3

Competition and Regulatory Issues

Introduction

3.1 During the course of its first review period, the committee was presented with competition and regulatory issues arising from the implementation of the Government's National Broadband Network (NBN) policy. A number of these matters were raised in the committee's First Report and have been updated to take into account additional information received, and recent developments reported in the Government's 23 September 2011 NBN rollout Performance Report.

3.2 This chapter includes discussion on the competition and regulatory issues pertaining to: the Binding Definitive Agreements between the NBN Co Limited (NBN Co) and Telstra and the NBN Co and Optus, Telstra's Structural Separation Undertaking (SSU) and draft Migration Plan, the NBN Co's Special Access Undertaking (SAU) and Wholesale Broadband Agreement (WBA).

3.3 In addition, issues such as competition and pricing concerns raised by Retail Service Providers (RSPs) and the engagement of private sector equity to fund the NBN are also discussed.

Binding Definitive Agreements with Telstra and Optus

Background

3.4 On 7 April 2009, the Government announced the establishment of NBN Co to: design, build (over an eight year period)[1] and operate a 'wholesale-only national high-speed broadband network for all Australians' which would be capable of delivering speeds of up to 100 Megabits per second (Mbps) at a cost of up to $43 billion.[2] The purpose of the NBN would be to connect all premises across Australia, to improve service delivery in areas such as education and health, and more broadly drive productivity growth, thereby enhancing Australia's international competitiveness.'[3]

3.5 The Government's 2009 NBN policy (including the establishment of NBN Co) was intended as a micro economic reform measure designed to improve the competitive dynamics of the Australian telecommunications sector. Structural reform would be through the required separation 'between the infrastructure provider and retail service provider.' In 2009, the Government stated that the structural separation nature of the reform would mean 'better and fairer infrastructure access for service providers, greater retail competition, and better services for families and businesses.'[4]

3.6 By implementing structural reform of the telecommunications industry, the NBN policy would have a significant impact on Telstra as the highly integrated and dominant industry incumbent.[5]

1 Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Bill (CCS Bill) 2010, Explanatory Memorandum (EM), Regulation Impact Statement, p. 9.

2 Hon Kevin Rudd MP, Prime Minister, Hon Wayne Swan MP, Treasurer, Senator the Hon Penny Wong, Minister for Finance and Senator the Hon Stephen Conroy, Minister for Broadband, Communications and the Digital Economy, 'New National Broadband Network', *Joint Media Release*, 7 April 2009; NBN Co, 'NBN Co and Telstra reach heads of agreement', *Media Release*, 20 June 2010, p. 2.

3 Hon Kevin Rudd MP, Prime Minister, Hon Wayne Swan MP, Treasurer, Senator the Hon Penny Wong, Minister for Finance and Senator the Hon Stephen Conroy, Minister for Broadband, Communications and the Digital Economy, 'New National Broadband Network', *Joint Media Release*, 7 April 2009.

4 Hon Kevin Rudd MP, Prime Minister, Hon Wayne Swan MP, Treasurer, Senator the Hon Penny Wong, Minister for Finance and Senator the Hon Stephen Conroy, Minister for Broadband, Communications and the Digital Economy, 'New National Broadband Network', *Joint Media Release*, 7 April 2009.

5 Telstra has ownership of the only copper network, larges cable and mobile network, and 50 per cent share of Australia's largest subscription television provider, Foxtel, CCS Bill 2010, EM, p. 2.

3.7 Structural reform of the telecommunications industry would include: Telstra's structural separation, draft migration plan, and the commercial agreements between NBN Co and Telstra.[6]

3.8 Subsequently, the Government introduced three pieces of legislation which were passed in 2011 and are the foundation for the Government's NBN policy. These are the: *Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Act 2011* (Cth)[7], (the CCS Act), the *National Broadband Network Companies Act 2011* (Cth), and *Telecommunications Legislation Amendment (National Broadband Network Measures- Access Arrangements) Act 2011* (Cth).

3.9 The CCS Act contains a 'package of legislative reforms aimed at enhancing competitive outcomes in the Australian telecommunications industry and strengthening consumer safeguards'. These reforms include:

- 'addressing Telstra's vertical and horizontal integration' by requiring Telstra to either voluntarily structurally separate or be subject to mandatory functional separation;
- 'streamlining the access and anti-competitive conduct regimes, and strengthening consumer safeguard measures such as the Universal Service Obligation, the Customer Service Guarantee and priority assistance; and
- measures to improve regulatory enforcement.'[8]

3.10 The aims of the legislative framework implementing the NBN were also incorporated into the Government's Statement of Expectations (SoE) delivered to NBN Co in December 2010.

3.11 Prior to passing of the CCS Act and associated NBN legislation, following a year of negotiations between NBN Co, Telstra and the Government, on 20 June 2010, the parties entered into a non binding Financial Heads of Agreement (FHA).[9]

3.12 The FHA outlined 'the high level terms and conditions for the timing of the decommissioning of Telstra's copper and Hybrid Fibre Coaxial (HFC)

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6 Australia Competition and Consumer Commission, (ACCC) 'Assessment of Telstra's Structural Separation Undertaking and draft Migration Plan', 30 August 2011, p. 1.

7 This Act was presented to the Parliament as the Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Bill 2010 and passed on 29 November 2010. It replaced the Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Bill 2009 which lapsed at the end of the 42nd Parliament.

8 CCS Bill 2010, EM, p. 1.

9 CCS Bill 2010, EM, p. 2.

networks (subject to certain exclusions).' The FHA would enable the 'progressive migration of customer services from Telstra's copper and subscription television cable networks' to the NBN, and thereby 'deliver ... structural reform of the telecommunications sector.'[10]

3.13 In this way, the FHA also foreshadowed how Telstra would participate in the rollout of the NBN.

3.14 The FHA was estimated to be worth around $11 billion[11] to Telstra[12] and would reduce overall NBN rollout costs by:

- 'giving NBN Co access to Telstra's existing infrastructure such as underground ducts', and pits and manholes, lead in conduits, backhaul including use of dark fibre[13] and, 'exchanges and transmission.'[14]
- 'Enabling decommissioning of the copper access network as the fibre network is rollout out.'[15]
- 'Allowing for the progressive migration of customer services from Telstra's copper and subscription television cable networks' to the NBN.[16]

3.15 Just over a year later, on 23 June 2011, following further negotiation between NBN Co and Telstra, the parties arrived at a Binding Definitive Agreement.[17]

3.16 In addition to the signing of the Telstra Agreement, on 23 June 2011, NBN Co signed a Binding Definitive Agreement with Optus.

Telstra Agreement

Background

3.17 The NBN Co's Binding Definitive Agreement with Telstra (the Telstra Agreement) consists of four documents[18] which, together with the

10 CCS Bill 2010, EM, p. 2.

11 The $11 billion consists of approximately $9 billion in value from the terms of the Telstra Agreement and $2 billion from the Government public policy reforms, NBN Co, 'NBN Co and Telstra reach heads of agreement', *Media Release*, 20 June 2010, p. 1.

12 NBN Co, 'NBN Co and Telstra reach heads of agreement', *Media Release*, 20 June 2010 p. 1.

13 NBN Co, 'NBN Co and Telstra Sign Binding Definitive Agreements', *Media Release*, 23 June 2011, p. 3.

14 NBN Co, Frequently Asked Questions, <www.nbnco.com.au>

15 NBN Co, Frequently Asked Questions, <www.nbnco.com.au>

16 CCS Bill 2010, EM, p. 2.

17 NBN Co, *Corporate Plan 2011-2013*, p. 85.

structural separation of Telstra, form the basis of Telstra's participation in assisting with the rollout of the NBN.[19]

3.18 Completion of the Telstra Agreement is a key assumption made under the NBN Co Corporate Plan and provides for the decommissioning of the Telstra network, with significant existing Telstra infrastructure made available to the NBN Co 'at the prices set out in the FHA.'[20]

3.19 The NBN Co has stated there are three main components of the Telstra Agreement which are beneficial to the NBN Co, Telstra and the Australian taxpayer. These components are:

- It grants NBN Co access to Telstra facilities and infrastructure over a minimum period of 35 years, ensuring that the fibre optic component of the National Broadband Network, serving 93% of premises, can be rolled out efficiently and avoids duplicating infrastructure;
- It provides for the progressive disconnection of Telstra's copper and Hybrid Fibre Coaxial (HFC) customers (other than HFC pay-TV customers) and NBN Co will be Telstra's preferred fixed-line network;
- In addition, NBN Co and Telstra have negotiated interim arrangements for immediate access to Telstra infrastructure.[21]

3.20 The NBN Co stated that the benefit of the Telstra Agreement in regard to the NBN rollout would be to avoid duplication of existing infrastructure, reducing the cost of NBN build and so reducing the risk of delays and potential disruption to local communities. The NBN Co commented:

> The outcome, we believe, is good for taxpayers and good for the broader community. We will, in making use of Telstra's facilities, avoid duplicating existing infrastructure. The deal reduces our costs to build the NBN, it reduces the risk of delays and, very importantly, it reduces potential disruption to local communities.[22]

18 These four documents are: the Implementation and Interpretation Deed, the Subscriber Agreement, Infrastructure Services Agreement, and Access Deed. NBN Co, 'NBN Co and Telstra Sign Binding Definitive Agreements', *Media Release*, 23 June 2011, p. 4.

19 NBN Co, 'NBN Co and Telstra Sign Binding Definitive Agreements', *Media Release*, 23 June 2011, p. 4.

20 NBN Co, *Corporate Plan 2011-2013*, p. 51.

21 NBN Co, 'NBN Co and Telstra Sign Binding Definitive Agreements', *Media Release*, 23 June 2011, p. 1.

22 Mr Mike Quigley, CEO, NBN Co, Transcript of Evidence, Canberra, 5 July 2011, p. 2.

3.21 Through the decommissioning of its copper network and HFC capability, the Telstra Agreement would also assist Telstra to 'progressively structurally separate.'[23]

3.22 Under the Telstra Agreement, there are nine 'conditions precedent' (CP) which must be either satisfied or waived for the Telstra Agreement to be completed.[24]

3.23 The CP are outlined under the Implementation and Interpretation Deed (IID) which is the first of the four documents which form part of the Telstra Agreement.

3.24 The CP for completion of the Telstra Agreement are:

- 'approval by each of Telstra's and NBN Co's shareholders of the proposed transaction;'
- Australian Competition and Consumer Commission (ACCC) 'acceptance of a [structural separation undertaking] (SSU) and approval of a Final Migration Plan in a form approved by Telstra and NBN Co and those documents come into force in accordance with the Telecommunications Act;
- the [Telecommunication Universal Service Management Agency] (TUSMA) Agreement and the Information Campaign and Migration Deed being entered into by Telstra and the Commonwealth in a form acceptable to NBN Co;
- the Commonwealth amending legislation or establishing other arrangements to implement its Greenfields policy in a form acceptable to Telstra and NBN Co;
- the Commonwealth introducing legislation considered necessary or desirable by the Commonwealth and NBN Co to facilitate NBN Co's rollout, in a form acceptable to Telstra and NBN Co;
- separate Australian Tax Office private tax rulings relevant to each party that confirm the tax treatment of elements of the transaction being acceptable to Telstra and NBN Co respectively;
- if NBN Co notifies Telstra of a change to its stated intention, as at the execution date, to roll out fibre to 93% of premises in Australia at the

23 Australian Communications and Media Authority, Major Changes to Australian Telecommunications Announced, *Media Release*, 23 June 2011.

24 NBN Co, 'NBN Co and Telstra Sign Binding Definitive Agreements', *Media Release*, 23 June 2011, p. 4.

execution date, Telstra being satisfied that the change does not adversely affect Telstra;

- the parties agreeing to an initial plan establishing a program for the handover of specified infrastructure under the ISA over the course of NBN Co's Rollout; and;
- any other matters that the parties agree to be a condition precedent. Telstra has requested that NBN Co confirms that NBN Co has arrangements in place to ensure the cessation of supply by Telstra of certain products occurs in a non-discriminatory way.'[25]

3.25 Approval of the Telstra Agreement by Telstra shareholders occurred on 18 October 2011, with the only CP remaining to be satisfied, the ACCC acceptance and approval of Telstra's SSU and Draft Migration Plan.

Telstra's Structural Separation Undertaking and Draft Migration Plan

3.26 The structural separation of Telstra is designed to deliver greater competition across the telecommunications industry by replacing Telstra as the dominant market player and owner of telecommunications infrastructure with the NBN, a wholesale-only, open access network.[26]

3.27 Telstra's structural separation is defined by the ACCC as 'the legal separation of Telstra's assets and activities into separate corporate entities with entirely separate owners/shareholders.'[27]

3.28 The CCS Act establishes the framework 'within which Telstra can' choose to 'structurally separate and migrate its customer base'[28] or if it does not structurally separate, be subject to functional separation.

3.29 Structural separation includes:

- 'commitments by Telstra to cease the supply of specified services over networks under its control from the designated day – which is expected to be the day on which the construction of the new wholesale-only NBN will be concluded; and
- Equivalence and transparency measures regarding access to Telstra's key wholesale services in the period leading up to the designated day.[29]

25 NBN Co, 'NBN Co and Telstra Sign Binding Definitive Agreements', *Media Release*, 23 June 2011, pp 4 and 5.

26 CCS Bill EM, p. 1.

27 CCS Bill EM, p. 1.

28 Shareholder Ministers, *Statement of Expectations*, December 2010, p. 3.

3.30 Telstra's draft migration plan outlines how and over what period 'Telstra will cease supplying copper and most HFC services – including wholesale services (where they are supplied) – as part of the migration of the NBN.'[30]

3.31 If the structural separation option is not followed, functional separation would require Telstra to:

- 'Conduct its network operations and wholesale functions at arm's length from the rest of Telstra;
- Provide the same information and access to regulated services on equivalent price and non-price terms to its retail business and non-Telstra wholesale customers; and
- Put in place and maintain strong internal governance structures that provide transparency and reassurance for the regulator and access seekers that equivalence arrangements are effective.'[31]

3.32 While processes for either Telstra's structural or functional separation are provided for under the CCS Act, the Government's preferred option is for Telstra to structurally separate and 'accordingly the' CCS Act 'gives priority to a genuine structural separation process over the functional separation process.'[32]

3.33 On 29 July 2011 and 24 August 2011, as required under the CCS Act[33], Telstra lodged its SSU and Draft Migration Plan respectively[34], with the ACCC for review.[35]

ACCC Review

3.34 The *Telecommunications Act 1997* (Cth) requires the ACCC to undertake consultation on Telstra's draft migration plan and while it is not a requirement for the ACCC to do the same for Telstra's SSU, given 'the significance of the SSU in facilitating structural reform', the ACCC has undertaken a similar consultation process for the SSU.[36]

29 ACCC, 'Assessment of Telstra's Structural Separation Undertaking and draft Migration Plan', 30 August 2011 (Discussion Paper) p. 1.

30 ACCC, Discussion Paper, p. 1.

31 CCS Bill Explanatory Memorandum, p. 2.

32 CCS Bill Explanatory Memorandum, p. 2.

33 CCS Bill Explanatory Memorandum, p. 2.

34 ACCC, Discussion Paper, p. 6.

35 CCS Bill Explanatory Memorandum, p. 2.

36 ACCC, Discussion Paper, p. 6.

3.35 In assessing and accepting the SSU, the ACCC would have to 'be satisfied that competition and consumer interests are supported by the specific reforms that have been proposed', ... 'particularly during the progressive transition to the new industry structure.'[37] Should the SSU and draft Migration Plan be accepted and approved by the ACCC, this would provide various protections 'from competition laws to facilitate' Telstra's structural separation.'[38]

3.36 On 30 August 2011, the ACCC released its discussion paper on Telstra's SSU and draft Migration Plan for comment with submissions sought by 27 September 2011.[39]

3.37 In its discussion paper, the ACCC stated that, as the SSU did not include a compliance plan for structural separation, the SSU would not be accepted in its present form. The SSU would need to be resubmitted by Telstra 'in a form that fully complies with the legislative requirements.'[40]

3.38 The ACCC's preliminary view of the draft Migration Plan was that it accords with all of the statutory criteria.[41]

3.39 The ACCC outlined specific matters of concern, a number of which were serious enough for the ACCC to form the view that these matters would 'militate against ACCC acceptance of' the SSU. These are:

- There needs to be a clear and enforceable commitment to an 'equivalence of outcomes' that enables wholesale customers and Telstra's retail businesses to gain access to key input services of equivalent quality and functionality
- clarification of the mechanisms that would ensure the proposed equivalence and transparency measures remain fit for purpose for the duration of the interim period.'
- The inclusion of 'arrangements between Telstra and NBN Co that include the parties' ability to vary the arrangements without further scrutiny by the ACCC.'[42]

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37 ACCC, Discussion Paper, p. 1.

38 ACCC, Discussion Paper, p. 1.

39 ACCC, Discussion Paper, p. 5.

40 ACCC, Discussion Paper, p. 2.

41 ACCC, Discussion Paper, p. 5.

42 ACCC, 'ACCC calls for comment on Telstra's structural separation undertaking and draft migration plan', *Media Release*, 30 August 2011.

Industry Comments

3.40 While generally supportive of the structural reform of the telecommunications industry, Optus expressed concern about the equivalence and transparency of the Telstra SSU. In outlining its concerns about the SSU, Optus stated:

> One of the principles we have been saying for a number of years around telco reform is that you must have the ability to have equivalence of access or equivalence of outputs between Telstra's retail customers and its wholesale customers. In other words, and this is one of the principles we put forward some time ago, we would ideally like to see a contract between Telstra network services and its retail arm which was in some way comparable to the contract they had between us or access seekers and Telstra wholesale, and then a level of transparency around those contracts. That would enable a number of things: No. 1, price comparability, which is one of our major concerns; No. 2, operational performance capability in terms of provisioning of services, billing, fault rectification and a range of other things that go to the heart of making sure there is an equivalence of outputs to access seekers and Telstra retail and a level of transparency; and, No. 3, a level of scrutiny by an independent regulator with powers to enforce compliance of that equivalence and transparency.[43]

3.41 Internode was also supportive of the structural reform of industry, but also expressed concerns about the SSU and stated:

> Under Telstra's SSU, which effectively replaces the existing regulatory regime, competitive providers like Internode will be worse off. We will have significantly less or in fact almost no recourse to the ACCC, and under that SSU Telstra will largely get to set all of the prices and access terms by which they deign to provide wholesale access to the old copper network. This is access that will be required for at least the next decade, which is in fact about as long as the entire industry has been providing DSL. So we are about to lock in a regulatory regime for the next decade yet in the course of the last decade we have seen massive shifts in broadband service, particularly DSL service. We have seen the retail prices spiral downwards. We have seen speeds ramp up. Now we are going to lock it down at, we assert, an access cost that

43 Mr Maha Krishnapillai, Director of Government and Corporate Affairs, Optus, Transcript of Evidence, Sydney, 24 October 2011, p. 38.

> is somewhat worse than our current wholesale pricing from Telstra.[44]

3.42 Internode was of the view that Telstra's market dominance would continue, and that smaller telecommunications providers such as Internode would be worse off because:

> ...they are likely to cost us more but they leave us largely at the mercy of Telstra, who can set the access pricing and the terms and conditions under which they provide the pricing, provide the only forum in which we can complain about that pricing and provide almost no transparency as to how they actually came up with the pricing.[45]

3.43 Internode also stated that it had discussed its concerns with the ACCC.

3.44 Vodafone's main concern about the SSU (as discussed with the ACCC) is that there is an inadequate separation between Telstra's wholesale and retail businesses. Vodafone explained:

> In particular, there are a number of aspects and approval processes within Telstra Corporation, as opposed to their retail and wholesale arms, that are still retained by Telstra Corporation and have a significant bearing on both wholesale and retail operations. For example, the Telstra Corporation part of the business still retains the pricing approval process for both retail and wholesale, and we think that that does not really lend itself to an adequate amount of separation.[46]

3.45 Vodafone was also concerned that there be regulatory oversight of market behaviour to ensure consumers are not take advantage of when new competition is introduced into the telecommunications market.[47]

Agreement Negotiation, Review and Completion Timeframes

3.46 Signing of the Telstra Agreement represents 'the conclusion of nearly two years of detailed negotiations' between NBN Co, the Government and Telstra.[48] The NBN Co Corporate Plan makes the assumption that the

44 Mr John Lindsay, General Manager, Regulatory and Corporate Affairs, Internode, Transcript of Evidence, Sydney, 24 October 2011, p. 57.

45 Mr Lindsay, Internode, Transcript of Evidence, Sydney, 24 October 2011, p. 57.

46 Mr Matthew Lobb, General Manager, Industry Strategy and Public Policy, Vodafone Hutchison Australia, Transcript of Evidence, Sydney, 24 October 2011, p. 59.

47 Mr Lobb, Vodafone, Transcript of Evidence, Sydney, 24 October 2011, p. 59.

48 NBN Co, 'NBN Co and Telstra Sign Binding Definitive Agreements', *Media Release*, 23 June 2011, p. 2.

Telstra Agreement would be completed and approved by the ACCC by 30 June 2011.

3.47 While the Telstra Agreement was arrived at prior to the end of June 2011, the timeframe for the completion of the Agreement has taken longer than expected as the two CP of: Telstra Shareholder approval and ACCC consideration and approval of Telstra's SSU and draft migration plan had not occurred within this timeframe.

3.48 In addition, the termination arrangements (under the IID) for the Telstra Agreement provides that 'if the CP are not satisfied or waived by 5 pm on 20 December 2011, then the IID, unless varied by prior agreement, will automatically terminate', and the three remaining documents forming the Telstra Agreement 'will not come into force and effect'.[49]

3.49 The NBN Co stated that if the 20 December 2011 timeframe for satisfying all the CP is not met, then:

> ...the interim access provisions will continue in force for a period of 10 years to support Telstra infrastructure in use or ordered by NBN Co at that time. Those interim access provisions include a process the parties will follow to deal with any continuing need NBN Co has for access to Telstra infrastructure on expiry or early termination of the provisions.[50]

3.50 The ACCC's acceptance and approval of Telstra's SSU and draft migration plan is a CP of the Telstra Agreement, without which the Agreement cannot be completed.[51]

3.51 In reference to whether the ACCC would complete its review of the SSU and Draft Migration Plan before 20 December 2011, it stated:

> The resources are considerable. We have an entire branch dedicated to the consideration of the structural separation undertaking. On the time frames, I am going to give you the same answer that Rod Sims, our chairman, gave ... in Senate estimates last week which was that we are moving as quickly as we can. The issues are important ... but we give no guarantee as to when they might be concluded.[52]

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49 NBN Co, 'NBN Co and Telstra Sign Binding Definitive Agreements', *Media Release*, 23 June 2011, p. 5.

50 NBN Co, 'NBN Co and Telstra Sign Binding Definitive Agreements', *Media Release*, 23 June 2011, p. 5.

51 Mr Michael Cosgrave, General Manager, Communications Group, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 10.

52 Mr Cosgrave, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 4.

3.52 In an update on the status of the Telstra Agreement, the NBN Co stated, following ACCC approval of the Telstra SSU and draft migration plan, Shareholder Ministers must endorse the Agreement, but before this occurs Telstra will need to resubmit its SSU to the ACCC. Telstra is expected to take place in November 2011. In the event of a variation to the 'material value' to the Telstra Agreement as a result of any changes made, Telstra shareholders will be given an opportunity to vote on any changes. The NBN Co stated:

> The ACCC has to accept Telstra's SSU and approve the migration plan and then NBN Co's shareholder, the Australian government, has to endorse the deal before the agreements become binding. Before these approvals can happen, as Telstra noted in its advice to the ASX, Telstra has to submit a revised SSU, which it expects to do in coming weeks following its current discussions with the ACCC.
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> While Telstra expects that the issues raised by the ACCC can be addressed without a material impact on shareholder value, it has indicated that if any material change does occur, shareholders will have an opportunity to vote on such changes. In any case we will not know the outcomes and what they mean for the shareholder approval process until these issues are resolved. While the focus of industry has been on Telstra's transparency and equivalence arrangements set out its SSU, the definitive agreements are also the subject of scrutiny by the ACCC.
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> Against this background, until all the conditions precedent have been met and the final agreements are available to the Telstra and NBN Co. boards and to the government, no further documentation regarding agreements can be released.[53]

3.53 When asked whether any delay to the ACCC process for consideration of the Telstra SSU and migration plan would be a cause of concern for the NBN Co, Mr Mike Quigley, CEO stated:

> ...it would cause me concern. I am keen to have the deal done so we can get on with it and have some surety. We are working at the moment under an interim agreement. That interim agreement is not the final agreement. There are certain restrictions on it. We are not free to do all the things that we would like to do to get on with the job.[54]

53 Mr Quigley, NBN Co, Transcript of Evidence, Sydney, 24 October 2011, pp 1-2.

54 Mr Quigley, NBN Co, Transcript of Evidence, Sydney, 24 October 2011, p. 3.

Optus Agreement

3.54 While the Binding Definitive Agreement between NBN Co and Optus (the Optus Agreement) was not included in the NBN Co Corporate Plan, the $800 million value of the Agreement to Optus 'is financially beneficial to NBN Co resulting in an improvement in NBN Co's internal rate of return when compared to the...Corporate Plan.'[55]

3.55 The Optus Agreement provides that as the NBN is progressively rolled out, Optus will decommission its HFC network and migrate its customers to the NBN. The rate of decommissioning HFC networks and the migration of customers will mirror the NBN rollout.[56]

3.56 Optus stated that under the Agreement, its HFC network will be decommissioned with the exception of the part of the network used for Optus' fibre component for its mobile backhaul and other corporate customers.[57]

3.57 The Optus Agreement, similarly to the Telstra Agreement is subject to approval by the ACCC, and confirmation of tax treatments. At the time of writing, neither the ACCC nor the Australian Taxation Office (ATO) have issued decisions on the agreement.[58]

Future Third-Party Ownership of Optus' HFC Network

3.58 At the committee's hearing on 24 October 2011, there was some doubt as to whether Optus could sell its HFC network to a third party and whether that third party would then be able to offer broadband services over the Optus network. Optus stated:

> The general principle is no; we have effectively made a sale of our HFC network and capacity to NBN Co. and agreed a migration strategy across to NBN Co. So the principle is fairly clear.[59]

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55 NBN Co, 'NBN Co and Optus Sign Binding Agreement', *Media Release*, 23 June 2011.
56 NBN Co, 'NBN Co and Optus Sign Binding Agreement', *Media Release*, 23 June 2011.
57 Mr Krishnapillai, Optus, Transcript of Evidence, Sydney, 24 October 2011, p. 37.
58 NBN Co, 'NBN Co and Optus Sign Binding Agreement', *Media Release*, 23 June 2011.
59 Mr Krishnapillai, Optus, Transcript of Evidence, Sydney, 24 October 2011, p. 40.

Additional Agreement Issues

Non Disparagement Clause

3.59 Both the Telstra and Optus Agreements contain a clause which precludes Telstra and Optus from marketing wireless services on the basis of comparable or equal performance standards as provided by an NBN service. The NBN Co described these clauses as 'an agreement to not present [the wireless network] as a replaceable—substitutable—service'.[60]

3.60 Optus explained the practical interpretation of the clause for it and Telstra and stated:

> ...the key is that [neither Telstra nor Optus] can make claims around the performance standards of wireless broadband versus an NBN service.[61]

3.61 Importantly, this does not prevent either company from marketing wireless services. Under its Agreement, Optus commented that it:

> ... cannot go out and undertake certain marketing activities ... which, for want of a better term, will be sledging type activities—saying that the wireless service is superior to the fixed broadband service.[62]

3.62 The NBN Co clarified what is permissible under the Agreements and what is prohibited under the non disparagement clause and stated:

> I do not think anywhere in the clause there is the word 'criticism'. It says that the wireless services are not substitutable for fibre today. That is what we are trying to make clear: that they are not substitutable.[63]

3.63 While there is provision in trade practices legislation to deal with misleading comments which could be made in regard to marketing of wireless services, the NBN Co stated that the purpose of the non disparagement clause is to prevent in the future any delay which may be experienced through litigation.[64]

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60 Mr Quigley, NBN Co, Transcript of Evidence, Sydney, 24 October 2011, p. 17.

61 Mr Krishnapillai, Optus, Transcript of Evidence, Sydney, 24 October 2011, p. 39.

62 Mr Andrew Sheridan, General Manager, Interconnect and Regulation, Optus, Transcript of Evidence, Sydney, 24 October 2011, p. 39.

63 Mr Quigley, NBN Co, Transcript of Evidence, Sydney, 24 October 2011, p. 18.

64 Mr Quigley, NBN Co, Transcript of Evidence, Sydney, 24 October 2011, p. 18.

3.64 Optus stated that while the non disparagement clause provides no more or less than what is required under current trade practices legislation and that it will not prevent Optus from marketing its wireless service. Optus commented that:

> We have not seen that as anything more or less than what will be required under trade practices legislation today— that we cannot make claims about the performance of our wireless network being superior in a way that it is not. We will still continue to aggressively market wireless broadband throughout that period.[65]

3.65 The NBN Co also stated that the effect of the clause would be to protect shareholder interests and secure the NBN investment. The NBN Co commented:

> All [NBN Co is] trying to do is write a clause into a document that protects the shareholders' interests. As I have said repeatedly, we are all in favour of as much mobile penetration as can possibly happen because we are seeing an increasing number of mobile devices in use driving up our usage on fixed line networks which makes our business case a little more secure.[66]

3.66 The NBN Co also stated that more broadly, the non disparagement clause component of the Telstra and Optus Agreements provides a 'constraint [that] is only one that makes good sense'. Further, as taxpayer funds are being used to enable decommissioning of the copper network and structural separation, 'it makes perfectly good sense to make sure that Telstra continues to use the fixed line service.'[67]

3.67 The Department of Broadband, Communications and the Digital Economy (DBCDE) added that the non disparagement clause component of the Telstra and Optus Agreements is under consideration by the ACCC. The DBCDE also 'expressed confidence that the ACCC would treat [these clauses] as they have throughout the [SSU] process, as being a particularly important outcome.'[68]

65 Mr Krishnapillai, Optus, Transcript of Evidence, Sydney, 24 October 2011, p. 39.

66 Mr Quigley, NBN Co, Transcript of Evidence, Sydney, 24 October 2011, p. 18.

67 Mr Quigley, NBN Co, Transcript of Evidence, Sydney, 24 October 2011, p. 18.

68 Mr Peter Harris, Secretary, DBCDE, Transcript of Evidence, Sydney 24 October 2011, p. 18.

Workforce Retraining

Retraining Funding Deed with Telstra

3.68 Under the Telstra Agreement, the Government will provide $100 million to Telstra to assist it in the retraining and redeployment of its staff which are affected by reforms to the structure of the telecommunications industry.[69] The Retraining Funding Deed (RFD) sets out the terms on which the Government will provide this funding to retrain certain staff over an eight year period.

3.69 Concluding on 20 June 2019, the RDF requires Telstra to give priority to retraining staff who currently work on the copper and HFC networks, including the wholesale copper workforce and the direct field support workforce. Telstra will give priority to retraining its employees in NBN related technical, process and system activities.[70]

3.70 Payments to Telstra will commence after it submits to and receives approval from the DBCDE for an initial training plan and budget.[71] The training plan must cover a three year period and include an outline of training targets which will set out the skills required and the training courses to be developed or refreshed. [72] Telstra must also provide six monthly reports to the Government on progress against training plans, and a more detailed annual report which includes report on these matters.[73]

3.71 Under the RFD, Telstra must consult with stakeholders in respect of the development of training plans and use funds to develop and deliver training courses that facilitate the following objectives:

- to support the availability of an appropriately trained workforce for the NBN; and
- to establish a retraining arrangement for Telstra staff who may otherwise have faced redundancy due to the rollout of the NBN.[74]

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69 DBCDE, *Submission 3.2*, p. 1

70 DBCDE, *Submission 3.2*, p. 1.

71 Mr Quinlivan, DBCDE, Transcript of Evidence, Sydney, 24 October 2011, p. 2.

72 Ms Pip Spence, First Assistant Secretary, NBN Implementation Division, DBCDE, Transcript of Evidence, Sydney, 24 October 2011, p. 2.

73 DBCDE, *Submission 3.2*, p. 1.

74 Telstra, 'Telstra signs NBN Definitive Agreements', *Media Release*, 23 June 2011.

Optus Employees

3.72 In contrast to the Telstra Agreement, the Optus Agreement does not involve a component of public grants for retraining of Optus staff. Outlining the different objectives of the two agreements, the DBCDE stated:

> The negotiations with Telstra were designed to develop both something that was in the public interest and had value for them. We were not at any point negotiating with Optus on a similar basis. So the Optus negotiation is entirely conducted between NBN Co. and Optus. The Telstra negotiation was effectively a tripartite arrangement. It involved the government negotiating as well as NBN Co. with Telstra. It had a different objective, which was the migration, the overall agreement, to structurally separate and migrate. So the purpose behind obtaining sufficient value for Telstra to agree to do that, in a public policy sense, was not just the ability to retrain workers—which we think is quite an important public policy interest in its own right—but was the structural separation outcome from the ability for Telstra to accept a certain price for a certain set of functions in order to free up its network for a competitive-neutral telecommunications industry for the future.
>
> The negotiation with Optus was an NBN negotiation entirely of a commercial nature around migration, so the ... retraining for Optus, would clearly not be a matter for Mr Quigley. It would be a matter for ministers to consider should they believe there is a need to do so.[75]

Special Access Undertaking

Purpose

3.73 Under trade practices law, the NBN Co will voluntarily lodge a SAU with the ACCC. The SAU 'is intended to provide regulatory certainty to an investor in relation to the issues covered by the SAU and for the term of the SAU.' The SAU is also designed to provide market certainty 'about the way NBN Co will engage and operate for the term of the SAU.'[76]

75 Mr Harris, DBCDE, Transcript of Evidence, Sydney, 24 October 2011, pp 8-9.

76 NBN Co, *Corporate Plan 2011-2013*, p. 106.

3.74 The SAU 'will cover key price and product aspects of access to NBN Co's fibre, wireless and satellite networks' as well as a number of 'non-price terms and conditions.' The NBN Co Corporate Plan states that the following product aspects are proposed to be addressed in the SAU:

- 'Descriptions of the wholesale Layer 2 services and products that NBN Co intends to supply;
- Initial fibre, wireless and satellite wholesale product sets and some conditions of supply;
- NBN Co's product development, variation and withdrawal processes.
- NBN Co proposes to include the following price aspects in the SAU:
  - ⇒ Pricing principles and methodology;
  - ⇒ Initial pricing for key wholesale products;
  - ⇒ Ongoing price regulation for certain wholesale products.
- Detailed long-term constraints on total revenue able to be earned by NBN Co, using a Regulatory Asset Base methodology;
- Cost prudency commitments in relation to the Regulatory Asset Base;
- NBN Co's non-discrimination commitments; and
- Reporting procedures.'[77]

3.75 In July 2011, the NBN Co released a SAU discussion paper and the third version of its WBA for industry comment. The SAU discussion paper:

- 'describes the key commitments that NBN Co intends to make in its SAU',
- outlines the 'proposed approach to pricing of key "Price Controlled Offers", the operation of NBN Co's proposed Regulatory Asset Base, and long term revenue constraint methodology.'
- 'Providing an ongoing role for the ACCC over the term of the SAU, to ensure the commitments made in the SAU continue to remain relevant as the industry evolves.'[78]

3.76 The NBN Co sought Industry feedback by 19 August 2011.[79]

77 NBN Co, *Corporate Plan 2011-2013*, p. 106.

78 NBN Co, 'SAU Discussion Paper and Wholesale Broadband Agreement', *Media Release,* July 2011, p. 1.

79 NBN Co, 'SAU Discussion Paper and Wholesale Broadband Agreement', *Media Release,* July 2011, p. 1.

3.77 In its Corporate Plan, the NBN Co stated that the finalisation of the SAU was dependent on:

- 'key policy matters such as the number and location of Points of Interconnect [POIs][80] and the required approach to uniform national wholesale pricing.' and
- A preference to wait until proposed NBN legislation was enacted.[81]

3.78 At the committee's 24 October 2011 hearing, the NBN Co stated that it was still in discussions with the ACCC in regard to the SAU, which were 'going well' and that it would publish its SAU as soon as it was able to.[82]

3.79 Further the NBN Co stated:

> We are hoping that [the SAU] will be lodged shortly. We are still in discussions with the ACCC on that. I flagged at estimates that we have shifted certain parameters around that agreement. I am looking to simplify it somewhat. That drafting is underway now. I continue to have discussions with the ACCC.[83]

3.80 The ACCC recently stated that the NBN Co has indicated it intends to provide an SAU to the ACCC for consideration in November 2011.[84]

Timeframe for ACCC Consideration

3.81 The ACCC is required to assess the NBN Co's SAU against 'reasonableness criteria' as provided for under trade practices legislation. These criteria include the: 'promotion of competition, encouraging economically efficient investment in and use of infrastructure, legitimate business interests of access providers, interests of access seekers and direct costs.'[85]

80 A Point of Interconnect (POI) is the point of connection to the NBN Co access capability for Retail Service Providers and Wholesale Service Providers. 'In the field, this is the physical port on the Ethernet Fanout Switch located at NBN Co's POI, where an Access Seeker connects to establish exchange of traffic with NBN Co's network.' NBN Co, *Corporate Plan 2011-2013*, 17 December 2010, p. 157.

81 NBN Co, *Corporate Plan 2011-2013*, p. 107.

82 Mr Quigley, NBN Co, Transcript of Evidence, Sydney, 24 October 2011, p 11.

83 Mr Quigley, NBN Co, Transcript of Evidence, Sydney, 24 October 2011, p 16.

84 ACCC, Correspondence to Baker and McKenzie, 11 November 2011, p. 2.

85 NBN Co, *Corporate Plan 2011-2013*, p. 107; Mr Michael Cosgrave, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 8.

3.82 The statutory timeframe for ACCC consideration and either rejection or acceptance of the SAU is six months, ‘subject to extensions of time and stop-clocks.’[86]

3.83 The ACCC commented that its consideration of the NBN Co SAU could take between six and twelve months depending on the suitability of the SAU lodged with the ACCC and the comments made around it.[87]

3.84 When asked about the consequence of ACCC rejection of the SAU, the ACCC commented that:

> Provided we have a regulated service—which we should have by that stage—if the commission's position differed from what was in the SAU, it would be open to access seekers to ask the commission to make an access determination in ways that, in all likelihood, reflected areas that the commission had concerns with. The commission could take a fairly swift reactive move in the event it found an undertaking unacceptable.[88]

Wholesale Broadband Agreement

Purpose

3.85 The NBN Co’s Corporate Plan 2011-2013 provides for development of a WBA which the takes the form of an agreement between NBN Co and a RSP which purchases wholesale broadband services from the NBN Co. The WBA sets ‘out the complete terms and conditions of access to all of the services and products being provided over’ NBN Co’s ‘fibre, wireless and satellite networks’.[89] More specifically, it sets out:

> ..the arrangements for the delivery of commercial services over the NBN encompassing such matters and products and price, service levels, technical information, credit policies and future product development.[90]

86 NBN Co, *Corporate Plan 2011-2013*, p. 107.

87 Mr Cosgrave, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 9.

88 Mr Cosgrave, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 13.

89 NBN Co, *Corporate Plan 2011-2013*, pp. 106-107.

90 NBN Co, ‘NBN Co offers clarity and transparency on pricing and regulatory approach’, *Media Release*, 28 July 2011.

3.86 After a ten month industry consultation process,[91] ahead of moving into the commercial launch of its services in October 2011, on 28 July 2011, the NBN Co released version three of the WBA.[92]

3.87 In addition to being the contractual vehicle for the supply of its services to customers, the WBA will have the regulatory purpose, as required under legislation, of 'declaring' NBN Co's services.[93]

3.88 In the period leading up to the release of version three of the WBA, the NBN Co completed two separate public consultation processes, public workshops, and performed 'customer deep dives', involving more than 100 hours of face-to-face discussions. Of its WBA industry consultation process, the NBN Co stated:

> This engagement has allowed NBN Co to respond to customer concerns in a manner that it believes balances the legitimate interests of end users, customers and the objectives of the NBN.[94]

3.89 As the WBA 'guarantees equivalence' in NBN Co's dealings with RSPs, the WBA will be an identical document for all RSPs. Until the final version of the WBA is approved, NBN Co has signed interim agreements or a Standard Form of Access Agreement (SFAA) with already participating RSPs in NBN trial sites.[95] The SFAAs put in place will be replaced with a WBA once it has been finalised.[96]

Industry Comments

3.90 Optus was of the view that there were 'a number' of the terms and conditions in the WBA that had direct implications for its pricing policy, in particular liability issues. Optus commented that the WBA is a 'very complex document', and it is taking 'some time' to work through it.[97]

3.91 Optus stated that NBN Co has put its pricing into the market in terms of expected wholesale rates and is billing RSPs on an interim basis, reflecting some of the retail prices that have already been released. Although some

91 NBN Co, 'SAU Discussion Paper and Wholesale Broadband Agreement July 2011', *Media Release*, July 2011.

92 NBN Co, *Corporate Plan 2011-2013*, pp. 106-107.

93 NBN Co, 'SAU Discussion Paper and Wholesale Broadband Agreement July 2011', *Media Release*, July 2011.

94 NBN Co, 'SAU Discussion Paper and Wholesale Broadband Agreement July 2011', *Media Release*, July 2011.

95 Mr Quigley, NBN Co, Transcript of Evidence, Sydney, 24 October 2011, pp. 5, 6.

96 Mr Quigley, NBN Co, Transcript of Evidence, Sydney, 24 October 2011, p. 6.

97 Mr Krishnapillai, Optus, Transcript of Evidence, Sydney, 24 October 2011, pp. 37, 41, 42.

RSPs have chosen to release their prices with caveats, Optus was not prepared to release its prices until it had finalised terms and conditions under its WBA with NBN Co.[98] Optus commented:

> There are a number of terms and conditions in that contract which have direct implications for our pricing policy. We are very keen to release our pricing, as you can imagine, but we also know that we have to work out on what basis the contract with NBN Co will be finalised. We have talked about some of those issues in the broad. Issues around liability in particular, are ones that we have to factor into our cost pricing and therefore our pricing for customers.[99]

3.92 Further, Optus stated that an important factor in discussing the WBA with NBN Co was that the ACCC had to agree to the terms of the provision of NBN Co's wholesale services to RSPs. Optus advised that this process had not yet begun.[100]

3.93 Internode[101] stated that a transition is underway towards commercial operations for the NBN. While Internode's customers have had a 'paid-for' ADSL service and a free trial service from NBN Co, it is now charging for its services. While there is no contractual certainty of supply of services until a WBA is signed, Internode was of the view that it is 'inconceivable that NBN Co would withdraw these services' in the interim.[102]

3.94 Internode raised concern about RSPs signing an interim agreement with the NBN Co on the grounds of differing concessions between individual agreements. Internode stated:

> What concerns me about the wholesale broadband agreement is that they have actually offered us a wholesale broadband agreement and asked us to sign it. But of course it is subject to the proviso that all of the retail service providers will end up with the same agreement. So what I would really like to understand is how, if we signed it and Optus, for instance, managed to win some concessions in the agreement, then that change in the wholesale

98 Optus: Mr Sheridan, Transcript of Evidence, Sydney, 24 October 2011, p. 41; Mr Krishnapillai, Optus, Transcript of Evidence, Sydney, 24 October 2011, p. 42.

99 Mr Krishnapillai, Optus, Transcript of Evidence, Sydney, 24 October 2011, p. 37.

100 Mr Sheridan, Optus, Transcript of Evidence, Sydney, 24 October 2011, p. 41.

101 Internode is the fifth largest RSP in Australia, with about 30 per cent of its customers in South Australia: Mr Lindsay, Internode, Transcript of Evidence, Sydney, 24 October 2011, p. 49.

102 Mr Lindsay, Internode, Transcript of Evidence, Sydney, 24 October 2011, pp. 48.

> broadband agreement would be applied to the agreement we have.[103]

3.95 Internode stated that it had 'a high degree of confidence' that there will be 'very few changes' to the final WBA that will materially affect the cost of using the NBN and that the WBA will need to be settled by the end of November 2011.[104]

3.96 Vodafone Hutchison Australia (Vodafone) stated that the SAU and WBA establish the NBN Co's 'fundamental commercial relationships'. Vodafone stated that both documents will 'evolve' over time, and that the NBN Co has made a range of commitments about how it will consult with industry as these documents change.[105]

3.97 Further, Vodafone was of the view that the regulatory oversight of that evolutionary process is important, and that this point needs to be clarified about the assessment process about to be undertaken by the ACCC.[106]

Recourse to ACCC

3.98 While the ACCC has a role in assessing the NBN Co SAU, it does not have a role in assessing the WBA. The ACCC raised concerns that the five year term that was being applied to interim agreements ahead of a finalised SAU would mean that RSPs would not have recourse to the ACCC under these agreements. The ACCC stated that the SAU should set the framework under which the WBA could be entered into. The ACCC commented:

> ...we did have a concern about was the term of the access agreement that NBN Co. was seeking to have access seekers enter into which was a five-year access agreement. That poses a concern largely because of the hierarchy stack, if I can out it that way, that exists in the legislation. ...The stack effectively places access agreements at the top of the pyramid and then a cascade below that has access to terminations and access undertakings—it might be the other way round, but various determinations by the commission. That is intended—and the commission have no issue with this—to encourage agreement between access providers and access seekers. The difficulty is that, in the event that people enter

103 Mr Sheridan, Optus, Transcript of Evidence, Sydney, 24 October 2011, p. 53.
104 Mr Lindsay, Internode, Transcript of Evidence, Sydney, 24 October 2011, p. 56
105 Mr Lobb, Vodafone, Transcript of Evidence, Sydney 24 October 2011, p. 59.
106 Mr Lobb, Vodafone, Transcript of Evidence, Sydney, 24 October 2011, p. 59.

> access agreements, clearly they have no recourse to the commission.
>
> The clear intent always was that there would be a framework set by an access undertaking that would be considered and, if suitable, accepted by the commission. That access undertaking would be the framework under which access agreements were then entered into.[107]

3.99 The ACCC raised its concern with the NBN Co which responded by extending its trial agreements until the end of November 2011. The ACCC preference is that only 'substantive agreements' be entered into, but that where this is not possible, where access seekers encounter difficulties under interim agreements, they have recourse to a 'regulatory backstop' with the ACCC.[108]

3.100 In addition, in response to industry concern about regulatory uncertainty in the absence of the SAU, the NBN Co recently announced that it had:

> ...reduced the initial term of its WBA to 12 months and established a bilateral and multilateral Contract Development Process to further enhance the long term WBA whilst the SAU is being considered by the ACCC.[109]

Competition and Pricing

Background

3.101 In the committee's First Report, issues were raised in relation to how the implementation of the NBN would affect competition at various levels in the telecommunications industry and more broadly the Australian economy.

3.102 The main competition issues mentioned in the First Report were the impact on competition of: the structural separation of Telstra, the wholesale, open access structure of the NBN, pricing of access to the NBN, how the use of different broadband technologies may affect the cost and price of the NBN, and the ACCC's decision to increase the number of POIs from 14 to 121.

107 Mr Cosgrave, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 1.

108 Mr Cosgrave, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 12.

109 NBN Co, Wholesale Broadband Agreement (WBA), Media Release, 21 November 2011.

3.103 The focus in the First Report was how NBN access pricing and how the cost of physical capital was impacting on competition among RSPs, especially small RSPs.

3.104 The RSPs have again expressed concern about the impact on competition of access pricing under the NBN, the absence of competition in backhaul in some areas and the impact of the ACCC's decision to increase the POIs from 14 to 121.

Points of Interconnect

3.105 The ACCC stated that its decision that the POIs be increased from 14 to 121 was intended to create greater competition for RSPs. Part of the ACCC's decision-making process for determining POI numbers involved taking into consideration: existing infrastructure use, existing competition and the long-term interest of end-users.[110]

3.106 The ACCC's initial determination on POI numbers was based on maintaining 'competition between the backhaul providers' so that 'there was not an over build by NBN Co or existing infrastructure providers.' This would need to be balanced by 'competition between transmission providers' to each POI.[111]

3.107 The ACCC implemented its approach by:

> ...recommending that competition principles be adopted and then worked with NBN Co. to come up with a mechanism, proposed by NBN Co., which would do two things—firstly, select points of interconnect where there was already competition between at least two backhaul providers and, secondly, ensure that there was a reasonable prospect that those providers would still engage in competition once the POI was built and that there was an element of overlay which allowed for an actual network architecture to be constructed.[112]

3.108 Through this process, the ACCC proposed that there should be approximately 120 POIs. The ACCC then asked for industry comment on its POI proposal and based on comments received, the ACCC increased the number of POIs to 121. Since then, following negotiation with Telstra, there have been 'a few minor variations' to the location of POIs. Location

110 Dr Robert Nicholls, General Manager, Convergence and Mobility Branch, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 2.

111 Dr Nicholls, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 2.

112 Dr Nicholls, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 2.

changes reflect 'where there is power, water and space in Telstra exchange buildings. The outcome .... is that Telstra will provide 111 exchange buildings and that ten new buildings are being built by NBN Co.'[113]

3.109 Internode stated that POI locations were chosen arbitrarily and only 'the potential' for competitive backhaul, rather than the 'actual physical presence of' competitive backhaul was taken into account by the ACCC. Internode explained the barrier created for RSPs providing services in regional areas where there is limited competitive backhaul present and stated:

> The barrier or challenge for existing regional service providers is that they have all the overheads of connecting to the NBN and all of their existing overheads of running their existing network, which they are already operating on very squeezed margins because as soon as they look even vaguely viable Telstra starts marketing up against them, as is their right. But it means that, in the build-up to the NBN, those regional service providers face significantly increased costs as a dual network operation overhead, which is likely to spell the end for most of them. It is also worth noting there are relatively few regional-only service providers.[114]

3.110 Internode added that the problems it had encountered with the absence of competitive backhaul in regional areas meant 'a huge amount of uncertainty as to what it will cost' Internode to provide a service in regional areas and so may not choose to do so.[115]

3.111 In response to Internode's concern, the ACCC stated:

> Regardless of who provides backhaul, somebody incurs the cost of the backhaul from regional areas to metropolitan points of presence. In coming up with our advice on points of interconnect, we had to make a choice: should that be monopoly provided by NBN Co. or should that be competitively provided by the five competitors. ... Our advice was that competition would yield the best outcomes. There will still be a cost of transmission between metropolitan areas and regional areas. The only difference between whether there are 14 points of interconnection or 121 is whether that cost is incurred by NBN Co. or incurred by

113 Dr Nicholls, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 2.

114 Mr Lindsay, Internode, Transcript of Evidence, Sydney, 24 October 2011, p. 50.

115 Mr Lindsay, Internode, Transcript of Evidence, Sydney, 24 October 2011, p. 50.

> competitors who are seeking to provide services on a competitive basis to [RSPs] such as Internode.[116]

3.112 The ACCC explained that it understood that there are trade-offs in the advice it provided on POIs, but that the basis of its decision was on 'a belief in competition that existed providing the best outcomes.'[117]

3.113 The ACCC welcomed the NBN Co's announcement of a wholesale charge rebate in response to the concern raised by RSPs such as Internode above.[118]

3.114 The rebate is intended to 'make it cheaper and easier for broadband service providers to start offering services to consumers and businesses over the NBN.' The rebate is provided 'on capacity charges in the early days of the network's establishment.'[119]

3.115 The rebate is for 'the wholesale charge for the first 150 Mbps per month on its Connectivity Virtual Circuit until there are 30 000 premises passed in a connectivity serving area, which connects' to a POI.[120]

3.116 Australia On Line was of the view that the NBN Co's announcement of rebates to assist RSPs 'would not materially lower the prohibitive costs of servicing ... customers via the NBN.'[121]

3.117 Australia On Line, similarly to Internode, also stated that it would be more difficult under the increased number of POIs to provide services to rural and regional areas. Australia On-Line stated:

> It will cost Australia On Line **15 fold** more to service its existing national customer base via the NBN than is currently the case. This increase represents a dramatic imposition of mountainous barriers to entry to the national retail broadband. This **15 fold** increase in costs is a direct result of increasing **17 fold** the number of POI that are required to connect nationally via the NBN compared to that required to connect nationally to the ADSL network. It currently requires 7 POI to connect nationally to the ADSL network and the NBN requires 121 POI to connect nationally to the NBN. In the event that NBN Co rebates all our NBN connection charges, it will

116 Dr Nicholls, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 3.

117 Mr Cosgrave, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 3.

118 Mr Lindsay, Internode, Transcript of Evidence, Sydney, 24 October 2011, p. 50.

119 NBN Co, 'NBN Co makes it cheaper for service providers to start up on the NBN', *Media Release*, 9 August 2011.

120 NBN Co, 'NBN Co makes it cheaper for service providers to start up on the NBN', *Media Release*, 9 August 2011.

121 Australia On-Line, *Submission 1.1*, p. 1.

> still cost Australia On Line **14 fold more** to connect nationally via the NBN than is currently the case via the ADSL network. The cost to connect to the NBN with NBN rebates would be $647,350 per month for National connection which is still **14 fold more** than our current cost of $45 773 per month for national connection to the ADSL network.[122]

3.118 Both Internode and Australia On Line stated that the higher cost of providing a broadband service in regional and remote areas means less choice and so less overall competition for this service in these areas.[123]

Loss of Infrastructure

3.119 Internode also raised the issue of the sunk cost it has incurred resulting from lost infrastructure through NBN overbuild. This situation will be similar for most RSPs who have invested in infrastructure to enable them to provide a service. As previously outlined, Telstra and Optus will be compensated for their loss of infrastructure in the NBN overbuild through the Telstra and Optus Agreements.[124]

3.120 Internode outlined its total investment in infrastructure and was concerned that in addition to not receiving compensation for its lost infrastructure, would have to pay to remove its existing infrastructure from Telstra exchange buildings. Internode stated:

> Our investment in DSLAMs per exchange runs between $100,000 and $200,000 per exchange site—some even more. We have 200 sites. We have invested a lot in this infrastructure ... [and once the NBN comes through] ... Then it is obsolete. There is some concern that we may actually have to pay Telstra fees in order to remove it from the exchange building.[125]

Basic Package Pricing

3.121 The NBN Co's pricing of the NBN for RSPs consists of: Access Virtual Circuit (AVC) and Connectivity Virtual Circuit (CVC). The basic price offered by the NBN Co for an RSP to access services from the NBN is $24 per month across all three technologies (fibre, wireless or satellite) at a

122 Australia On-Line, *Submission 1.1*, pp 2-3.

123 Mr Lindsay, Internode, Transcript of Evidence, Sydney, 24 October 2011, p. 50; Australia On-Line, *Submission 1.1*, p. 2.

124 Mr Lindsay, Internode, Transcript of Evidence, Sydney, 24 October 2011, p. 52.

125 Mr Lindsay, Internode, Transcript of Evidence, Sydney, 24 October 2011, p. 52.

downstream speed of 12 Mbps. On top of this is a CVC charge of $20 per Mbps which adds approximately $1 per 'average end user for a 12/1 Mbps service with current average data usage.' The NBN Co is expected to lower its pricing as it expects that 'increased usage ... will be adjusted on a yearly basis to reflect take up rates, average speed increases and usage increases.[126]

3.122 The RSP would then charge a price in addition to the $24 (plus the CVC charge) to take account of any over heads, charges and taxes, with the inclusion of a profit margin.

3.123 Table 3.1 shows the NBN Co's pricing of access to the NBN for RSPs.

Table3.1 Traffic Class 4 Access Virtual Circuit Peak Information Rate Charges per month excluding GST

Downstream/ (PIR Mbps)	Upstream / (PIR Mpbs)	Fibre	Wireless	Satellite
12	1	$24*	$24	$24
25	5	$27	$27	$27
25	10	$30	$30	$30
50	20	$34	$34	$34
100	40	$38	$38	$38
250	100	$70	$70	$70
500	200	$100	$100	$100
1000	400	$150	$150	$150

*Note: AVC Pricing for Fibre at $24 per month from Financial Year 2012 to Financial Year 2019, steadily decreasing to $23 per month by Financial Year 2040.

Source NBN Co Corporate Plan 2011-2013, p. 101.

3.124 Five RSPs have released their pricing under the NBN. Two of the larger RSPs, Telstra and Vodafone have not yet released any prices for NBN products.

3.125 Internode was of the view that NBN Co's usage fees for RSPs is too high, with the overall pricing geared toward providing a quick return to the Government's investment in the NBN.

126 NBN Co, *Corporate Plan 2011-2013*, pp. 101-103.

3.126 Prior to the release of the NBN Co's rebate on capacity charges, (which Internode stated has resolved the issue it raised about barriers to entry for small RSPs), Internode was concerned that it would not be able to afford access for high speed end users and that the CVC charge of $20 per Mpbs is arbitrarily set. In regard to the CVC price Internode stated:

> ... the charge for the CVC at $20 a megabit is a fairly arbitrary number. It is not really in line with the experience of network operators to date where you achieve an economy of scale as the volume of traffic increases. NBN Co. are proposing to charge all access seekers, regardless of scale, this $20 a megabit fee. That does not recognise that, over a fairly short time frame, end users are likely to use the network more and as a result require more capacity and that is actually going to end up driving costs up for retailers. But for operators like Internode—we have 200 exchanges with our own DSLAM equipment, which is the equipment that is the other end of the ADSL service—and operators like Optus, who are in the same boat, largely our backhaul networks, particularly around the capital cities, are fixed cost. As the traffic on those networks rises, our costs remained largely static, so in fact our cost per megabit to use those networks falls because the traffic rises and the cost stays the same.[127]

3.127 Internode is offering NBN access packages ranging from $49.95 per month for its basic 12 Mbps service to $165 per month for a terabyte. Internode explained its pricing strategy and stated:

> Our entry level service at 12 megabits with 30 gigabytes of included data costs $30 for the phone service plus $20 for the internet service. So it is a $49.95 entry level service, which we think is a fairly reasonable and affordable price point for most people. Our entry level 100 megabit service, which also includes a phone line, is effectively $30 plus $45—again, for a 35 gigabyte usage allowance. To put that in perspective, the average Internode customer uses 18 gigabytes a month. So that entry level service is more than sufficient for the average customer. It is worth noting that there are outliers to that 18 gigabytes. There are some people who download an awful lot and we provide services that allow them to do that. In case somebody wants to ask the question: we do offer a true terabyte service for $165 a month. We find that

127 Mr Lindsay, Internode, Transcript of Evidence, Sydney, 24 October 2011, p. 49.

> most people wanting that are actually business customers. A terabyte is a huge amount of data.[128]

3.128 Initially, Internode had released a higher priced package, which it lowered once the NBN Co provided a rebate on capacity charges for the first 150 Mbps per month on the CVC.[129]

3.129 Optus stated that it had waited to announce its pricing packages under the NBN as it had been working on its WBA with the NBN Co which would have an impact on Optus pricing. Optus stated:

> We are working through the implications of a couple of things, the main one being the wholesale broadband agreement with NBN Co. There are a number of terms and conditions in that contract which have direct implications for our pricing policy. We are very keen to release our pricing, as you can imagine, but we also know that we have to work out on what basis the contract with NBN Co. will be finalised. We have talked about some of those issues in the broad. Issues around liability in particular are ones that we have to factor into our cost pricing and therefore our pricing for customers.[130]

3.130 On 9 November 2011 Optus announced seven pricing packages which would commence in NBN trial sites from 21 November 2011. Packages start at $39.99 per month for 40 Gigabytes (GB) of data when bundled with an Optus post paid mobile service and rise to $129 per month for up to 1000 GB of data.[131]

3.131 Vodafone stated that it had not announced its pricing packages under the NBN, as it was in trial mode and 'focused on the operational and technical aspects of the NBN'.[132]

3.132 The ACCC stated that the cost of usage fees and the impact on small RSPs, especially the provision of NBN services in regional remote areas would be within the ACCC purview in its consideration of the SAU.[133]

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128 Mr Lindsay, Internode, Transcript of Evidence, Sydney, 24 October 2011, p. 48.

129 Mr Lindsay, Internode, Transcript of Evidence, Sydney, 24 October 2011, p. 51.

130 Mr Krishnapillai, Optus, Transcript of Evidence, Sydney, 24 October 2011, p. 37.

131 Optus, 'New Era of Competition as Optus announces reveals NBN pricing', *Media Release*, 9 November 2011.

132 Mr Lobb, Optus, Transcript of Evidence, Sydney, 24 October 2011, p. 60.

133 Mr Cosgrave, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 4.

Voice Only Services

3.133 Historically, the telecommunications industry has been dominated by the Public Switched Telephone Network (PSTN). The rollout of the NBN will decrease the use of the PSTN with more telecommunications being delivered via high quality Voice over Internet Protocol (VoIP) services. The NBN Corporate Plan indicates that this transfer from old technologies to newer services will equate to a decline in voice revenues but will be substituted by increasing broadband revenue noting, 'business models continue to shift from toll calling charges to access charges'.[134]

3.134 The Corporate Plan also indicates:

> The significant investment by Internet Service Providers in Digital Service Line Access Multiplexers and other equipment in order to provide broadband services over copper is expected to be redirected to content, service differentiation and value added services over the NBN, fuelling the development of new applications and innovation that will drive consumer demand.[135]

3.135 There are concerns that, under NBN Co's wholesale packages combining voice and data services, RSPs will only provide voice services through a combined package. NBN Co stated:

> ...that anyone in Australia who currently accesses a fixed voice-line service will continue to be able to do so. Customers in areas that we serve with the NBN fibre network will continue to have access to voice-only services over a Telstra copper line, up until the NBN fibre service is rolled out in their area. After the NBN fibre is rolled out, the agreement with Telstra means that customers will be able to access a voice-only service over this new infrastructure. ... Customers in [the wireless and satellite footprints] will continue to have access to fixed voice line services over a Telstra copper line. This is the arrangement where in that last notionally 10 per cent the copper service will remain.[136]

3.136 After the NBN rollout, the prices at which Telstra can offer these services will remain subject to specific retail price controls. Telstra's carrier licence conditions require it to offer low-income packages for access to a fixed line telephone service. Similarly, the Low Income Measure Assessment Committee will continue to work with Telstra to ensure low-income

134 NBN Co, *Corporate Plan 2011-2013*, p. 30.

135 NBN Co, *Corporate Plan 2011-2013*, p. 30.

136 Mr Quigley, NBN Co, Transcript of Evidence, Canberra, 13 October 2011, p. 2.

products are offered. Further, NBN Co's commercial agreement with Telstra provides that customers accessing special services will continue to have those services provided at no increased cost on the fibre network. The NBN Co commented:

> When it comes to providers other than Telstra, I understand there is no obligation upon them to provide discounted services to people on low incomes. This obligation remains solely with Telstra.[137]

3.137 Since the committee's First Report, iPrimus has released a voice-only service priced at $24.95 per month, using the fibre network infrastructure. The NBN Co commented on such services, arguing that:

> ... while there may not be RSPs other than Telstra offering services to those who qualify for low-income assistance, there will still be voice-only options at reasonable rates.[138]

3.138 The Australian Communications Consumer Action Network (ACCAN) was concerned that there were not more than one voice service provider announcing pricing. The ACCAN stated:

> It does concern me, but I do get some hope that Primus announcement is the first of more. To be perfectly frank, in that regard it is keeping prices to an amount, which we are pleased about. Of course we will be tracking it very carefully over time to see whether or not they stay at that level. We have assurances from NBN Co. that over time prices will come down. We will have to see if that happens.[139]

3.139 The ACCC stated that it would monitor the provision of voice only services offered as this service is important to 'a substantial proportion of the Australian public.' The ACCC stated:

> I know this has been the subject of some discussion between [committee members] and NBN Co. I have seen [NBN Co] point [the committee] to some initial offers from retail service providers that include the provision of voice only services at rates broadly equivalent with what are currently offered in the market by such products as Telstra's HomeLine Budget. It is an issue we will certainly keep under examination, because I would accept that the

137 Mr Quigley, NBN Co, Transcript of Evidence, Canberra, 13 October 2011, p. 2.

138 Mr Quigley, NBN Co, Transcript of Evidence, Canberra, 13 October 2011, p. 2.

139 Ms Teresa Corbin, CEO, Australian Communications Consumer Action Network (ACCAN), Transcript of Evidence, Sydney, 25 October 2011, p. 19.

> provision of voice only services is important to a substantial proportion of the Australian public.[140]

Other Issues

Universal Service Obligations

3.140 The objective of the Universal Service Obligation (USO) is to ensure basic voice telephony and payphone services are reasonably and equitably accessible to all Australians. As a universal service provider (USP), Telstra is required to ensure that its services meet this obligation.[141]

3.141 The Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Bill (TLA Bill) was presented on 20 October 2011 to amend the regulation of Telstra following reform of the telecommunications industry and the establishment of the NBN Co. The TLA Bill received royal assent on 10 December 2010.[142]

3.142 The Explanatory Memorandum to the TLA Bill stated there are difficulties with USO requirements. It stated that:

> ..current requirements imposed on the primary universal service provider (currently Telstra) are imprecise and difficult to enforce.[143]

3.143 Seeking to overcome these difficulties, the *Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Act 2010* (Cth) (TLA Act) provides for the Minister to determine the minimum performance benchmarks which USPs must meet to fulfil their responsibilities. Further, it specifies maximum periods of time for new connections, fault rectification and reliability standards.[144]

3.144 Under the TLA Act, the Minister has the power to issue written determinations providing rulings and performance standards for the provision, maintenance and location of payphones. There must be public

140 Mr Cosgrave, ACCC, Transcript of Evidence, Sydney, 25 October 2011, p. 10.

141 *Telecommunications (Consumer Protection and Service Standards) Act 1999* (Cth).

142 House of Representatives, *Votes and Proceedings No. 21*, Wednesday, 9 February 2011, p. 285.

143 Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Bill, (EM) p. 2.

144 Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Bill, EM, p. 2.

consultation and notification of proposals to remove payphones. Those who may be adversely affected by such a proposal may request the Australian Communications and Media Authority (ACMA) to direct the USP not to remove that service. Matters which ACMA must consider when making such a direction are also specified in the TLA Act.

3.145 Under its licence conditions and the USO, Telstra is required to provide discounted phone-line rental services. The ACCAN stated that the current price for this service is $20.95 per month but is soon to be increased to $22.95 per month.[145] Telstra also offers other services including pensioner discounts, a bill assistance program, and sponsored access providing telephony services for people who seek shelter within emergency accommodation. Generally supportive of these services, Ms Teresa Corbin, Chief Executive Officer of ACCAN stated:

> We have been on the record for some time as saying that, whilst we really welcome these measures and they are very valued, particularly by people who provide emergency assistance for people in financial hardship, we would like these services to be expanded to be broader than just Telstra. At the moment a low-income consumer does not have a choice. They have to go to Telstra if they want to access these benefits.[146]

Telecommunications Universal Service Management Authority

3.146 On 23 June 2011, the Government and Telstra agreed on a package of measures that 'will ensure basic universal telecommunications service standards during and after the NBN rollout'.[147]

3.147 As part of this package of measures, the TUSMA will be established to assume responsibilities for administering the USO and other public interest services. From 1 July 2012, the TUSMA will ensure:

- 'all Australians have reasonable access to a standard telephone service;
- payphones are reasonably accessible to all Australians;
- the ongoing delivery of the Emergency Call Service by Telstra;
- the ongoing delivery of the National Relay Service;

145 Ms Corbin, ACCAN, Transcript of Evidence, Sydney, 25 October 2011, p. 18.

146 Ms Corbin, ACCAN, Transcript of Evidence, Sydney, 25 October 2011, p. 18.

147 The Hon Julia Gillard MP, Senator the Hon Stephen Conroy, Senator the Hon Penny Wong, 'Government and Telstra agree on package of consumer measures' *Joint Media Release*, 23 June 2011.

- that appropriate safety net arrangements are in place that will assist the migration of voice-only customers to an NBN fibre service as Telstra's copper customer access network is decommissioned; and
- technological solutions will be developed as necessary to support continuity of public interest services (i.e. public alarm systems and traffic lights)'.[148]

3.148 The Telecommunications Universal Service Management Agency Bill 2011 (TUSMA Bill) was introduced into the House of Representatives on 2 November 2011.[149] The TUSMA Bill is part of a package of legislation: the Telecommunications Legislation Amendment (Universal Service Reform) Bill 2011 (Universal Service Reform Bill) and the Telecommunications (Industry Levy Bill) 2011.

3.149 The TUMSA Bill's Explanatory Memorandum provides that the structural separation of Telstra and the changes to the telecommunications industry will also require the service delivery arrangements for the USO to transition to a model where the Government will contract with service providers for the supply of these important services.[150]

3.150 The TUSMA Bill:

- provides for the establishment of TUSMA as the statutory agency that will have the responsibility for the effective implementation and administration of service agreements or grants that deliver universal service and other public policy telecommunications outcomes;
- sets out TUSMA's corporate governance structure and reporting and accountability requirements;
- provides for the Minister, subject to the scrutiny of Parliament, to set the standards, rules and minimum benchmarks for TUSMA's contracts and grants; and
- sets out arrangements for consolidating the two current USO and National Relay Service industry levy regimes into a single regime to contribute funding towards TUSMA's costs.[151]

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148 ACMA, 'Major changes to Australian telecommunications announced', *Media Release*, 23 June 2011.

149 House of Representatives, *Votes and Proceedings No 77*, 2 November 2011, p. 1034.

150 The Telecommunications Universal Service Management Agency Bill 2011 (TUSMA Bill), EM, p. 4.

151 TUSMA Bill, EM, p. 2.

3.151 Under the Universal Service Reform Bill, the Minister may permit USO regulatory obligations to be progressively lifted from Telstra subject to a number of preconditions being met in relation to Telstra's contractual and regulatory compliance and performance.[152] Legislative responsibility will be placed on TUSMA to ensure the service agreements or grants that it has in place effectively deliver public interest policy objectives.

3.152 At the Senate Environment and Communications Legislation Committee hearing on the TUSMA Bill, the Minister for Broadband, Communications and the Digital Economy stated:

> TUSMA will also have a role in implementing safety net arrangements for migration of voice-only customers from Telstra's copper network to the NBN in fibre areas.[153]

3.153 The DBCDE stated that under the new USO regime, the USO standards that are currently in place will be maintained and any impact of these standards will be through TUSMA, jointly funded by industry and the Government.[154]

3.154 The Minister for Broadband, Communications and the Digital Economy provided information on the projected costs of TUSMA's operation:

> ... for the first time Government will also be making a substantial contribution towards TUSMA's costs and delivery of key telecommunications public interest safeguards to provide a smooth transition to industry. The budget contribution will be at least $50 million in 2012-13 and 2013-14 and then $100 million each financial year thereafter.[155]

3.155 The DBCDE also commented that less would be spent on delivering the USO over time as there are structures and incentives in place for continued improvement. The DBCDE stated:

> You may well pay less, because there are specific provisions there to encourage change. There will be a technology review at 10 years but there is also a proposition that the parties will continue at any point in time [to discuss] how to more efficiently deliver a USO at an earlier point than 10 years, which cannot be unreasonably

152 TUSMA Bill, EM, p. 2.

153 Senator the Hon Stephen Conroy, Minister for Broadband, Communications and the Digital Economy, Transcript of Evidence, Senate Environment and Communications Legislation Committee, Canberra, 18 October 2011, p. 60.

154 Mr Harris, DBCDE, Transcript of Evidence, Sydney, 24 October 2011, p. 17.

155 Senator Conroy, Transcript of Evidence, Senate Environment and Communications Legislation Committee, Canberra, 18 October 2011, p. 60.

> rejected. We have structures and incentives in place ... to encourage this.[156]

3.156 The cost of continuing USO delivery under new USO arrangements is $290 million.[157]

3.157 The Senate Environment and Communications Legislation Committee is currently inquiring into the legislative package.

Pricing, Affordability and USOs

3.158 The ACCAN was concerned that under the newly emerging telecommunications environment, affordability of basic services would decrease, thereby increasing the digital divide. The ACCAN stated:

> Currently our assessment is that the entry level offers over the NBN are comparable to what is available in the market today and download speeds will be improved. ... The problem is that we do not want to increase the digital divide for people on low incomes. People who have a problem affording the internet now, probably will continue to do so. [158]

3.159 To address the potential for any increase in the 'digital divide', the ACCAN proposed a broadband low-income measures scheme, that is:

> ... somewhat akin to the low-income measures for phone services that exist now and which Telstra is required to provide. We are thankful that the government and NBN Co have assured us that the low-income measures for phone services will continue at the same price.[159]

Private Sector Equity Engagement

Background

3.160 In Chapter 2 of the First Report, the committee addressed funding of the NBN.[160] The First Report stated that the Government:

156 Mr Harris, DBCDE, Transcript of Evidence, Sydney, 24 October 2011, p. 17.

157 Mr Harris, DBCDE, Transcript of Evidence, Sydney, 24 October 2011, p. 16.

158 Ms Corbin, ACCAN, Transcript of Evidence, Sydney, 25 October 2011, p. 18.

159 Ms Corbin, ACCAN, Transcript of Evidence, Sydney, 25 October 2011, p. 15.

160 See Joint Committee on the National Broadband Network, First Report, August 2011, *Review of the Rollout of the National Broadband Network* (JCNBN), pp 34-36.

- intended the NBN be jointly funded through public and private sector investment,[161] and
- expected to divest itself of its interest in NBN Co within five years of the completion and operation of the NBN.[162]

3.161 On 20 December 2010, the Government estimated the total capital expenditure for the NBN at $35.9 billion, with the Government expected to contribute $27.5 billion in rollout equity.[163] The peak funding requirement for the project is estimated to be $40.9 billion. The Government stated that it would fund its investment in the NBN through the Building Australia Fund, and the issue of Aussie Infrastructure Bonds to the public.[164]

3.162 On 22 June 2011, the Government and NBN Co entered into an equity funding agreement, whereby the Government provides assurances to NBN Co that it will provide equity funding to NBN Co until 30 June 2021, unless the agreement is terminated earlier. The Government is expected to provide funding sufficient to meet the forecast of expenditure outlined in the NBN Co Corporate Plan. The total funding pursuant to the agreement is capped at $27.5 billion, excluding any amounts payable in the event of termination. As at 23 September 2011, a total of $1.362 billion in equity has been made available to NBN Co.[165]

3.163 The committee undertook to examine whether, given Part 3, Divisions 2 and 3, of the *National Broadband Network Companies Act 2011* (Cth) (the Companies Act), there are provisions for the Government to attract private equity during the construction phase of the NBN, thereby enabling an earlier return to taxpayers.[166]

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161 Hon Kevin Rudd MP, Prime Minister, Hon Wayne Swan MP, Deputy Prime Minister and Treasurer, Hon Lindsay Tanner MP, Minister for Finance and Senator the Hon Stephen Conroy, Minister for Broadband, Communications and the Digital Economy, 'New National Broadband Network', *Joint Media Release*, 7 April 2009.

162 Hon Kevin Rudd MP, Prime Minister, Hon Wayne Swan MP, Deputy Prime Minister and Treasurer, Hon Lindsay Tanner MP, Minister for Finance and Senator the Hon Stephen Conroy, Minister for Broadband, Communications and the Digital Economy, 'New National Broadband Network', *Joint Media Release*, 7 April 2009.

163 Hon Julia Gillard MP, Prime Minister, Hon Wayne Swan MP, Deputy Prime Minister and Treasurer, Senator the Hon Penny Wong, Minister for Finance and Deregulation and Senator the Hon Stephen Conroy, Minister for Broadband, Communications and the Digital Economy, 'Government Releases NBN Co Corporate Plan', *Joint Media Release*, 20 December 2010.

164 NBN Co, *Corporate Plan, 2011-2013*, p. 133.

165 Shareholder Ministers, *Submission 19*, p. 2

166 JCNBN, p. 55.

Legislative Provisions

3.164 As prescribed in Division 2 of Part 3 of the Companies Act, privatisation of NBN Co is expected to occur after:

- The Minister for Broadband, Communications and the Digital Economy declares that the NBN is built and fully operational.
- The Productivity Commission (PC) has concluded an inquiry into the NBN.
- The PC's report has been referred to and reported on by a Parliamentary Joint Committee on the ownership of NBN Co.
- The declaration by the Minister for Finance and Deregulation, that conditions are suitable to sell NBN Co, has not been disallowed by either House of the Parliament,[167]

3.165 If these conditions have been met, the Finance Minister may then declare that conditions are suitable 'for the entering into and carrying out' of a scheme for selling NBN Co.[168]

Timeframe

3.166 In relation to the equity agreement between the Government and NBN Co, the Government stated that its investment provides market certainty and certainty for NBN Co to 'enter into the long term commercial contracts needed to deliver the Government's NBN policy objectives.'[169]

3.167 The committee sought information on whether it would be in the national interest to bring forward the timeframe for private equity engagement. The DBCDE advised that the Implementation Study undertaken by McKinsey & Company/KPMG noted that private equity should not be introduced before privatisation, as it would be too expensive and constrain the Government's ability to get its policy and regulatory settings right before allowing private ownership. It would also lead to a substantial distraction for management, both for initial transactions and in an ongoing basis. This applies to both cash and any proposals to sell assets in return for equity.[170]

3.168 The NBN Co Corporate Plan contemplates private equity in the context of debt funding with 2015-16 the first opportunity for this to occur. The

167 *National Broadband Network Companies Act 2011* (Cth) s 47.

168 *National Broadband Network Companies Act 2011* (Cth) ss 50(2), 51(2) and 53.

169 Australian Government, *Statement of Expectations*, 20 December 2010 (SOE), p. 12.

170 DBCDE, *Submission 3.3*, p. 2.

Companies Act provides for the sale 'within five years' of the Government's interest in the NBN once it is fully built and operational, subject to the conditions for such a sale.[171]

Cost/Benefit and Capital Structure

3.169 The committee asked what would be the cost/benefit to the economy of bringing forward the introduction of private equity. The DBCDE advised that the McKinsey & Company/KPMG Implementation Study concluded that use of private equity to fund the NBN would be more expensive than use of government equity.

3.170 Under the Companies Act, the Commonwealth must retain total ownership of the NBN Co, until certain provisions of the Act are satisfied.[172]

3.171 The reasoning underpinning this finding was that Government was better able to manage public sector risk, than a mix of both public and private sector risk.[173]

3.172 The committee also asked what determining the 'optimum capital structure' for NBN Co would entail, and how this process could be undertaken. The DBCDE advised that, in accordance with the Governance Arrangements for Commonwealth Government Business Enterprises (GBE) of June 1997, in relation to financial governance, each GBE should have a target optimal capital structure. This is the combination of financial liabilities and equity used to fund the assets of the GBE, agreed annually between the directors and Shareholder Ministers in the corporate plan consultation process.[174]

Equity Agreement

3.173 The committee asked about the equity agreement between the Government and NBN Co, the review process and any variations to equity requirements since the formation of NBN Co.

3.174 The DBCDE stated that funding for NBN Co will be reviewed annually, as part of the corporate planning process. As a result of a review, the Government may either terminate the equity funding agreement, or vary

171 Ms Stacie Hall, First Assistant Secretary, Government Business, Special Claims and Land Policy, Department of Finance and Deregulation, Transcript of Evidence, Sydney, 24 October 2011, p. 20.

172 National Broadband Network Companies Bill 2010, EM, p. 6.

173 DBCDE, *Submission 3.3*, p. 2.

174 DBCDE, *Submission 3.3*, p. 3.

the annual or total equity funding commitment to NBN Co, in accordance with the most recently endorsed corporate plan.[175]

3.175 The DBCDE also advised that NBN Co's Corporate Plan, sets the basis of its equity requirements. The NBN Co Corporate Plan provides that total expenditure for the NBN is estimated to be $35.9 billion. This is less than the Government's original $43 billion estimate, partly due to the Telstra Agreement. The 2013-2015 Corporate Plan will be the basis for NBN Co's equity requirements.[176]

Commercial-in-Confidence Material

3.176 In its First Report, the committee noted that NBN Co had not provided information, or had not answered questions, on commercial-in-confidence grounds.[177] Such gaps in available material had limited the scope of the committee's inquiry. Similar experiences have also affected the gathering of evidence for this report.

3.177 On several occasions, the question of access to, or disclosure of, commercial-in-confidence material by parties involved in the rollout of the NBN was discussed at public hearings.

3.178 The DBCDE commented on the nature of commercial-in-confidence material, and the interests involved:

> ... commercial-in-confidence is not just a matter for the Government or even for NBN Co as a government-owned instrumentality to say that it will or will not give the committee access in those circumstances. We would have to bring Telstra into this as well. That said, everything we have done to date has been designed to maximise the transparency of documents. ... We have attempted to make these things as transparent as we can. I see no reason why that attitude will not continue, but we would have to consult with Telstra to be sure that they too were satisfied.[178]

175 DBCDE, *Submission 3.3*, p. 4.

176 DBCDE, *Submission 3.3*, p. 4.

177 JCNBN, p. 21.

178 Mr Harris, DBCDE, Transcript of Evidence, Sydney, 24 October 2011, p. 12.

3.179 The DBCDE undertook to examine the relevance of the public interest test in assessing what material should be considered commercial-in-confidence.[179]

Concluding Comments

Telstra's Structural Separation Undertaking

3.180 The committee notes the information it has received regarding the Telstra and Optus Agreements including Telstra's SSU and draft migration plan, and review of these documents by the ACCC.

3.181 The committee is concerned about a number of the issues raised by industry groups in relation to the equivalency and transparency considerations arising from the Telstra SSU. The committee understands this issue has been raised as a point of concern with the ACCC during the course of its review of the SSU, and prior to the release of its SSU discussion paper.

3.182 In addition, the committee understands that ACCC approval of the Telstra SSU is a condition precedent for the completion of the Telstra Agreement, and ACCC approval must be given by 20 December 2011. The committee understands parties are continuing to discuss issues as they arise. Further, the committee understands that the ACCC has dedicated considerable resources to its review of the Telstra Agreement and, while it has not guaranteed to hand down its decision within a specified timeframe, the ACCC has stated that it is working to conclude its consideration as quickly as possible.

Non Disparagement Clause in the Telstra and Optus Agreements

3.183 The committee understands the non disparagement clause included in the Telstra and Optus Agreements prevents Telstra and Optus from marketing its wireless product against the NBN for periods of 20 and 15 years respectively.

3.184 The committee understands the effect of the non disparagement clause would be similar to the immunity which is afforded under trade practices legislation.

179 Mr Harris, DBCDE, Transcript of Evidence, Sydney, 24 October 2011, pp 11-12.

3.185 The non disparagement clause appears to try to inhibit Telstra and Optus from competing against the NBN. Optus has, however, stated that this clause will not prevent it from aggressively advertising its wireless services.

3.186 The NBN Co stated that the intent of the non disparagement clause is to protect shareholder and taxpayer investment by avoiding any delay which may be experienced from litigation for possible breach of trade practices law in the event the proposed clause was not included in either of the Agreements.

3.187 The committee understands the ACCC is reviewing the terms of both the Telstra and Optus Agreements and awaits the ACCC findings on this matter.

Special Access Undertaking

3.188 The NBN Co's SAU (while a voluntary undertaking by NBN Co) is an important document which will include the key price and product elements of NBN access, as well as including non price terms and conditions.

3.189 The SAU is also the framework which will set out the pricing and non pricing parameters which will impact on the WBA. It is important that the SAU be lodged with the ACCC for its consideration before any WBAs are entered into between the NBN Co and RSPs.

Wholesale Broadband Agreement

3.190 The WBA sets out arrangements relating to NBN commercial service delivery by RSPs. Lodgement of the SAU is important to the WBA as the SAU sets the framework that will enable RSPs to enter into WBAs with the NBN Co with certainty.

3.191 Concerns have been raised about RSPs signing interim agreements for a five year term because, while, as there is no SAU in place, these RSPs have no recourse to the ACCC if they encounter difficulties as result of the conditions they have signed up to in interim agreements.

3.192 In response to industry concerns surrounding regulatory uncertainty in the absence of a SAU, the NBN Co has announced that its interim agreements will have a 12 month term.

3.193 The NBN Co has indicated its intention to lodge its SAU with the ACCC for consideration in November 2011.The committee is of the view that the NBN Co should finalise its SAU and lodge it with the ACCC for assessment without further delay.

Competition and pricing for Small Retail Service Providers

3.194 The committee again received evidence about the ACCC decision to increase the POIs from 14 to 121. The committee noted the evidence it received on the impact of this decision on small RSPs to provide services in regional and remote areas, where there tends to be either limited or absent backhaul competition.

3.195 The committee also understands that in early August 2011, the NBN Co announced it will provide a rebate on capacity charges to alleviate the kind of barrier to entry concerns that were raised by small RSPs.

Basic Package Pricing

3.196 The committee notes that only a hand full of RSPs have released NBN pricing packages, with the cheapest of these packages starting at around $35 per month delivering 12 Mbps of data.

3.197 The committee acknowledges that, while this price is comparable to the current cost of packages, the price may still be too high for low income households to gain access to the NBN. The committee also understands from the NBN Co Corporate Plan, that in time as take up of NBN services increases, the cost of these services is likely to decrease.

3.198 The committee is unaware of how the NBN Co arrived at its Connectivity Virtual Circuit (CVC) charge, and suggests the calculation of the CVC charge be explained and communicated to industry stakeholders by the NBN Co.

Voice Only Service

3.199 Under existing Universal Service Obligation (USO) arrangements, universal service providers are legally obliged to provide access to telephony services. Although they will continue to do so under the reformed USO arrangements, concerns were raised that voice only pricing plans under the NBN were not being offered more broadly by RSPs. Similarly, there are concerns that RSPs are choosing to bundle services and offer pricing on packaged services rather than a stand-alone voice only service. If consumers are only able to access bundled packages, parts of the Australian community may be disadvantaged should they wish to access voice services only.

3.200 The committee understands the ACCC will monitor voice only services as it is an important issue which impacts on a potentially large number of consumers.

Commercial-in-Confidence Material

3.201 The committee aims to avoid situations where it might form a view that relevant material was being withheld because it might be commercial-in-confidence. It believes that resolution of what items can be considered validly as commercial-in-confidence would assist in the examination of the rollout of the NBN. The committee noted the DBCDE's undertaking to examine the public interest test to assess whether material is commercial-in-confidence. The committee is yet to receive the DBCDE's advice on this question.