



Comments on Telecom's Submission (Public Version (there is no confidential version))

This note comments upon Telecom's public submission of 13 March on the Draft Reconsideration of D582 issued on 21 February 2007.

I note that Telecom agrees that the new basket method is an improvement on the WARP update methodology. However, Telecom raises a number of points which should not pass without comment.

1 Cost of data

I note that Telecom agrees that there is a competitive market in international data transmission. While it may not always be the cheapest provider, it should not object to using its own tariff for this purpose. It provides a consistent benchmark that should be close to market.¹

For the domestic transmission cost, Telecom is happy to provide its own wholesale tariff. But, it has chosen a "high volume" (>30Mbps) purchase which may not be representative of what the larger ISPs are actually using. The Commission should determine whether the \$80 per Mbps per month is the appropriate rate to use. If not, a higher priced (lower volume) rate from Telecom's wholesale rates should be used.

These prices for capacity have to be weighted by traffic shares. I am told that the suggested assumption that 14% of traffic is domestic is too high. The shares of international and domestic traffic vary with the mix of business and residential customers. Telecom's high domestic traffic share may reflect a higher proportion of business customers.

Finally, the weighted price per Mbps per month has to be converted into the cost of a GB per month. The conversion algorithm depends upon a number of parameters. Telecom assumes that a 1Mbps link can be run at full capacity all month to yield 320.84 GB over a

¹ It does not take much of a difference for ISPs to shift between providers of international capacity; switching costs are low and large volumes on small differences are worth taking.

month (para 39). On conservative assumptions (see box below), it is a third less at 207 GB per month.

Conversion of Mbps to GB per month

Bits / Byte	8
Potential Mbytes /s	0.125
Link efficiency	64%
Mbytes/s	0.08
Seconds per month	2,592,000
Data GB pm	207

2 Overage and “budget”

Telecom argues that overage on the Basic Plan should be priced as part of the retail price for that plan.

In making this argument, Telecom uses a supporting hypothetical example in which *“Telecom could “buy back” the Gbytes that the customer didn’t use at some appropriate rate.”* (para 20). If this argument is correct, this also supports the argument, in my initial report on this reconsideration, that Telecom has a “budgeted” amount of usage. In order for such rebates to be transparent to customers, the budget and the cap must be the same (some other amount between actual usage and the cap would be difficult to communicate to customers in a rebate scheme). If Telecom can imagine retail customers being rebated for use under their cap, why should not wholesale customers enjoy the same avoided cost savings?

3 VP costs

It should be noted that Telecom was the first to market with an uncapped plan (ie Go Large), which encourages the high volume customers who impose congestion costs on others. I am told that Darryl Burn (ihug) wrote to David Baker of the Commission about the impact of Telecom’s Go Large plan on the ISP market, which included a section on the contribution of Telecom’s Go Large to poor backhaul performance. Why should Telecom ask for the extra costs of VP capacity that it has helped to cause?

4 ISP costs

The original UBS decision for Telstra Clear looked at ISP and also retail costs. Telstra Clear argued, based on benchmarking analysis,² that the costs were considerably higher than the \$8.89 which is currently assumed. If ISP costs are now going to be part of the current Reconsideration, surely the 16% mark-up assumed to represent retail costs avoided should be re-visited too? Presumably, the costs of retail service have increased too although a fixed percentage on a declining retail price means that the corresponding dollar amount allowed for retail costs is falling.

² See para 374 in Determination 568

5 Underlying Data

Telecom has, again, not provided data underlying the proposed methodologies. The dangers are illustrated by what happened in respect of Determination 582, which underlay the appeal, my affidavit in that appeal, and the information that came out as a consequence. This time, it appears that Telecom is not even giving the information to the Commission.

6 Margin analysis

The Commission's proposal does not require any more of Telecom than it should be doing for itself when it does its internal business case for new prices and products (see my initial report on the draft determination for the Reconsideration).

7 Summary

As noted earlier, the parties have more confidence in the new model proposed by the Commission than the WARP model. ,

John de Ridder
21 March 2007

Biographical Note:

John de Ridder is a telecommunications economist who spent ten years in corporate and wholesale pricing roles at Telstra. This experience included Telstra's first Competition Notice for anti-competitive broadband pricing. Over eighteen years at Telstra he was:

- Chief Economist in Corporate Finance where he influenced the environment for competition with numerous studies on international price benchmarking, natural monopoly and universal service. These include the world's first costing of the universal service obligation where he led the Telstra team.
- The first Commercial Manager of Telecom's Interconnect Unit where he helped negotiate the commercial framework for interconnection with the Regulator (AUSTEL) and then the first comprehensive interconnect agreement with the new entrant (Optus).
- Manager Pricing Strategy in Telstra Corporate Marketing where he was directly involved in all aspects of retail pricing from the start of competition in fixed and mobile networks. This role included managing price caps, leading a pricing strategy study which set the direction for the pricing of Telstra's fixed, mobile and broadband services and optimising retail and wholesale prices across the company.
- Manager Data Pricing in Telstra Wholesale where he priced broadband access and data products to other service providers and provided internal advice on key regulatory issues.

John has also worked for economic and management consulting firms in the UK (DRI/McGraw-Hill) and Australia (IBIS) as well as in the planning departments of major corporations in both countries (Shell and ICI). He is now assisting corporations and government agencies (OECD and APEC) in countries grappling with competition issues in telecommunications. He is also the author of the column "Economuse" in the influential Australian newsletter, "Exchange".