Who should we fear most – Telstra or NBN Co.?

The ACCC continues to hammer Telstra while mollycoddling NBN Co. This is short-sighted.

The ACCC is currently reviewing the pricing of Telstra's seven regulated fixed line services (ULLS, LSS, WLR, LCS, FTAS, FOAS and wholesale ADSL) and NBN Co.'s access services. The first covers only the next four years but the latter will affect the affordability of fixed communication services for the next decade and beyond.

It has always been recognised that the fixed network is essentially a fixed cost business so that as customers move from fixed to mobile lines or use fewer voice lines with broadband, the remaining users carry an increased burden of costs. The ACCC seems to accept that and says some sensible things about how the NBN should affect its determination of access prices – but there are clearly some issues it is still trying to work through.

With yesterday's draft decision on Telstra's access prices, the ACCC has missed another opportunity to help manage the transition to the NBN.

As explained in this column (15 October 2014), the ACCC's approach to providing industry certainty in 2009 was to provide a glide path to higher access prices. This was howled down by access-seekers and the ACCC backed-off quickly. It is still cowed because its current idea of certainty is not to change anything.

In fact, it does make a uniform slight reduction in the prices across all regulated fixed line services to maintain price relativities and "promote a degree of stability for industry, which will assist in the transition to the NBN and be in the interests of end users".

This is pretty dumb even though it looks like the idea of a uniform percentage price change (but an increase rather than a decrease) came from Telstra. It's dumb because it will not lead to increased competition in the short term and because it makes it harder to wean providers off copper to the NBN. The cheapest NBN wholesale service is $24 pm and the average NBN wholesale ARPU is nearly $40 pm. Compare those levels with $16 pm for unbundled local loop (ULLS Bands 1-3). This is not about stability but about a smooth transition to the NBN, which involves a step change in the access prices that access-seekers face.

At the same time, the ACCC is far too relaxed about NBN Co. pricing. It is taking submissions (due by 27th March) on its first determination on NBN Co.'s long term revenue constraint methodology (LTRCM) for FY2014. According to the ACCC, the methodology "creates an incentive for NBN Co. to operate prudently and efficiently".

But, while the ACCC disallows all capital expenditure incremental to the NBN from Telstra's total forecast capital expenditure for the period 2014–15 to 2018–19, it simply accepts the nearly $2bn in costs already incurred by NBN Co without question in assessing its allowable revenues.

More importantly, prudence should not be confined to examining costs. On the revenue side, the

ACCC seeks only to ensure that NBN Co. has not exceeded the maximum regulated prices allowed under the special access undertaking (SAU).

Is it prudent to leave money on the table?

NBN Co.'s 2014-2017 Corporate Plan forecasts that total revenues will increase from $61m in FY2014 to $160m in FY2015. Let's hope so – that $61m is half what the 2012-2015 plan forecast. In any case, NBN Co. is no shape to be giving money away. But it is.

From 1st February, CVC prices were reduced from $20 per Mbps to $17.50. This is Option 3 from the ideas that NBN Co. kicked around last year (see Hobson's Choice, CommsWire 18 August 2014).

In the September Quarter of 2014, CVC revenue accounted for a quarter of NBN Co. revenue. So, with no change in CVC pricing and the same proportion of total revenues, CVC revenues should account for $40m of NBN Co. revenue in FY2015. But, the CVC price reduction will reduce that revenue by $5m in one year.

Does the ACCC care? No. In fact, NBN Co. will not lose $5m but gain it later with interest (at the risk free rate plus 3.5%) under the initial cost recovery account (ICRA). The ICRA is the accumulation over time of the difference between NBN Co.'s actual revenues and the revenues it is allowed to earn.

NBN Co. can be careless about revenues forgone today when it has a regulatory compact to reclaim it later with interest. That is not prudent.

Also, NBN Co. has persuaded the ACCC to ignore the $181 million of interest is has earned on equity injections before they are spent (i.e. treat as "unregulated revenue"). That increases the ICRA by the same amount and this amount increases at a regulated interest rate more than double what NBN Co. must also be getting on term deposit.

The ICRA (future allowed revenue increases) stands at around $4 billion now and is increasing. It is not the manner in which this is recovered over time – the spectre of CVC price increases – that is the problem but the use of the ICRA itself. It hangs over the heads of all access-seekers and may explain why they have built up their profit margins (see price competition has stalled).

The ACCC says that stability on Telstra's regulated fixed access prices "will promote competition in the transition to the NBN" (Press Release, 11 March). In my view, it will neither promote competition nor smooth the transition to the NBN.

In any case, these are short term objectives. Important as they are, the bigger issue is long term. How do we ensure the affordability of the NBN in the long-term? To-date, the ACCC's decisions will not contribute to long-term affordability of access. While the ACCC continues to put pressure on Telstra's access prices, it seems blind to the pent-up price increases it has encouraged at NBN Co.

John de Ridder