

Submission of NBN Co to Competition Policy Review

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1 Executive Summary

NBN Co welcomes the opportunity to respond to the Competition Policy Review Issues Paper. This submission outlines NBN Co's preliminary response to the following issues raised in the Issues Paper:

- the extent to which the framework regulating the supply of super-fast broadband services to retail and small business end-users strikes an appropriate balance between the promotion of competition, economic efficiency and the achievement of wider policy objectives;
- the appropriateness of the regime of statutory exceptions and exemptions in the *Competition and Consumer Act 2010* (Cth) (**CCA**); and
- the importance of the authorisation regime in the CCA being flexible and transparent.

As the Review Panel has noted, competition issues in the regulation of fixed-line broadband are currently being considered as part of the Independent Cost-Benefit Analysis and Regulatory Review for the National Broadband Network, conducted by an expert panel led by Dr Michael Vertigan AC (**Vertigan Panel**). The Review Panel's Terms of Reference state that the Review Panel may, where appropriate, draw on, but should not duplicate or re-visit the work of the Vertigan Panel.

Accordingly, this submission also outlines NBN Co's position on certain key issues being considered by the Vertigan Panel, should the Review Panel wish to draw on these in its work. NBN Co has prepared this submission on the basis of current policy and regulatory settings.

NBN Co was established with a mandate to provide access to affordable fast broadband services to all premises in Australia. NBN Co operates under a market structure and regulatory framework designed to:

- allow it to achieve the Government's policy objectives;
- promote retail competition in the provision of fixed-line broadband services; and
- address the challenges facing competition arising from the dominance of Telstra as a vertically integrated network provider.

In considering whether there is a need for further competition-related reform in the telecommunications sector, NBN Co considers that, on the whole, the telecommunications access regime contained in Part XIC of the CCA operates effectively, such that major changes to the regime are not required at this stage. Part XIC has been the subject of continuing review and reform; it is now well understood by industry, and the original rationale for introducing the regime remains applicable today. However, there are some areas where amendments to the regime may be appropriate in order to ensure that the regime best promotes the long-term interests of end-users.

NBN Co considers that the regime of statutory exemptions and exceptions in the CCA is appropriate and works well. The regime relevantly allow for the implementation of Government policy which involves conduct that may raise concerns under Part IV of the CCA. The NBN regulatory framework includes two statutory exemptions, which endeavour to facilitate key pillars of the Government's policy relating to the rollout of the NBN and implementation of structural industry reforms.

The authorisation framework and the ACCC's approach in assessing authorisation applications under the CCA must remain flexible and transparent in order to deal with increasingly complex and long-term commercial arrangements in the telecommunications and other infrastructure industries in a timely manner.

2 Government-provided goods and services

Section 3 of the Review Panel's Issues Paper seeks comments on whether government-provided goods and services are delivered in a manner conducive to competition, while meeting other policy objectives.

NBN Co's operations are an example of the provision of goods and services by Government in a manner conducive to competition while achieving the Government's wider policy objectives.

NBN Co was established by the Federal Government in April 2009 to build and operate a super-fast National Broadband Network, with the objective of providing access to affordable fast broadband services to all premises in Australia.¹ NBN Co was created as a wholesale-only, open access network provider, in order to promote retail competition and address the longstanding challenges facing competition in the Australian telecommunications industry arising from the market dominance of Telstra as a vertically integrated network provider:

The Australian telecommunications market is characterised by a very strong and highly integrated incumbent, Telstra... Partly because of this integration, Telstra has been able to maintain a dominant position in virtually all aspects of the market, despite more than 10 years of open competition. It is the Government's view that Telstra's high level of integration has hindered the development of effective competition in the sector.

The National Broadband Network (NBN) will deliver a wholesale-only, open access telecommunications market structure, transforming the competitive dynamics in the Australian telecommunications industry.²

In addition, to address these challenges and to promote NBN Co's ability to achieve the Government's objectives, the legislative framework seeks to ensure that any other super-fast broadband networks being rolled out in Australia operate on a level playing field with NBN Co. Such networks are required to operate on a wholesale-only basis and offer access seekers a Layer 2 bitstream service. It is expected that NBN Co will operate as a national monopoly wholesale provider of fixed-line network services between the Point of Interconnect (**POI**)³ and end-user premises.⁴ This is particularly the case given that fixed-line telecommunications infrastructure often displays strong natural monopoly characteristics.

The fact that NBN Co is required to operate on a wholesale-only, open access basis, coupled with the need for NBN Co to recover its costs and earn a reasonable rate of return, minimises the risk of NBN Co engaging in anti-competitive conduct, and is conducive to the development of a vibrant digital economy. Additional protections are provided through the broader regulatory framework in which NBN Co operates, including in the recent amendments to the telecommunications access regime.

These issues are discussed further below.

¹ Prime Minister and Minister for Broadband, Communications and the Digital Economy, Media Release, 'New Broadband Network', 7 April 2009

² Explanatory Memorandum to the Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Bill 2010, p 2

³ A POI is the inter-network location where traffic is exchanged between one network and another

⁴ With the exception of existing fixed line infrastructure – see Minister for Finance and Deregulation and Minister for Broadband, Communications and the Digital Economy, Statement of Expectations, December 2010, p 4

2.1 Natural monopoly characteristics of fixed-line telecommunications infrastructure

Fixed-line telecommunications infrastructure often displays natural monopoly characteristics, where one firm is able to produce a given set of outputs at a lower cost than two or more firms. As much has been noted by key industry stakeholders, including the ACCC, the Productivity Commission and Treasury.⁵ Where a natural monopoly exists, competitive entry by a second firm may be privately profitable but is economically wasteful. Hence, productive efficiency is maximised where only one firm serves the entire market.

Fixed-line broadband networks often display natural monopoly characteristics due to the strong presence of economies of density (arising from large sunk costs and very low marginal costs) and economies of scale and scope. As a result, the extent to which infrastructure based competition is efficient and sustainable is limited.

As the Review Panel has noted, Government intervention in a market may be necessary in some cases, such as where there are natural monopolies, or to ensure the provision of social welfare services. The establishment of NBN Co as a monopoly fixed-line network between the POI and the end-user premises is an example of such intervention, given that:

- fixed-line broadband networks often display natural monopoly characteristics; and
- it is likely to be uneconomic to rollout a super-fast broadband network in some areas of Australia.

NBN Co notes that the Vertigan Panel is currently considering the nature of infrastructure-based competition that NBN Co should face.

2.2 Vertically integrated network providers

Microeconomic reform and regulation of the telecommunications industry in Australia has traditionally sought to address issues arising from the dominance of Telstra as a vertically integrated network provider operating a number of networks with natural monopoly characteristics. These concerns have been noted by the ACCC:

As the vertically integrated provider of access to the ubiquitous fixed-line network, Telstra has had the incentive and ability to favour its retail businesses over its wholesale customers. This has allowed Telstra to maintain a dominant position in downstream markets and has hindered the development of fully effective competition.⁶

As stated above, NBN Co was created in response to these concerns as a wholesale-only, open access network, with clear line of business restrictions, in order to '*transform the competitive dynamics in the Australian telecommunications industry*'.⁷

In addition, the *Telecommunications Act 1997* (Cth) (**Telecommunications Act**) was amended to create a framework for the voluntary structural separation of Telstra.⁸ In February 2012, the ACCC accepted Telstra's Structural Separation Undertaking and migration plan, which outlines how Telstra will progressively migrate voice and broadband services from its copper and HFC networks to the NBN. Together, these reforms attempted to 'once and for all' address the competition issues arising from Telstra's vertically integrated structure and dominant market position.

⁵ See ACCC, 'ACCC submission to the Independent Cost Benefit Analysis Review of Regulation first issues framing paper', 14 March 2014 (**ACCC Vertigan Submission**), p 4; Productivity Commission, 'Telecommunications Competition Regulation Inquiry Report', 20 September 2001, pp 23-28; Treasury, 'Submission to the independent cost-benefit analysis and review of regulation for the National Broadband Network: Regulatory issues framing paper', 19 March 2014, p 2

⁶ ACCC Vertigan Submission, p 5

⁷ Explanatory Memorandum to the Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Bill 2010, p 2;

⁸ See Telecommunications Act, Part 33

2.3 The objectives of Government

The Government has expressed its objectives for NBN Co in a series of Statements of Expectations and communications from Shareholder Ministers.

The Government issued its first Statement of Expectations to NBN Co in December 2010, which reflected the Government's central policy objective for NBN Co:

*to deliver significant improvement in broadband service and quality to all Australians, address the lack of high-speed broadband in Australia, particularly outside of metropolitan areas, and reshape the telecommunications sector.*⁹

The most recent Statement of Expectations issued to NBN Co (in April 2014) sets out the current Government's policy objectives for NBN Co:

The Australian Government is committed to completing the National Broadband Network ('NBN') and ensuring all Australians have access to very fast broadband as soon as possible, at affordable prices, and at least cost to taxpayers...

*The Government intends the NBN to be a wholesale-only access network, available on equivalent terms to all access seekers, that operates at the lowest practical levels in the network stack. The Government expects completion of the NBN will result in the structural separation of Telstra and a competitive market for retail broadband and telephony services.*¹⁰

This Statement of Expectations directed NBN Co to transition from a primarily fibre-to-the-premises model to the 'optimised multi-technology mix' model set out in NBN Co's Strategic Review of December 2013. The design of this model is to be guided by the Government's policy objectives of providing download data rates (and proportionate upload rates) of at least 25 megabits per second to all premises and at least 50 megabits per second to 90 per cent of fixed line premises as soon as possible. NBN Co is required to achieve these objectives while operating as a commercial entity.

Additionally, NBN Co is charging access seekers uniformly for services across NBN Co's network for all technologies and for the basic service offering (uniform national wholesale pricing (**UNWP**)).¹¹ A natural consequence of this policy is that the provision of broadband infrastructure by NBN Co in areas which are uneconomic to serve is funded by a cross-subsidy which is internal to NBN Co. While the April 2014 Statement of Expectations does not refer to an objective of UNWP, the Coalition's broadband policy of April 2013 suggested that, under a Coalition Government, any UNWP arrangements contained in an NBN Co undertaking accepted by the ACCC will become uniform national wholesale price **caps** for directly comparable products.¹²

NBN Co's ability to provide access to affordable fast broadband to all Australians via an internal cross-subsidy may be significantly compromised if NBN Co were to face infrastructure competition from network providers which focussed only on areas which were economic to serve. Consequently, NBN Co has submitted to the Vertigan Panel that, should competition regulation allow opportunistic market entry in high-value, low-cost to serve areas, the Vertigan Panel would need to consider alternative models of funding for areas which are uneconomic to serve, such as subsidy mechanisms or industry levies, in order to achieve the Government's broader policy objectives. Further – and critically – the introduction of any additional infrastructure based competition would necessarily require an assessment of the appropriateness of the entire regulatory framework, which is premised on the assumption that NBN Co will operate as a monopoly wholesale local access provider.

⁹ Minister for Finance and Deregulation and Minister for Broadband, Communications and the Digital Economy, Statement of Expectations, December 2010

¹⁰ Minister for Communications and Minister for Finance, Statement of Expectations, April 2014

¹¹ Minister for Finance and Deregulation and Minister for Broadband, Communications and the Digital Economy, Statement of Expectations, December 2010

¹² The Coalition's Plan for Fast Broadband and an Affordable NBN, April 2013, p 8

2.4 The current market structure and regulatory regime

NBN Co submits that the current regulatory regime generally works well in:

- allowing NBN Co to achieve the Government's objective of ensuring that all Australians have access to affordable very fast broadband, while facilitating competition in downstream markets; and
- ensuring there is limited incentive and scope for NBN Co to seek to earn economic profits and exercise any market power to the detriment of competition.

This follows inevitably from:

- the major policy decisions made to date concerning the rollout of a high speed broadband network by NBN Co on a wholesale only, open access basis; and
- the need for NBN Co to recover its costs and earn a reasonable rate of return.

Key elements of the current regulatory regime are addressed below.

Promoting the long-term interests of end-users

The current regulatory regime is underpinned by the objective of promoting the long-term interests of end-users.¹³ There is a broad acceptance of the usefulness and meaning of this concept, which has framed the regulation of telecommunications since 1997. The promotion of the long-term interests of end-users is measured against the following objectives:

- promoting competition in markets for listed services;
- achieving any-to-any connectivity in relation to carriage services that involve communication between end-users;
- encouraging the economically efficient use of, and the economically efficient investment in:
 - (i) the infrastructure by which listed services are supplied; and
 - (ii) any other infrastructure by which listed services are, or are likely to become, capable of being supplied.

NBN Co submits that the long-term interest of end-users objective is appropriate as it seeks to promote the welfare of Australians, which is consistent with the overall object of the CCA.¹⁴ The long-term interests of end-users objective recognises that competition is not an end in itself, but rather is a process by which economic efficiency is achieved, which must be considered in the context of wider social objectives. This was emphasised in the Hilmer Report:

Competition policy is not about the pursuit of competition for its own sake. Rather, it seeks to facilitate effective competition in the interests of economic efficiency while accommodating situations where competition does not achieve economic efficiency or conflicts with other social objectives. These accommodations are reflected in the content and breadth of application of pro-competitive policies, as well as in the sanctioning of anti-competitive arrangements on public benefit grounds.¹⁵

Further, the long-term interests of end-users objective seeks to strike a balance between the promotion of competition and economically efficient investment. This is important because fixed-line telecommunications infrastructure often displays natural monopoly characteristics, and the telecommunications industry generally is characterised by phased investments of a sunk nature, and declining marginal costs. As an example, the objective of promoting competition may suggest setting infrastructure access prices at a level close to marginal costs. However, such a policy would significantly deter investment by infrastructure providers, and the cost of this effect would therefore likely outweigh any benefits arising from competition.

¹³ See CCA s152AB

¹⁴ See CCA s2

¹⁵ Independent Committee of Inquiry, 'National Competition Policy', 1993, p 6

See also Productivity Commission, 'Telecommunications Competition Regulation Inquiry Report', 20 September 2001, pp 4, 153

NBN Co's wholesale-only mandate

To ensure that NBN Co remains a wholesale-only operator, the scope of NBN Co's commercial activities is constrained by the *National Broadband Network Companies Act 2011* (Cth) (**NBN Co Act**). This legislation imposes restrictions on NBN Co's business activities (sometimes referred to as line of business restrictions), including provisions that have as their object ensuring that:

- the supply of services by NBN Co is effectively wholesale-only;¹⁶
- NBN Co does not supply a content service;¹⁷
- NBN Co does not supply services other than an enumerated list of services;¹⁸ and
- NBN Co does not supply non-communications goods.¹⁹

Consequently, NBN Co can only supply services to:

- carriers and carriage service providers; and
- specified utilities, in which case the NBN Co services may only be used for the utilities' own use and must not be resupplied.

NBN Co's wholesale-only mandate has also been given effect to in its constitution.²⁰ In addition, the Communications Minister has the power to require NBN Co to supply, or not supply, particular services.²¹

NBN Co's open access mandate

Part XIC relevantly provides that all eligible services supplied by NBN Co must be declared services for the purpose of Part XIC. An eligible service may be declared by the ACCC, or is deemed to be a declared service if NBN Co has in place a Special Access Undertaking (**SAU**) or a standard form of access agreement in respect of that service. NBN Co is required to have in place a standard form of access agreement for all declared services it supplies.

In supplying declared services, NBN Co is obliged to comply with the 'Category B' (NBN Co specific) standard access obligations, which require NBN Co to:

- supply any declared services which relate to NBN Co to an access seeker, upon request, so that the access seeker can provide carriage services and/or content services to end users;
- enter into an access agreement with a service provider, on request, on the terms and conditions set out in a standard form of access agreement;
- not discriminate between access seekers in supplying declared services and in undertaking a number of specified related activities;
- lodge with the ACCC all access agreements to which NBN Co is a party and all variations to those access agreements; and
- provide the ACCC with a statement about any differences between an access agreement it has entered into and an SAU or access determination that relates to the service the subject of the access agreement.

The ACCC has the power to scrutinise any SAU prepared by NBN Co, and to specify terms and conditions in an access determination if the ACCC does not consider NBN Co's terms to be reasonable. Further, if prompt action is required, the ACCC can act swiftly by issuing Binding Rules of Conduct. An access seeker may acquire a declared service from NBN Co on the terms and conditions set out in an access determination or in Binding Rules of Conduct if it is unable to reach an agreement with NBN Co.

¹⁶ NBN Co Act, s9

¹⁷ NBN Co Act, s17

¹⁸ NBN Co Act, ss 5 and 18

¹⁹ NBN Co Act, s19

²⁰ See rule 4.1.1

²¹ NBN Co Act, Part 2, Division 6

Level playing field arrangements

Amendments were made to the Telecommunications Act and the CCA to ensure that NBN Co competes on a level playing field with any other superfast broadband networks being rolled out in Australia. We describe these amendments and their objectives below.

To establish a level playing field, a number of legislative amendments were made, including:

- Parts 7 and 8 of the Telecommunications Act, which require superfast broadband networks built or upgraded after 1 January 2011 servicing residential and small business customers to operate on a wholesale-only basis and to offer access seekers a Layer 2 bitstream service. The Minister has the power to exempt networks from the requirements of Parts 7 and 8. To date, five exemptions have been granted.
- Under amendments made to Part XIC of the CCA, the ACCC is required to declare that a specified layer 2 bitstream service supplied using a designated superfast telecommunications network is a declared service. Providers of these layer 2 bitstream services are then subject to the same standard access obligations as NBN Co including an obligation to supply on a non-discriminatory basis. The ACCC may make an access determination or binding rules of conduct in relation to these services.
- Special arrangements apply in new real estate developments. These arrangements are set out in the Fibre in New Developments Policy Update of June 2011.

It is important to note that Parts 7 and 8 of the Telecommunications Act do not establish NBN Co as a statutory monopoly – they do not prohibit or preclude market entry. To the contrary, a new entrant into the fixed line telecommunications market has the choice to either invest in competitive infrastructure or to seek access to declared services through the telecommunications access regime under Part XIC of the CCA.²² New entrants investing in super-fast broadband networks are required to operate on a wholesale-only basis, and therefore on a level playing field with NBN Co and Telstra.²³ Parts 7 and 8 are therefore intended to achieve ‘competitive neutrality’ among network providers in the industry, including NBN Co.

This is reflected in the Explanatory Memorandum to the legislation which implemented the level playing field provisions:

Amongst other things, the NBN Implementation study identified that difficulties could arise for the delivery of the Government's NBN policy objectives as a result of NBN Co being subject to strict regulatory requirements while competing against other, less regulated, providers of superfast broadband. In particular, the study noted the scope for competing providers to target high-income and low-cost, high-density areas, operate as vertically-integrated providers and advantage themselves over independent retail service providers (RSPs) on the NBN and ignore technical specifications employed by NBN Co. This could mean that where other providers rolled out superfast networks in advance of the NBN, these would not deliver consumers in those areas the same benefits as the NBN. Moreover, by cherry-picking high-value markets such providers could undermine NBN Co's ability to deliver the Government's policy objectives for the NBN nationally. The Implementation Study therefore recommended that the Government look at measures to provide a more level playing field for all superfast broadband networks....

Together these amendments should ensure that end-users have access to the same high-quality superfast broadband services, regardless of the network provider, and assist the NBN in meeting its objectives nationally by ensuring it operates on a more level regulatory playing field.²⁴

The level playing field provisions seek to strike a balance between the objectives of promoting competition, achieving structural separation and ensuring end-users have access to affordable fast broadband services. NBN Co submits that it is too early to assess whether the provisions will operate to achieve their originally intended purpose.²⁵

²² This choice is not inconsistent with Part IIIA of the CCA, which also establishes an access regime for essential facilities but do not preclude investment by a new entrant in alternative facilities

²³ NBN Co is required by legislation to operate on a wholesale only basis while Telstra Corporation Limited is prohibited by legislation to supply retail fixed line services after the Designated Day using a network it either owns or controls

²⁴ Explanatory Memorandum to the National Broadband Network Companies Bill 2010 (Cth), Telecommunications Legislation Amendment (National Broadband Network Measures – Access Arrangements) Bill 2010 (Cth), pp 13-14

²⁵ See CCA s2

2.5 NBN Co's mandate to operate efficiently and commercially

The current regulatory framework requires (and incentivises) NBN Co to achieve the Government's objectives while operating efficiently and commercially, thereby promoting retail competition and the long-term interests of end-users.

The mandate to act efficiently and commercially is made clear by the Statements of Expectations issued to NBN Co, and is reflected in each corporate plan endorsed by the Shareholder Ministers under the terms of the Equity Funding Agreement with the Commonwealth.

Further, NBN Co is regulated by the Commonwealth Government Business Enterprise Governance and Oversight Guidelines (October 2011) (**GBE Guidelines**), which provide that:

A principal objective for each GBE is that it adds to its shareholder value. To achieve this it is required to:

a. operate efficiently, that is, at minimum cost for a given scale and quality of outputs;

b. price efficiently...taking into account economic forces...

c. earn at least a commercial rate of return, given the obligations...to price and operate efficiently:

i. This means recovering the full cost of the resources employed, including the cost of capital; and

ii. Each GBE is to work towards a principal financial target and a dividend policy, agreed in advance with the Shareholder Ministers, with the principal financial target to be set on the basis that each GBE should be required to earn commercial returns at least sufficient to justify the long-term retention of assets in the business, and to pay commercial dividends from those returns.²⁶

While the GBE Guidelines do not have the force of law, NBN Co is expected to adhere to them as a prescribed GBE.²⁷ Further, under the terms of the Equity Funding Agreement with the Commonwealth, NBN Co's ability to receive continued funding from the Commonwealth is dependent upon NBN Co complying with the GBE Guidelines.²⁸

In addition to these regulations, NBN Co's SAU, approved by the ACCC in December 2013, contains provisions which incentivise NBN Co to operate efficiently and commercially. In particular, the SAU sets out long-term pricing controls and prevents NBN Co from recovering costs which the ACCC considers have not been prudently incurred.

The SAU sets initial prices for NBN products which are comparable to current prices for copper and hybrid fibre coaxial services so as to encourage migration to the NBN. The long-term price controls in the SAU prevent NBN Co from raising its prices by more than CPI minus 1.5% in any year of the SAU period. NBN Co's prices will therefore decrease in real terms during the term of the SAU, providing significant price certainty for access seekers.

As stated by the ACCC:

restrictions on how [NBN Co's] prices may change over time creates incentives for NBN Co to invest in the network efficiently because it will not be able to increase prices above the price controls to recover costs. This in turn provides an incentive for NBN Co to incur only efficient costs.²⁹

In the context of very substantial up-front capital commitment, the long-term price controls mean that cost recovery is dependent in part on users migrating to higher speed services with higher data usage. This

²⁶ GBE Guidelines at 1.8

²⁷ NBN Co is a prescribed GBE for the purposes of s5 of the CAC Act, and it is intended to be prescribed as such for the purposes of s8 of the Public Governance, Performance and Accountability Act 2013 (Cth) (**PGPA Act**)

²⁸ As well as other requirements, such as compliance with the reporting and governance framework set out in the in the *Commonwealth Authorities and Companies Act 1997* (Cth) (**CAC Act**)

²⁹ ACCC, 'NBN Co Special Access Undertaking Final Decision', 13 December 2013, p 89

incentivises NBN Co to develop innovative products in order to facilitate migration, which in turn promotes competition in the retail market.³⁰

The SAU also sets out NBN Co's Long Term Revenue Constraint Methodology (*LTRCM*), which allows NBN Co the opportunity to recover its prudently incurred costs over time (inclusive of an appropriate rate of return in accordance with the Government's directives), but no more. The LTRCM is consistent with the 'Building Block' revenue methodologies used by the ACCC and other regulators in a range of industries. The LTRCM strengthens NBN Co's incentive to operate and invest efficiently, thereby promoting the long-term interests of end-users.

2.6 International precedent

There is international precedent for developing a market structure involving a broadband network provider which is structurally or functionally separate from any downstream provider and which is subject to non-discrimination and open access arrangements.

The wholesale only, open access model adopted in Australia for the delivery of the NBN is similar to models adopted in several overseas jurisdictions. Each of Singapore, New Zealand and the United Kingdom has sought to supply high-speed broadband services using structural and/or functional separation between passive infrastructure and active infrastructure layers, so that the services are provided efficiently and pro-competitively. Consistent with the approach in Australia, the arrangements in each of these jurisdictions involve:

- an active ongoing role by Government with respect to the rollout of next generation broadband infrastructure;
- open access obligations in relation to the network provider;
- non-discrimination rules, set out in undertakings entered into by the network provider and/or operating by virtue of the separation models; and
- a universal service obligation in some form, either through legislation or as part of other regulations surrounding the establishment of the high-speed broadband service.

³⁰ See: ACCC, 'NBN Co Special Access Undertaking Final Decision', 13 December 2013, p 11

3 Potential competition-related reforms in the telecommunications sector

Section 3 of the Review Panel's Issues Paper seeks comments on whether there is a need for further competition-related reform in infrastructure sectors with a history of heavy government involvement, and in particular, on the priorities for competition policy reform in the telecommunications sector.

The CCA contains two Parts which are specific to the telecommunications industry:

- Part XIB: a regime regulating anti-competitive conduct; and
- Part XIC: a telecommunications access regime.

The Vertigan Panel is currently conducting a review of the telecommunications industry access arrangements, including Part XIC, as required by s152EOA of the CCA. This Section outlines NBN Co's position on the application and effectiveness of Part XIC, should the Review Panel wish to draw on this in its work.

3.1 Part XIC of the CCA

NBN Co considers that, on the whole, Part XIC operates effectively and wholesale changes to the regime are not required at this stage. The regime is now well understood by industry, and the original rationale for introducing the regime remains applicable today.

While Part XIC has been the subject of continuing review and reform, there remain some areas where amendments to the regime may be appropriate in order to ensure that the regime best promotes the long-term interests of end-users.

(a) Part XIC has been subject to extensive review

Part XIC is an established regime which has been the subject of continuing review and reform. NBN Co outlines these below.

Productivity Commission review 2001

The need for an industry-specific access regime was reiterated by the Productivity Commission in its 2001 report concerning telecommunications competition regulation.³¹ The Productivity Commission recommended that Part XIC be retained, despite the views of some industry participants that Part IIIA provided a sufficient regulatory framework. The Productivity Commission concluded that:

[There] is a good case for an access regime to apply to telecommunications.

With appropriately set access prices, such an approach is more likely than other measures to increase efficient competition in final markets with gains, such as, lower retail prices, greater innovation and product differentiation, and heightened incentives for cost cutting by the incumbent.

While there are few policy relevant features that are unique to telecommunications, the overall combination of features does appear to make telecommunications different from other regulated utilities in some policy relevant dimensions. These include the speed of market and technological change, and the relevance of network effects.³²

³¹ Productivity Commission, Telecommunications Competition Regulation, Inquiry Report, Report No 16, 20 September 2001

³² Productivity Commission, Telecommunications Competition Regulation, Inquiry Report, Report No 16, 20 September 2001, p 243

Subsequent reform of Part XIC

Subsequent to the Productivity Commission's review, a series of reforms to Part XIC were introduced:

- In 2002, two changes were made that aimed to facilitate investment in new telecommunications infrastructure by extending the existing provisions relating to exemptions and undertakings:³³
 - an extension of the ability of the ACCC to grant exemptions from standard access obligations in respect of services not yet in existence; and
 - amendment of the provisions relating to access undertakings by permitting the ACCC to accept undertakings from both existing and potential access providers, irrespective of whether the services concerned had been declared or were yet in existence.
- Further, the objects clause was refined to refer to promoting the economically efficient use of, and the economically efficient investment in, the infrastructure by which listed services are supplied.
- In 2005, further amendments were made to facilitate faster, more predictable processes for the ACCC's consideration of access exemption applications, access undertakings and access disputes, and to provide enhanced enforcement options. The object of these changes was '*to encourage greater investment in telecommunications infrastructure and to increase the effectiveness of the regime*'.³⁴
- In 2010, amendments were made to address industry concerns about the operation of the access regime, in relation to the 'negotiate/arbitrate' model.³⁵ Under this model, if parties could not agree on the terms of access to a declared service, either party could refer the dispute to the ACCC for arbitration. In the industry's experience the model did not operate effectively. The model was abandoned and in its place, a mechanism was introduced for the ACCC to set up-front prices and non-price terms which would act as a default benchmark if agreement on terms could not be reached.³⁶

This change formed part of a package of legislative reforms directed at enhancing competitive outcomes and strengthening consumer safeguards in the Australian telecommunications industry. Measures were also introduced preparing for the introduction of the NBN. The amending legislation also introduced changes associated with the structural separation of Telstra.

- In 2011, Part XIC was subject to further amendments,³⁷ which, coupled with the NBN Co Act, were designed to give effect to the Government's vision of NBN Co operating on a wholesale-only, open access basis. The detail of these legislative reforms is discussed above.

(b) The rationale of Part XIC remains applicable today

The rationale for introducing Part XIC was to provide an access regime for the telecommunications industry designed to accommodate the unique characteristics of that industry. In particular, when Part XIC was introduced into what is now the CCA, the telecommunications industry was described as a '*complex, technically detailed network industry*', attended by '*particular policy interests*'.³⁸

³³ Regulation Impact Statement, Telecommunications Competition Bill 2002 (Cth)

³⁴ Explanatory Memorandum to the Telecommunications Legislation Amendment (Competition and Consumer Issues) Bill 2005 (Cth)

³⁵ Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Act 2010 (Cth)

³⁶ See Explanatory Memorandum to the Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Bill 2010 (Cth)

³⁷ Telecommunications Legislation Amendment (National Broadband Network Measures – Access Arrangements) Act 2011 (Cth)

³⁸ Explanatory Memorandum to the Trade Practices Amendment (Telecommunications) Bill 1996 (Cth)

The Second Reading Speech to the Bill which introduced Part XIC in 1996 explained Parliament's approach as follows:

*the government's philosophy in preparing the telecommunications access regime has been to follow an approach based on part IIIA of the Trade Practices Act as far as practicable – nevertheless, to introduce some additional refinements to ensure that the arrangements will work effectively for the telecommunications industry.*³⁹

The discrete regime introduced by Part XIC reflected:

- **A unique objective:** the objective of Part XIC is expressed to be the promotion of the long-term interests of end-users.⁴⁰
- **The rapid rate of technological change:** this sets the telecommunications industry apart from other industries that exhibit natural monopoly characteristics and requires a regime sufficiently flexible to respond to technological developments. The Second Reading Speech to the 1996 Bill noted the fast past of change in the telecommunications industry, and stated that carriers and service providers:

*must be given the flexibility to engage in normal competitive conduct' and that 'Australian consumers will not benefit from regulation that unnecessarily hampers the ability of operators to respond to the market.'*⁴¹

- **The particular significance of network effects:** Part XIC provides that, in applying the long-term interests of end-users test, regard must be had to the objective of achieving any-to-any connectivity. As the Second Reading Speech to the 1996 Bill noted:

*This any-to-any feature – and the Government's commitment to promote the diversity of carriage and content services available to end users – requires an access regime that includes additional features to those contained in the general access regime in part IIIA.*⁴²

In NBN Co's view, the rationale behind Part XIC remains as applicable today as it was on enactment.

(c) Maintaining Part XIC facilitates industry certainty

Industry and the ACCC understand Part XIC well. In particular, there is broad acceptance of the usefulness and meaning of the long-term interests of end-users test, being the objective of Part XIC by reference to which the ACCC makes its decisions in relation to the Part's operation.

Given the period for which it has been in place, and the numerous ACCC and Australian Competition Tribunal decisions which have applied the long-term interests of end-users test, it is now well understood by industry stakeholders.⁴³

³⁹ House of Representatives, Hansard, Trade Practices Amendment (Telecommunications) Bill 1996 (Cth), Second Reading Speech, 5 December 1996, p 7804

⁴⁰ CCA s152AB

⁴¹ House of Representatives, Hansard, Trade Practices Amendment (Telecommunications) Bill 1996 (Cth), Second Reading Speech, 5 December 1996, p 7803

⁴² House of Representatives, Hansard, Trade Practices Amendment (Telecommunications) Bill 1996 (Cth), Second Reading Speech, 5 December 1996, p 7804

⁴³ See, for example: Seven Network Limited (No 4) [2004] ACompT 11, [120]; Application by Chime Communications Pty Ltd (No 2) [2009] ACompT 2 (27 May 2009), pp 12-14; and ACCC, 'Assessment of FANOC's Special Access Undertaking in relation to the Broadband Access Service – Draft Decision', December 2007, pp 32-33

3.2 The practical operation of Part XIC could be improved

As outlined above, NBN Co believes that Part XIC remains the appropriate mechanism for access regulation in the telecommunications industry. However, in NBN Co's practical experience there are some ways in which Part XIC could be amended to operate more effectively. NBN Co has elaborated on these in detail in submissions made to the Vertigan Panel.⁴⁴

(a) Every eligible service provided by NBN Co must be declared

The effect of the Part XIC regime is that, before NBN Co can supply an eligible service, for whatever purpose, the service must be declared. This regime ensures that NBN Co, in providing core access services as a monopoly provider, operates on an open access basis and is subject to regulatory oversight, and that the obligations set out in any accepted SAU apply. In practice however, the requirement that all eligible services supplied by NBN Co must be declared services has resulted in inefficiencies and operational difficulties for NBN Co in three key areas:

- (i) the conduct of trials and the provision of test services –making these services subject to regulation under Part XIC is operationally onerous for NBN Co and provides little benefit for access seekers;
- (ii) the provision of temporary services related to integrating other networks into the NBN – such services should not be subject to regulation under Part XIC; and
- (iii) non-bottleneck services – NBN Co should have the ability to apply to the ACCC for an anticipatory exemption of a non-bottleneck service from the declaration requirements.

(b) The non-discrimination obligations

As mentioned above, NBN Co's non-discrimination obligations formed part of legislative reforms designed to enshrine NBN Co's mandate as a wholesale-only, open access provider. However, in practice, the non-discrimination obligations go well beyond what is required to ensure that NBN Co's activities are in the long-term interest of end-users, and have led to significant operational difficulties and inefficiencies for NBN Co.

Traditional concerns about discrimination relate to discrimination by a vertically integrated dominant provider in favour of its retail arm, to the detriment of competition in downstream markets. As a wholesale-only, open access provider, these concerns do not apply to NBN Co. Further, there is minimal risk of NBN Co discriminating in favour of larger access seekers to the detriment of competition in downstream markets. As the ACCC has recognised:

*natural incentives for [wholesale-only] operators to discriminate between access seekers to the detriment of competition in downstream markets is greatly diminished relative to vertically integrated operators.*⁴⁵

This point was also made in an expert report by Alexander Sundakov provided to the Vertigan Panel in April 2014. This report concluded that NBN Co does not have an incentive to discriminate to the detriment of competition in downstream markets, noting that:

*an efficient and competitive market among downstream access seekers - while obviously being in the public interest - also best serves the interests of the access service provider.*⁴⁶

Given NBN Co's wholesale-only, open access mandate, the original drafting of the non-discrimination obligations contained an exception for discrimination where it aids efficiency, and for activity relating to pilots, trials and the provision of information about a service.⁴⁷ These exceptions passed through the House of Representatives but were removed in the Senate, with Independent Senator Nick Xenophon arguing that the exception for volume discounts would result in Telstra and Optus dominating the telecommunications market while smaller providers were marginalised. NBN Co rejects this argument, as there are several reasons why NBN Co would be incentivised to discriminate in favour of smaller access seekers. In particular, NBN Co

⁴⁴ NBN Co, 'Submission of NBN Co to Expert Panel in response to the Consultative Paper for the Purposes of Section 152EOA of the Competition and Consumer Act 2010', April 2014

would be incentivised to promote competition in downstream markets, and to promote innovation by smaller, niche retail service providers, in order to encourage take-up of the NBN. NBN Co could thereby maximise its ability to efficiently recover its costs and achieve the Government's wider policy objectives.

Accordingly, NBN Co has submitted to the Vertigan Panel that the non-discrimination obligations should be less restrictive in their operation. In particular, NBN Co considers that the non-discrimination obligations contained in s152AXC should be subject to an efficiency exception, and that the supplementary obligations in s152AXD should be repealed in full, or in the alternative, amended to include the exceptions contained in the original draft legislation regarding pilots, trials, and the provision of information about a service.

(c) Other changes to Part XIC

NBN Co has also submitted to the Vertigan Panel that the operation of Part XIC could be improved in other ways, including changes related to:

- lodgement obligations regarding access agreements and statements of difference;
- the operation of the ACCC's Notice To Vary power in assessing SAUs;
- the operation of the fixed principles provisions in s152CBAA of the CCA; and
- the restrictions on NBN Co's investment activities and supply of goods and services.

⁴⁵ ACCC Vertigan Submission, p 25

⁴⁶ Alexander Sundakov, 'Economic Effects of Non-Discrimination Provisions for NBN Co', April 2014, p 2

⁴⁷ See Telecommunications Legislation Amendment (National Broadband Network Measures – Access Arrangements) Bill 2010 (Cth)

4 Exemptions and exceptions under the CCA

4.1 Introduction

NBN Co wishes to comment on the effectiveness of the exceptions provided for in s51 of the CCA, particularly s51(1) which provides for the authorisation of conduct that may otherwise be perceived as raising concerns under Part IV, where that conduct is specifically authorised by law.⁴⁸ Section 51(1A) of the CCA requires that the law specify the person who is authorised to engage in the conduct, the place where the conduct is to occur, and the other attributes of the conduct.

NBN Co submits that these provisions of s51 are appropriate. The provisions relevantly allow for the implementation of Government policy and the realisation of its associated public benefits, in circumstances where that conduct may otherwise raise concerns under Part IV of the CCA. The provisions allow government to provide a level of certainty to industry players, and reduce any litigation risk for the entities implementing government policy.

The form of the provisions in s51 ensure that any exceptions:

- are considered and approved by elected representatives of the Commonwealth or the relevant State or Territory;
- will only include specific conduct which is considered necessary to comply with the relevant law, thereby limiting any impact the exception may have on other parties; and
- will not prevent the ACCC from regulating other conduct, or even from regulating the authorised conduct in circumstances where ACCC supervision or approval is built into the terms of the statutory exception.

The ACCC monitors legislation that authorises such conduct or that provides for regulations to be made authorising particular conduct.⁴⁹

NBN Co therefore submits that provisions of s51 are consistent with the objects of the CCA, being the enhancement of the welfare of Australians through the promotion of competition, fair trading and consumer protection.

4.2 Statutory authorisation: the NBN regulatory framework

The NBN regulatory framework contains two statutory exemptions that authorise conduct:

- Section 577A of the Telecommunications Act; and
- Section 151DA of the CCA.

These statutory exceptions endeavour to facilitate key pillars of the Government's policy relating to the rollout of the NBN and implementation of structural industry reforms. These exceptions provide a degree of certainty to the industry, while still allowing the ACCC to monitor and have a role in the authorisation of conduct. NBN Co addresses these exceptions below.

⁴⁸ In this context, a 'law' may refer to an Act of the Commonwealth or States, or regulations made under such Acts, as well as enactments, ordinances or regulations made by the various Territories. However, 'regulations' in this context may not authorise conduct which occurs more than two years after those regulations came into operation: s51(1C)(c)

⁴⁹ A list of such legislation is available on the ACCC's website: <http://www.accc.gov.au/about-us/australian-competition-consumer-commission/legislation/exceptions-under-commonwealth-state-territory-legislation>

4.3 Section 577BA of the Telecommunications Act

As stated above, the structural separation of Telstra, together with the creation of NBN Co, were key pillars of the Government's policy to transform the competitive dynamics in the Australian telecommunications industry.

To facilitate the structural separation of Telstra and the migration of customers to the NBN, NBN Co entered into binding Definitive Agreements with Telstra in June 2011. The Definitive Agreements provide for NBN Co to pay Telstra progressively for the disconnection of customers from Telstra's legacy fixed-line networks (other than HFC pay-tv customers). Further, the Definitive Agreements allow NBN Co to access Telstra infrastructure over a minimum 35-year period, reducing duplication and enabling efficient use of existing infrastructure.

By facilitating the structural separation of Telstra and the migration of customers to the NBN, the Definitive Agreements promote retail competition and support NBN Co's ability to rollout a national broadband network, recover its costs and achieve the wider policy objectives of Government. The Definitive Agreements therefore promote the long-term interests of end-users.

To allow for and to '*promote the national interest*' in structural reform of the telecommunications industry, s577BA of the Telecommunications Act authorises certain types of conduct by Telstra and NBN Co for the purposes of s51(1) of the CCA. In particular, this section authorises:

- the Definitive Agreements between Telstra and NBN Co, and certain conduct giving effect to those agreements;
- Telstra's Structural Separation Undertaking given under s577A of the CCA, accepted by the ACCC in February 2012; and
- conduct which Telstra is required to engage in to comply with an undertaking in force under s577A.

NBN Co submits that these statutory exemptions are appropriate: the exemptions are necessary to give effect to Government policy. Importantly, s577BA provides that authorisation of the relevant conduct is subject to the ACCC's approval of Telstra's Structural Separation Undertaking. This demonstrates that a statutory exception can itself include a role for the ACCC in authorising the conduct, in addition to the usual role that the ACCC would retain for all other conduct that has not been authorised by the exception.

4.4 Section 151DA of the CCA

As stated above, NBN Co offers uniform national wholesale pricing for NBN services by charging access seekers uniformly for services across NBN Co's network for all technologies and for the basic service offering. UNWP ensures that access seekers face the same total wholesale cost for services between any premises and the relevant POI.

The number and geographic location of NBN Co's POIs determines:

- the boundaries of the NBN;
- the extent to which backhaul is required by each retail service provider; and consequently
- the benefits that can be achieved through UNWP – if NBN Co had numerous, highly distributed POIs across Australia, access seekers would be required to purchase large amounts of backhaul services, in addition to the services NBN Co provides at uniform national prices. This may result in significant cost differential between the provision of urban and regional services, despite NBN Co's implementation of UNWP.

Section 151DA of the CCA authorises certain types of conduct by NBN Co for the purposes of s51(1) of the CCA. In particular, the CCA authorises NBN Co to:

- (a) refuse to permit interconnection at a location which is not a listed POI;
- (b) refuse to supply (or refuse to offer to supply) a designated access service; and
- (c) engage in conduct generally;

where that conduct or refusal is reasonably necessary to achieve uniform national pricing of eligible services supplied by NBN Co.

NBN Co supports these exceptions in principle: the exemptions endeavour to give effect to Government policy, and allow for the ACCC to play a role in their operation.⁵⁰ As these exemptions are yet to be relied upon, it is appropriate they remain until their operation is tested.

⁵⁰ The Government requested the ACCC to provide the Government with advice on the number and location of initial POIs that would best meet the long-term interests of end-users in October 2010 and that Government accepted the ACCC's advice. After a public consultation and confirmation process, the ACCC published a final list of 121 POIs in November 2012, as required by s151DB of the CCA

5 Authorisation and notification provisions of the CCA

NBN Co welcomes the updated Authorisation Guidelines issued by the ACCC in June 2013, which reflect the ACCC's current approach to assessing applications for authorisation under the CCA. It is important that the authorisation provisions in the CCA, and the ACCC's application of those provisions, remain flexible and transparent in order to deal with increasingly complex and long-term commercial arrangements in the telecommunications industry in a timely manner.

5.1 Length of authorisation

The current authorisation regime allows the ACCC to grant authorisation for a limited period of time on a case-by-case basis.⁵¹ As noted in the ACCC's Authorisation Guidelines, most authorisations are granted for a period of up to five years, although authorisation for longer periods may be appropriate for arrangements that require significant investment, which are only likely to proceed if the proposed conduct is authorised for a longer period.⁵²

NBN Co submits that the changing nature of the market structure and regulation of the telecommunications industry, as well as ongoing developments in other infrastructure industries, mean that authorisation applications may involve increasingly complex commercial arrangements requiring significant investment. Such arrangements may therefore require authorisation for longer periods in order to proceed. NBN Co acknowledges that this will create challenges for the ACCC and submits that the legislative provisions governing authorisations and the ACCC's Guidelines should be periodically reviewed and updated where appropriate to ensure that they allow the ACCC to assess such applications in a timely and responsive manner.

5.2 Quantification of public benefits

The ACCC Guidelines note that, while the CCA does not require the ACCC to quantify the public benefits and detriments likely to result from proposed conduct, the ACCC encourages applicants to quantify the size of claimed benefits and detriments, particularly with complex applications.⁵³ Further, the ACCC Guidelines acknowledge that in many cases it will not be possible to credibly quantify public benefits and detriments, and that such cases:

will usually need to be qualitatively assessed and must have a sufficient basis for concluding that the benefits and detriments are likely to result.

In practice, a qualitative assessment involves making a judgment about the existence and size of the public benefit and detriment based on a set of indicators derived from:

- *the facts of the application*
- *the analytical framework under which the various effects of proposed conduct are identified and analysed according to the relevant market/area of competition to determine which effects are likely to be more significant than others*
- *interested party submissions and other relevant material available to the ACCC.*⁵⁴

NBN Co submits that the quantification of the public benefits and detriments of longer-term arrangements is likely to be particularly complex and challenging. Accordingly, in cases where it is extremely challenging, or

⁵¹ CCA s91(1)

⁵² ACCC, 'Authorisation Guidelines', June 2013, p 68

⁵³ ACCC, 'Authorisation Guidelines', June 2013, p 63

⁵⁴ ACCC, 'Authorisation Guidelines', June 2013, p 64

even not possible, to credibly quantify public benefits and detriments, the ACCC should transparently articulate the way in which it considered benefits and detriments, and ensure that its decision makes clear the expert and other evidence the ACCC has had regard to in forming its decision. This will ensure that the ACCC's qualitative assessment of the arrangements will continue to be rigorous and transparent. It will also ensure that the applicant, affected parties and the public have a proper understanding of the nature and significance of the relevant public benefits and detriments identified and of the ACCC's decision-making process.