



# **Submission on the Vertigan Review Regulatory Issues Framing paper**

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# 1 INTRODUCTION

The Nextgen Group (Nextgen) welcomes the opportunity to make this submission on the Vertigan Review's 'Regulatory Issues Framing Paper' to the Expert Panel.

We appreciate that the structural and regulatory matters canvassed in the Framing paper are of utmost importance to the future of Australia's telecommunications sector, and the panel — in considering these matters — has a task which is both large and potentially wide ranging.

We also appreciate that in developing the Framing Paper, and questions therein, the Panel was responding to the terms of reference provided to it by the Minister for Communications.

We note that the current Review is taking place following many years of debate and discussion about, opportunities for the reform of Australia's telecommunications sector and potential pathways towards new, sustainable industry structures which would encourage competition, innovation and investment.

We also note that the current Review is taking place following the decision of the former Government to develop a National Broadband Network (NBN), and assign responsibility for this to a new publicly owned entity, NBN Co.

As the NBN was intended to be the main vehicle for transformation of the sector, and NBN Co the main vehicle for the realisation of long pursued structural separation, both the NBN and NBN Co are necessarily under close consideration as part of the current review process. While there have been some well documented issues with implementation of the NBN since its announcement in April 2009, Nextgen remains broadly supportive of the initiative given its capacity to modernise the domestic sector and support increased and ongoing participation in the emergent global, digital economy. As such, within the attached submission Nextgen affirms that is reasonably comfortable with the structural model which has been pursued in recent years, with most our concerns relating to two issues which are regulatory in nature, but have potential structural implications. These issues are:

- 1) The possibility of competing FTTB infrastructure being permitted; and
- 2) The remit assigned to NBN Co, and in particular constraints on the activities which NBN Co is allowed to undertake.

In brief we see issue (1) above as a potential threat to a range of objectives associated with the current structural model for the sector, including structural separation, NBN Co's commerciality, competitive market outcomes and the long term interests of end users. In order to protect the integrity and robustness of the current structural model, Nextgen is of the view that the development of competing FTTB infrastructure should not be permitted at the current point in time. To a certain extent issue (2) above is the corollary of issue (1) — while there is merit in protecting NBN Co's remit to be the monopoly provider of local network access services, this remit needs to be accepted for the benefit of the sector more broadly. That is, NBN Co should be subject to specific and firm constraints about the activities which it can undertake and this includes limitations on the ability to enter into market segments which are already competitive.

It is our view that appropriate resolution of the issues above along with confirmation of the sector's overarching structural and regulatory settings will help provide industry participants with the certainty they need to continue with current investment plans and explore future commercial opportunities.

Nextgen looks forward to ongoing participation in the current Review process.

## 2 RESPONSE TO QUESTIONS

In this section we set out our responses to the questions raised in the Framing Paper.

1. What broader structural model or models for the industry should the panel consider? Why? Should the panel be considering significantly different industry scenarios to those outlined above? If so, what are those scenarios and why should they be considered?

Nextgen is supportive of the 'current' structural model which has been pursued by both industry and government in recent years — that is, a structural model characterised by:

- Structural separation, encompassing the establishment of NBN Co as a monopoly, wholesale only provider of local access network services and the corresponding, progressive shift out of local access, fixed-line network services by Telstra;
- 121 designated Points of Interconnection (POI), connecting dispersed local access networks to established backhaul transmission infrastructure; and
- Competition in market segments both upstream and downstream of the local access network.

Nextgen is supportive of this model because:

- It entails a marked shift away from the model which had previously applied (i.e. a vertically integrated incumbent, which controlled the primary access network and held a dominant market share in both upstream and downstream markets), and long been detrimental to both competitive dynamics and consumer interests;
- NBN Co has been given a clear remit to be both open access and non-discriminatory, meaning there is increased scope (relative to previous arrangements) for healthy competitive dynamics in the telecommunications sector, especially in downstream, retail markets which will in turn deliver benefits to end users;
- NBN Co's monopoly status — and direction to be national in nature — is amenable to the social equity objectives which have long characterised the local telecommunication sector, given Australia's unique geographical attributes;
- It recognises the substantial commercial investments which have already been made in fibre assets and other telecommunication facilities, and offers the ability to harness these in the pursuit of consumer interests;
- It establishes the foundation for moving beyond copper as the primary means for consumers to utilise telecommunication services, appropriately positioning Australia for increased participation in the growing Digital Economy and the realisation of associated social and economic benefits. While fixed line infrastructure is perhaps not as prominent in public discourse (or the eyes of consumers) as mobile infrastructure, it is — and will remain — the backbone of the telecommunications sector; and
- Industry has — in large — embraced the model and correspondingly adjusted business models and investment strategies, with implementation of these already in train. Any move away from the current structural model will entail additional costs for the industry, with the level of these costs likely to be positively correlated with the level of change.

Nextgen is aware that most discussion of alternative structural models, in recent times, has been focused on the possibility of allowing the development of competing FTTB infrastructure. This is not a model which is supported by Nextgen as holistically we do not believe it can offer the same benefits we associate with the current model, as outlined above. Furthermore, as outlined in our response to question 2 overleaf, we are of the view that there are multiple tradeoffs between any competing FTTB infrastructure and some of the other objectives associated with Australia's telecommunications sector, including structural separation, NBN CO's commerciality, realisation of a competitive market structure and promotion of the long term interest of end users (LTIE).

2. Should the panel consider and adopt working assumptions other than the ones outlined on page 5 above? How should the assumptions be prioritised and trade-offs assessed?

Nextgen is of the view that the working assumptions within the Framing Paper are — in large — an appropriate starting point for current purposes.

In Table 1 below we have ranked the working assumptions in terms of the priority which we attach to them. In order to support the consideration of these assumptions and a practical assessment of the trade-offs which exist between them we have also nominated what we interpret as being the essence of each assumption. While this approach carries the risk of possible misinterpretation, it has the benefit of making each assumption more amenable to ranking and the subsequent assessment of tradeoffs where they exist.

Table 1 Nextgen's initial ranking of the working assumptions, in order of priority

Rank	Working assumptions	Essence
1	➤ rollout of the NBN will achieve the structural separation of Telstra in respect of retail fixed network services supplied in the mass market	Structural separation
2	➤ NBN Co will operate on a commercial basis and is a key mechanism to ensuring that the government's broadband policy objectives are met	Commerciality
3	➤ in so far as a network owner has a substantial degree of market power, there should be safeguards against behaviour that provides advantages to its own upstream or downstream operations over those of competing providers that cannot reasonably compete without access to its network	Competition policy / Appropriate regulation
4	➤ any restrictions imposed by policy, statute or regulation on commercial investment in and supply of telecommunications services should be no greater than needed to promote the long-term interests of end-users and should be subject to periodic, transparent and independent review to ensure their benefits exceed their costs	Appropriate regulation / Infrastructure based competition / LTIE
5	➤ broadband services providing defined minimum upload and download data rates should be generally available to all end-users, along with such other broadband products as market participants (including NBN Co, in the case of wholesale products) choose to provide.	Universality / Service standards
6	➤ regardless of where they reside or carry on a business, end-users should have access to designated services at an affordable price, with any subsidies inherent in that supply being as transparent and efficiently delivered as reasonably possible	Transparent subsidies
7	➤ NBN Co will primarily operate at Layer 2 in the service stack to provide scope for downstream innovation and product differentiation	NBN remit
8	➤ there should be no restrictions on retail level competition, other than those needed to provide for end-to-end connectivity and to protect consumers (where such protection is reasonably necessary)	Appropriate regulation
9	➤ in respect of each of the areas noted above, regulation should be no more intrusive or burdensome than needed, and should be proportionate, transparent, predictable and accountable in its operation	Appropriate regulation

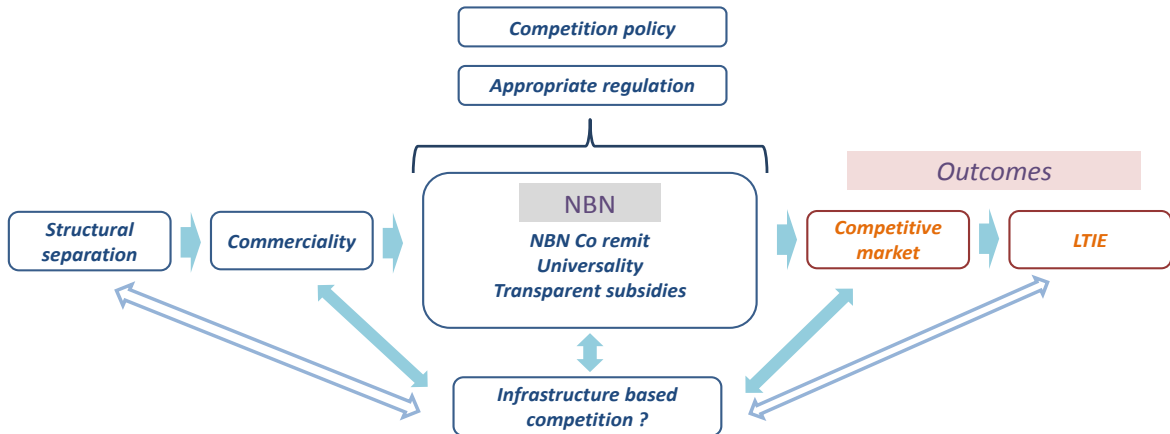
Before considering the rankings above and the rationale associated with these it is noted that there is particular breadth to the assumption we have ranked number (4) — while we support the sentiment of this assumption, this does not extend to support for the possibility of infrastructure based competition in the form of competing FTTB builds or similar, duplicative downstream investments.

In simple terms our ranking of each working assumption (as above) reflects our view that there is a clear *hierarchy* to the policy (as in regulatory and structural) considerations associated with the NBN.<sup>1</sup> In order to illustrate this hierarchy, and support the identification of consequential trade-offs, we have developed the conceptual schematic presented overleaf.

Consistent with our ranking of the working assumptions above, the schematic highlights that structural separation and commerciality are of primary importance because these considerations create the foundation — in broad terms — for the sector as a whole. Affirmation of these objectives should, in turn, inform the overarching policy and regulatory framework for the industry, within which NBN Co has a clearly specified (and constrained) remit to facilitate the provision of broadband services to end users, aided by transparent subsidies where required. By restricting NBN Co to their

<sup>1</sup> This hierarchy is most pronounced with respect to the assumptions we have ranked 1-4.

remit the industry, as a whole, will be better positioned for the realisation of a competitive market and improvements in the LTIE.



As shown above, we see infrastructure based competition — as in competing FTTB infrastructure — as a tangential matter (albeit a crucial one) which has the potential to create adverse impacts in a number of other areas. Noting that the discussion of this issue is largely hypothetical at the current point in time, potential impacts we associate with competing FTTB infrastructure include:

- Moves by multiple players to enter this space — noting Telstra’s public statements that they would expect to be active in the FTTB space if others were so permitted, such a development could compromise the realisation of structural separation;
- Impacts on the commerciality of NBN Co due to the potential leakage of a substantive number of premises from their ‘monopoly’ access layer footprint — if this leakage were to create funding gaps there may be moves to recover these from NBN Co’s end users, which would clearly be detrimental to them; and
- Impacts on the overall competitiveness of the market — noting that there are many unanswered questions about the appearance or form of any competing FTTB infrastructure in particular, there would appear to be potential for such a development to impact on competitive dynamics within the markets as a party other than NBN Co would own and control localised parts of the local access network. Key unanswered questions include:
  - Would the owners of the infrastructure in question be restricted to the provision of wholesale only services, or would they be able to make a retail offer?
  - Would open access provisions be attached to the infrastructure in question, and if so what would that mean for the owner(s) and the aspiration for uniform wholesale prices?
  - Would the end users in buildings services by competing FTTB infrastructure have any choice in terms of their service providers?

Collectively the points above are key reasons why Nextgen is not supportive of the proposition for there to be competing FTTB infrastructure based competition.

**Key tradeoffs between the working assumptions**

Based on our ranking of the working assumptions, key tradeoffs we have identified in the broad structural and regulatory space include:

**i. NBN Co commerciality and infrastructure based competition**

As outlined above, any moves to permit competing FTTB infrastructure could result in a number of potential adverse impacts. Of these, we believe the potential impact on the commerciality of NBN Co is the most important consideration. Thus, there is a tradeoff between NBN Co’s commerciality and infrastructure based competition. Because NBN Co — and by extension its commerciality — is essentially the vehicle for transforming the industry, this should not be compromised by competing investment.

It is our view that the main benefit of competing FTTB activity — namely earlier access to the NBN for those concerned — can be realised via efforts to accelerate the rollout of the NBN.

## ii. Competitive market outcomes and NBN Co's remit

Nextgen is of the view that NBN Co has — as it currently stands — an appropriate remit, namely to be a wholesale only provider of local access network services. This remit is instrumental to the realisation of competitive market outcomes, however, the realisation of competitive market outcomes is also dependent on the absence of any NBN related market distortions. This means that NBN Co should be constrained in its ability to broaden its remit and/or participate in other market segments. Put another way, there is a tradeoff between realising competitive market outcomes and the scope of activities NBN Co is permitted to undertake.

Despite the rollout of the NBN still being in its relatively early stages Nextgen is concerned that NBN Co is already endeavoring to move beyond its remit. One example of such an activity is NBN Co's proposed Cell Site Access Service (CSAS), whereby NBN Co would avail access to its base stations and transit infrastructure in order to support improved competition in the mobile sector. It is our view that such activity is (a) outside NBN Co's remit and (b) has the potential to create significant distortions in the local telecommunications sector, diminishing industry investment incentives in a way that could freeze the current national footprint for fibre capacity (i.e. why would further investments be made if there was a risk that NBN Co might move into the corresponding market, leveraging its public funding?).

In its recent submission to the Federal Government's Discussion paper on the Mobile Coverage Programme Nextgen submitted that if NBN Co is to have a role in programme implementation, an independent body such as the ACCC may need to be involved in determining the circumstances in which NBN Co's fixed wireless assets can be used to support improved coverage and competition in regional areas so that market distortions and competitive neutrality issues are avoided.

## iii. Competition policy and appropriate regulation

Nextgen is of the view that competition policy is broad in nature, while regulation tends to be more directed or targeted — as such, the former should set the tenor for the latter. The implication of this proposition in the current context is that competition policy should provide direction about the appropriate role of a GBE (i.e. NBN Co) with regulation (i.e. the Special Access Undertaking or SAU) giving more granular effect to this.

One cornerstone of competition policy is the principle of competitive neutrality, which essentially contends that a publicly owned body should not enjoy any commercial or business advantages on the basis of its public ownership. If NBN Co is to move outside of its remit and seek to undertake activities in segments of the market which are competitive it is likely they would be acting counter to the principle of competitive neutrality.

## 3. Should NBN Co continue to be subject to wholesale-only (structural separation) and open access requirements? If so, to what extent and under what circumstances, if any, should those obligations apply to other market participants?

Yes — Nextgen is of the view that wholesale-only and open access requirements are the defining attributes of NBN Co's remit, and as such NBN Co should continue to be subject to these.

Two other circumstances where we see the possible use of wholesale-only and open access requirements are (a) competing FTTB infrastructure and (b) infrastructure investments in regional and rural areas for the dual purpose of supporting both fixed-wireless and mobile services.

In relation to competing FTTB infrastructure the use of wholesale-only and open access requirements would support structural separation but may diminish the incentives for such investment. We anticipate that in this situation issues may also arise about how the regulatory framework would be used to support the aspiration for universal access prices, and how this might interface with the overarching commerciality of NBN Co.

In relation to infrastructure investments in regional and rural areas, the case for using wholesale-only and open access requirements would be strongest in respect of any infrastructure funded (or partially funded) by the government in support of social equity objectives. Nextgen notes, for example, that the RBBP (Regional Backbone Blackspots Program) infrastructure which we manage was funded by the government and is accompanied by both wholesale-only and open access requirements.



4. Should all market participants, including NBN Co, be subject to the same regulations to the greatest possible degree or are specific regulations that do not apply across the board necessary and justifiable in some areas? To the extent to which there should be specific regulations, what is the purpose, nature and scope of the differences?

NBN Co's status as a publicly owned entity, established primarily to facilitate structural separation in a competitive industry means that they should be subject to specific regulatory oversight as currently effected through the Special Access Undertaking (SAU). Aside from this special treatment of NBN Co, there is merit in seeking to have a consistent regulatory framework, although the applicability or otherwise of this will typically depend on the specific activities which an industry participant engages in and/or their capacity to exercise market power.

5. To what extent should competitive neutrality between NBN Co and other market participants be ensured and if so, how?

If NBN Co moves beyond its remit and into segments of the market which are competitive it is likely they would be acting counter to the principle of competitive neutrality. Because compliance with competitive neutrality is not an optional choice for NBN Co as long as they continue to be a publicly owned entity, we would expect to see in such situations:

- NBN Co's competitive neutrality policy, including discussion about how the principle of competitive neutrality applies to NBN Co's activities;
- An explanation of how NBN Co proposes to manage or ring-fence activities in its different areas of focus (i.e. its areas of remit on one hand, and its participation in competitive markets on the other), including:
  - discussion of how neutrality is achieved with respect to both tax and financing matters;
  - discussion of how neutrality is achieved with respect to NBN Co's assets and any consequential usage of dark fibre or managed transmission services which have been leased from Telstra;
- A clear statement of NBN Co's commercial and non-commercial objectives or obligations; and
- Details on whether or not 'open access' provisions would apply to the assets used to support participation in any given competitive market.

6. Where providers other than NBN Co supply fixed network services, should there be provisions that ensure consumers secure particular outcomes, for instance by comparison to those generally available from NBN Co?

Nextgen interprets this question as going to the possibility of competing FTTB infrastructure, something we see as essentially a hypothetical possibility at the moment and one with numerous tradeoffs as outlined above. As we are not supportive of competing FTTB infrastructure we have no comments on this question at the current point in time.

7. Where an infrastructure provider other than NBN Co delivers outcomes comparable to those delivered by the NBN, what obligations or restrictions should apply on NBN Co? For example, should NBN Co be preventing from overbuilding that network?

Nextgen interprets this question as going to the possibility of competing FTTB infrastructure, something we see as essentially a hypothetical possibility at the moment and one with numerous tradeoffs as outlined above. As we are not supportive of competing FTTB infrastructure we have no comments on this question at the current point in time.

8. Were NBN Co to be restricted in supplying services in areas serviced to a specified standard by other network operators, what undertakings, if any, should those operators be required to give about their ongoing performance? Noting links with question 3 in relation to wholesale-only and open access requirements, would it be sufficient to rely on Part XIC processes to secure access to services on these networks, or on Part XIC processes that were further refined?



Nextgen interprets this question as going to the possibility of competing FTTB infrastructure, something we see as essentially a hypothetical possibility at the moment and one with numerous tradeoffs as outlined above. As we are not supportive of competing FTTB infrastructure we have no comments on this question at the current point in time.

9. What are the essential characteristics that service provided over a network other than NBN Co's should have to meet for those services to be seen as operating on an NBN-comparable basis?

Nextgen interprets this question as going to the possibility of competing FTTB infrastructure, something we see as a hypothetical possibility at the moment and one with numerous tradeoffs as outlined above. As we are not supportive of competing FTTB infrastructure we have no comments on this question at the current point in time.

10. To what extent should the provision of non-commercial services by NBN Co be funded through cross-subsidies, and if so, what safeguards, if any, should apply to those cross-subsidies?

Under NBN Co's original business model — in general terms — service provision in regional and rural areas was to be subsidised by service provision in metropolitan areas (i.e. services in regional and rural are, in essence, non-commercial). We understand that this approach is largely based on social equity objectives which have long characterised the Australia's telecommunication sector, given our unique geographical attributes. Nextgen is supportive of this general business model but also considers that there are limits as to the extent to which NBN Co's ongoing commerciality can be ensured through the use of cross-subsidisation arrangements. The two main sources of risk to the 'general business model' appear to be:

- i) Low uptake of NBN Co's services by consumers; and
- ii) Revenue leakage due to the allowance of competing FTTB infrastructure.

Nextgen has no comments in relation to scenario (i) above. In the case of scenario (ii) though, were this to occur it would presumably be on account of a decision by government, in which case it could seem unreasonable to dial up cross-subsidisation arrangements (i.e. user charges) in the event that NBN Co's commerciality consequentially came under financial pressure. In this situation any financial shortfalls may need to be met by the government, and potentially orientated towards regional and rural areas due to the higher costs of service provision in those areas relative to metropolitan areas. Such funding could be justified on the basis of social equity objectives under the guises of a community service obligation (CSO), and sourced from general consolidated revenue.

Outside of the scenarios above, were NBN Co is engaged in the provision of non-commercial services the reasons for this activity would need to be clear. If these services were outside NBN Co's remit and/or not within NBN Co's Statement of Expectations, their costs should not be met through the use of cross subsidisation arrangements. Wherever such services were supplied in the context of participating in a competitive market (i.e. the mobile sector), Nextgen is of the view that NBN Co would be responsible for recovering the associated costs in a way that was consistent with the principles of competitive neutrality (i.e. in a way that was transparent and not distortionary to any of the markets which NBN Co participates in).

11. Were it not feasible or sustainable in a competitive market for NBN Co to earn sufficient revenue to enable it to cross-subsidise uneconomic customers, how should services to those customers be provided and funded?

In the scenario canvassed the general options for supporting service provision would appear to be:

- (a) the use of cost recovery (i.e. user pays) arrangements;
- (b) government funding under the guises of a CSO, with the funding sourced from general consolidated revenue; or
- (c) some hybrid of (a) and (b).

12. What approach should be taken in new developments? Do they raise particular structural regulatory issues?

Nextgen is not overly concerned with the specifics of the approach or approaches used for new developments, but for reasons of consistency with the broader regulatory paradigm the main structural regulatory issues where particular attention would be required are structural separation, wholesale only and open-access provisions.

13. Should responsibility for the economic regulation of telecommunications remain with the ACCC?

Nextgen is cautious about any changes to the current regulatory arrangements for the telecommunications sector in Australia — as such our view is that responsibility for the economic regulation of the telecommunication sector should remain with the ACCC.

To the extent which any changes in existing regulatory provisions is being canvassed, Nextgen would be interested in understanding the nature of these proposed changes, and their ability to be accommodated in current regulatory arrangements as a starting point.

More broadly given there are various bodies with regulatory oversight of the telecommunications sector (i.e. ACCC, ACMA and the TIO) we believe it is important for the government to ensure there is consistency in the actions of these bodies, and a minimisation of regulatory burden.

### 3 CONTACT DETAILS

Nextgen's contact details in respect of the Vertigan Review are as follows:

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Nextgen is happy for the above contact details to be included in any summary of our submission that is published by the Panel.