

**Telstra submission to the Bureau of Communications Research NBN non-commercial services  
funding options consultation paper**

**5 June 2015**

## Executive summary

Telstra welcomes the opportunity to comment on the Bureau of Communications Research (BCR) consultation paper “*NBN non-commercial services funding options*” (**the paper**).

We understand that the proposal for a new funding arrangement to support NBN Co’s provision of non-commercial services is motivated by two related considerations:

- The benefits of increased transparency around the cost of “non-commercial services” described in the paper as services delivered by NBN Co where costs exceed revenues over time and illustrated by fixed wireless and satellite services; and
- The need to address impacts on NBN Co’s business case resulting from the emergence of competing fixed network infrastructure.

Because network infrastructure providers competing with NBN Co do not currently have any obligation to support the provision of non-commercial services it is likely that without intervention they will continue to expand their network footprints in low cost and/or high density areas, compromising NBN Co’s ability to deliver the core objective of the National Broadband Network (NBN) policy to improve broadband accessibility and quality for all Australians.

The development of a solution to this issue requires the following considerations:

- Clearly defining non-commercial services – this will support the subsequent costing of their provision;
- Quantifying the cost of provision – as the services are ‘non-commercial’ Telstra considers use of an avoidable or incremental cost methodology is appropriate;
- Confirming the design of a funding arrangement – a per service charge collected from the carriers competing against the NBN for commercial services is the most suitable approach and will also supports competitively neutral outcomes; and
- Clarifying eligibility for the per service charge – the charge should only apply to networks that are competing with the NBN and were not contemplated when the NBN Co business case was developed. Existing corporate fibre networks and other networks pre-dating the NBN should be excluded.

In addition to the points above, it is important that the approach ultimately recommended to Government by the BCR is focussed specifically in the problem at hand, namely the emergence of fixed network infrastructure which is competing with NBN Co and impacting its ability to maintain a cross-subsidy. Attempting to solve different problems, or adopting a solution which has impacts beyond the central identified problem above, could be accompanied by a risk of further unintended problems and/or possible market distortions.

Telstra agrees that ongoing provision of non-commercial services over the NBN requires a sustainable approach as this will ensure all Australians will have access to high speed broadband services irrespective of where they live. As a national service provider with a long history of service provision to regional and remote customers, for the purposes of ensuring NBN Co’s business model remains sustainable, we consider that the above approach will deliver a positive outcome for all Australians.

## Introduction

Telstra is pleased to comment on the Bureau of Communications Research (BCR) consultation paper “NBN non-commercial services funding options” (**the paper**).

Set out below is Telstra’s response to the general issues raised by the paper. Telstra’s responses to the specific questions posed by the BCR are set out in **Attachment A**.

## Problem to be addressed by a new NBN non-commercial funding arrangement

We understand that the proposal for a new funding arrangement to support NBN’s provision of non-commercial services is motivated by two related considerations:

- The benefits of increased transparency around the cost of “non-commercial services”; and
- The need to address impacts on NBN Co’s business case resulting from the emergence of competing fixed network infrastructure.

Telstra agrees that ongoing provision of non-commercial services over the NBN requires a sustainable approach to funding. This will ensure all Australians will have access to high speed broadband services irrespective of where they live. As a national service provider with a long history of service provision to regional and remote customers, including as the Government’s designated Universal Service provider, we understand that the continued supply of non-commercial services is an important part of achieving the goal for all Australians to have access to high speed broadband services.

Under current arrangements fixed networks that compete with NBN are not required to contribute to the cost of providing non-commercial services. This situation places NBN Co at a cost disadvantage, and the resultant uneven playing field creates an incentive for NBN Co’s competitors to expand their activities. This could, over time, erode the ability NBN Co to sustainably provide non-commercial services.

This situation suggests that a solution is required to restore a level playing field and ensure that non-commercial services are sustainably funded. Assuming no external source of subsidy is available, there will be a need to transparently and equitably apportion the cost of providing non-commercial services between NBN and its competitors.

## Defining non-commercial services

In the paper the BCR indicates that an NBN non-commercial service is one delivered by NBN Co where costs exceed revenues over time. The BCR goes on to conceptually illustrate that the revenues from fixed wireless and satellite services fall short of the costs of delivering these services.

While Telstra agrees that non-commercial services should be determined with reference to their cost and the revenue they are likely to generate, Telstra believes that it would be useful for the BCR to more clearly define what services supplied by NBN Co broadly constitute non-commercial services. This definition should in turn provide the basis for quantifying the cost of non-commercial services in a clear and transparent manner.

## Quantifying the cost of non-commercial services

Telstra considers the avoidable or incremental cost approach to be the most appropriate methodology for costing the provision of NBN Co’s non-commercial services.

Application of this cost method would involve measuring the incremental cost (net of extra revenue) incurred by NBN Co from providing the non-commercial services (or alternatively, the net cost that would be avoided if those services were not provided). It excludes the costs and revenues that NBN Co would incur or earn if NBN Co did not supply those non-commercial services.

This cost approach is likely to minimise the impact that any levy would have on commercial customers (i.e. those supplied by fixed line infrastructure, and possibly some fixed wireless services), while also continuing to provide the incentive for NBN to continue to supply non-commercial services.

The measurement of avoidable costs and revenue should be based on the completed NBN business case, and the timeframe for the analysis should extend beyond the time the NBN rollout has been completed. This would ensure that any calculation of the net loss of providing non-commercial services does not capture NBN Co's start-up costs of supplying these services, as these costs would be recovered over time irrespectively. Future costs would need to be discounted back to current dollars.

Because the focus of the avoidable cost approach is on the net cost of service provision, there will need to be regard for all revenue generated from the defined non-commercial services and the assets which support them as part of the quantification exercise.

In addition to some customer revenues, revenues generated as a result of ancillary services, such as NBN Co's proposed Cell Site Access Service, would also need to be accounted for, as these involve usage of NBN fixed wireless infrastructure in one form or another. Similarly, any 'self service' by NBN Co involving the use of non-commercial assets — possibly transit requirements for example — should also be provided for if relevant.

Telstra is of the view that visibility about disaggregated changes in cost is not required, but the methodology by which costs are quantified must be documented.

### Funding arrangement

Telstra submits that a per Service in Operation (SIO) charge is the most preferable of the funding arrangements identified in the consultation paper for the following reasons.

- The SIO charge option would ensure that end users buying commercial services would face the same liability, regardless of their network or retail service provider, which would ensure fairness.
- While funding the net cost of non-commercial services from the tax base may reduce the dead-weight loss, this is unlikely to be practicable. Further, the issues identified in the paper can be addressed by a SIO charge funding arrangement as well as if funding came from the general tax base.
- As noted earlier the key issue is fixing incentives to support competitive market outcomes and the realisation of a level playing field for both NBN Co and its direct competitors. As a per service charge can be applied directly to NBN Co's network level competitors it is simple and understandable, and also meets the transparency and efficiency principles outlined in Table 3 of the paper.

Telstra anticipates that there could be a number of surmountable implementation issues associated with the use of a SIO charge arrangement which will require further exploration. First there is the possibility for NBN Co's contributions to the cost of providing non-commercial services to net out (as mentioned in the consultation paper). Second, there is also a question as to how and by whom a per SIO charge would be collected. And a third issue could be whether or not the charge is dependent on a service being 'in operation' or whether it applies when a premises is 'passed'.

Telstra also believes that the funding arrangements for non-commercial services should be kept separate from those which apply in the context of the Universal Service Obligation. The methodology is different, the funding arrangements (actual and proposed) have different objectives, the services funded have different footprints and there are also differences in terms of the (actual and proposed) funding eligibility and bases for calculation. Telstra cannot identify any efficiencies from combining funding arrangements for the provision of non-commercial services and the USO at the current point in time, and believes there is a risk of reduced transparency were they combined. Thus, the arrangements should be kept discrete.

## Eligibility for the SIO charge

Telstra considers that the use of a service standard to determine eligibility for the SIO charge as proposed in the consultation paper is too broad. The charge should be applicable to NBN Co's fixed network competitors, as it is these parties which are potentially compromising NBN Co's ability to sustainably fund the ongoing provision of non-commercial services.

Networks that are not directly competing with the NBN for commercial customers within NBN Co's original remit and were contemplated by the original business case should not be captured by the new funding arrangement, as these networks do not impact NBN Co's ability to fund the provision of non-commercial services.

### Competing networks not contemplated by original NBN Co business case

Following the transition to a multi-technology model for the NBN, the possibility of competing network builds utilising vectoring (or other) technologies became apparent, especially in the context of new Fibre-To-The-Basement or Fibre-to-the-Building network extensions for Multi-Dwelling Units (MDUs). Such builds are in direct competition with the NBN and are the primary source of adverse impacts on NBN Co's ongoing ability to fund the provision of non-commercial services because they seek to connect premises which NBN Co — in time — would have connected.

Furthermore, technical issues including possible interference where there are multiple providers utilising vectoring technology in a given MDU may constrain NBN Co's ability to overbuild competing networks.

As these networks compete directly against NBN Co, and their existence has an impact on NBN Co's original business case, it is appropriate that they are subject to the proposed funding arrangement.

### Networks contemplated by original NBN business case

In contrast to the situation outlined above, there are a number of established high speed networks within Australia which existed at the time the NBN business case was developed. Some of these networks were assumed to co-exist with the NBN or to be candidates for acquisition by NBN Co. They were not seen as competitors to NBN and were not a threat to NBN's funding of non-commercial services. On this basis these networks — which include corporate fibre networks — should not be captured by the proposed funding arrangement.

Telstra suggest that the BCR should nominate a cut-off date for excluding networks contemplated by the original NBN business case from eligibility for the proposed new funding arrangement. As a date of 1 January 2011 has been recently used in similar contexts (i.e. the Carrier Licence Conditions (Networks supplying Superfast Carriage Services to Residential Customers) Declaration 2014), such a date could be applied in the interests of consistency.

### Networks in new developments

In relation to networks in new developments, Telstra considers that with the recent change in Government policy. NBN comparable networks should be eligible for the charge. Although the previous new developments policy, Fibre in New Developments (FIND) Policy, contemplated the possibility of third party network build, the updated policy has expanded the possibility for competition in the build and operation of competing infrastructure in new developments. As these networks will impact on the NBN business case which was developed in the context of the FIND policy, these networks should also be eligible for the charge.

However, as many new development networks have been built without consideration of a non-commercial service charge, there should reasonably be an exemption for networks that are built or in construction prior to the introduction of a non-commercial charge.

### Mobile networks

Telstra would also support the BCR's view that this approach would not include mobile broadband networks. This is also in alignment with our principle articulated that networks which are not directly competing with NBN for commercial customers within NBN's original remit and were contemplated by the original NBN business case should not be captured by the new funding arrangement.

### **Administration**

Telstra agrees that the BCR's proposed structure of an industry fund, contributed to by eligible payees and administered by a body such as the ACMA is a reasonable way to administer the proposed funding arrangement.

**Attachment A – Telstra’s response to BCR questions**

	<b>BCR Question</b>	<b>Telstra Response</b>
1	Is measuring NBN Co’s satellite and fixed wireless service costs on a commercially focused basis appropriate?	As outlined in the body of our submission, Telstra believes that the avoidable or incremental cost approach is the most appropriate methodology for quantifying the cost of NBN Co’s non-commercial services.
2	Is it appropriate to consider commerciality on a network ‘cluster’ basis?	Telstra is comfortable with commerciality being assessed on a network ‘cluster’ basis provided this reconciles with the use of an avoidable cost approach.
3	Is FY2040 at an appropriate time period for assessing NBN non-commercial services?	Use of FY2040 as the time period for assessing NBN Co’s non-commercial services appears to be appropriate, and is preferable to a shorter period.
4	Are the proposed principles relevant and applicable when considering NBN non-commercial service funding arrangements?	The proposed principles appear to be relevant and broadly applicable. In relation to the equity principle, there is a question about whether any instances of non-equitable outcomes are best addressed through safety net measures as opposed to the proposed new funding arrangement.
5	Should the BCR consider additional principles? If so what are they?	<p>Telstra submits that there may be a need to include principles relating to cost allocation, due to the likelihood of fixed wireless assets being used for purposes other than the provision of non-commercial services (i.e. a possible future Cell Site Access Services product). Further exploration of how cost allocation principles interact with the avoidable cost approach and its focus on net costs may be required.</p> <p>Standard cost allocation principles cover matters such as allocating costs on the basis of relative usage, establishing casual relationships to support cost allocation and ensuring no cost is allocated more than once.</p>
6	To what extent could financial reporting support transparency of the allocation of equity, debt and revenues towards non-commercial services?	<p>Telstra is unsure about the extent to which financial reporting might support transparency around the allocation of equity, debt and revenues towards the provision of non-commercial services.</p> <p>While these may be important considerations, Telstra submits that it is also important for there to be transparency around both the methodology which will be used to quantify the cost of non-commercial services and the methodology which will be used to apportion these costs to eligible parties.</p>

7	<p>What issues are associated with maximising economic efficiency in developing NBN non-commercial service funding arrangements?</p>	<p>Key issues for maximising the economic efficiency of the funding arrangements for the provision of NBN Co's non-commercial services would appear to include:</p> <ul style="list-style-type: none"> <li>- Having a clear definition of non-commercial services to guide the application of a funding framework</li> <li>- Using a transparent methodology for quantifying the cost of providing non-commercial services, so this is no higher than need be</li> <li>- Using clear cost allocation rules, where appropriate, to manage instances of shared asset use and/or self service</li> <li>- Having an element of flexibility in the framework itself, so that changes in the status of a given area or cluster (as in a shift from non-commercial to commercial) or technology (reducing the costs of service provision) can be incorporated in a timely manner.</li> </ul>
8	<p>In designing NBN non-commercial services, how can pro-competitive market conditions for the provision of both non-commercial and commercial services best be achieved?</p>	<p>In principle, Telstra always supports competitive markets as delivering the best outcomes from consumers. However, in designing any NBN services, the foundation principle of the Governments NBN policy of a wholesale only, ubiquitous layer 2 service provider with legislated limits on competition needs to be considered. In this context, Telstra supports contestability in commercial areas, but does not support contestability in non-commercial areas where this would entail the redirection of subsidies to the competing party. Such a step would seem to muddy the water around the NBN construct itself, and would reflect a change in policy which has not been fully explored.</p>
9	<p>What issues are associated with developing sustainable NBN non-commercial service funding arrangements?</p>	<p>As outlined in the consultation paper, there are two dimensions to the sustainability of NBN Co's non-commercial service funding arrangements — the sustainability of the base funding sources, and the sustainability of the supply obligation as expressed through the Statement of Expectations. Telstra believes that the current proposal for a new proposed funding mechanism will help support the sustainability of the base funding sources over time but is not in a position to comment on the sustainability of the supply obligation.</p>
10	<p>What equity issues need to be considered as a result of NBN non-commercial service funding arrangements?</p>	<p>Telstra submits that if the levy is uniform (on a per SIO basis) for both NBN Co and network providers competing with NBN Co, this will promote a level playing field and competitively neutral outcomes, and by extension reduce the potential for equity issues to arise.</p>



11	What are appropriate mechanisms to ensure equitable outcomes?	Consistent with the response to question 10 above, the pursuit of a uniform levy — applied to network providers competing with NBN Co on a per SIO basis — appears to be the most appropriate approach for ensuring equitable outcomes.
12	Is a discounted cash flow methodology based on NBN Corporate Plan projections an appropriate approach to modelling NBN non-commercial service losses? If not, why not?	Yes, but those cash flows should relate to only what is avoidable or incremental to the supply of non-commercial services.
13	What, if any, issues arise in using NBN Co Corporate Plan financial estimates for the purpose of assessing NBN non-commercial service losses?	Telstra supports the proposal to use NBN Co Corporate Plan financial estimates — updated with actual figures as they become available — for the purpose of assessing NBN non-commercial service losses. The main issues with this approach would appear to be ensuring NBN's data interfaces with an avoidable cost framework, actual cost and revenue data is incorporated in a timely manner, and ensuring instances of shared asset use and self service are appropriately catered for.
14	Is a fully allocated cost approach appropriate for the treatment of NBN non-commercial services? What are the strengths and limitations of this approach?	As outlined in the body of our submission, Telstra believes that the avoidable cost approach is the most appropriate methodology for quantifying the cost of NBN Co's non-commercial services.
15	What are the relevant issues in determining a discount rate for NBN non-commercial services?	<p>Telstra notes that in the current context, the focus is on a discount rate for the non-commercial component of the NBN rather than the NBN initiative as whole.</p> <p>In general terms the prevailing market conditions are clearly relevant to the determination of a discount rate, with these conditions reflected in decisions about both the risk free rate and market risk premium (MRP).</p> <p>At a more granular level, relevant factors may include the opportunity cost of the capital associated with availing non-commercial services, the opportunity cost of both spectrum and satellite capacity used for the provision of non-commercial services, the risk of mobile substitution and the timing of benefits from the provision of non-commercial services.</p>
16	What relevant discount rate should be considered for NBN non-commercial services?	As outlined above, there are numerous considerations associated with the choice of an appropriate discount rate in the context of NBN Co's non-commercial services. As Telstra has not worked through all of these considerations (and others which may be relevant), it is not in a position to nominate a specific discount rate but instead submits that — on balance — this rate should be higher than those identified in the consultation paper.

17	What issues arise when considering the application of a terminal value for calculating NBN non-commercial services?	Key issues for the consideration of a terminal value would appear to include the accuracy of growth assumptions underlying the terminal value, the interface between this terminal value and the discount rate adopted for the purposes of considering non-commercial services, and appropriately factoring in life cycle uncertainty factors including the possibility of technology obsolescence. A terminal value may introduce a degree of uncertainty in the determination of a SIO charge that is unreasonable. This would certainly be the case if the terminal value is dated after 2040, and the SIO charge can be changed prior to that date to address any uncertainties.
18	What are the key sensitivities or scenarios which should be considered?	Key sensitivities which should be considered include: <ul style="list-style-type: none"> <li>- The impact of variations in the chosen discount rate</li> <li>- Life cycle considerations, including the possibility of technological changes, changes in the relative price of different technological options over time and the risk of obsolescence viz-a-viz initial or existing</li> </ul>
19	Should NBN Co contributions towards NBN non-commercial services, and funding to deploy and maintain these services, be made via a Commonwealth account?	Yes, as this will help support transparency.
20	What issues should be considered when examining industry funding eligibility?	Eligibility for the new funding arrangement should be based on networks which are directly competing with NBN Co and were not contemplated by the original NBN Co business case, as these networks may — over time — impact NBN's ongoing ability to fund the provision of non-commercial services.  Networks which are not directly competing with NBN Co and were contemplated by the original Co NBN business case should not be captured by the new funding arrangement, as these networks do not impact NBN Co's ability to fund the provision of non-commercial services.
21	Is it reasonable to apply a service standard to determine eligibility? If so, is a high-speed broadband speed criteria based on a minimum download speed of 25 Mbps reasonable?	Telstra considers that the use of a service standard to determine eligibility — as proposed in the consultation paper — is too broad. The focus, as outlined above, should be on networks that are directly competing with NBN Co and were not contemplated by the original NBN Co business case.
22	In the context of NBN non-commercial services, what issues should be considered regarding eligible revenue or other eligibility thresholds?	Telstra does not support the use of a revenue threshold because this may create an incentive for competing providers to fall below it, and bypass making any contribution to the cost of providing non-commercial services. Such an outcome would equate to non-level playing field, which is contrary to

		one of the objectives associated with the proposed new funding arrangement.
23	To what extent is it appropriate to consider proportionality when developing funding arrangements?	<p>Telstra believes that it is not appropriate to consider proportionality in terms of either market share or revenue as a criterion for determining eligibility for any future funding arrangement. Rather proportionality should be considered in terms of the proportional impact of any (eligible) competing network on NBN Co's ability to fund the provision of non-commercial services.</p> <p>With reference to the statement within the consultation paper (p.28) that "industry levy calculations are typically based on determining an overall funding requirement as well as a calculation for the percentage contribution required from each eligible industry participant based on the chosen eligibility requirements", we agree that this approach is pragmatic and submit that the percentage contribution should be framed on a per-SIO basis if possible. Such an approach will support proportionality as levies would be collected from competing network operators only to the extent that they impact NBN Co's original business case and corresponding ability to fund non-commercial services. As noted in our submission, we anticipate that there may be some implementation issues associated with the suggested funding approach that require further exploration.</p>
24	It is practical to consider contestability in the provision of NBN non-commercial services?	Telstra believes it is not appropriate, at the current point in time, to consider contestability in the provision of NBN non-commercial services.
25	Would bill transparency arrangements be beneficial?	At a wholesale level only.
26	Is it feasible for NBN non-commercial services to be reflected on end user invoicing?	No. This is unnecessary red tape that will not deliver benefits to consumers at a retail level and will impose costs on the network operators who would then need to provide additional information on customer bills. This is ultimately up to the retail service provider.
27	Is there opportunity to amend the existing USO/TIL collection arrangements to include NBN non-commercial services collection arrangements – noting that industry funding eligibility may be different?	Telstra believes that the arrangements for the provision of non-commercial services should be kept separate from those which apply in the context of the USO. These areas are distinct from one another and have different objectives, different footprints, different funding eligibility and different bases for calculation. The USO is a retail service provision obligation designed to provide a safety net for customers at a retail level, not a wholesale infrastructure obligation.

		<p>However, we do not object to the proposed structure of an industry fund, paid into by eligible payees and administered by the ACMA.</p>
28	<p>To what extent will elements of the SAU need to change to accommodate the introduction of NBN non-commercial service funding arrangements?</p>	<p>As noted in the consultation paper, the establishment of a new funding framework for the provision of non-commercial services is likely to have implications for the Initial Cost Recovery Account (ICRA) within the SAU. These implications could extend to what gets included in the ICRA in the first instance, and its extinguishment over time including provision for industry contributions. In addition to clarifying these implications, Telstra submits that the SAU more broadly may require amendment to reflect the definition on non-commercial services and whether or not these are formally designated as a community service obligation by the Government.</p>