

Supplementary submission to the Joint Standing Committee on the NBN

About Vocus

Vocus is a specialist fibre and network solutions provider operating Australia's second-largest intercapital network. Vocus is also the fourth-largest NBN Retail Service Provider (RSP) via our Dodo, iPrimus, Commander and wholesale businesses, with over 535,000 connected users (7.2% market share).

In total, the Vocus terrestrial network is ~30,000km of high-performance, high-availability fibre optic cable supported by the 4,600km Australia-Singapore Cable and the 2,100km North West Cable System between Darwin and Port Hedland. Vocus owns a portfolio of brands catering to enterprise, Government, wholesale, small business and residential customers across Australia and New Zealand.

Executive Summary

Vocus provided a submission to the Committee's inquiry on 17 January 2020. This supplementary submission addresses the substantial changes which have occurred in the market since that date.

Vocus' original submission focused on NBN's behaviour in the competitive enterprise and government telecommunications market (the Enterprise market). In that submission we noted that Vocus has been, and continues to be, a supporter of NBN in Enterprise. NBN's Enterprise business provides the opportunity to improve competition in underserved areas; to improve retail market competition by virtue of NBN's position as a wholesale-only, transparent, and non-discriminatory provider; and to support and encourage more private investment.

Vocus called on the Committee to make two key recommendations to ensure NBN met its policy objectives in the Enterprise market:

1. NBN should honour its wholesale-only remit and not engage directly with end-users; and
2. NBN should not overbuild competitive fibre.

In late January 2020, NBN announced changes in its approach to the Enterprise market to address both of these issues. Vocus welcomed these changes which endorse the fundamental role of infrastructure investment and competition in delivering the best outcomes for end-users. However, there continue to be issues with NBN's behaviour towards Enterprise end-users which see the company acting outside its wholesale-only remit and against the spirit of the decisions taken in January.

To expand on Vocus' original submission in light of recent events, this supplementary submission also responds to the Committee's Terms of Reference regarding "current pricing structures, including wholesale pricing, affordability and take-up, particularly as they relate to low-income and rural and regional customers".

Dramatic changes in broadband consumption due to COVID-19 have, to date, been addressed by temporary measures put in place by NBN to ensure that consumers have been able to use services as-normal. However, these measures do not provide any long-term certainty for either consumers or Retail Service Providers (RSPs) given that bandwidth consumption has reached a 'new normal' at levels far higher than anyone could have predicted prior to COVID-19.

To address this, Vocus submits that NBN should fundamentally reform its wholesale pricing to be affordable, predictable and simple. To achieve this, NBN should abolish CVC, offer flat-rate speed tiers, and eliminate complexity resulting from discounts, non-recurring charges and rebates.

The delivery of the business segment strategy, including to enterprise and government customers, and small to medium businesses

In late January, NBN announced two key changes to its approach to the Enterprise market. First, NBN proposed a solution to make efficient use of existing fibre infrastructure rather than wastefully overbuilding it. Second, NBN ceased the practice of entering into direct contracts with Enterprise end-users for fibre builds.

NBN deserves credit for taking action to address industry's concerns, and Vocus continues to support NBN's presence in the Enterprise market. Vocus is one of the largest providers of NBN Enterprise services, with substantial market share of Enterprise Ethernet and business Satellite services.

However, there remain ongoing issues with NBN's updated approach which should be addressed if NBN is to remain within its wholesale-only remit.

1. Changes to NBN's Enterprise Build Contracting Model

Vocus' original submission proposed that NBN should honour its wholesale-only remit by not engaging directly with end-users in the competitive Enterprise market. To address the issue, on 30 January 2020 NBN announced changes to its Enterprise build contracting model "so that RSPs will in all cases have the direct contractual relationship with enterprise customers."¹

Industry was invited to provide feedback to a consultation paper (to which Vocus responded) and NBN subsequently issued a 'close out paper' on 19 June 2020 providing guidance on its proposed new approach, to be finalised in an updated Technology Extension Contract (yet to be released at time of writing).²

While these changes addressed the issue of NBN entering into direct *contracts* with end-users, it did not address the issue of NBN's direct *engagement* with end-users and intermediaries who work with end-users in relation to NBN technologies but are not RSPs.

The manner of NBN's direct engagement goes against the spirit, if not the letter, of NBN's January announcement. NBN's Industry Engagement staff continue to directly influence, or seek to influence, contracts between RSPs and end-users. This includes payments by NBN to intermediaries and undermines RSPs' relationships with not only their customers, but also with NBN – and this has continued to occur since NBN's decision to cease direct contracts with end-users.

RSPs must be able to compete fairly for Enterprise customers without interference from the wholesale provider. To this end, Vocus reaffirms its original position that NBN must not engage with Enterprise end-users:

- on any pricing discussions, including but not limited to RSP pricing and setting expectations on up-front fibre build costs (particularly when they are non-binding estimates or indicative prices that are not supported by solution design or detailed feasibility checks that are led by the RSP)
- in a manner that promotes any particular RSP (all RSPs should be engaged with by NBN in a non-discriminatory, transparent, and equivalent manner)
- in relation to influencing channel partnerships and relationships at the Retail level
- concerning the detail of their RFPs and tender design, or proportion of the end user's sites to be migrated to NBN services
- to design possible solutions for their connectivity needs
- concerning the mix of access technologies

These actions see NBN operating outside its wholesale-only remit and competing against the RSPs which are meant to be NBN's customers.

NBN should also enhance its internal governance procedures to ensure it acts in a non-discriminatory and transparent manner. If the Industry Engagement team is unable to conduct itself within NBN's wholesale-only remit, and in accord with the spirit of NBN's decisions announced in January, this team should be disbanded.

¹ 'NBN Co evolves enterprise contracting model' 30 January 2020

² NBN Co's Industry Consultation Close Out Paper, Evolving NBN Co's Enterprise Build Contracting Model, 19 June 2020

2. Dark fibre procurement consultation process

To address the issue of overbuilding competitive fibre, on 28 January 2020 NBN announced a new process to “explore possible approaches for the procurement of additional dark fibre services from network carriers in customer locations already served by existing fibre.”³ Industry was invited to provide feedback to a consultation paper (to which Vocus responded) and Vocus is engaged in a ‘proof of concept’ procurement process being run by NBN.

While dark fibre procurement is, in principle, preferable to NBN overbuilding existing fibre, we are yet to see how often the process will be utilised and whether or not NBN continues to overbuild existing fibre once the process is operational. If there are still instances where NBN overbuilds competitive fibre, the company should be required to provide transparency regarding its decision and a financial justification for the overbuild to ensure such costs are ‘prudent and efficient’, as described in the NBN Special Access Undertaking (SAU). The issue of financial transparency is described in more detail below.

Transparency of NBN’s Enterprise vs residential businesses

Vocus submits that the Committee should consider greater financial transparency for NBN’s competitive Enterprise businesses, particularly in regard to cross-subsidisation from its monopoly residential business.

NBN’s dark fibre consultation paper (page 8) states: “The establishment of a standard process should enable nbn to utilise a third-party’s dark fibre connection service where the expected overall economic costs and/or time to delivery are less than nbn otherwise faces in deploying its own infrastructure (including a commercial cost of capital no less than the rate agreed with the ACCC in its Special Access Undertaking).”

There is a risk that NBN could avoid the procurement of existing competitive fibre by claiming to have a lower cost to overbuild using its own infrastructure, when such costs may be dependent on cross-subsidisation from its Government-subsidised monopoly residential network and/or NBN’s relatively low 3.2% rate of return.

Additionally, as Vocus and other telcos have raised in submissions to the Committee, NBN has offered prices for fibre upgrades which can make it more expensive for RSPs to use a mix of their own fibre and NBN fibre when compared to the cost of using 100% NBN fibre. This volume-discount pricing model could undermine the dark fibre procurement process by making the cost of using existing fibre appear to be higher than the cost of overbuilding.

Increased financial transparency of NBN’s Enterprise business could help to alleviate these issues and ensure that NBN does not have an unfair competitive advantage by virtue of its Government ownership or opaque pricing.

The issue of financial transparency for NBN’s competitive Enterprise business was recently canvassed by the ACCC as part of its Long Term Revenue Constraint Methodology (LTRCM) Determination, which forms part of the ACCC’s price regulation under the NBN Special Access Undertaking.

The call for increased transparency was supported by submissions from Telstra and the Australian Communications Consumer Action Network (ACCAN), which stated: “Cross subsidising the enterprise market with revenue from the residential market would be to the detriment of consumers in both markets. ACCAN is concerned that cross subsidising increases the likelihood of predatory pricing that would dampen competition in the enterprise market, which over a longer period may eliminate competitors.”⁴

In its final report, the ACCC stated: “In relation to the appropriate recognition and distinction of commercial and non-commercial costs, we agree that additional transparency are likely to be desirable,” adding that “current arrangements do not provide for the identification of costs and revenues associated with different services.”⁵

³ [NBN Co commences industry consultation on dark fibre procurement for Enterprise Ethernet connections](#), 28 January 2020

⁴ [ACCAN submission to ACCC Long Term Revenue Constraint Methodology 2018–2019 Draft Determination](#), 29 May 2020

⁵ [ACCC Long Term Revenue Constraint Methodology 2018–19 Final Determination and Price compliance reporting 2018–19](#), 26 June 2020

Current pricing structures, including wholesale pricing, affordability and take-up, particularly as they relate to low-income and rural and regional customers

Vocus submits that NBN should fundamentally reform its wholesale pricing to be affordable, predictable and simple. To achieve this, NBN should abolish CVC, offer flat-rate speed tiers, and eliminate complexity resulting from discounts, non-recurring charges and rebates.

NBN's pricing model is made up of two components: first, the Access Virtual Circuit (AVC) which is a fixed monthly charge according to a user's chosen speed tier and increasingly comes with a 'bundled' amount of capacity. Second, Connectivity Virtual Circuit (CVC) which is a charge for capacity, purchased by RSPs to provide sufficient overall bandwidth at peak times across their NBN user base to ensure all users can access the broadband speeds they have paid for.

In short, CVC should be abolished. Consumption-based wholesale pricing creates false scarcity and is inconsistent with market reality and consumer needs. The majority of broadband consumers are on unlimited download plans, so they pay a predictable, flat monthly rate⁶. However, given the CVC charge is based on capacity used by consumers for their service, RSPs therefore have to pay an unpredictable, variable monthly wholesale rate to ensure consumers have a consistent customer experience at all times. In this equation, the risks of increasing CVC consumption to cover peak usage periods and associated higher charges are borne by RSPs, while the rewards go to NBN. The outcome is that RSPs are squeezed between providing a good experience with price certainty for customers and uncertain growing wholesale costs. This will ultimately lead to a less competitive RSP market for consumers and poorer customer experiences.

In the absence of such fundamental reforms, NBN should quickly move to reduce CVC prices across the speed tiers and provide for regular and appropriate indexation of CVC inclusions to account for real-world increasing data demand. Data usage has continued to outpace CVC inclusions, entrenching the challenge of providing affordable broadband to price-sensitive consumers in particular. Vocus submits that increases to included bandwidth should occur every six months, by at least 500kbps or a pre-determined amount based on an agreed compound annual growth rate (CAGR) for data. The increase in CVC inclusions should not increase wholesale prices given that bandwidth in core networks becomes cheaper over time.

Consumption-based pricing has resulted in increasing retail broadband prices as part of the switch to NBN. NBN's pricing model disadvantages low-income users seeking more affordable broadband plans by 'bundling' disproportionately higher amounts of CVC with more expensive AVCs, making low-end plans relatively unattractive for RSPs to sell. The affordability issue is exacerbated by the fact that NBN's pricing structure does not sufficiently differentiate pricing to provide an upgrade path from entry-level plans onto higher-speed plans – largely due to CVC.

To illustrate this point, NBN's current pricing and speed tier bundles for AVC + CVC are:

- 12Mbps bundle at a wholesale price of \$35 with 1Mbps of CVC included
- 25Mbps: \$37 with 1.25Mbps
- 50Mbps: \$45 with 2.25Mbps
- 100Mbps: \$58 with 3.75Mbps

Under this structure, a 50Mbps bundle costs 29% more than 12Mbps – but includes 125% more CVC. Similarly, a 100Mbps bundle costs 66% more than 12Mbps but includes 275% more CVC.

This price structure negatively impacts affordability because low-speed users are not necessarily low-bandwidth users. Vocus' network data shows that, on average, a 50Mbps user consumes 30% more CVC than a 12Mbps user – yet NBN includes 125% more CVC with a 50Mbps bundle. As a result, RSPs are disincentivised from offering products suitable for low-income users because they are required to purchase more CVC 'overage' for low-end products relative to high-end products.

The relative value of an entry-level broadband plans will continue to diminish as CVC demand increases. If an RSP were to purchase identical amounts of CVC for 12Mbps and 50Mbps services, a 12Mbps plan

⁶ [ACMA Communications Report 2018-19](#), 71% of users on unlimited plans at June 2019

would cost just \$0.80 less than a 50Mbps plan with 2.25Mbps of CVC. According to the latest ACCC data, the amount of CVC per user is 2.5Mbps (averaged across all speed tiers).⁷

Low-end plans have effectively been priced out of the market. This exacerbates the challenge of connecting the unconnected – currently more than 4 million homes passed by the NBN have yet to connect⁸. There is little incentive for an RSP to sell a 12Mbps or 25Mbps plan if they can sell a 50Mbps plan at approximately the same retail price, once CVC costs have been accounted for. In addition, if the lowest wholesale price for a plan is \$35, then it is impossible for RSPs to make positive margins at what were previously entry level Retail price points of less than, or in the range of, \$50 to \$60.

This issue is being canvassed by the ACCC in its inquiry into NBN access pricing, where it has noted: “We found that NBN Co’s changed approach to access products and pricing significantly reduced the commercial viability of lower-yielding, lower speed access products. In some circumstances, lower speed NBN access products had even become more expensive than its higher speed access products, and placed firms that continued to sell them at a competitive disadvantage.”⁹

Vocus notes that as of 20 August 2020 the ACCC has sought feedback on a proposal from NBN Co that aims to address concerns about entry-level pricing and wholesale service standards¹⁰. Vocus is currently considering the ACCC’s consultation paper on these issues.

Vocus agrees with the comments of ACCC Chair Rod Sims, who said: “There is a fundamental question of fairness here for those on low incomes.”¹¹

Abolishing CVC would allow NBN to offer flat-rate speed tiers, removing unnecessary operational and financial complexity for RSPs while providing simplicity and certainty for consumers. NBN could further simplify its pricing by eliminating discounts, non-recurring charges and rebates, which lead to significant administrative and operational complexity for RSPs, increasing operating costs and impacting margins.

Compliance with the NBN Statement of Expectations (SoE) and adequacy of that Statement

While NBN has made progress in addressing the two key issues with its Enterprise business outlined in Vocus’ original submission, Vocus maintains its view that the current SoE should be updated to allow the Government to provide NBN with clear policy objectives in the competitive Enterprise market.

An updated SoE should be drafted to allow for NBN to play a constructive role as a wholesaler in the Enterprise market: improving retail competition and allowing NBN to make a return, while also recognising the role of infrastructure competition and rewarding private infrastructure investment. As detailed earlier in this submission, guidelines should be set for NBN’s behaviour in this market to ensure that RSPs are able to compete fairly for Enterprise customers without interference from the wholesale provider.

With the network rollout now effectively complete, Vocus also submits that an updated Statement of Expectations should address fundamental issues with NBN’s wholesale pricing model which, if left unaddressed, will inevitably result in higher retail broadband prices as consumption continues to increase.

The current SoE published in August 2016 states that “The Government is committed to completing the network and ensuring that all Australians have access to very fast broadband as soon as possible, at affordable prices, and at least cost to taxpayers,” Vocus submits that NBN’s consumption-based pricing model does not ensure all Australians have access to broadband at affordable prices, and that the completion of the network rollout provides the Government with the opportunity to reassess its expectations of NBN in this regard.

Please direct any questions regarding this submission to:

Luke Coleman, Head of Government and Corporate Affairs

24 August 2020

⁷ [ACCC NBN Wholesale Market Indicators Report](#) June 2020

⁸ [NBN Weekly progress report](#)

⁹ [ACCC inquiry into NBN access pricing Position Paper](#), April 2020

¹⁰ [ACCC “Feedback sought on NBN pricing, service proposals”](#) 20 August 2020

¹¹ ACCC Chair Rod Sims [Speech to CommsDay Summit](#), 8 April 2019