TELSTRA CORPORATION LIMITED

Submission to the Australian Competition
and Consumer Commission

CBD and Metro DTCS Exemption Applications

Telstra Response to Submissions of Interested Parties on ACCC Discussion Paper

PUBLIC VERSION

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Overview

Telstra wishes to bring to the Commission's attention several concerns with information provided to the Commission by Optus[1], Internode[2], AAPT[3], PIPE[4] and the Competitive Carriers' Coalition[5] in their submissions.

This submission should be read in conjunction with Mike Smart's supplementary report which provides a critique of the economic aspects of the interested parties' submissions and with Telstra's earlier submissions in support of the Exemption Applications. See **Attachment 2** for a copy of Mike Smart's supplementary report.

Capitalised terms used in this submission but not defined have the same meaning given in Telstra's earlier submissions.

Telstra acknowledges the importance of all parties likely to be affected by the Commission's decision being granted an opportunity to provide their views as to whether granting the Exemptions would be in the LTIE.

Nevertheless, Telstra is concerned that interested parties have purported to provide material facts to the Commission, without providing adequate reference to the sources of those facts. In some instances, submissions by interested parties on important issues amount to no more than bare assertions.

Telstra considers that in general, the Commission should give a lesser weight to such "facts". In some instances, where evidence to support factual assertions is entirely lacking, the Commission should place no weight on such assertions.

In addition, Telstra believes it important that its views on some of the arguments made by interested parties be placed on the public record.

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1 Optus, Optus Submission to Australian Competition and Consumer Commission on Telstra's December 2007 Exemption Applications for Tail End and Inter-Exchange Transmission Capacity Services (Confidential version), April 2008.

2 Internode, Telstra's Transmission Exemption Application - Submission by Internode.

3 AAPT, Submission by AAPT Limited and PowerTel Limited to the Australian Competition and Consumer Commission in response to the Discussion Paper Telstra's Transmission Exemption Applications, February 2008.

4 PIPE Networks, Telstra's Transmission Exemption Applications, 14 March 2008.

5 Competitive Carriers' Coalition, Submission on behalf of the Competitive Carriers' Coalition, Inc. in relation to Telstra's Declaration Exemption Applications, March 2008.

1. Common issues

a. Misguided assertions about the reliability and completeness of Market Clarity data

Internode and Optus have questioned the reliability and completeness of Market Clarity's data, suggesting that Telstra has relied on data to select competitive ESAs that is based on supposition rather than fact.

Internode asserts:

> "Market Clarity frequently refers to 'likely' routes or 'likely' connections throughout its report but without categorically stating that it knows a purported route or connection exists."[6]

> "The accuracy of Market Clarity's Access Fibre Availability report is again brought into focus at clause 4.3, where Market Clarity states that 'due to time limitations, this phase of my analysis was restricted to the nominated Band 1 and Band 2 ESAs located in NSW…'. Given the nationwide breadth of Telstra's exemption application, we consider that Telstra should have ensured that Market Clarity had sufficient time to conduct a full analysis rather than be forced to rely upon unreliable conjecture."[7]

Similarly, Optus asserts:

> "Optus considers that the evidence relied on by Telstra is unreliable and may overestimate the amount of relevant fibre infrastructure in a given ESA since it;
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> "…
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> "(f) relates to fibre infrastructure in ESAs located in NSW only in the December report (clause 4.3). Given the nation-wide nature of Telstra's exemption application, Optus submits that its evidence is wholly insufficient."[8]

Internode's and Optus' criticisms fail to give justice to the rigour of Market Clarity's research. They also mistake the necessary disclosure which any independent expert must make as to the scope of their inquiry and the assumptions they have made for "unreliability" or conjecture. Contrary to Optus' and Internode's assertions, Market Clarity's conclusions are based on a careful analysis of hard evidence. There is no reliance on conjecture.

Market Clarity's report was conducted in two phases:

(a) First, it conducted a study based on existing data held by Market Clarity on the presence of "access fibre" in ESAs throughout Australia. This process is described in detail in

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6 Internode, p. 2.
7 Internode, p. 2.
8 Optus, paragraph 3.5.

sections 2 and 3 of Market Clarity's report, and the relevant results are set out in Appendix 4 of its report; and

(b) Second, to corroborate this evidence, it conducted a study focussing on NSW Band 1 and 2 ESAs on the presence of "inter-exchange network (IEN) fibre". This process is described in detail in section 4 of Market Clarity's report, and the relevant results are set out in Appendix 5 of its report.

The references to 'likely' routes or 'likely' connections in Market Clarity's report only occur in relation to the second phase special study of NSW ESAs for inter-exchange fibre as explained in section 4 of its report. Market Clarity documents its conclusions in the second phase clearly in Appendix 5, Table 4 of its report. In doing so, Market Clarity carefully distinguishes between two categories:

(a) "Known IEN Fibre"; and

(b) "Likely IEN Fibre",

and reports IEN counts for each category in separate columns in Appendix 5 - Table 4.

Importantly in Telstra's inter-exchange transmission exemption applications, Telstra has only relied on the data in the "Known IEN Fibre" columns for the NSW ESAs to identify the ESAs in NSW that meet the criteria of having at least 3 competitor IEN fibres. Hence Internode's attempt to cast doubt on the report by reference to its use of the word "likely" is both misguided and irrelevant.

b. Misreading of BIS Shrapnel building count

Some interested parties have also made claims based on an incorrect interpretation of the data in the BIS Shrapnel report on CBD infrastructure.

For example, Internode incorrectly asserts that BIS Shrapnel's data and Mike Smart's "development" of it showed that 100% of buildings assessed were fibred by Telstra. Internode states:

> "We consider that the 2001 BIS Shrapnel report sheds interesting light on Market Clarity's data and the further development of that data by Mr Smart. As shown by Mr Smart, BIS Shrapnel's data showed that 100% of 5500 buildings assessed were fibred by Telstra. The implication of Market Clarity's data and Mr Smart's arguments, which present a significantly lower percentage, is that Telstra must have actually removed its cable from buildings in order for its market proportion to have dropped so much. This is ludicrous.

We have never heard of a carrier removing fibre from a building once installed. We severely doubt the veracity of Market Clarity's data and Mr Smart's claims."[9]

Similarly, Optus' assertions show that Optus has clearly misunderstood how Mike Smart used that data in reaching his conclusions:

"According to research by BIS Shrapnel (2001) referred to by Smart (p21) Telstra's fibre network is connected close to 100% of buildings."[10]

The BIS Shrapnel report[11] (Exhibit 5-6 - reproduced below) sets out the number of buildings connected by fibre for each carrier. Nowhere in the BIS Shrapnel report does it state that the 5500 buildings connected by fibre by Telstra represent 100% of buildings which could potentially be connected by fibre.

9 Internode, p. 3.

10 Optus, paragraph 4.19.

11 BIS Shrapnel, Telecommunications Infrastructures in Australia 2001, December 2001. This report is available on the following webpage: http://www.accc.gov.au/content/index.phtml/itemId/790654.

Exhibit 5-6: Local Access Fibre Optic Network Rollout

Operator	Coverage	Investment	Infrastructure	Capacity
AAPT	Sydney, Melbourne, Brisbane, Adelaide, Canberra and Perth(p)		Fibre Length - 350km (2000) - 670km (2001) Building wired* - 150 units (2000) - 250 units (2001)	165Mbps to 2.4Gbps
Agile	Adelaide CBD			
Amcom	Perth CBD, Adelaide CBD, Darwin CBD(c) and Hobart CBD(c)	$30m (1999-2002)	Fibre Length - 310km (2000) - 500km (2001) - 610km (2002) Building wired – 220 units (2000) – 270 units (2001)*	
Davnet	CBDs in Sydney, Melbourne, Brisbane and Perth	$35m** (by 2000) ($12m per 100 buildings)	Building wired - 70 units (2000) - 120 units (2001) - 300 units (2002)	10Mbps to 1Gbps
Ipera	Newcastle CBD	$1m*	Fibre Length - 4km (2000)* - 8km (2001)	72Gbps (including dark fibre)
C&W Optus	9 CBDs (Sydney, Melbourne, Brisbane, Canberra, Adelaide, Perth, Darwin, Hobart and Launceston)		Fibre length - 1,750km (000) - 1,783km (2001) - 1,810km (2002) Building wired - 1,200 units (2000) - 1,230 units (2001) - 1,300 units (2002)	155Mbps
Telstra	CBD areas in Sydney, Melbourne, Brisbane, Canberra, Adelaide, Perth and Hobart		Fibre length = 32,000km Building wired = 5,500 units (as at 2001)	155Mbps
PowerTel	Sydney, Melbourne, Brisbane, Gold Coast, Newcastle(c) and Canberra(c)	$250m (including trunk optic fibre network)	Fibre Length - 195km (1999) - 480km (2000) - 600km (2001) - 650km (2002) Building wired - 200 units (1999) - 320 units (2000) - 400 units (2001)	N x 155Mbps
Primus	CBDs in Sydney, Melbourne, Brisbane, Adelaide, Canberra and Perth(c)	$30m (2000)** $20m (2001)**	Fibre length - 100km (2000) - 150km (2001)	620Mbps

Operator	Coverage	Investment	Infrastructure	Capacity
Swiftel	Perth CDB	$4m (2000) $2m (2001)*	Fibre length - 15km (2000) - 20km (2001) - 25 to 30km (2002) Building wired - 20 units (2001) - 30 units (2002)	2.5Gbps
TransACT	Canberra metro	$80m (including DSL network)	Reaching 100,000 homes in Canberra	2.5Gbps
UE Com	CBD areas Sydney, Melbourne and Brisbane	$32m* (2000-2001)	Fibre length - 1100km (2000) - 2000km (2001) - 2500km (2002) Building wired - 255 units (2000) - 300 units (2001) - 400 units (2002)	
WorldCom	CBD areas Sydney and Melbourne	$100m*	15km (1999)	2Mbps to 1Gbps

* sourced from media publications
** sourced from BIS Shrapnel's estimates

The Table 5.4 presented in Mike Smart's statement is an exact reproduction of a table in the ACCC's report *Future Scope of the Local Carriage Service - Final Decision*.[12] The Commission observed at the time of this report in 2002 that "*where buildings are wired to other carriers, these building are also likely to be wired to Telstra*". As a result, the Commission in Table 5.4 set out that Telstra's percentage of buildings wired is 100%. It appears that the Commission did not intend the 100% figure to suggest that Telstra has fibre connection to 100% of buildings. Rather, the figure is intended to set a relative benchmark with the Telstra number being 100% for the purposes of comparing the ratio of (i) the number of building connections of non-Telstra carriers to (ii) the number of building connections of Telstra.[13] In any event, Telstra disputes any claim that Telstra's optical fibre network is connected to every building in CBD areas. Telstra also disputes whether the Commission's assertion that buildings wired to other carriers "*are also likely to be wired to Telstra*" is valid in the current market circumstances.

In Mike Smart's report, he notes the difficulties of comparing Market Clarity's data with the BIS Shrapnel data in Table 5.4. In paragraph 62 of his report, Mike Smart addresses these difficulties by comparing the ratio of (i) non-Telstra building connections to (ii) the sum of building connections for all carriers in each of the BIS Shrapnel and Market Clarity reports. Mike Smart explains that he generated the sum total number of buildings wired, which he did by using the

12 ACCC, Future Scope of the Local Carriage Service - Final Decision, July 2002, p. 25. This report is available on the following webpage: http://www.accc.gov.au/content/index.phtml/itemId/772159.

13 This interpretation is consistent with the methodology used in the ACCC's draft decision report: ACCC, Future Scope of the Local Carriage Service - Draft Decision, September 2001, p. 26, where the Commission summed the number of connections for all carriers in order to assess the 'market share' of building connections of non-Telstra carriers.

data in the column entitled "Buildings wired" in Table 5.4. Mike Smart does not make any express representation or use of the 100% figure which the Commission attributed to Telstra.

Unfortunately, Internode and Optus misrepresent the data in Table 5.4, as presented in Mike Smart's report, by using the Telstra 100% figure at face value without having full regard to:

(i) the original data of BIS Shrapnel;

(ii) the ACCC report from which the table was extracted; or

(iii) Mike Smart's explanation of his use of the data in Table 5.4.

c. IEN connectivity

A number of the submissions from interested parties significantly misconstrue what kind of fibre Market Clarity has reported in its IEN fibre study.

Market Clarity has confirmed, by letter attached in **Attachment 3**, that in its report a fibre owner was counted as having IEN fibre in a particular ESA only if all of the following conditions were met:

- That fibre owner's IEN fibre in that ESA was part of a transmission fibre route that passes through the ESA and crosses into at least one other ESA;
- The IEN fibre was known to have an access point ("drop-in point") and associated termination equipment within that ESA; and
- The IEN fibre was capable of being connected to that carrier's fibre-optic network.

Isolated fibre (i.e., fibre not connected to at least two ESAs) was not counted by Market Clarity as IEN fibre. Market Clarity also specifically indicated the number of carriers (including Telstra) whose IEN fibre are connected to the Telstra exchange in the relevant ESA. In doing so, Market Clarity has carefully distinguished between:

(a) the number of IEN carriers that were known to be connected to the Telstra exchange; and

(b) the number of IEN carriers that were likely to be connected to the Telstra exchange,

in each case based on the data held by Market Clarity.

2. Optus

Optus does not oppose Telstra's exemption applications with regard to IEN DTCS. It notes that it is "*possible that there is sufficient inter-exchange transmission infrastructure in the proposed exemption areas to preserve competition in the absence of declaration*".[14]

2.1 Market definition

The market definition issues raised in the Optus submission are discussed in the supplementary report by Mike Smart. In summary, he observes that Optus' restrictive market definition is both unnecessary and impractical.[15]

2.2 Alternatives to DTCS

The Optus submission goes to some lengths to argue against the inclusion of microwave or satellite as possible competing transmission infrastructure. However, the Telstra application did not rely on competitive discipline that might arise from these alternative platforms. Accordingly Optus' comments are irrelevant.

Optus also states that it has not been using ULLS as a substitute for Telstra transmission tail services. While Optus presents data on increases in the number of ULLS and the number of transmission tail services purchased from Telstra, this data does not prove that ULLS is not a substitute for tail transmission. The data simply indicates that there is significant growth in ULLS (due to growth in end user demand for DSL-based broadband services) and in tail transmission. Telstra's observation that symmetrical transmission can be supplied using ULLS remains correct. Indeed, Optus has itself acknowledged this when it suggests at paragraph 4.12(d)(ii) that "*in many CBD buildings Telstra can deploy low bandwidth services over existing copper infrastructure at considerably less cost than the cost of delivery over fibre*". Telstra would add that this observation applies equally to Optus, particularly since Optus has access to the copper infrastructure at regulated prices which are substantially below cost. Telstra believes that service providers are able to use ULLS to provision services such as business grade DSL services, and that business grade DSL is a partial substitute for tail transmission.

Optus also argues at length that the difficulty in obtaining ULLS from Telstra at certain exchanges, notwithstanding declaration of that service, renders it ineffective as a means of third

14 Optus, paragraph 1.9.
15 Smart Supplementary Report, section 3.1.

party provision of transmission tail service. As stated later in section 3.2, exchange capping is not an issue for all but 3 ESAs. Accordingly, there will generally be no difficulty in using ULLS.

Assessment of the level of competition

Elsewhere, Optus wrongly suggests that Telstra's assessment of the level of competition is contrary to the data on which Telstra relies. Optus states:[16]

> "Further, Optus notes that Telstra's approach on the level of competition in the nominated ESAs appears to be inconsistent with the findings Telstra has relied on in the Market Clarity report. In many of the nominated ESAs, Market Clarity appears to have reported that there is only one access fibre infrastructure owner,[12] which appears to be at odds with Telstra's contention that there are three or more access fibre owners present in the ESAs in the exemption application.[13]"
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> 12 Appendix 4, Table 1: To name a few: Ashfield NSW, Bankstown NSW, Baulkham Hills NSW, Blakehurst NSW, Botany NSW, Carlingford NSW, Castle Hill NSW, Concord NSW, Coogee NSW, Cremorne NSW, Cronulla NSW, Dee Why NSW, Five Dock NSW (and a number of other ESAs).
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> 13 "A metropolitan exchange service area associated with a capital city should be included in the exemption application if and only if: …the exchange service area has 3 or more access fibre owners" Smart, p19

As set out in section 1(a) above, in relation to NSW ESAs the Market Clarity study was conducted in two phases. The counts of access fibre may in some cases be different in the phase 2 study (in Appendix 5) compared to the phase 1 study (in Appendix 4). The second study involved closer scrutiny of the existing data using street-by-street level mapping, and the making of follow-up enquiries and analysis to verify the existence or absence of fibre. In most cases, more fibre was identified in phase 2 compared to the phase 1. In a small number of cases, the counts of fibre in phase 2 may have reduced due to discovery of inherent inconsistencies in the primary data collected by Market Clarity. However, in Telstra's inter-exchange transmission and tail transmission exemption applications, Telstra has relied on the data in the Appendix 5 in precedence over Appendix 4 for the NSW ESAs. Mike Smart stated this clearly in paragraph 51 of his statement.

2.3 Barriers to entry

Cost estimates in Lordan statement

The barriers to entry section of the Optus submission focuses on the market for CBD tail transmission over fibre. Optus challenges cost estimates presented in the Lordan report and presents alternative costs based on its own recent tenders for fibre tail installation in the

16 Optus, paragraph 3.6.

Melbourne CBD. Optus criticises the payback period analysis in the Smart report on several grounds, including its reliance on the Lordan cost estimates.

The Optus confidential submission is critical of the cost analysis presented in the Lordan statement, saying that Craig Lordan had substantially underestimated these costs (paragraph 4.9). This complaint is odd because Mr Lordan's cost estimates for individual buildings in Melbourne were higher than the cost estimates presented by Optus.

A detailed reply by Craig Lordan to the criticisms of the Lordan statement is presented separately in his accompanying Supplementary Report. See **Attachment 4** for Craig Lordan's Supplementary Report.

However that level of detail is not necessary to establish an important error in Optus' analysis. Optus states that in a costing exercise it has carried out recently, the cost of construction of access fibre infrastructure to buildings in the Melbourne CBD was in the range of **[Optus c-i-c]**.[17] Mr Lordan estimated that the cost of constructing access fibre to the most expensive building in the Batman ESA in Melbourne was $489,000 , assuming the necessity of constructing new conduit For the Exhibition ESA the equivalent cost was $366,000 and for Lonsdale it was $165,000.[18]

Optus' complaint is that Mr Lordan's cost estimates are too low, yet they are substantially higher than those quoted by Optus. This basic fact is not clear from the Optus submission because it compares the Lordan cost estimates with its own on a per metre basis. This per metre cost comparison is misleading because the route distances for the Optus buildings are much shorter than those for the buildings studied by Mr Lordan and some of the fibre construction costs are distance-independent. The per metre cost comparison is also largely irrelevant to the extent that CBD tail transmission pricing is distance-independent.

At any rate, the cost information provided by Optus does not invalidate the use of the Lordan cost estimates in the Smart payback period calculation. The Lordan cost estimates are higher, so the payback period calculation is conservative. Mr Lordan's 75th percentile costs for the Melbourne CBD range from $100,000 for the Lonsdale ESA to $216,000 for the Exhibition ESA.[19] This range is quite similar to the cost range cited by Optus, although somewhat higher. If anything, the cost information provided by Optus supports the figures used in the Smart payback period analysis.

Insufficient detail in Optus' costings

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17 Optus, paragraph 2.18.
18 Lordan statement, 20 December 2007, paragraph 6.25.
19 Lordan statement, 20 December 2007, paragraph 6.41.

Optus has provided costings for fibre connections to four sites in Melbourne, then compared these costings on a per-metre basis with Craig Lordan's costings. Mr Lordan notes in his supplementary report that this type of comparison is misleading and inappropriate, especially as the distances for the sites he costed are all considerably greater than Optus'.[20] Mr Lordan notes that per metre costs decrease with distance.[21]

On this basis, the Optus criticism of Mr Lordan's costings should not be given any weight. Optus also claims Mr Lordan's costs are too low, yet they are significantly higher than Optus' costings.

If it is Optus' contention that Mr Lordan's costing methodology would give results that are unreasonably low for a site equivalent to those costed by Optus, that claim is not made out. Before such a claim could be made out, Optus would need to satisfy the Commission on all of the following points:

(1) the sites for which Optus presents costings are representative of buildings in the Melbourne CBD, and were not selected because they posed particularly costly connection problems (such as, for example, very expensive forecourt material to be restored);

(2) where the Optus costing included leased duct, how were leasing costs taken into account--were they capitalised? If so, what project life and discount rate were used?

(3) the unit costs for trenching, surface restoration, supply and installation of fibre-optic cable, termination, etc. were appropriate;

(4) what specific cost advantage does Optus believe Telstra has that would enable it to deliver these fibre tails at lower cost than Optus? Does Optus believe that the Telstra tail price would be lower than Telstra's costs of supplying the service?

Yet Optus' submission addresses none of these.

Payback analysis for CBD fibre tails

Telstra refers to, and adopts the conclusions in, Mike Smart's supplementary report which provides a critique of the economic aspects of Optus' criticisms of the payback analysis for CBD fibre tails.[22]

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20 Lordan Supplementary Report, paragraph 3.25.
21 Lordan Supplementary Report, paragraph 3.19.
22 Smart Supplementary Report, section 3.2.

2.4 Efficiency

The efficiency points raised in the Optus submission are discussed in the supplementary report by Mike Smart. In summary, he concludes that Optus' theoretical arguments in favour of continued declaration over CBD tail transmission contain a number of unstated assumptions that are contradicted by practical experience to date and the pattern of actual competitive infrastructure rollout.[23]

2.5 Competition

Optus states that the proposed exemptions would harm access seekers' ability to compete by removing their ability to access the tail-end DTCS.[24] The proposed exemption areas were selected on the basis that three or more independent firms owned fibre in the ESA, that payback periods for fibre to CBD buildings were short, and that declared ULLS was available to provide up to 2 Mbps transmission tail services to the majority of end-user premises in metropolitan ESAs. Given these rules for selecting ESAs for exemption, it does not appear correct to claim that the proposed exemptions would remove the ability of access seekers to obtain tail-end transmission services.

Optus states that the arena for competition in CBD areas would be limited to those CBD buildings which it is economic for multiple operators to serve.[25] Based on Mike Smart's analysis of the cost and commercial feasibility of connecting CBD buildings to fibre presented in connection with the Telstra application, most CBD buildings would be economic.[26] As noted above, the quantitative information provided in the Optus confidential submission supports this conclusion, notwithstanding Optus' claims to the contrary.

Optus states further that *"[t]o achieve the same level of competitive access as that provided by the DTCS would appear to require all carriers active in the market to duplicate Telstra's CBD infrastructure on a large scale."*[27] The Market Clarity CBD fibred buildings report indicates that this level of competitive build has taken place already, at least in Sydney, Melbourne, Brisbane, Perth, Adelaide and Canberra. Given this fact, Optus' statement that *"[s]ignificant investment in access fibre infrastructure by multiple carriers is extremely unlikely, due to the significant barriers to entry…"* [28] cannot be given any weight. It is nothing more than a statement of a hypothesis that has been disproven by actual experience in the marketplace.

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23 Smart Supplementary Report, section 3.3.
24 Optus, paragraph 5.3.
25 Optus, paragraph 5.6.
26 Smart Statement, paragraphs 63-73.
27 Optus, paragraph 5.6.
28 Optus, paragraph 5.7.

While critical of Telstra's tail-end exemption applications, Optus notes that the impacts on competition of the proposed IEN DTCS exemptions are likely to be less significant, stating that *"[t]here may be sufficient existing infrastructure on the IEN routes proposed for exemption to preserve competition"*.[29]

2.6 Timing

Commencement of exemptions

Optus proposes that there should be a phase-in period of at least 24 months before the exemptions come into effect.[30]

Telstra considers that Optus' proposal would not be in the LTIE for the following reasons:

- The ESAs subject to the exemptions are already effectively competitive and any adjustment period that may be required for current efficient users of DTCS in the Exemption Area to make alternative arrangements (if required) does not constitute a threat to downstream competition. A number of carriers can now supply relevant downstream services on this basis; and

- If there are on balance economic benefits from the immediate commencement of the exemptions (as Telstra believes there are), there is a cost from delay in terms of benefits foregone.

Furthermore the Commission did not consider a phase-in period was required at all for the exclusion of inter-capital routes from declaration in both 1998[31] and 2001[32], and the exclusion of certain capital-regional routes from declaration in 2004[33]. There is no basis for suggesting that the operation of Telstra's exemption, once granted, should be delayed.

Duration of exemptions

Optus seeks a two year time limit on exemptions from the declared DTCS to permit an impact

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29 Optus, paragraph 5.9.

30 Optus, paragraph 6.1.

31 ACCC, Competition in data markets – A final report on whether to declare certain ISDN services, and whether to amend declarations for the digital data access service and transmission capacity under Part XIC of the Trade Practices Act 1974, November 1998.

32 ACCC, Domestic Transmission Capacity Service - A final report examining possible variation of the service declaration for the domestic transmission capacity service, May 2001.

33 ACCC, Transmission Capacity Service: Review of the declaration for the domestic transmission capacity service, Final Report, April 2004.

assessment to guide future policy after that point.[34] This would be counter-productive, as the short length of the proposed exemption period may itself serve to limit the effectiveness of the exemption.

The aim of exemption is, at least partly, to stimulate new investments in competitive infrastructure. However, investments that have a payback period of more than two years (as most infrastructure investments do) will not be forthcoming if there is no certainty of regulatory policy beyond that initial period. If investments are deterred by this uncertainty, then the benefits of exemption will be truncated. The impact assessment may find that exemption did not live up to expectations, and the return to declaration would take on the character of a self-fulfilling prophecy.

In order to avoid this undesirable chain of events, a longer exemption period is necessary. In the Exemption Applications, Telstra suggests that the exemption should not expire before 31 December 2012.

34 Optus, paragraph 6.3.

3. Internode

3.1 Enduring bottleneck

Appropriateness of Telstra methodology

Internode's submission makes several criticisms of Telstra's methodology for determining the presence of competing fibre optic owners. However, these criticisms are based on a misunderstanding of the approach taken by Market Clarity in both the ESA fibre report and the CBD buildings fibred report.

In stating that *"Telstra has done little more than identify the existence of other carriers' fibre cable within the exchange service areas (ESA) for which it seeks exemptions"*,[35] Internode fails to recognise that Market Clarity's IEN report has gone to great lengths to establish that the competitor-owned fibre identified within each of these ESAs is inter-exchange fibre which would permit a connection from that ESA to any other ESA served by that carrier over its own fibre or other fibre-based service leased from another provider.[36] Where this fibre is known to be connected to the Telstra exchange, Market Clarity reports this fact, too. This establishes that the IEN cable identified by Market Clarity is capable of providing inter-exchange transmission services.

Internode then further criticises the Market Clarity CBD Fibred Buildings Report, stating that:

> "For instance, we are not told whether this fibre is between POPs located on different floors of the building, between a POP and a radiocommunications device located in or atop the building, providing an internal link or local area network that only services one customer in different locations in a single building or CBD, or between a customer in the building and the building's MDF. There is no substantiation that the existence of fibred buildings is evidence that accessible tail-ends exist."[37]

However, Internode appears to have ignored the introductory section of Market Clarity's report where it states:

> "Market Clarity conducted the assessment of CBD fibred buildings on behalf of Mallesons Stephen Jaques, in order to address the following questions:
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> 1. The number of buildings in the CBD areas of Australian capital cities (i.e. Sydney, Melbourne, Brisbane, Perth, Adelaide, Canberra, Hobart and Darwin) directly connected to a given carrier's optical fibre network.

35 Internode, p. 1.

36 In a limited number of cases two or more IEN fibre rings of a particular carrier may be connected by fibre links owned by a different carrier, but they were only included in the Market Clarity count if the route served by the different carrier was exempt from DTCS declaration (meaning that competition was judged to be sufficient for transmission on that route).

37 Internode, p. 1.

2. The aggregate number of buildings in the CBD areas of Australian capital cities directly connected to optical fibre networks."[38]

Clearly, Market Clarity's survey includes only buildings directly connected to the fibre optic network of the given carrier. Fibre connections that are only between floors of a building or otherwise entirely within the building were not counted. On that basis it is clear that all the fibred buildings which were counted have accessible tail ends.

Replicability of DTCS

Internode implies, without justification, that a viable DTCS competitor to Telstra must necessarily have a ubiquitous transmission network, and since none do, according to Internode's unsubstantiated assertion, Telstra faces no competitive discipline in DTCS.

Internode states that *"[w]e consider that access seekers are unlikely to be able to acquire services in many geographic areas in the absence of declaration and as a result would be unable to reach or supply their customers."*[39] It is important to bear in mind that Telstra's application for exemption only covers those ESAs for which there are at least two independently owned fibre-based alternatives to Telstra. It is difficult to see how Internode's stated concern can possibly apply to those ESAs.

Internode also raises the issue of Telstra's unused excess capacity as a potential entry deterrent. Factual information presented in connection with Telstra's application shows that competitive entry is taking place, including duplication of IEN and tail fibre connections. In light of this information, any deterrent effect of unused excess capacity appears insufficiently strong to pose the type of problem that Internode describes.

Is DTCS an enduring bottleneck

Internode makes a number of incorrect assertions in relation to the issue of whether DTCS should be considered an enduring bottleneck. For example:

- Transmission network build is said to remain a "*virtually unassailable barrier to entry*".

  Telstra comment: Telstra's applications for exemption and supporting evidence (including the Market Clarity report) provide incontrovertible evidence of significant

38 Market Clarity, Research Report - Access Fibre Availability, Transmission Services, and Inter-Exchange Network Connectivity, 19 December 2007, p. 5.
39 Internode, p. 2.

market entry in respect of both IEN and tail transmission. Contrary to Internode's assertion, the barriers to entry are clearly and demonstrably assailable.

- The Market Clarity report is said not to enable any form of assessment of the possibility of interconnection between Telstra exchanges and fibre owned by other providers.

  Telstra comment: In fact, Market Clarity's report for NSW indicates, for each ESA, the number of fibre owners that connect to the Telstra exchange.

- Telstra's application is said *"to rely upon unreliable conjecture",* for the reason that Market Clarity's research was restricted to NSW ESAs.

  Telstra comment: There is no reliance upon conjecture. The only ESAs for which exemption was sought are those for which Market Clarity was able to complete its research. Applications for exemption were only made for ESAs where the relevant data is complete.

  In respect of Telstra's exemption applications for CBD IEN transmission and metropolitan IEN transmission which are a subset of Telstra's Exemption Applications, Telstra has sought exemption for ESAs in states other than NSW in the absence of IEN data for those states based on Mike Smart's inductive rule, which is explained in Telstra's response to question 3(a) of the Commission's information request and which was applied using the counts of access fibre infrastructure owners for those ESAs in Market Clarity's report.

- Telstra is said to provide little cogent evidence *"that DTCS bottlenecks are removed in any of the relevant ESAs or from any of the relevant services".*

  Telstra comment: The evidence presented by Telstra was quite specific to the ESAs over which exemption is sought, demonstrating that 3 or more independent fibre owners existed in each one. Internode appears to be unaware that the Commission has previously held that where 3 or more fibre owners provide service, the service should not be treated as a bottleneck.

- The Market Clarity CBD fibred buildings report is said to present data that is *"unrealistic and unreliable."* This assertion is founded on two tenets:

  - Internode's understanding that the vast majority of buildings are fibred by Telstra, with a significant percentage fibred only by Telstra; and

- A comparison between the recent Market Clarity building count and the 2001 BIS Shrapnel building count.

  Telstra comment: Internode's first tenet is logically inconsistent with the data. In each of Sydney, Melbourne, Brisbane and Perth, there are more non-Telstra building fibre connections than there are Telstra building fibre connections.[40] Allowing for the possibility that some buildings are counted more than once, if the majority of buildings were fibred only by Telstra (as Internode supposes), then the remaining buildings would necessarily each be fibred by multiple other carriers. It does not seem plausible that it could be economic for three or more carriers to construct fibre to certain buildings while it was uneconomic for any of them to construct fibre to a Telstra-fibred building. Internode's undocumented and seemingly unsupportable "understanding" should be rejected.

  Internode's second tenet is that because the 2001 BIS Shrapnel report had a much higher building count than the 2007 Market Clarity report, the latter must be incorrect, or else large numbers of buildings that were fibred have subsequently been disconnected—said by Internode to be a "*ludicrous*" possibility. There is in fact an alternative explanation for this difference in total buildings counted, which was provided at footnote 20 of Mike Smart's report:

  > "In summing the number of buildings wired across carriers, buildings wired by more than one carrier will be counted more than once. This issue affects both the Market Clarity and BIS Shrapnel tables equally. I note that the total buildings wired reported by BIS Shrapnel is higher than the total reported by Market Clarity. This difference is likely to be explained by two factors. First, the Market Clarity table presented here explicitly canvasses only Sydney, Melbourne, Brisbane, Adelaide and Perth as these cities are the focus of the present application. Second, it is likely that the BIS Shrapnel study is not limited to the band 1 exchange service areas of cities, as the Market Clarity table is."[41]

  Accordingly, Internode's inference is incorrect. Internode has not established that the Market Clarity report is either unrealistic or unreliable.

- Internode states that removal of the DTCS declarations would strand access seekers' customers and infrastructure, making new customers impossible to reach.

  Telstra comment: To the contrary, the fact that exemption is only sought in ESAs where three or more fibre owners operate ensures that this type of stranding will not occur.

40 See also the RP Data report which Telstra has submitted to the ACCC in response to the ACCC's recent information request, which provides an overall count of buildings in CBD areas.

Internode's opinion on connectivity post-exemption is contradictory to the Commission's view in its 2004 Declaration.[42]

3.2 Market definition

Substitutes for DTCS

Internode asserts that ISPs acquiring ULLS services face significant hurdles, such that it is difficult to consider ULLS as an adequate substitute for DTCS, even at low bandwidths. In particular, Internode claims that Telstra has imposed many artificial constraints on access ULLS seekers in terms of a steadily increasing list of full or capped exchanges where there is no space for access to install DSLAMs or the core MDF is full.

Telstra has provided information on the issue of capped exchanges in its response to question 7(b) of the Commission's information request which Telstra submitted on 30 June 2008.

As of July 2008, only three out of the 145 exchanges that are the subject of Telstra's exemption applications are on the capped Telstra Equipment Building Access (TEBA) list. These are:

- Pitt Street (PITT) - listed as both MDF and Racks Capped;
- Roma Street (RASH) - listed as both MDF and Racks Capped; and
- Nerang (NERG) - listed as potential.

Of these, the exchange at RASH is in the process of being decommissioned and moved to another building, while the exchange at PITT is capped only because the power sub-station serving the exchange is at the limit. A power upgrade by the local power utility is required before any more equipment can be installed at PITT.

On that basis, Internode's concerns on "capped" exchanges and Telstra's "artificial constraints" are not supported by the empirical evidence.

Definition of exemption areas

Telstra's choice of exemption areas was based upon the transparent application of an objective eligibility rule. It was not designed to lead to problems for access seekers, as Internode asserts. Exemption is not sought for ESAs where there may be coverage gaps or where access would be

41 Smart Statement, footnote 20.

unavailable from carriers other than Telstra.

3.3 Competition

Internode provides no evidence to support its assertion that the provision of wholesale broadband and fixed telephony services is reliant on Telstra or that Telstra is also dominant in the provision of downstream retail services.

3.4 Efficiency

Internode asserts that exemption would not affect Telstra's incentives and plans to invest. This answer is purely speculative.

Internode also states that "*Telstra is already recovering far in excess of its legitimate commercial interests in providing the DTCS. If the declaration is removed, competition will be reduced, allowing Telstra to recover an even greater return on its assets*."[43]

First, there is no basis for the claim that Telstra recovers '*far in excess of its legitimate commercial interests*'. Second, even if this assertion were correct, which it is not, it would certainly not constitute a reason to continue declaration.

3.5 Lack of awareness of market conditions

The following claims made by Internode are based on, and show, a lack of awareness of current market conditions:

- *question 5 - appropriateness of Telstra exemption area—geographic dimension*

Internode claims that there is insufficient competition to break the geographic dimensions down to individual ESAs.

The appropriateness of the geographic dimension of the Telstra exemption area is discussed in the supplementary report by Mike Smart. In summary, he concludes that Internode's claim appears inconsistent with standard practice in market definition. Normally, the finer the geographic disaggregation of markets, the more difficult it is to establish the sufficiency of competitive activity.[44]

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42 2004 Declaration, p. 47.
43 Internode, p. 10.
44 Smart Supplementary Report, section 4.

- *question 15 and 16 - what alternative DTCS providers and technology operate in each ESA?*

Internode states that it has no information on alternative DTCS providers. Its answer indicates a lack of awareness of developments in the market, such as the extent of infrastructure investment by competitive operators as evidenced the number of fibre owners identified in the Market Clarity reports and the availability of alternative data services functionally equivalent to Telstra's DTCS.

Market Clarity's Access Fibre Availability Report sets out the various fixed line services provided by competing access fibre owners. These services include leased line services, which are technical substitutes to Telstra's transmission capacity service. Other services identified by Market Clarity include ATM, Frame Relay, Ethernet services, and Private Network IP services. Each of these are "transport products" and therefore capable of being used to support applications that are similar to Telstra's transmission capacity service, at least in a functional sense. PIPE confirms that Ethernet, dark fibre technologies, ULL and LSS are effective substitutes for Telstra's wholesale transmission service.[45]

- *question 19, 20 and 21 - alternative wholesale providers use and their planned investments?*

Internode states that it has no information on alternative providers infrastructure and investments. This answer again indicates a lack of awareness of developments in the market, and is not a statement to which any weight can be given.

- *question 22 - any-to-any connectivity*

Internode's opinion that granting the exemption applications would affect any-to-any connectivity is contrary to the Commission's view in its 2004 Declaration.[46]

- *question 23 and 29 - efficient use of infrastructure*

Internode's reply supposes that Telstra would withhold transmission capacity in the event of exemption. As there are three or more fibre owners in each of the ESAs for which exemption is sought, any such foreclosure strategy would likely be defeated by supply from an alternative fibre owner. Internode's position is ill-founded.

Internode raises the issue of Telstra's spare fibre capacity and a potential entry deterrence effect. Factual information presented in connection with Telstra's application shows that competitive

45 PIPE, pp 2-3.
46 2004 Declaration, p. 47.

entry is taking place. Any deterrent effect of unused excess capacity appears insufficiently strong to pose the type of problem that Internode describes.

3.6 Substantial differences between the submissions of Internode and PIPE

As Mike Smart observes in his supplementary report, Internode and PIPE appear to have different business models.[47] Internode's difficulty in supporting issues raised by the Exemption Applications may reflect limitations in its own business model. However the relevant consideration for the Commission in making its decision on the exemption applications is the promotion of the LTIE, rather than the promotion of particular business models.

- *question 8 - is there a discrete IEN market in CBD and metro areas?*

Internode claims there is no discrete IEN market, but the submission of co-competitor PIPE says there is.[48]

- *question 11 - accuracy of Telstra submissions on level of competition*

Contrary to Internode, the PIPE submission states that Telstra's submissions are relatively accurate on this point.[49]

Internode states that *"[r]emoving declaration would remove any bargaining tool that access seekers currently have"*. The Mike Smart statement, in noting the lack of DTCS disputes to date, was making the point that this bargaining tool is not being used.[50] Clearly that is not to say that it would never be used (and indeed a small number of access disputes have previously been notified to the Commission), but it is obvious that to date, there has not been the need for the Commission to determine any issues concerning DTCS, as parties have been able to agree matters commercially.

Internode goes on to criticise the Smart statement for failing to provide substantiation of its conclusions regarding competitor fibre build. However, Mike Smart's conclusions were substantiated at length with empirical data.

- *question 14 - would competition in downstream markets be effective absent DTCS declaration?*

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47 Smart Supplementary Report, section 4.
48 PIPE, p. 3.
49 PIPE, p. 3.
50 Smart Statement, 20 December 2007, paragraphs 93-97.

Internode claims that competition would be ineffective in the absence of DTCS declaration, but the PIPE submission adopts a contrary view to Internode on this question.[51]

Internode ignores the existence of effective competition in the markets in which DTCS is supplied. The existence of effective competition strongly suggests that prices in the downstream market should not increase post exemption.

- *question 17 and 18 - would alternative DTCS providers pose meaningful constraint and would Telstra continue to provide DTCS if exemptions were granted?*

Internode doubts that alternative providers would pose meaningful constraint on DTCS pricing and considers that Telstra would be very unlikely to continue to supply DTCS absent declaration. However PIPE adopts a contrary view to Internode on both these questions.[52]

Internode's answer is speculative, as it ignores:

(a) the degree to which Telstra is constrained by the presence of alternative suppliers in the areas in question and that this will continue to be the case after exemption if granted; and

(b) that Telstra would be incented to continue supplying the DTCS given the significant amount of sunk investment involved in deploying optical fibre.

- *question 28 - would exemption encourage efficient investment by competitors?*

Internode considers it unlikely that anybody would be willing or able to commit to investment to replicate DTCS. Again PIPE adopts a contrary view to Internode on this question,[53] suggesting that Internode's concerns may have more to do with its particular business model as well as its lack of awareness of particular market developments.

51 PIPE, p. 4.
52 PIPE, p. 4.
53 PIPE, p. 5.

4. PIPE

The PIPE submission makes a number of points that are supportive of Telstra's position. Significantly, PIPE provides qualified support for Telstra's exemption application, stating that "*PIPE Networks does not oppose Telstra's transmission exemption applications as all of these measures will in PIPE Networks' opinion promote the long-term interests of end-users*".[54] The "measures" referred to by PIPE includes access to Telstra exchanges, which Telstra considers competitors already enjoy.[55]

PIPE makes the following specific statements that are supportive of Telstra's position:

- Telstra's submissions about the level of competition in the nominated ESAs are relatively accurate;[56]
- Competing fibre owners present in the relevant ESAs are able to replicate Telstra DTCS services in CBD areas;[57]
- Competing fibre owners present in the relevant ESAs are partially able to replicate Telstra DTCS services in metropolitan areas;[58]
- There is a discrete inter-exchange transmission service market in CBD and metropolitan ESAs;[59]
- ULLS would represent an adequate substitute for DTCS tails of 2 Mbps or less if the ULLS service is capable of attaining 2 Mbps bandwidth;[60]
- Competition would be effective in the absence of DTCS with respect to the exchanges from which PIPE operates;[61]

54 PIPE, p. 2.
55 The issue of capped exchanges is not material in Telstra's view. Only two or three ESAs that are the subject of Telstra's exemption application are subject to capping. In any event, the fact an exchange is capped does not in itself imply that there is no access at all. Capped exchanges tend to be those where a number of competitors have already installed equipment and there is no longer any space available. Hence, capped exchanges may be considered to be exchanges where access is available rather than not available.
56 PIPE, p.3.
57 PIPE, p.2.
58 PIPE, p.2.
59 PIPE, p.3.
60 PIPE, p.3.
61 PIPE, p.4.

- Alternative DTCS providers would provide a meaningful competitive constraint on Telstra;[62]

- Telstra's DTCS services in CBD areas are not enduring bottlenecks.[63]

PIPE specifically states that its responses are provided to questions that are within the scope of PIPE's experience and expertise. For this reason, while Telstra does not necessarily agree with every statement made by PIPE, Telstra believes that PIPE's submission should be viewed as having substantial weight and credibility.

62 PIPE, p.4.
63 PIPE, p.3.

5. AAPT

First, AAPT fundamentally misunderstands the criteria for the making of an exemption order under section 152AT of the Trade Practices Act 1974. AAPT asserts:

> "AAPT considers that s152AT(4) sets a high threshold requiring Telstra to prove, with a high degree of certainty, that granting the exemption will in fact promote the LTIE..."[64]

There is no basis in law for this assertion. Indeed the language of "proof" is foreign to the exercise of an administrative decision maker's power of the kind contemplated by section 152AT. Section 152AT(4) simply requires that the Commission be "satisfied" that granting the exemption promotes the LTIE. There is no warrant for the assertion that Telstra bears the onus of "proving" anything. Furthermore, nowhere in section 152AT(4) does it require the Commission to be satisfied to a high degree of certainty.

Second, AAPT makes an unsubstantiated assertion that Telstra is earning above normal profits on metro and regional DTCS services.[65] No evidence is provided to support this claim which, in any case, Telstra rejects.

Finally, Telstra refers to Mike Smart's supplementary report which provides a critique of the economic aspects of paragraphs 10, 15 and 16 of AAPT's submission.[66]

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64 AAPT, paragraph 4.
65 AAPT, paragraph 11.
66 Smart Supplementary Report, section 5.

6. Competitive Carriers' Coalition

Like AAPT, the Competitive Carriers' Coalition fundamentally misunderstands the criteria for the making of an exemption order under section 152AT of the Trade Practices Act 1974.

Telstra refers to its response to the Competitive Carriers' Coalition submission, which Telstra has submitted in connection with the WLR/LCS exemption applications.[67]

Telstra Corporation Limited

31 July 2008

67 Telstra, WLR/LCS Exemption Applications - Telstra Response to the Submission of Nicholls Legal entitled "Submission on behalf of the Competitive Carriers' Coalition, Inc. in relation to Telstra's declaration exemption applications", April 2008.