM roll out. Although there is currently no ubiquitous fixed line alternative to Telstra's CAN, in many parts of Australia there are several alternatives to Telstra's infrastructure that are used by access seekers to supply competitive services to Telstra's retail and wholesale ADSL services. These alternatives are outlined in section 3.3, above.
63. In the presence of effective competition, regulated access is unlikely to promote the LTIE. "Effective competition" is described by Littlechild as a dynamic market process, characterised by eliminating excess profits, discovering more efficient methods of production, and determining what customers want.²⁴ Telstra considers that the concept of "effective competition" - which has been central to all recent economic and legal consideration of access regulation - is the appropriate theoretical framework against which the Commission should consider the geographic scope of any declaration of the wholesale ADSL service.
64. The concept of effective competition is a core objective of European telecommunications regulatory policy, and is encapsulated in the "Three Criteria Test" set out in a European Parliament Directive on a common regulatory framework for electronic communication networks and services. The "Three Criteria Test" - which has been applied by a number of European national regulatory authorities - assesses the need for regulation (and conversely, where regulation is not needed) as follows:
- a. the presence of high and non-transitory entry barriers, whether structural, legal or regulatory in nature;
 - b. markets the structure of which does not tend towards effective competition over the relevant time horizon; and
 - c. the application of competition law alone would not adequately address the market failures concerned.
65. Development in the deployment of alternative infrastructure has been uneven across Australia (with most competitive infrastructure concentrated in the CBD and metropolitan areas). As a result, there is a similar geographic unevenness in the competitive environment for the supply of wholesale and retail broadband services. The presence of extensive DSLAM-based infrastructure (together with mobile and fixed wireless broadband, direct fibre and HFC infrastructure) throughout much of metropolitan Australia means that there is deep, effective competition for the supply of broadband services in these areas.
66. In light of the extensive facilities-based competition (which is explored in section 3.4, above), Telstra considers that the Commission should restrict the scope of any declaration of

²⁴ Littlechild, S. "The Nature of Competition and Regulatory Process", *Intereconomics* 2011/1, pp. 10-17.



wholesale ADSL. In the following section, Telstra sets out two mechanisms by which the Commission might achieve such a restriction.

4.1. Applying the Commission's threshold for effective competition

67. Telstra considers that the Australian Competition Tribunal's (**Tribunal's**) threshold test for the WLR/LCS and PSTN OA exemptions provides a workable benchmark test as to whether a particular exchange is effectively competitive. Although the Tribunal's threshold test ignores competitive constraints arising from the presence of fixed wireless, HFC, Greenfield, CBD fibre and (most notably) mobile wireless broadband services, it nevertheless provides a robust and conservative methodology.
68. To adapt for the differences between the WLR/LCS/PSTN OA voice resale services and the wholesale ADSL service, Telstra proposes that the Tribunal's threshold test could be amended as follows:
- a. the test could take into account LSS lines (which were excluded in the context of examining competition and capacity with respect to voice services); and
 - b. rather than evaluating the market share of access seekers against the total number of CAN lines within an ESA, comparison could be made against the sum of the total number of Telstra-supplied DSL and unbundled (LSS and ULLS) services.²⁵
69. Applying this modified threshold, Telstra estimates that, as at September 2011 (the most recent period for which CAN RKR data is available), 361 ESAs would qualify as being effectively competitive with respect to DSL services (**361 ESAs**). Telstra submits that the 361 ESAs should be excluded from the scope of the declaration.
70. An examination of market data for the 361 ESAs clearly reveals their competitive characteristics:

²⁵ The Tribunal's threshold test only examined those retail and wholesale services it considered directly relevant to assessing whether or not an ESA could be construed as "effectively competitive" in the context of WLR, LCS and PSTN OA. Specifically, it examined data on the total number of basic access services within an ESA, the number of WLR services and the number of ULLS acquirers. However, in order to undertake a similar analysis for wholesale ADSL services, Telstra adapted the Tribunal's approach. The modified threshold is an ESA where there are:

- (1) Three or more ULLS or LSS –based competitors
- (2) An Aggregate Market Share equal to or greater than 30%; and
- (3) ULLS/LSS Spare capacity equal to or greater than 40% of WDSL SIOs in that ESA.

Where, *Aggregate Market Share* is calculated as the sum of ULLS SIOs, LSS SIOs, WDSL SIOs and ULLS/LSS Spare Capacity, divided by the Total number of DSL SIOs in that ESA. and *ULLS/LSS Spare Capacity* is calculated by reference to Tribunal's deeming rule (75% of ULLS and LSS SIOs).

[c-i-c commences] [c-i-c]

71. [c-i-c] [c-i-c ends].
72. Clearly, the presence of DSLAM-based infrastructure is impacting on DSL market outcomes at both the retail and wholesale layer. This is unsurprising given the extensive deployment of competitive DSLAM infrastructure within these ESAs. Although the Tribunal's threshold applies to ESAs in which there are at least three DSLAM-based service providers, [c-i-c commences] [c-i-c] [c-i-c ends].
73. The deepening of DSLAM-based infrastructure has resulted in more intense competition at both the retail and wholesale layer within the 361 ESAs. This is reflected in [c-i-c commences] [c-i-c] [c-i-c ends].
74. The competitive market outcomes within the 361 ESAs provide clear evidence of effective competition in those areas. It is unnecessary (and would not be in the LTIE) for any declaration of wholesale ADSL to extend to these areas.

4.2. A more conservative approach – accounting for resale competition

75. In its final decision on whether to maintain or remove the geographic exemptions in relation to WLR/LCS and PSTN OA services (**Final Decision**), the Commission expressed the view that it was necessary to look not only at market outcomes at the retail layer, but also at the wholesale layer.
76. Telstra does not agree that it is necessary for there to be an active competitive market for resale services in order to constrain Telstra (due to the competitive constraint provided by the threat of entry by infrastructure-based access seekers, coupled with the constraints imposed via self-supply of services). Nevertheless, it is clear that there is an active, highly competitive market for resale DSL services throughout metropolitan Australia. As the Commission noted in its Final Decision, *"There are a number of carriers, including Telstra, Optus and AAPT, which currently offer wholesale DSL services."*²⁶
77. If the Commission remains concerned that effective competition at the wholesale layer requires the active presence of major alternative resale DSL suppliers (in addition to Telstra), then the Commission could exclude from the wholesale ADSL declaration *only those ESAs in which there is active competition in the market for resale DSL services*. If such a limitation were adopted, the declaration would apply to all ESAs save for those in which Telstra Wholesale (and other DSL resale providers) face direct competition from alternative resale DSL providers, in addition to competition from access seekers self-supplying using the ULLS and LSS.
78. Based on publicly available information, three service providers with extensive DSLAM networks currently provide resale DSL services in direct competition with Telstra. These are Optus²⁷, TPG (which offers resale services through its Soul brand)²⁸ and iiNet (which provides wholesale DSL, and other services, using iiNet's extensive DSLAM network)²⁹.

²⁶ See p. 38 of the Final Decision.

²⁷ See <http://www.optus.com.au/porta/site/wholesale>.

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79. As at September 2011, Telstra estimates that 285 ESAs meet the modified Tribunal criteria (set out above) *and* have at least 3 major providers of wholesale DSL services (Telstra, Optus, iiNet or TPG) (**285 ESAs**).
80. Information on each of these 285 ESAs is set out in Annexure B.
81. As would be expected, the 285 ESAs exhibit highly competitive outcomes (even more so than the 361 ESAs). These outcomes are illustrated in the table below:

[c-i-c commences] [c-i-c]

82. [c-i-c].

83. [c-i-c] [c-i-c ends].

84. Within these 285 ESAs are the 16 Band 1 ESAs (**16 ESAs**) within Australia's major capital cities. The 16 ESAs are exempt from the WLR and LCS declarations and Telstra submits that (if it declares the wholesale ADSL service) the Commission should maintain consistency with existing declarations and exclude the 16 ESAs from the scope of the wholesale ADSL declaration.
85. Within the 16 ESAs, Telstra competes not only with self supply and resale supply based on ULLS and LSS services, but also faces competition from alternative fibre-based access networks. Although the presence of fibre infrastructure in CBD areas distinguishes the 16 ESAs from the majority of metropolitan (Band 2) ESAs – including the remaining 269 ESAs that meet the modified Tribunal criteria, and in which there are at least three major providers of wholesale DSL – a comparison of the market outcomes shows that they are similarly competitive to the remainder of the 285 ESAs. [c-i-c commences] [c-i-c] [c-i-c ends].

4.3. Conclusions on exclusion of the 285 ESAs from the scope of the declaration

86. Even if the Commission does not agree with Telstra's adaptation of the Tribunals' threshold criteria (used to determine the 361 ESAs) or the construction of the more conservative criteria that also assesses whether there are at least three major providers of wholesale DSL services in an ESA, Telstra maintains that all available market evidence supports the exclusion of the 285 ESAs.
87. A simple examination of the market structure in these ESAs (in terms of number of ULLS/LSS acquirers and number of retail and wholesale DSL service providers present in each ESA) and the market outcomes (in terms of the market shares of Telstra and unbundled service providers) clearly shows that those ESAs are effectively competitive. Therefore, if the Commission remains minded to declare wholesale ADSL, it should exclude the 285 ESAs identified in Annexure B from the declared service.

²⁸ See further <http://soulaustralia.com.au/wholesale/internet.html>.

²⁹ See <http://www.aapt.com.au/wholesale>.

05 WHOLESALE ADSL SERVICE DESCRIPTION

88. If the Commission decides to declare the wholesale ADSL service, it is critical that the service description adopted in the declaration is clear, workable and appropriate.
89. To ensure that the eligible service is described *"in a manner which provides sufficient clarity for application of the SAOs"*,³⁰ Telstra proposes the following amendments to the Commission's draft service description. These amendments will also align the service description more closely with the *Telecommunications (Regulated Services) Determination (No. 1) 2011 (Ministerial Determination)*.³¹
90. First, Telstra proposes inserting the words *"internet-grade best efforts"* into the description of *"asymmetric digital subscriber line access service"* to clarify that the availability or performance of the service to be supplied may vary, depending on the capacity, distance to the DSLAM, technical capability or other technical matters affecting the network. This amendment also takes into account the fundamentally variable nature of ADSL technology and the fact that there are many parameters affecting performance of that technology which are outside the service provider's control. For example, an end user that lives close to an exchange will likely experience better performance than an end user who lives further from the exchange. The words *"internet-grade best efforts"* are commonly understood in the industry (both locally and internationally) to refer to such limitations.³²
91. Second, Telstra proposes inserting a definition of *"Asymmetric Digital Subscriber Line technology"* by referring to the ITU-TG.992 Recommendations. Doing so provides greater clarity regarding the service to be supplied. As the Commission acknowledges, *"some degree of technical specification will be required"*³³, and the Recommendations are the definitive – and internationally understood – industry standard for Asymmetric Digital Subscriber Line technology.
92. Third, Telstra proposes inserting the words *"twisted pair"* that *"runs from the end-user network boundary to the nearest upstream exchange or RIM or CMUX"* in sub-paragraph (a) of the service description to ensure that the service being referred to is one which is provided over a twisted metal pair, as opposed to other technology.
93. Fourth, Telstra proposes inserting the words *"has an underlying voiceband PSTN service operating over it"* in sub-paragraph (a) of the service description to ensure consistency between provision of the service over different declared services.
94. Fifth, Telstra proposes inserting the words *"over a transport layer to aggregate communications to the point of interconnection"* to more closely align with the Ministerial Determination.

³⁰ Discussion Paper, p. 26.

³¹ Telstra notes that it agrees with the Commission's approach to developing a service description as described on p. 26 of the Discussion Paper.

³² See, for example, http://www.internode.on.net/residential/adsl_broadband/easy_reach/faq/;
http://www.bellsouth.com/consumer/inetsrvcs/inetsrvcs_fa_terms.html.

³³ Discussion Paper, p. 25.

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95. Sixth, Telstra proposes amending the definition of “*network network interface*” to refer instead to “*point of interconnection*”. This amendment simplifies the definition and more closely aligns the definition with the Ministerial Determination. The amendment also avoids the use of an overly technical term which does not assist in interpreting the service description.
96. Finally, Telstra agrees with the Commission that the proposed service description (including with Telstra’s proposed amendments) does not include the modem or in-premise wiring.³⁴
97. Telstra’s proposed amendments to the service description are in redlining below:
-

Proposed service description

The asymmetric digital subscriber line access service is an *internet-grade, best efforts point-to-point service for the carriage of communications in digital form between a ~~network network interface that is a point of interconnection~~ and an *end-user network boundary-user network interface* that*

- (a) Is supplied: ~~(a)~~ by means of *Asymmetric dDigital sSubscriber lLine (ADSL) technology-* ~~(b)~~ over a ~~customer access network that includes twisted~~ metallic pair that:
- (i) runs from the *end-user network boundary to the nearest upstream exchange or RIM or CMUX; and*
 - (ii) has an underlying *voiceband PSTN service operating over itath;*

and

- (b) uses
- (i) ~~Asymmetric upstream and downstream data rates~~
 - (ii) ~~(#)~~ *A static layer 2 tunnelling protocol (L2TP) over a transport layer to aggregate communications to the point of interconnection.*

Definitions

Where words or phrases used in this declaration are defined in the *Competition and Consumer Act 2010* or the *Telecommunications Act 1997*, they have the meaning given in the relevant act.

Asymmetric Digital Subscriber Line technology or ADSL means the protocols, recommendations and standards set out in the *ITU-TG.992 Recommendations*.

Layer 2 has the same meaning as in the *Open System Interconnection (OSI) reference model for data exchange*.

³⁴ Discussion Paper, p. 26.

~~A network network interface that is a~~ **point of interconnection** means an interface that is:

- (a) a physical point of interconnection which allows the interconnection of facilities in accordance with subsection 152AR(5) of the *Competition and Consumer Act 2010*; and
- (b) located in the same state/territory that the access provider associates with the exchange service in which the **end user network boundary network interface** is located.

An ~~user network interface~~ **end-user network boundary** means the boundary point of the **telecommunications network** that is:

- (a) associated with the end-user premise; and
 - (b) ascertained in accordance with section 22 of the *Telecommunications Act 1997*.
-

06 DURATION OF DECLARATION

98. Telstra strongly believes that if the Commission does decide to declare wholesale ADSL, then the declaration should be of a short duration. Telstra considers that the Commission should align the end date of any wholesale ADSL declaration with that already set for the fixed services, i.e. 31 July 2014.
99. The evidence presented in the previous sections of this submission shows that facilities-based competition has been driving more investment and greater innovation in the products being delivered to end users. In addition, the number of wholesale ADSL services has been in steady decline for a number of years. Statements by access seekers suggest that they expect DSLAM investment to continue in the future, even in the transition to NBN.³⁵
100. Declaring wholesale ADSL for the period to 31 July 2014 would provide an opportunity for both the Commission and industry to assess whether or not continued declaration of the service is necessary beyond that time. In light of anticipated changes to services, market conditions and supply trends as the NBN rollout gathers pace, declaration of wholesale ADSL services for a longer period would be inappropriate.

³⁵ Telstra refers the Commission to section 3.5 of this submission.



07 PRICING METHODOLOGY OF WHOLESALE ADSL

7.1. The appropriate price terms to include in an IAD

101. The Commission has suggested that if it declares wholesale ADSL, it will publish an IAD, and it intends to set prices on the basis of RMRC. Telstra provides the following comments on that approach.
102. In the context of highly competitive metropolitan areas and nationally consistent retail pricing, the most effective pricing methodology is the RMRC approach set out in Telstra's SSU (**RMRC methodology**).
103. The RMRC methodology can be implemented in the form of an IAD by referencing the relevant schedules of the SSU in any IAD. Alternatively, the Commission could simply replicate the drafting.
104. The RMRC methodology has been developed and subjected to public consultation in the context of Telstra's SSU. Telstra made the first confidential version of that calculation available to the Commission on 9 September 2011. A public version of the calculation was made available to participants of the Commission's public consultation on the SSU on 10 November 2011. Following comments from the Commission, Telstra sent a revised version to the Commission on 18 November 2011.

7.2. The RMRC methodology would promote the LTIE

105. The last version of the RMRC calculation begins with the weighted average of all BigPond and Telstra Business Broadband ADSL retail prices (after discounts) and subtracts the fully allocated retailing costs (including a fair economic return for retailers) associated with the supply of those ADSL services.
106. The RMRC methodology calculates wholesale port prices to be \$30 and \$37 per service per month in zone 1 and zone 2/3, respectively, and \$55 per mbps per month for AGVC. These price points deliver considerable savings for the majority of wholesale customers. [c-i-c commences] [c-i-c] [c-i-c ends].
107. Prices based on the RMRC methodology would promote the following three competitive objectives:
 - a. creation of efficient incentives for new suppliers to enter new parts of the ADSL market;
 - b. discouragement of exit by efficient firms; and
 - c. expectations of fair rates of return by efficient wholesale customers.
108. New entry is promoted by the RMRC methodology as the margin between wholesale and retail prices is higher than the efficient incremental cost for a telecommunications company to enter new parts of the ADSL market. This is because RMRC uses fully allocated retail costs, which are



higher than the incremental costs of supplying ADSL.³⁶ Indeed, RMRC might create a margin between retail and wholesale prices that encourages some inefficient entry.

109. The RMRC methodology would discourage efficient providers from exiting the ADSL market. The RMRC methodology would provide for a margin between retail and wholesale prices which is greater than the costs that could be avoided by efficient wholesale customers if they were to cease supplying ADSL. Exit from the market by some inefficient firms might also be discouraged by adoption of the RMRC methodology, given the margin between retail and wholesale prices would be greater than the costs that could be saved even by some inefficient firms.
110. The fully allocated retail cost in the RMRC methodology also includes a weighted average cost of capital applied to all capital attributable to the retailing of ADSL services. This means that the margin between retail and wholesale ADSL prices under the RMRC approach includes a fair competitive rate of return for wholesale customers supplying retail ADSL.
111. Indeed, since the fully allocated retail costs used in the RMRC calculation are Telstra's costs, the RMRC methodology allows for wholesale ADSL customers who are more efficient than Telstra to earn margins which exceed fair economic margins. However, given the level of competition in the market, it can be expected that these greater margins would be eroded in the long term.
112. In addition, the RMRC methodology encourages efficient investment in infrastructure needed by wholesale customers to supply retail ADSL services on the basis of wholesale ADSL, since it allows for a fair economic return for firms that are at least as efficient as Telstra is at the retail layer. As noted above, while more efficient resellers might earn higher margins in the short term, competition would be expected to erode these margins to a competitive level over time.
113. Similarly, the RMRC methodology would also encourage efficient investment in infrastructure needed to supply wholesale ADSL and/or self supply using ULLS, LSS and other bypass opportunities. This is because Telstra's wholesale ADSL price would be set on the basis of a nationally averaged retail price (which is constrained by bypass competition in metropolitan areas), less retailing costs. Investors in this type of infrastructure will be left with a return as high as the competitive retail market would otherwise bear³⁷ – in other words, their return would be no higher or lower than the competitive margin.

7.3. The RMRC methodology addresses concerns raised by the Commission

114. In the Discussion Paper, the Commission raises a concern that the current level of wholesale ADSL prices might be above what would be expected in a competitive market.³⁸ Adopting the

³⁶ Telecommunications operators that begin to supply new ADSL customers, would incur only incremental costs in the supply of those new ADSL customers. Fully allocated costs include those incremental costs and the common costs that would be incurred by new entrants whether they begin to supply new ADSL customers or not.

³⁷ This assumes there is no double marginalisation resulting from independent supply of the wholesale and retail ADSL vertical stages of production. However, since the majority of ISPs that bypass wholesale DSL (that is, ULLS, LSS based ISPs) vertically integrate the wholesale and retail ADSL vertical stages of production, no double marginalisation would be likely to occur.

³⁸ Discussion Paper, p. 18.

RMRC methodology would mean that wholesale ADSL prices would reflect competitive market prices.

115. Telstra's retail ADSL prices are constrained by bypass competition in zone 1 areas. As set out in section 3, competition in these areas arises because of the alternative supply opportunities taken up by suppliers, using ULLS and LSS based supply, mobile broadband and, in the case of Optus and TransAct, HFC networks. [c-i-c commences] [c-i-c] [c-i-c ends]. The RMRC methodology determines wholesale ADSL prices for both zones 1 and 2/3 based on those retail prices that are constrained by competition in zone 1. Fully allocated retailing costs, including a fair economic return, are subtracted from these retail prices. There is no supra-competitive margin added to the wholesale ADSL price in any zone. Thus, resulting wholesale prices for all zones are based on and are reflective of the competitive retail prices for ADSL services supplied in CBD and metropolitan areas.
116. The Commission is also concerned with respect to vertical price squeezing in relation to the supply of wholesale ADSL.³⁹ The RMRC methodology ensures that there is a more than sufficient margin between retail and wholesale prices for efficient competitors to supply the same retail ADSL services that Telstra supplies.
117. In addition, the Commission has expressed concerns regarding potential delays between Telstra's release of new retail prices and the finalisation of negotiations for Telstra's wholesale pricing. The RMRC methodology would pass through material changes in Telstra's retail prices to wholesale prices before Telstra implements that material retail price change. All immaterial price changes would be passed through in the six-monthly update of the RMRC calculation.
118. Further, the Commission has suggested that AGVC charges for competing providers are high, and that Telstra does not incur similar charges, potentially preventing access seekers from competing in emerging content delivery markets.⁴⁰
119. First, Telstra's supply of retail ADSL services requires Telstra to incur the cost of transporting traffic throughout Australia, in a similar way to the AGVC charge. While Telstra does not incur the same marginal cost as wholesale customers, Telstra has incurred significant upfront capital costs in providing sufficient backhaul capacity. With the considerable growth in backhaul demand, these costs have been substantial. Wholesale customers are not required to make the same upfront capital expenditures and are not subject to the associated risk of such upfront outlays. Thus, while wholesale customers may face higher marginal costs than Telstra, they benefit from avoiding the upfront outlays to which Telstra is subject.
120. Second, the initial adoption of the RMRC methodology would result in substantial reductions to the AGVC charge for the majority of customers. Of course, wholesale customers have and will continue to be able to negotiate alternative AGVC prices with Telstra.
121. Third, the RMRC methodology would automatically reduce wholesale ADSL prices, including the AGVC component, to account for increases in backhaul demand from Telstra's retail ADSL customers. Therefore, to the extent that Telstra's participation in emerging content delivery

³⁹ Discussion Paper, p. 18.

⁴⁰ Discussion Paper, p. 18.

markets increases the backhaul demands from Telstra's retail ADSL customers, and if the cost of the additional backhaul is not recovered separately from the emerging content delivery services, then Telstra's wholesale ADSL prices will fall commensurately.

122. Telstra understands that the Commission intends to consult on longer-term pricing issues as part of a Final Access Determination inquiry⁴¹. Telstra will make submissions in relation to those issues at that time.

⁴¹ Discussion Paper, p29.

08 CONCLUSION

123. Telstra considers that the Commission does not have a sufficient evidentiary basis to conclude that declaration of wholesale ADSL would promote the LTIE, as required by s 152AL of the CCA. The broadband market is already highly competitive, particularly in CBD and metropolitan areas, due to substantial (and increasing) facilities-based competition. Declaration of wholesale ADSL would dampen incentives for access seekers to continue investing in DSLAMs (and related infrastructure), which enable them to provide competitive ULLS and LSS-based offerings. For these reasons, declaration of wholesale ADSL is both unnecessary and inappropriate.
124. Further, there is no new evidence of a deterioration in market conditions or anti-competitive outcomes which warrants a departure from the “wait and see” approach adopted by the Commission in April 2011. Telstra’s behaviour in the broadband market remains competitive, commercially rational and economically efficient. Further, the obligations to which Telstra has committed in the SSU (which are largely equivalent to the SAOs) render declaration of wholesale ADSL unnecessary. Such declaration is also not a necessary precondition for the Commission’s approval of the SSU – rather, the terms of the SSU provide a compelling reason for the Commission not to declare wholesale ADSL at all.
125. If the Commission does decide to declare the wholesale ADSL service (notwithstanding the absence of any reasonable basis for doing so), Telstra submits that:
- a. at the very least, the 285 ESAs should be excluded from the scope of the declaration. In these areas, declaration of wholesale ADSL would clearly be contrary to the LTIE;
 - b. the Commission’s draft service description for wholesale ADSL should be amended (in the manner proposed by Telstra) to ensure that it is both clear and workable for all parties; and
 - c. the end date of the declaration should be 31 July 2014, to align with the fixed line services declarations.
126. Finally, if the Commission publishes an IAD in respect of wholesale ADSL, the IAD should adopt Telstra’s RMRC pricing methodology. This methodology (which has already been subject to public consultation) would be the most effective, and the fastest to implement. The price points calculated by reference to Telstra’s RMRC methodology deliver considerable savings to the majority of wholesale customers.

09 ANNEXURE A – RESPONSES TO QUESTIONS

This Annexure contains Telstra's responses to the questions posed in the Commission's Discussion Paper.

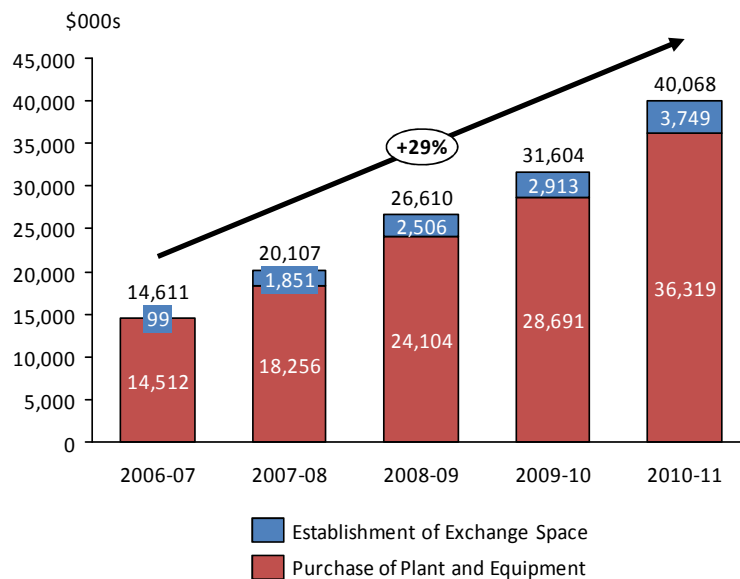
No	Question	Telstra's Response
1	What is the relevant market for the purpose of this Discussion Paper and the application of the LTIE test?	As set out in section 3.3 of this submission, Telstra believes that the relevant market is national in scope. Telstra competes nationally in supplying broadband services to end users, including by offering nationally consistent retail prices. However, contrary to the conclusion reached by the Commission in the Discussion Paper, the relevant (national) broadband market is already highly competitive.
2	Do you consider that Telstra's wholesale terms and conditions inhibit competition? If so, what have been the effects on the ability of access seekers to compete?	Telstra refers the Commission to sections 3.6, 3.7 and 3.8 of this submission.
3	Do access seekers have data to indicate the effect of Telstra's access terms on their ability to compete? Please indicate the relevant market shares of customers on-net and off-net.	As this question is directed at access seekers, Telstra does not consider it necessary to respond.
4	Are there any instances whereby delays in the negotiation of revised wholesale DSL charges following Telstra's retail price changes have affected the ability of access seekers to compete? If so, please specify the duration and impact of the delays.	Telstra has previously addressed these concerns in correspondence with the Commission and reiterates that immediately after releasing (lower) retail prices, Telstra offers lower prices to its wholesale customers. Telstra also refers the Commission to section 7.3 of this submission.
5	Do you consider that Telstra's wholesale	Telstra refers the Commission to sections 3.6, 3.7 and 3.8 of this submission (in relation to Telstra's wholesale terms

	terms and conditions restrict the nature of service offerings? For example, the provision of large data quotas and retail products such as IPTV and multimedia content.	and conditions) and section 3.4 of this submission (in relation to the expansion in available service offerings).
6	Are there any business cases that have been or could be frustrated as a result of the pricing of AGVC?	Telstra refers the Commission to section 7 of this submission. Telstra remains committed to negotiating with its wholesale customers and where those customers have specific requirements relating to their business cases, Telstra will consider those requirements. For example, and [c-i-c] commences [c-i-c] [c-i-c ends].
7	Are there instances where access seekers provide DSL services on more competitive terms if they use their own DSL network or where supply of wholesale ADSL is available from another provider? If so, please detail the differences.	Telstra refers the Commission to section 3.4 of this submission.
8	Could early termination charges discourage access seekers from providing services over alternative networks?	Telstra refers the Commission to section 3.9 of this submission.
9	Are there any instances of price discrimination between access seekers? If so, what is the basis for the price discrimination and what are the effects on the ability of access seekers to compete?	Telstra refers the Commission to sections 3.6, 3.7 and 3.8 of this submission.
10	Are there any instances of price	Telstra refers the Commission to sections 3.6, 3.7 and 3.8 of this submission.

	discrimination on access seekers that choose to use their own infrastructure or an alternative wholesale supplier to the incumbent?	
11	Are there any instances of access terms such as volume commitments and minimum spend restrictions? If so, do the set targets reflect ordinary growth rates or do they rely on migration onto the Telstra network?	Telstra refers the Commission to sections 3.6, 3.7 and 3.8 of this submission.
12	Do you consider that it is imperative to have a pre-existing subscriber base prior to the rollout of the NBN? If so, will an existing market share provide a material comparative advantage? If so, how?	Telstra refers the Commission to section 3.5 of this submission.
13	Are access seekers concerned about Telstra migrating its customers onto the NBN and contractually "locking in" customers by specifying a minimum term or imposing prohibitive switching fees?	As this question is directed at access seekers, Telstra does not consider it necessary to respond.
14	Are there any other potential risks to competition that may arise in the transition to the NBN if wholesale ADSL is not regulated? If so, what are they?	Telstra refers the Commission to sections 3.4 and 3.5 of this submission.

15	Has the NBN changed the strategic importance/value of expanding during the transitional period leading up to the NBN? Why or why not?	Telstra refers the Commission to sections 3.4 and 3.5 of this submission.
16	On the NBN, do you anticipate increased competition to take place on value-added retail services such as IPTV? Are access seekers considering deploying value-added services during the transition to NBN?	Telstra refers the Commission to sections 3.4 and 3.5 of this submission.
17	Does investment in value-added retail services such as IPTV require greater customer scale, and if so, to what extent would a declaration of wholesale ADSL offer opportunities to obtain this scale?	<p>A range of ISPs currently offer IPTV services.</p> <p>In addition to Telstra's T-Box service, the FetchTV service is currently offered by iiNet (including its recently acquired Internode subsidiary) and Optus), with TPG offering its own IPTV-content.</p> <p>However, it is important to note that the majority of ISPs do not currently offer IP-TV services over resale lines and Telstra's wholesale ADSL service does not offer multicast capability.</p>
18	Do you consider that declaration of wholesale ADSL will promote competition in the transition to the NBN? Why or why not?	Telstra refers the Commission to sections 3.4 and 3.5 of this submission.
19	What impact would declaration have on the objective of achieving any-to-any connectivity in relation to carriage services that involve communication between end users?	Telstra agrees with the Commission that when considering services that do not require user-to-user connections – such as wholesale ADSL services – this criterion is generally less important.

<p>20</p>	<p>If the ACCC were to declare a wholesale ADSL services, is it likely that access seekers continue to invest in DSLAMs where it is efficient to do so?</p>	<p>Telstra refers the Commission to section 3 (and, in particular, section 3.4) of this submission.</p> <p>Telstra further notes that it is unlikely that the current highly-competitive market for ADSL services would have evolved (either with respect to retail or wholesale services) if the Commission had imposed declaration as the market developed.</p> <p>The importance of regulatory forbearance can be observed when comparing the expansion of service offerings and competition for broadband, IPTV and video-on-demand services supplied over DSLAMs and related hardware to voice services supplied over the same hardware. Broadband internet services (as well as IP-TV and video-on-demand services) are largely unregulated.</p>
<p>21</p>	<p>Does investment in DSLAM infrastructure enhance the ability of access seekers to differentiate products, through increased functionality and service quality?</p>	<p>Telstra refers the Commission to section 3 (and, in particular, section 3.4) of this submission.</p>
<p>22</p>	<p>Are significant opportunities for efficient investment in competing DSL networks – in terms of either expansion of the existing DSLAM footprint or increased investment in areas that have already attracted ULLS/LSS based competition? Is this likely to change over time?</p>	<p>Telstra refers the Commission to section 3 (and, in particular, section 3.4) of this submission.</p>
<p>23</p>	<p>What impact does the NBN have on incentives to invest in DSLAM infrastructure?</p>	<p>Telstra refers the Commission to section 3.5 of this submission.</p> <p>In addition, Telstra notes that access seekers' financial statements confirm that they are continuing to invest substantially in infrastructure, including in establishment of exchange space.</p> <p>For example, iiNet's financial statements reveal the following: <u>iiNet cash flows to investing activities, 2006-07 to 2010-11.</u></p>



Public statements made by access seekers (as set out in section 3.5 of the submission) are also consistent with recent market trend data shared with Communications Day by Ericsson and Alcatel-Lucent, key suppliers of DSL hardware. Ericsson Australia's broadband strategy manager, Colin Goodwin, has stated:

"Each year we expect our DSL sales figures to stall in anticipation of the NBN build, but - as has been the case for several years now - in 2010 we actually sold more DSLAMs than in the previous year."⁴²

A further aspect of the NBN that is driving additional DSLAM investment has been the deployment of the Regional Broadband Blackspots Program as part of the NBN rollout. As noted by the Department,

Construction along all five RBBP links—Geraldton, South West Gippsland, Victor Harbor, Broken Hill and Darwin—is now complete. New and improved services are already offered by internet service providers in

⁴² 'Key telco vendors see no slowdown in DSL deployment spend', *Communications Day* Issue 4012 (30 June 2011).

		<i>Geraldton, Victor Harbor and South West Gippsland. Nextgen is currently in the process of connecting retail service providers to the new competitive backbone link in Broken Hill and along Darwin, Emerald and Longreach route.</i> ⁴³
24	Could declaration of wholesale ADSL promote efficient investment in infrastructure that will be used to interconnect on the NBN or provide value-added retail services?	<p>NBN Co has 121 POIs due to the presence of competitive backhaul infrastructure supplying these areas (as identified by the Commission). This infrastructure has, in many cases, been installed to service DSLAM investments. As such (and almost axiomatically), access seekers with significant DSLAM networks are likely to be best prepared to interconnect directly with the NBN.</p> <p>Any declaration of wholesale DSL – to the extent that it discourages otherwise efficient investment in DSLAMs (and related interconnect infrastructure) – may have the adverse outcome of leaving access seekers unprepared to fully exploit the potential benefits of the NBN.</p>
25	<p>If the ACCC declares a wholesale ADSL service:</p> <p>(a) What is an appropriate service description?</p> <p>(b) Should the service description cover wholesale ADSL services nationally, or be limited in geographic scope?</p> <p>(c) What is the appropriate duration of the declaration?</p>	<p>Telstra refers the Commission to Section 5 of this submission, where it has proposed amendments to the Service Description put forward by the Commission in the Discussion Paper. These amendments will ensure that the service is described in a manner which provides sufficient clarity and that it aligns more closely with the <i>Telecommunications (Regulated Services) Determination (No. 1) 2011</i>.</p> <p>As set out in Section 4 of this submission, Telstra believes that any declaration of wholesale ADSL should be restricted in geographic scope to areas in which there is limited competition. Telstra estimates that, at a minimum, there are 285 ESAs that should be excluded from a declaration of wholesale ADSL.</p> <p>Further, Telstra considers that if the Commission does declare wholesale ADSL, then the length of the declaration should be limited to 3 years. This will give the Commission and industry the opportunity to review whether the declaration remains appropriate, particularly given the likelihood of continued investment in facilities-based competition by access seekers and migration to the NBN.</p>

⁴³ See http://www.dbcde.gov.au/funding_and_programs/national_broadband_network/national_broadband_network_Regional_Backbone_Blackspots_Program.

010 ANNEXURE B – DATA ON THE 285 ESAS

[c-i-c commences] [c-i-c] [c-i-c ends]

011 ANNEXURE C – EXPERT REPORT OF [c-i-c commences] [c-i-c] [c-i-c ends]

Annexure C is the confidential report prepared by [c-i-c commences] [c-i-c] [c-i-c ends], dated January 2012.