

**FURTHER EXPERT REPORT ON THE SUBMISSIONS OF OPTUS AND THEIR EXPERTS
IN RELATION TO THE ASSESSMENT OF THE COMPETITIVE EFFECTS OF THE
TELSTRA/TPG TELECOM REGIONAL MOCN AGREEMENT**

1. I have been asked by Gilbert+Tobin to comment on recent submissions of experts instructed by Optus in connection with the ACCC's consideration of the application for merger authorisation by Telstra and TPG. These submissions are a further or supplementary report by HoustonKemp dated 26 October 2022 ('HoustonKemp Second Report') and a report by AlixPartners UK LPP ('AlixPartners') dated 25 October 2022. I provided an expert report to the ACCC dated 20 May 2022 ('Feasey First Report') and a further report dated 25 July 2022 ('Feasey Second Report') responding to an earlier HoustonKemp report and to a report by CEPA. In both of my reports I concluded that the proposed transaction should be authorised by the ACCC because it would not, or would not be likely, to result in a substantial lessening of competition. My letter of instructions in relation to this report are at Annexure A.
2. Given the time available to me and point at which we are at in these proceedings, I do not in this report seek to comment on every point raised by either HoustonKemp or AlixPartners. The fact that I do not comment does not mean that I necessarily agree with them. But at this stage I think it is more important to focus on the key points of contention between us. As was the case with earlier reports from Optus' experts, HoustonKemp and AlixPartners often take different approaches to each other on the same issue so I discuss both in each section. In doing so, I assume that the reader will be familiar with my earlier reports and HoustonKemp's earlier report but I reference them where appropriate.
3. The issues I think it important to focus on and which I discuss in this report are:
 - a. The overall significance of the transaction in terms of effects on competition in the relevant Australian mobile markets.
 - b. The impact of the transaction on prices in the short term.
 - c. The impact of the transaction upon Optus' incentives and ability to invest, and therefore upon the likely level of investment which Optus would in fact make, in the factual and in the counterfactual considered by Optus and its experts which involves Optus sharing its network and spectrum in the RCZ with TPG.

d. Overall conclusions in light of these points.

4. I confirm I have read the Harmonised Expert Witness Code of Conduct and agree to bound by it.

The overall significance of the transaction in terms of effects on competition in the relevant Australian mobile markets

5. In proceedings like this, the ACCC will already know that it is not uncommon for parties to exaggerate the magnitude of the likely effects of a transaction (whether positive or negative) and to compress the timescales within which changes are likely to occur. In my opinion, this is particularly the case when it comes to some of the claims being made by Optus and its experts in connection with this transaction. In my submissions I have sought to emphasise that and explain why I think any effects of the transaction are likely to be relatively limited¹. Given some of the exaggerated claims that appear in the AlixPartners report I think it important to restate my position here.

6. First, the transaction relates to a part of a national market in which less than a fifth of the customers reside and in which Telstra already has 3,700 mobile sites and will acquire access to at most only 169 sites, out of a national total of over 11,000 sites. In a network sharing counterfactual, Optus might also acquire access to a few hundred sites in an area in which it already has around 2,500² and when it also has over 8,600 sites nationally³. This means that any benefits from access to the TPG spectrum will apply to less than a third of the sites in the national networks that Telstra, Optus (or TPG) operate and that any reductions in average network costs, which are the basis on which mobile operators set nationally averaged prices, will also be correspondingly limited. This point is important to emphasise when some reports continue to characterise sharing benefits as if the transaction involves a sharing of the entire national networks of Telstra and TPG or that a network sharing counterfactual would involve a similar national arrangement between Optus and TPG.

¹ Feasey Second Report para.10.

² Note, Telstra estimates the number of Optus' sites as 2,500 in the 17% Regional Coverage Zone. TPG estimates this to be around 2,300.

³ Site numbers from ACCC Mobile Infrastructure Report 2022, p.5 at <https://www.accc.gov.au/system/files/Mobile%20Infrastructure%20Report%202022.pdf>

7. Second, as AlixPartners accept⁴ and as I have noted previously, Telstra's competitive advantages when competing for customers who value coverage and services in the RCZ have and will remain very considerable, irrespective of whether the transaction occurs or not. Telstra currently serves the majority of the customers who reside in the RCZ⁵ and I would expect them to continue to do so in a network sharing counterfactual as well as the factual.
8. Third, to the extent that the transaction enables TPG to compete more effectively with Telstra and Optus, TPG will be starting from a position in which it has historically been by far the weakest and least attractive of the three operators for those who value services in the RCZ. The idea that TPG would immediately or even quickly acquire a very significant share of customers from Optus as a result of the transaction is, in my view, highly implausible. Those customers who might be expected to value coverage and quality in the RCZ, being those that reside in the RCZ, only represent around 14% of Optus' total customers⁶. I also cited evidence from the ACCC in my First Report⁷ to suggest that only around a third of customers in metropolitan areas will value coverage and service in the RCZ. We also know that a disproportionate share of these customers are served by Telstra, given its superior network and services in the RCZ (as well as its superior coverage in remote rural areas beyond the RCZ). If, for example, 24% of Optus existing metro customers were to value coverage and service in the RCZ (consistent with Optus' share of customers who reside in the RCZ) then the share of existing Optus customers for which TPG might plausibly be able to compete as a result of the transaction would represent no more than a third of Optus' existing customer base⁸. In practice, I would expect TPG to only be able to acquire a small proportion of these customers and to require several years in which to do so.
9. HoustonKemp do not agree with me and argue that nationally averaged prices ensure that changes in the RCZ will affect all customers nationally, even if the magnitude of the effect on a per customer basis will be 'dampened'⁹. This might be the case if all customers in Australia valued coverage and services in the RCZ, but as I have noted above, we have evidence to suggest that this is not the case¹⁰. In my view, the most important effects of the transaction on the conduct of

⁴ AlixPartners para 77.

⁵ Feasey First Report, footnote 61; AlixPartners para 92.

⁶ If Optus serves 24% of the customers nationally who live in the RCZ and these represent 17% of all customers but Optus has a market share nationally of around 30% then around $(0.24 \times 17 / 30)$ or 14% of all Optus' customers reside in the RCZ. In Feasey First Report footnote 61 I said Optus' share in the RCZ was 23%. Aetha in their report dated 27 July 2022 say 25.5% (p.7). I adopt 24% here and small differences do not affect the point I am making.

⁷ Feasey First Report para 71.

⁸ $10 + (0.24 \times 90)$.

⁹ HoustonKemp Second Report para 42-3.

¹⁰ Indeed, if competition occurred on this basis it seems unlikely that TPG would have the market share that it does.

the firms and outcome of the market relate to customers who might be affected by the changes which result from the transaction, which are the sub-set of customers who value services and coverage in the RCZ¹¹.

10. Fourth, to the extent that a counterfactual involved TPG and Optus sharing a network and spectrum and this enables Optus to compete more effectively with Telstra and TPG for customers who value coverage and service in the RCZ, the effects will be similarly limited. Telstra would continue to have access to 50% more sites in the RCZ and will have almost three times more customers who reside in the zone and more customers who value coverage outside of it than Optus and TPG combined. TPG's capacity to add traffic to Optus' network in such a counterfactual by acquiring customers from Telstra will be less than its capacity to generate wholesale revenues for Telstra by acquiring customers from Optus in the factual. Moreover, as I discuss further below, access to TPG spectrum in such a counterfactual would have little, if any, impact upon Optus' ability to compete for customers who value services in the RCZ under any reasonable assumption about traffic growth or TPG customer acquisitions because Optus will already be able to accommodate any additional demand using its existing spectrum resources.
11. I recognise that, over many years and far into the future, it could be that the accumulated impact of effects which I consider to be of marginal significance in my assessment would be more significant in either the factual or a network sharing counterfactual. However, I have seen no evidence in the proceeding that would mean this was anything more than speculation of a kind to which I think no weight should be attached. In my experience competition authorities undertake assessments over a period in which effects are reasonably foreseeable and for which the evidence they have is probative. The relevant period can vary depending upon the nature of the industry. Some digital markets can involve a high degree of uncertainty, even over a 12 month period¹². However I have not seen anything in this particular case or from my understanding and experience of how telecommunications markets develop over time that leads me to think the assessment in this case is unusually uncertain or that the relevant time horizon should be longer than customary. I note, for example, that in the Telefonica Deutschland /E-Plus merger in Germany, for which there was no finite duration, the European Commission accepted remedies

¹¹ In other words, although I agree that absent geographic price discrimination mobile prices might rise or fall for all customers, irrespective of whether they value services in the RCZ or not, changes in the competitive constraints on the firms setting those prices arise from their competing for those customers who do value services in the RCZ. This might be thought of as the 'focal effect' of the transaction.

¹² The CMA in the UK has recently updated the [Merger Assessment Guidelines \(March 2021\)](#) to state that where there is greater uncertainty about how markets may develop does not mean that the requisite standard of proof cannot be met or is higher, see para 2.11. In this proceeding, I consider that this means that any findings about which there is uncertainty does not mean the applicants cannot satisfy the ACCC that the transaction should be authorised (or preclude the ACCC from not authorising).

(which must effectively address the adverse competitive effects that it found) which had an initial duration of 5 years and an option to renew for a further 5 years¹³. This suggests in that case the Commission assessed competitive effects over a relevant period of 5 but certainly no more than 10 years. That seems to me appropriate in this case too.

The impact of the transaction on prices in the short term

12. It appears to me that neither HoustonKemp nor AlixPartners are suggesting that the transaction should be prohibited on the grounds that (quality adjusted) prices will increase in the short term as a result of the transaction. Instead, each focusses upon the impact of the transaction on investment by Optus which I discuss in the next section.
13. In HoustonKemp's case, they agree that they omitted to consider the effect of the transaction on competition between TPG and Telstra in the factual and TPG and Optus in a network sharing counterfactual and seek to rectify this in the supplementary report¹⁴. However HoustonKemp ignore what I consider to be the most fundamental point, which is that the transaction provides TPG with the ability to compete much more effectively with Telstra by using the Telstra network than it would be able to compete in a counterfactual in which it shared Optus' significantly inferior network. By focussing only on TPG's incentives to compete and not ability, they ignore this point.
14. As regards incentives, HoustonKemp say that they cannot be certain whether, in a network sharing arrangement with either Telstra or Optus, TPG would have an incentive to compete with their partner or the degree to which they would do so¹⁵. I provided my views on the impact of wholesale charges on both TPG and the partner in my Second Report and do not repeat them here¹⁶. I concluded that the extent to which TPG would have an incentive to compete with Telstra or Optus is to some degree a factual one and note that this is now addressed in some detail by Compass Lexecon in their further report¹⁷.
15. Standing back, it would seem odd for TPG to enter into a transaction in which wholesale charges were at a level which did not enable TPG to compete for customers which the transaction was otherwise clearly intended to enable it to compete for. I also note that many of the arguments

¹³ Case M.7018- Telefonica Deutschland/E Plus, Annex C p.397 at https://ec.europa.eu/competition/mergers/cases/decisions/m7018_6053_3.pdf

¹⁴ HoustonKemp para 23.

¹⁵ HoustonKemp Second Report para 29.

¹⁶ Feasey Second Report para 49-55.

¹⁷ Second Expert Report of Dr Padilla dated 2 November 2022 para 3.14-3.44.

made by Optus and its experts about Optus' incentive to invest in its network, which I discuss in the next section, presuppose that TPG will be able to acquire customers from Optus, which must imply that they think that the wholesale charging arrangements in the transaction will both incentivise and enable TPG to compete to win customers from Telstra and Optus.

16. In any event, HoustonKemp now conclude that they are unable to draw any conclusions about the short term price effects of the transaction¹⁸. This means they cannot argue that the application could or should be rejected by the ACCC on the basis of adverse price effects.
17. Like HoustonKemp, AlixPartners also appear uncertain about the short term effect of the transaction on prices and seem reluctant to rely upon it when arguing that competition will be substantially lessened¹⁹. I remain of the view that the short term price effects of the transaction are clearly both significant and positive (in terms of exerting downward pressure on prices). The main reasons for my disagreement with AlixPartners are:
 - a. Like HoustonKemp, AlixPartners ignore the significant differences between the networks of Telstra and Optus in the RCZ and so assume TPG would be similarly positioned as a competitor to Telstra in the factual and in a network sharing counterfactual. I do not agree and consider that TPG will represent a significantly more effective pricing constraint upon Telstra in the factual than in such a counterfactual²⁰.
 - b. I do not accept that Optus, as the larger operator relative to TPG, will necessarily provide the main pricing constraint on Telstra in the factual or a network sharing counterfactual. I explained in my Second Report why smaller operators are often price leaders and larger operators tend to be price followers²¹. This is a point which HoustonKemp ignore but which AlixPartners recognise in their report, albeit in a different context²².
 - c. Even if I were to agree with AlixPartners that Optus would represent the principal pricing constraint upon Telstra in the factual, I think that the pricing constraint imposed by Optus would not change much as between the factual or a network sharing counterfactual because Optus' competitive position will not change much.

¹⁸ HoustonKemp para 117.

¹⁹ AlixPartners para 44 and 290(d).

²⁰ My view that TPG will be a significantly more effective competitor in the factual than a network sharing counterfactual is a relative statement and consistent with my view, discussed earlier, that TPG's acquisition of customers in the RCZ from Telstra and Optus will continue to be limited and will take time. TPG's acquisition of customers from Telstra and Optus in a network sharing counterfactual will be even more limited.

²¹ Feasey Second Report para 70.

²² AlixPartners para 296.

- d. I therefore remain confident that the key pricing effect attributable to the transaction derives from the change in TPG's competitive position and not Optus'.

18. In the longer term, AlixPartners argue that prices will be lower in a network sharing counterfactual as a result of additional network investments made by Optus²³. I discuss the effect of the transaction on Optus' incentive and ability to invest in the next section. However, when assessing prices in the longer term AlixPartners ignore that TPG will also be a less effective competitor and weaker pricing constraint on Telstra in such a counterfactual. The overall effect on prices in such a counterfactual will therefore depend on the relative significance of these two effects. AlixPartners do not undertake this assessment because they ignore the second effect.
19. In my view, for the reasons given in my Second Report, the 'TPG effect' will dominate in relation to prices in both the short and the long term²⁴. The Optus pricing effect associated with any additional investments in its network will be relatively insignificant because, as I discuss in the next section, the effect of sharing with TPG on Optus' ability and incentive to invest in a network sharing counterfactual will itself be relatively insignificant.

The impact of the transaction upon Optus' incentives and ability to invest, and therefore upon the likely level of investment which Optus would in fact make, in the factual and counterfactual

20. Given that HoustonKemp now have no clear position on short term price effects of the transaction, the only point about which HoustonKemp seem certain is that Optus would reduce its investment in the factual relative to a network sharing counterfactual²⁵. In coming to this view, I note that HoustonKemp place significant weight on the fact that Optus' management have said they would invest less, which is a point I addressed in my Second Report and evidence to which I would attach very little weight for the reasons given there²⁶.
21. So far as I can see HoustonKemp's position relies on the following logic:
 - a. Optus would invest less in its network than under prevailing conditions of competition as a result of the transaction because of the 'TPG effect'²⁷ (I explained in my Second Report why I do not agree with this²⁸).

²³ AlixPartners para 46.

²⁴ Feasey Second Report para 55.

²⁵ HoustonKemp Second Report para 119 and 124.

²⁶ Feasey Second Report para 87.

²⁷ HoustonKemp Second Report para 119 and HoustonKemp para 89-90.

²⁸ Feasey Second Report para 94-95.

- b. It is now unclear whether Optus would invest more or less than the prevailing conditions of competition in a counterfactual in which it shared its network with TPG²⁹ (I explained in my Second Report why I agree there is some uncertainty about this but greater certainty that the effect would not in any event be very significant³⁰).
- c. Less investment by Optus in the factual relative to prevailing conditions of competition will therefore also mean less investment by Optus in the factual compared to a network sharing counterfactual.

22. This logic is flawed. HoustonKemp has concluded that there could be either more or less investment by Optus in a network sharing counterfactual than under prevailing conditions but they are uncertain about which it is. That being so, they cannot be certain that the factual will involve less investment by Optus than a network sharing counterfactual. If such a counterfactual were to result in even less investment by Optus than in the factual then the factual will involve more investment by Optus than the counterfactual. Since any conclusion on the effect of the transaction for investment must involve comparison of the factual with a network sharing counterfactual and not with prevailing conditions of competition, HoustonKemp cannot be certain about the effect on Optus' investment of the transaction if they are uncertain about investment in such a counterfactual. The consequence of this is that HoustonKemp cannot offer any overall view on the competitive effects of the transaction insofar as it relates to investment by Optus.

23. HoustonKemp seem confused about my statement in my Second Report that mobile operators can invest both to seek to narrow differences between themselves and competitors and to differentiate themselves from their competitors³¹. There is no contradiction once it is understood that the incentive depends upon the relative market position of the operator. A leading firm like Telstra will, in my experience, seek to differentiate its services and network from its rivals in order to sustain premium prices in the market. Following firms like Optus or TPG will be seeking to narrow the gap, in terms of services and network, between themselves and the leading firm (and potentially between each other). They do so in order to be able to better acquire customers from the leading firm (which holds the largest part of the market) and thereby to realise economies of scale and improve the financial returns they earn on their fixed assets. I explained in my Second Report that competition between operators in Australia appears to have conformed

²⁹ HoustonKemp Second Report para 123. I note also that HoustonKemp criticise me (Second Report para 71) for not setting out in detail what the terms of a network sharing counterfactual between Optus and TPG would be. I think this is an unreasonable and unrealistic expectation. I did discuss counterfactuals in some detail in my First Report (para 39-43). To the extent that Optus has evidence as to what form such an arrangement would take, Optus is better placed to provide the ACCC with that evidence.

³⁰ Feasey Second Report para 104.

³¹ HoustonKemp Second Report para 64.

with this pattern, with operators succeeding to a greater or lesser degree through their investments (including investments in mergers and acquisitions) over the years³². My assessment of the transaction has been undertaken on the basis that these incentives will continue to apply in the future.

24. AlixPartners repeats and to some extent expands upon arguments about Optus' incentives and ability to invest that were made by CEPA in their report and which I have already addressed in my Second Report³³. AlixPartners consider that the impact of the transaction on investment by Optus is the key issue for the competitive assessment in this case and the basis on which they conclude there will be a lessening of competition.
25. The central contention of both AlixPartners and CEPA is that the effect of the transaction, by increasing the competitive constraint imposed by TPG and Telstra, will be to materially reduce Optus' incentive and ability to invest in its network, including in the RCZ³⁴. This is because, they say, TPG and Telstra will acquire customers from Optus as a result of the transaction and with fewer customers, Optus' ability to earn a return on additional network investments will be diminished. If Optus invest less as a result, the competitive constraint imposed by Optus on Telstra will diminish. This will in turn lead Telstra to also invest less in its network than it would otherwise in a network sharing counterfactual.
26. I noted in my Second Report the inconsistency between the view of Optus' incentives to invest that has been advanced by CEPA, and now by AlixPartners, and the view advanced by HoustonKemp³⁵. HoustonKemp considers that Optus' conduct in the factual will primarily be influenced by TPG, and that the improvement in TPG's service will weaken Optus' incentives to invest, whereas any improvement in Telstra's services would strengthen Optus' incentives to invest. HoustonKemp say that the 'TPG effect' will dominate and this is why Optus can be expected to invest less as a result of the transaction³⁶.
27. I challenged HoustonKemp's claim that Optus' management would distinguish between the competitive threats presented by TPG and those presented by Telstra in my Second Report. I argued that, rather than being at odds or in opposition with each other, the incentive to catch up or narrow the gap with both TPG and with Telstra would incentivise Optus to invest³⁷. This is because both TPG and Telstra provide a similar form of competition to Optus as a result of their

³² Feasey Second Report para 92.

³³ Feasey Second Report para 95.

³⁴ AlixPartners para 19 and 36.

³⁵ Feasey Second Report para 88.

³⁶ I discussed this at para 83-88 of Feasey Second Report.

³⁷ Feasey Second Report para 89 and 90.

joint use of the MOCN in the RCZ, albeit that Telstra retains some other advantages over TPG both within and beyond the RCZ which will mean it will remain an even stronger and more effective constraint.

28. It appears to me that AlixPartners (and CEPA) take the same view as I do and consider that Optus will be adversely affected in the factual by the loss of customers to both Telstra and TPG and that competition from Telstra will be similar in nature and effect to competition from TPG. This is in contrast to HoustonKemp's contention that these competitive forces will work in opposing directions.
29. The difference between HoustonKemp and AlixPartners/CEPA might, however, be explained by noting that HoustonKemp seem to be primarily concerned with Optus' incentive to invest (which it says will be weaker in the factual) and less with its ability to invest, whereas AlixPartners seem to be more concerned with ability, which they see as being a function of expected returns from the investment, and less with incentives. This means I think both HoustonKemp and AlixPartners/CEPA offer only a partial assessment and that a proper assessment requires consideration of both incentive and ability. For the reasons explained in my Second Report, I consider that Optus' incentives to invest will likely strengthen as a result of the transaction but that its ability will be somewhat (but not materially) diminished³⁸.
30. I think it is common ground that network investment decisions involve comparison of the cost of the investment with the revenues that are expected to be earned from both existing and any newly acquired customers. AlixPartners describe Optus' investments in 2015-17 as being predicated on expected gains in market share³⁹. Smaller operators will often invest and incur short term losses in order to acquire customers and access economies of scale and positive returns in the longer term⁴⁰. It is often the case, in my experience, that investments which are predicated upon acquiring new customers to make a return are more risky than those which rely upon the retention of existing customers because the results of the former activity tend to be more uncertain than the latter. It is not clear to me that Optus' past investments in its network in the RCZ have generated the positive returns that were expected. However, all investors know that past experience may not be a good guide to the future, and that losses incurred in the past are not relevant to the forward looking assessment of future investments. Crucially, the extent to which an operator will be willing to take risks with its capital will also depend upon the risks it faces of not investing. In the present case, the main effect of the transaction is to introduce a risk to Optus that it will begin to

³⁸ Feasey Second Report para 104.

³⁹ AlixPartners para 85.

⁴⁰ As recognised by AlixPartners at para 134.

lose customers who value services in the RCZ to TPG because the transaction will enable TPG to offer such services far more effectively and credibly than it has been able to do in the past or in a network sharing counterfactual. In contrast, the risk that Optus will lose customers who value coverage in the RCZ (and beyond) to Telstra already existed and is in my view unlikely to change much as a result of the transaction.

31. The management of Optus are therefore likely to face greater risks when making network investments as a result of the transaction but will also face greater risks of losing customers from not doing so. It is quite reasonable for the management of Optus to wish to reduce these risks. But it does not follow that the consequence of a higher risk environment in which to make investment decisions is that Optus will undertake less investment. If the costs or risk of not investing have become much higher, and the cost or risk of investing only somewhat higher, then Optus will continue to have strong incentives to invest in its network and these incentives may in fact be stronger than before. Indeed, in my view, this is a reasonable characterisation of the effect of the transaction upon Optus' investment incentives⁴¹.
32. AlixPartners note, correctly in my view, that decisions to invest will also anticipate the competitive response from the rival, which in relation to network investment in the RCZ is primarily Telstra as the owner of the rival network⁴². AlixPartners' position appears to be that in the factual Telstra will obtain significant benefits from the MOCN arrangement which would not be available to it in a network sharing counterfactual and that these will enable it to respond to any additional investments which Optus make by making investments of its own at lower cost. Optus' management will anticipate this and so will conclude that they can never make additional investments in the expectation of acquiring additional customers. AlixPartners conclude that, as a result, Optus will invest less in its network in the factual.
33. I do not agree. This is because, as I explained earlier in this report, I do not consider that the additional advantages in relation to the RCZ that Telstra derives from the MOCN arrangement to be particularly significant in the context of the advantages which Telstra already holds. The transaction specific effect is small. AlixPartners assert that there are advantages but do not offer any evidence as to their significance. The additional revenues and contribution to profits from payments received from TPG⁴³ are, in my view, relatively insignificant within the overall

⁴¹ Note that in a counterfactual which involved network sharing between TPG and Optus (as adopted by AlixPartners) I would expect Optus' incentives to invest to be lower because any benefits from the investment will be shared with TPG. I noted earlier that HoustonKemp accept that the incentive to invest in the counterfactual is uncertain, which I interpret to mean they also accept it could be weaker as well as stronger.

⁴² AlixPartners para 182 and 185.

⁴³ HoustonKemp say in their Second Report that the profit contribution from wholesale payments under the MOCN arrangement will be proportionately higher than the revenue contribution. They give no reason why this

competitive context for the reasons given earlier in this report and previously. I also see no reason why Optus would not respond to the greater threat from TPG. TPG's ability to acquire customers from Telstra and Optus, while improved by the transaction, must not be overestimated.

34. I therefore do not agree with AlixPartners that we will see 'substantial adverse effects' and 'immediate competitive harm'⁴⁴ because TPG will transfer its traffic in the RCZ to Telstra's network. These effects might be significant if the network sharing arrangement were national in scope, but it is not. Elsewhere in their report, AlixPartners accept that TPG will remain a weaker competitor than Optus notwithstanding the transaction⁴⁵. I consider this will be particularly so in the RCZ where TPG's retail presence and capability is more limited than Optus.
35. I consider that the most significant benefit Telstra will derive from the transaction is access to the TPG spectrum. I accept that this will enable Telstra to alleviate congestion and that this may make it harder for Optus to acquire from Telstra those customers who benefit from this⁴⁶. However, as noted earlier, Telstra has and will continue to retain significant advantages over Optus in terms of scale and investment capability in the RCZ and I observe that these advantages have not deterred Optus from investing in the RCZ in the past⁴⁷. Compared to these pre-existing advantages (which exist in both the factual and a network sharing counterfactual) I think any transaction-specific advantages that accrue to Telstra as a result of the transaction will have an insignificant effect on Telstra's ability to meet competition from Optus⁴⁸. AlixPartners' and Optus' position appears to be that the effect of the transaction on these comparative advantages will be so significant that Optus will give up any thought of being able to acquire customers from Telstra (or TPG) and will no longer contemplate investments which it would otherwise have made. As explained earlier, I think this is to greatly exaggerate the impact of the transaction on Telstra's ability to respond to

should be the case and in my experience the opposite is generally true (i.e. wholesale margins are typically significantly lower than retail margins). I explained in my reports why I expected TPG to be able to obtain favourable wholesale fees (which would reduce Telstra's margins) in return for allowing Telstra access to its spectrum, Feasey Second Report para 53.

⁴⁴ AlixPartners para 275.

⁴⁵ AlixPartners para 284.

⁴⁶ I note that AlixPartners seek to argue that Telstra obtains significant advantages from the transaction which will deter Optus from investing, on the one hand, but at the same time argues that any efficiency benefits Telstra derives from sharing spectrum are 'overstated' (para 306).

⁴⁷ I note that an Analysys Mason Network Cost Analysis report prepared for Optus dated 24 October 2022 states: 'Optus' network is significantly more expensive to operate per GB in the RCZ than Telstra's network' (p. 2). Although their modelling results are redacted, it seems to me likely that Optus' network would also continue to be significantly more expensive to operate in a network and spectrum sharing counterfactual and in the factual. In other words, I would not expect the factors which really influence the relative costs of Telstra and Optus in operating networks in the RCZ to be altered to any significant extent by the transaction.

⁴⁸ I note that AlixPartners have also ignored the possibility that the increase in competition from TPG as a result of the transaction will mean lower prices and margins for Telstra (and Optus), which may weaken Telstra's incentive to respond to investments made by Optus, relative to the prevailing competitive conditions in which Telstra's customers may profit.

any investments which Optus might make and to greatly exaggerate the effect of the transaction on Optus' incentive or ability to invest.

36. I accepted in my Second Report (and here) that Optus may have somewhat less ability to invest in the RCZ under the factual than a counterfactual involving network sharing between Optus and TPG⁴⁹. Both Telstra and Optus will gain something from sharing their networks with TPG. However, I take this view not because I agree with AlixPartners that Optus would have less ability to invest as a result of losing customers to Telstra and TPG in the factual, but because I think Optus' ability to invest will improve somewhat under a network sharing counterfactual relative to the factual. However, this improvement will be very marginal for two reasons. First, the revenues and profits which Optus will earn from variable wholesale fees paid by TPG in such a counterfactual will take time to accrue in exactly the same way as for Telstra in the factual, and I expect these fees to be lower than those Telstra will obtain in the factual. This is because I expect TPG to be a less effective competitor to Telstra (and Optus) if it shares Optus' network than if it shares Telstra's, given the superiority of the latter in the RCZ and the likely worse commercial terms TPG would obtain from Optus in a sharing arrangement⁵⁰, with the consequence that TPG will acquire (even) fewer customers and generate (even) less traffic in the RCZ than in the factual. Second, as explained in my Second Report and later below, Optus will derive much less benefit from the TPG spectrum than Telstra because the latter already experiences capacity constraints at sites in the RCZ whereas Optus does not⁵¹.
37. AlixPartners do not agree with me that Optus would derive minimal benefits from access to the TPG spectrum. They argue that even if Telstra does alleviate capacity constraints by sharing the TPG spectrum in the factual, these consumer benefits need to be offset by the loss of competition in the longer term that arises from depriving Optus of access to that same TPG spectrum⁵². I do not agree with AlixPartners' claim that sharing TPG's spectrum would 'materially reduce the costs of Optus and TPG to provide capacity in the RCZ' relative to the position which Optus would find itself in the factual⁵³. If Optus already has underutilised spectrum in the RCZ, as I understand it does, then the incremental cost to Optus of supporting additional traffic generated by either its own or TPG's customers will be negligible and broadly the same irrespective of whether it has access to the TPG spectrum or not. I certainly do not accept that the efficiencies to be derived from sharing the TPG spectrum are similar in nature and magnitude for both Telstra

⁴⁹ Feasey Second Report p.104.

⁵⁰ Feasey Second Report footnote 75.

⁵¹ Feasey Second Report para 103.

⁵² AlixPartners para 157.

⁵³ AlixPartners para 161.

and Optus when there are significant differences between them in terms of supply and demand in the RCZ.

38. I note that AlixPartners refer to a report by Analysys Mason, prepared for Optus, which appears to discuss the efficiencies Optus would derive from sharing the TPG spectrum⁵⁴. Since the relevant sections of both the AlixPartners report and the Analysys Mason report are heavily redacted, I am unable to assess the assumptions or results in the way that the ACCC will be able to do. I have also reviewed the report by Aetha, prepared for Telstra, dated 27 July 2022, which addressed similar issues. That said, I note the following:

- a. Each report takes a different approach to quantifying the benefits which Telstra and Optus might be expected to obtain from sharing spectrum and incorporating the traffic of TPG's retail customers onto their networks. Aetha models the effects for Telstra in a MOCN factual, but only considers how Optus could accommodate its own traffic absent a network sharing arrangement with TPG and does not consider a network sharing counterfactual. Analysys Mason models a counterfactual in which Optus has the benefit of network sharing with TPG. Both also model Telstra's position if it did not share its network, which is the case in any counterfactual. Aetha's model computes how much capacity each network will have available and expresses this in terms of the growth rate in traffic which the network can accommodate. Analysys Mason's model computes the impact of sharing on the unit cost of conveying traffic over the RCZ network (but not, it appears, the effect this will have on the average costs of conveying traffic on the network nationally which is what will inform retail prices).
- b. Both models assume some investment in additional sites in the RCZ each year to expand capacity irrespective of whether or not the operator is sharing with TPG⁵⁵.
- c. Both models show Telstra benefits from the transaction. Analysys Mason's model shows that Telstra will obtain lower costs in the factual relative to its costs of carrying traffic on a standalone basis in a network sharing counterfactual. These are obtained by Telstra being able to use the TPG spectrum to expand capacity rather than having to invest in additional sites⁵⁶. Aetha's model shows that Telstra will benefit in terms of expanding

⁵⁴ AlixPartners para 172-3 referring to Analysys Mason Network Cost Analysis Report dated 24 October 2022.

⁵⁵ Analysys Mason assume Optus adds sites (figures redacted) but seems to assume Telstra does not (p.6), Aetha (p. 5) assume 140 sites p.a. as the central case for all operators.

⁵⁶ I note that this comparison assumes that capacity will be exogenous and that Telstra would provision the same amount of capacity in its network in the RCZ irrespective of whether it does the transaction with TPG or not. I think it unlikely that Telstra would do this and more likely that Telstra would invest less and tolerate a greater degree of congestion in its RCZ network, as is currently the case in the absence of access to the TPG spectrum.

capacity and could accommodate significantly higher levels of traffic growth in the factual (~30% p.a. in the central case⁵⁷) than a counterfactual (in which it does not share a network with TPG) (~24% p.a.)⁵⁸. The Aetha results confirm that Telstra's network would be unable to accommodate most reasonable projections of traffic growth for Telstra's customers and would remain congested in any counterfactual but that traffic growth for both Telstra and TPG's customers will likely be accommodated without congestion in the factual.

- d. Analysys Mason's model shows that, like Telstra in the factual, Optus will benefit from lower costs of carrying traffic in a network sharing counterfactual. However, I cannot tell how much Optus would benefit or whether Optus' network unit costs in such a counterfactual remain higher or would become lower than Telstra's network unit costs. The report says only that Optus' network is 'significantly more expensive than Telstra's' when both are compared on a standalone basis⁵⁹. My expectation would be that Telstra's network costs would remain lower than Optus' in a network sharing counterfactual, given Telstra's pre-existing economic advantages in relation to the provision of services in the RCZ, and that the benefits to Optus of sharing with TPG in the RCZ would not be very substantial.
- e. The Aetha results show that Optus will have more spare capacity than Telstra to accommodate growth in the traffic of its own customers (or the acquisition of additional customers) in the factual (~35% vs ~30% p.a. in the central case⁶⁰) but, as noted above, Aetha does not model how much more capacity Optus might have in a network sharing counterfactual.

39. Although the redactions mean I cannot be definitive, I consider that both reports are likely to support my conclusion that Telstra will benefit from sharing the TPG spectrum to a much greater extent than Optus would. This is due to the spare capacity which Optus retains in its network as a result of its existing spectrum holdings and current and likely future traffic volumes. I recognise that it may be possible to conceive of scenarios in which this is not the case: for example, if I were to assume that Optus' traffic growth would far outpace Telstra's far into the future. However, I think it is only by adopting such unrealistic and asymmetric assumptions about traffic

⁵⁷ Aetha fig 1.3 p. 7.

⁵⁸ Analysys Mason's model assumes annual traffic of 30% in the base case, which is higher than the historic 26% p.a since June 2019 to which Aetha refer at p.7.

⁵⁹ Analysys Mason p.2.

⁶⁰ Aetha fig 1.3, p. 7.

growth that the models could be used to show Optus deriving significant benefits from the TPG spectrum, or greater benefits than Telstra⁶¹.

40. Overall, I continue to think that Optus is likely to have a greater incentive to invest in the factual to catch up with Telstra and TPG but, for the reasons just discussed, a marginally lesser ability to do so relative to a counterfactual involving network sharing with TPG. I therefore do not expect the impact of the transaction on Optus' investment decisions, whether to invest somewhat more or somewhat less, to be material either way. This means no more than that an increase in retail competition will likely increase the risks associated with making sunk investments in networks for all operators and that investing in less competitive and less risky conditions will generally be preferred by the owners of firms and providers of capital. It does not follow, however, that there will be less investment undertaken in more competitive markets or more investment will be forthcoming in less competitive conditions⁶². It therefore does not follow that Optus will decide to invest less if the transaction enables TPG to pose a significantly more effective competitive threat to Optus than it has done in the past or would do in a network sharing counterfactual.
41. I therefore strongly disagree with the claim of AlixPartners and the other Optus experts that the evidence shows that the transaction will have a 'materially negative impact on Optus' 5G investments'⁶³. I have yet to see anything in the submissions from Optus or its experts that would persuade me of such a conclusion.

Overall conclusions in light of these points

42. Although the expert reports in this proceeding have been extensive and the competitive assessment requires consideration of a number of quite complex potential effects, all involving some unavoidable degree of uncertainty, I think the critical points of disagreement between myself and Optus' experts are now relatively clear and straightforward.
43. The first is whether TPG will be a significantly more effective competitor (to Telstra and Optus) in a factual in which it obtains access to the Telstra network in the RCZ than in a counterfactual in

⁶¹ As AlixPartners rightly note (para 264), the issue is not the commercial benefits which either the parties to the transaction might gain or third parties might gain under alternative arrangements, but the effects for competition and consumers. I would add that it is not the purpose of merger assessments to allow third parties to be able to enter into arrangements which they failed to pursue earlier as a result of poor commercial judgments.

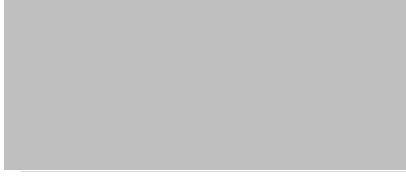
⁶² The ACCC will be aware that there has been considerable debate in the mobile industry as to the relationship between competition, as evidenced by the number of competitors, and investment levels by operators. A good overview, which concludes that there is 'no evidence that service quality increases when markets become more concentrated', was published by Ofcom in 2020, see https://www.ofcom.org.uk/_data/assets/pdf_file/0036/209799/market-structure,-investment-and-quality-in-the-mobile-industry-discussion-paper.pdf

⁶³ AlixPartners para 222.

which it obtains access to the Optus network. AlixPartners and others suggest that the difference would not be very great and the competitive constraint that TPG would provide would be similar in either case. I do not agree. The evidence is that Telstra's network in the RCZ is significantly better than Optus' and I would expect TPG to be able to provide a significantly greater competitive constraint to Telstra and Optus in the factual than in a network sharing counterfactual. To agree with AlixPartners and others I would have to be persuaded that Optus would invest enough to eliminate the differences between its network and Telstra's network in such a counterfactual. Even if I accept that Optus' ability to invest in its network will be improved by sharing with TPG, I have seen no evidence to suggest that the improvement would be of such magnitude that the difference in network coverage or quality between Telstra and Optus would be eliminated or even significantly reduced⁶⁴.

44. The second point of contention is whether Optus would invest more and thereby be a significantly more effective competitor in a counterfactual in which it obtains access to TPG's wholesale traffic and TPG's spectrum. AlixPartners and others argue that it would. Again, I do not agree. I think the evidence is that TPG's wholesale traffic will be of marginal benefit to Optus for many years (and even less benefit than to Telstra in the factual) and that Optus' existing spectrum holdings and likely traffic growth will mean that any benefits to be derived from TPG's spectrum will also be relatively insignificant. In my view, Optus will remain an effective competitor to Telstra irrespective of whether or not TPG's customers share the network of Telstra or that of Optus in the RCZ.
45. In my view, the assessment boils down to whether, overall, a substantial lessening of competition is likely to arise in the relevant markets when the number of competitors remains the same in the factual and counterfactual but one firm (TPG) will be a significantly more effective competitor in both the short and the longer term and another firm (Optus) may be marginally less effective competitors in the long term. My assessment is that no such substantial lessening of competition will or is likely to arise in these circumstances and that, accordingly, the ACCC should authorise the transaction.

⁶⁴ Elsewhere in their report, AlixPartners emphasise the difference between the Telstra and Optus networks in the RCZ (e.g. para 77 and 80).



Richard Feasey

10 November 2022



Annexure A: Letter of instructions



Special Counsel
Contact

Geoff Petersen
Geoff Petersen
T [REDACTED]

Our ref

GCP:1049539

9 November 2022

By email: [REDACTED]

Mr Richard Feasey

[REDACTED]
Dear Mr Feasey

Application to the Australian Competition and Consumer Commission for Merger Authorisation

- 1 We refer to our letter of engagement to you dated 29 April 2022, letter of instructions dated 19 May 2022 (**May Letter**) and further letter of instructions dated 22 July 2022 (**July Letter**). Defined terms in these letters have the same meaning in this letter.
- 2 We also refer to the submission from Optus in response to the ACCC's Statement of Preliminary Views dated 26 October 2022 (**Optus submission**), and the supporting reports of AlixPartners UK LPP (**AlixPartners**) dated 25 October 2022 (**AlixPartners Report**) and HoustonKemp dated 26 October 2022 (**Second HoustonKemp Report**).
- 3 This letter sets out further instructions for the preparation of an expert report in response to the reports of AlixPartners and HoustonKemp.

Instructions

- 4 Further to the questions and instructions set out in our May and June Letters, you are instructed to prepare a further written report which:
 - (a) addresses the matters raised in the AlixPartners Report and Second HoustonKemp Report, insofar as they relate to the questions asked of you in our May Letter and July Letter, and the opinions expressed in your expert report dated 20 May 2022 and further report dated 25 July 2022; and
 - (b) identifies any change to the opinions expressed in your report dated 20 May 2022 and further report dated 25 July 2022, and the reasons for any such changes.

Background documents and assumptions

- 5 In preparing your report, please consider the documents listed in **Schedule 1** and the factual assumptions and documents referred to in your May Letter and July Letter.

Expert witness code of conduct

- 6 We ask that you prepare your report in accordance with the requirements of the Federal Court's Expert Evidence Practice Note (GPN-EXPT) (**Practice Note**), which includes the Harmonised Expert Witness Code of Conduct (**Code**). A copy of the Practice Note (including the Code) was enclosed with your letter of engagement.

- 7 Under the Code, your report must clearly state the following:
- (i) your name and address;
 - (ii) an acknowledgement that you have read this code and agree to be bound by it;
 - (iii) your qualifications as an expert to prepare the report;
 - (iv) the assumptions and material facts on which each opinion expressed in the report is based (this letter of instructions may be annexed);
 - (v) the reasons for and any literature or other material utilised in support of each such opinion;
 - (vi) (if applicable) that a particular question, issue or matter falls outside your field of expertise;
 - (vii) any examinations, tests or other investigations on which you have relied, identifying the person who carried them out and that person's qualifications;
 - (viii) the extent to which any opinion which you have expressed involves the acceptance of another person's opinion, the identification of that other person and the opinion expressed by that other person;
 - (ix) a declaration that you have made all the inquiries which you believe are desirable and appropriate (save for any matter identified explicitly in the report), and that no matters of significance which you regard as relevant have, to your knowledge, been withheld from the court;
 - (x) any qualifications on an opinion expressed in the report without which the report is or may be incomplete or inaccurate;
 - (xi) whether any opinion expressed in the report is not a concluded opinion because of insufficient research or insufficient data or for any other reason; and
 - (xii) where the report is lengthy or complex, a brief summary of the report at the beginning of the report.

Next steps

8 We look forward to receipt of your report in due course.

Yours faithfully
Gilbert + Tobin



Geoff Petersen
Special Counsel



Simon Muys
Partner



Andrew Low
Partner



Schedule 1 – Documents provided

No.	Document description
1.	Optus: Submission in response to ACCC Statement of Preliminary Views - Telstra and TPG application for merger authorisation for proposed spectrum sharing in regional Australia (26 October 2022)
2.	AlixPartners: Assessment of the application for merger authorisation by Telstra and TPG (25 October 2022)
3.	HoustonKemp: Competitive effects of the proposed Telstra-TPG arrangement – Supplementary expert report of Greg Houston (26 October 2022)
4.	Aetha: Modelling of network capacity in the area covered by the proposed Telstra-TPG MOCN (27 July 2022) (confidential version)
5.	CompassLexecon: Report on behalf of TPG – Issues raised in the ACCC’s Statement of Preliminary Views on proposed Telstra/TPG Agreement (2 November 2022) (confidential version)
6.	Letter to ACCC dated 1 November 2022 regarding the draft section 87B Undertakings (confidential version)
7.	Draft section 87B Undertaking by Telstra and TPG to the ACCC: Joint Undertaking
8.	Draft section 87B Undertaking by TPG to the ACCC: TPG Sites Undertaking (confidential version)