Australian Government

Department of Communications and the Arts

Submission by the Department of Communications and the Arts to the Productivity Commission's Telecommunications Universal Service Obligation Inquiry

Background to the inquiry

The Terms of Reference for this inquiry indicate that the primary policy question to be addressed is to what extent, in the evolving telecommunications market, Government policies may be required to support universal access to a minimum level of retail telecommunications services.

Given the evolution in the telecommunications market, both in terms of market structure and technology, it is timely for the Government to consider, from a first principles basis, not only whether a telecommunications universal service obligation is required but also, if it is, what services it should extend to and how such a universal service obligation might be structured and funded. The Productivity Commission inquiry will provide the Government with information and advice to assist it to achieve an appropriate policy outcome on this important issue.

Existing USO

The existing telecommunications universal service obligation (existing USO) requires Telstra, as the primary universal service provider, to ensure that standard telephone services and payphones are reasonably accessible to all Australians on an equitable basis. A standard telephone service is defined in the *Telecommunications (Consumer Protection and Service Standards) Act 1999* as a voice telephony carriage service that passes the 'connectivity test', or another form of communication for end-users with a disability. The 'connectivity test' is passed if an end-user is ordinarily able to communicate, via that service, with other end-users with the same service.

At the time the existing USO was first put in place, standard telephone services and payphones were the primary base level retail telecommunications services available to consumers in Australia. Government wished to ensure that these basic telecommunications services were available to all Australians. Government intervention was seen as necessary to achieve this as there was concern that, as Australia's retail telecommunications market was opened up to competition, services would not be provided in some areas because it might not be commercially viable to do so.

Telstra, historically, has operated as a vertically integrated telecommunications company and so there has been some confusion as to whether the existing USO is both an infrastructure and service delivery obligation or only a service delivery obligation. The Department considers that it is clearly a service delivery obligation.

Other than the limited contractual obligations referred to in the Productivity Commission's consultation paper, there is no current obligation imposed on Telstra to use a particular type of technology or infrastructure to deliver the existing USO. For example, there is no regulatory obligation imposed on Telstra to deliver standard telephone services using fixed line infrastructure. Telstra already uses infrastructure other than fixed line services to deliver the existing USO.

In short, Telstra's obligation is to ensure that particular types of services (standard telephone services and payphones) are available to Australians on an equitable basis. The existing USO requires that Australians who receive the standard telephone service under that arrangement should receive the same standard telephone service that is available to those who have a choice of service provider. The same principle applies to the payphones service.

The existing USO, together with other public interest telecommunications services, are funded in part by direct Budget appropriations, and in part by the telecommunications industry levy (TIL) imposed under the *Telecommunications (Consumer Protection and Service Standards) Act 1999* and associated legislation. The policy rationale underlying the TIL, and the predecessor USO levy, was to ensure that the losses resulting from the fulfilment of the existing USO were shared equitably among carriers, in direct proportion to each carrier's share of the market for relevant services.

In its inquiry, the Productivity Commission will need to consider whether the existing USO remains an appropriate Government intervention, whether an alternative form of intervention is required (including how it would be structured if it was required) and how any intervention is funded.

Is a universal service obligation necessary in Australia today?

The Government has made a commitment to ensuring that, to meet Australia's economic and social needs, all Australians have access to very fast broadband as soon as possible, at affordable prices, and at the least cost to taxpayers. This commitment is being delivered by the rollout of the National Broadband Network (NBN). The NBN encompasses three broad types of infrastructure platforms, fixed line, fixed wireless and satellite. Each of these infrastructure platforms is able to be used to provide both data services and voice services.

The Government's funding of a ubiquitous wholesale network rollout is a unique policy and it has not been adopted in other jurisdictions. We believe it is necessary to take this policy into consideration in assessing whether a universal service obligation is necessary in Australia today.

The rollout of the NBN will provide a new universal communications platform allowing retail service competition whilst preserving access through statutory infrastructure provider of last resort (SIP) obligations and price cap arrangements, as explained below.

NBN Co Limited (nbn) has wholesale-only and non-discrimination obligations relating to the supply of its services to retail service providers (RSPs). These are designed to ensure that RSPs are able to access nbn infrastructure equitably and compete more effectively. There are a number of RSPs operating on the NBN, across all types of infrastructure, offering services to consumers in competition. Retail level competition is also supported by the structural separation of Telstra which the rollout of the NBN enables, meaning

Telstra as a retailer is not advantaged through its control of a ubiquitous underlying network.

In December 2014, the Government released its *Telecommunications Regulatory and Structural Reform Paper* (2014 policy paper). Amongst other things, the 2014 policy paper included a proposal to introduce obligations on nbn and, where appropriate, other network providers to require the provision of high speed broadband services. This SIP proposal would require nbn (and in some circumstances other carriers) to connect high-speed network infrastructure to premises.

In addition, nbn is subject to price cap arrangements, which enable nbn to adopt pricing that is competitive and that will ensure its infrastructure is used by RSPs in the delivery of services to consumers.

The NBN rollout, combined with the SIP proposal and the price cap arrangements, provide a universal infrastructure availability obligation, benefitting all Australians. This serves multiple policy objectives including objectives identified in the Productivity Commission's issues paper, such as the promotion of economic benefits, capturing network externalities, providing services that might otherwise by non-commercial, addressing social or equity concerns and ensuring accessibility of services. In light of this, there is the question of whether any additional retail services universal service obligation is actually required to replace the existing USO.

The Department would support the Commission considering whether there is a realistic prospect that, despite infrastructure being available to RSPs, a level of market failure is likely in that no RSPs choose to service some customers, for example, because of the limited profitability of those customers. If the Commission's analysis is that a risk of retail level market failure exists, the Department would support the Commission also considering whether this is a localised risk, applying only in specific areas or only to particular cohorts of Australians. If the Commission determined that a localised risk existed, this would mean that more targeted intervention may be more appropriate rather than Government intervention via a *universal* service obligation. Given consumers are likely to meet the costs of a service obligation via higher charges (see the section headed *Funding a universal service obligation* below), lower cost targeted intervention is likely to benefit consumers generally.

An example of targeted intervention is the Mobile Black Spot Program, which is discussed below.

Mobile services

The consultation paper notes that the question of Government intervention should depend on the costs of the intervention relative to the benefits. This is a particularly important issue to be considered if the Productivity Commission were to consider a universal service obligation that specifically prescribed that mobile services are made available to all Australians.

As noted in the Productivity Commission's consultation paper, there are currently three mobile services providers in Australia with their own networks, namely, Telstra, Optus and Vodafone. As a consequence, there is vigorous competition in the retail mobile services market, as evidenced by the heavy investment by the sector in improving transmission speed and coverage[1]. This competition has been achieved with very limited Government intervention.

The largest mobile network covers more than 99 per cent of the Australian population. Each of the other competing networks covers in excess of 95 per cent of the Australian population. Notwithstanding this expansive network coverage when measured by population, the largest network extends to only approximately 30 per cent of Australia's land mass. To extend any network to, for example, an additional 10 per cent of Australia's land mass would be a very significant cost with a very marginal impact in terms coverage of the population. The Department therefore considers that a mobile service specific universal service obligation would not be cost effective.

The mobile services market also provides an example of where a more targeted intervention by Government may be the most effective response to a market failure. The Government's Mobile Black Spots Program is an example of a more targeted intervention. That programme provides an incentive to network owners to maximise coverage in areas which would not otherwise be commercially viable without negatively impacting the vigorous competition that exists in the mobile services market.

Impact of regulation

We would support the Commission considering in its inquiry whether there are regulatory impediments that dampen competition in the delivery of retail telecommunications services to all Australians. If the inquiry concludes that such impediments exist, the appropriate response may not be the imposition of a new or modified universal obligation but may be an alternative regulatory response.

Contestability

If any form of universal service obligation or targeted intervention is recommended that is contractually based, we would support a contestable delivery model. Such a model is likely to be the most appropriate approach to ensuring that the community receives value for money.

The consultation paper notes that Australian pilot trials of competitive tendering for universal service delivery did not elicit competitive entry. This resulted from the circumstances that existed when the trials occurred. We note that, at that time, Telstra owned the significant infrastructure that would be required to deliver the existing USO. This made it difficult for other providers to compete in the delivery of the existing USO. The circumstances would be different for any future universal service obligation, given the changes in the telecommunications market.

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[1] In October 2015, Telstra announced its spending on its mobile network would reach $5 billion in the three years ended June 2017, representing a 25 per cent increase on the amount the company would normally spend on the network. Similarly, in early 2015, Optus announced its plans to sacrifice revenue growth and increase in its capital expenditure from $1 billion to $1.7 billion over the next 12 months, in order to compete with Telstra. VHA also committed an extra $1 billion to improve its network and reclaim lost market share.

Funding a universal service obligation

The consultation paper discusses the funding for the existing USO. The Government would expect that any funding model recommended by the Commission would be efficient, sustainable and transparent.

If a universal service obligation is supported by the Productivity Commission, the terms of reference for the inquiry ask the Commission to look at the funding for that obligation. This would require the Commission to consider whether the telecommunications industry levy (TIL), which provides a significant source of funding for the existing USO, is the appropriate model. As noted previously, the policy intent underlying the TIL (and its predecessor) was to ensure the losses resulting from the fulfilment of the existing USO were shared equitably among carriers. In a practical sense, the TIL is not absorbed by the telecommunications companies that are currently liable to pay it, but is passed on to consumers, meaning those consumers pay a higher costs for services as a result of the existing USO. The Department would support the Commission considering alternative policy approaches and models to the funding of any universal service obligation. Any impact on consumers in terms of higher costs for the delivery of telecommunications services should be transparent in the design of the funding model.

The Productivity Commission's consultation paper makes reference to the recommendation of the 2015 Regional Telecommunications Review that the Australian Government should establish a 'Consumer Communication Fund' to replace the telecommunications industry levy arrangements. That fund was recommended to support regional infrastructure and services, potentially the non-commercial NBN services and social equity elements. We note that the proposed fund was not supported by Government in its response to the 2015 Regional Telecommunications Review and we question the benefits of establishing such a fund solely for any new universal service obligation.

Given wider Commonwealth Budget pressures we do not consider that increased Budget funding of any new universal service obligation is a viable option.

Telecommunications consumer safeguards framework review

The consultation paper notes that there are a range of consumer safeguards that apply with respect to the delivery of telecommunications services and that universal service obligations in other jurisdictions address not only the availability of services but also affordability and accessibility.

The Government is proposing that reform of telecommunications consumer safeguards is undertaken in parallel with the Productivity Commission's inquiry. That reform will focus on, amongst other consumer protections, affordability and accessibility as important safeguards. We therefore do not consider that broader consumer safeguards should be addressed by this Productivity Commission inquiry.

Moving to a new model

It is important, if the Productivity Commission recommends any changes to the existing USO and those recommendations are accepted by the Government, that these changes are implemented in a considered and careful manner. It would be expected, in such circumstances, that there would be an appropriate period of time to allow for necessary changes to be made to the existing USO and connected contractual arrangements and implementation of any new arrangements. Accordingly, it would be expected that changes to the existing USO, and implementation of any new arrangements, would not occur until the NBN rollout was complete. According to NBN's latest Corporate Plan, the rollout is scheduled to reach 100% of Australian premises by 2020.

As noted in the consultation paper, the Commonwealth has entered into the Telecommunications Universal Service Obligation Performance Agreement with Telstra for the delivery of the existing USO. If the Productivity Commission does recommend an alternative universal service obligation, the Productivity Commission will need to take those contractual commitments into consideration in its report to Government.

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