

**Australian Competition and Consumer
Commission's submission to the
Productivity Commission's Position Paper
on International Telecommunications
Regulation**

1. Introduction

The Australian Competition and Consumer Commission's (ACCC's) comments on the Productivity Commission's Position Paper on International Telecommunications Regulation is intended to aid the Productivity Commission's analysis of international telecommunications regulation by extending or clarifying various matters discussed in the Position Paper. This submission also outlines recent developments in domestic telecommunications regulation that are potentially relevant to international telecommunications regulation. These include:¹

- ❑ the release of the ACCC's final decision on Telstra's domestic PSTN originating and terminating undertakings;
- ❑ the enactment of amendments to the *Trade Practices Act 1974*, which *inter alia* provide for additional competition monitoring by the ACCC;
- ❑ the release of the ACCC's draft *Record Keeping Rules for the Telecommunications Industry*; and
- ❑ the release of the ACCC's final Local Call Inquiry report, indicating the ACCC will declare four services: an unconditioned local service, local PSTN originating and terminating services and local call resale.

This submission follows the ACCC's submission to the Productivity Commission's Discussion Paper on International Telecommunications Regulation, where the ACCC outlined its telecommunications functions and responsibilities, and the application of the Trade Practices Act and *Telecommunications Act 1997* to international telecommunications operators.

The submission is structured as follows: the next part discusses telecommunications competition monitoring and reporting by the ACCC, Part 3 outlines the unacceptable international conduct provisions. Part 4 sets out the recent decision by the ACCC on Telstra's PSTN undertaking, and interconnection charging issues relevant to the Position Paper. Finally, Part 5 discusses the definition of Internet peering.

¹ The three reports can be downloaded from the ACCC's website (URL: www.accc.gov.au).

2. Telecommunications competition monitoring and reporting by the ACCC

The Productivity Commission proposes that:²

The ACCC consider extending the scope of its annual report on telecommunications charges paid by consumers to include prices paid for dedicated lines and data services, and to include information about the underlying costs making up the elements of international telecommunications services.

The ACCC considers telecommunications data collection and related research to be an important element in telecommunications regulation:

- to facilitate access pricing determinations and related interconnection issues;
- in anti-competitive conduct investigations; and
- to aid the analysis and evaluation of telecommunications regulation.

Developing detailed telecommunication service monitoring is a comprehensive task, requiring (in the absence of significant resources) an incremental approach to data collection.

Prices paid for dedicated lines and data services

At present, the ACCC is required to monitor and report, as soon as practicable after the end of each financial year, on charges paid by consumers for:³

- (a) listed carriage services;
- (b) goods for use in connection with a listed carriage services; and
- (c) services for use in connection with a listed carriage service.

In accordance with this provision, on 13 January 1999, the ACCC presented a report, *Telecommunications charges in Australia*, to the Minister for Communications, Information Technology and the Arts, which:

- examined the standard prices charged by Telstra between 1992 and 1998 for the majority of its price capped services;

² Productivity Commission (1999) '*International Telecommunications Market Regulation – Position Paper*', at p.86.

³ Section 151CM of the *Trade Practices Act 1974*.

- compared the price of Australian telecommunications services to similar services in comparable countries; and
- recommended an appropriate framework for future price monitoring.

In discussing the last matter, the ACCC noted that it intended to progressively extend price monitoring to a number of additional carriers and services. In extending price monitoring, the ACCC will assess whether the particular services are relatively important, have few or no substitutes, and/or are the subject of particular policy concern. As part of this assessment, the ACCC will consider the extent to which leased lines and data services meet these criteria.

Developing a future reporting framework will depend on Ministerial determinations under new sections 151CMA and 151CMB of the Trade Practices Act. These new provisions, enacted as part of the July 1999 amendments, require the ACCC to monitor and report to the Minister on such matters relating to competition in the telecommunications industry as are specified in a written determination made by the Minister. Reports can be tabled in Parliament or confidential, and can be made at regular intervals as specified by the Minister. The Minister has not, as yet, made any determination under the provisions.

Information about underlying costs of international telecommunication services

In April 1999, the ACCC released draft *Record Keeping Rules for the Telecommunications Industry*, which will facilitate the ACCC's competition regulation of the telecommunications industry by providing cost information of relevant carriers and carriage service providers. The draft Record Keeping Rules are more comprehensive than the Chart of Accounts and Cost Allocation Manual (COA/CAM) reporting system, which the ACCC currently collects.

The draft Record Keeping Rules propose the collection of detailed financial and usage information for both wholesale and retail services, including wholesale international long distance (non retail specific costs for providing international calls originating either within or outside Australia) and wholesale international leased lines (non retail specific costs for providing all non-switched leased capacity to/from a point outside Australia's territorial boundary).

The July 1999 amendments also provided for the ACCC to make directions requiring carriers or carriage service providers to prepare reports containing record-keeping information,⁴ and for the ACCC to disclose or require the disclosure of information kept under the record-keeping rules.⁵

⁴ *Ibid*, section 151BU.

⁵ *Ibid*, sections 151BUA, 151BUB and 151BUC.

3. ‘Unacceptable conduct’ by international telecommunications operators

Investigations under the unacceptable international conduct provisions

The Productivity Commission states that there have not been any complaints under the unacceptable international conduct provisions of the *Telecommunications Act 1996*. Rather, as noted by the ACCC in its submission to the Productivity Commission’s Discussion Paper on International Telecommunications Regulation, the ACCC has not undertaken any significant investigations of potential unacceptable international conduct.

It has, however, received a complaint under the provisions from Telstra, who alleged that the monopoly international carrier in Tonga, Cable & Wireless Tonga, refused to continue a direct bilateral relation with Telstra preferring instead that Telstra route all calls to Tonga via Cable & Wireless Optus. Telstra alleged that this may provide Cable & Wireless Optus with significant market power in relation to calls to Tonga. However, Telstra did not provide any substantiation of the assertion after a further request for information by the ACCC, and it is presumed the parties resolved any differences via commercial negotiation.

Remedies under the unacceptable international conduct provisions

The ACCC notes the Productivity Commission’s comments that:⁶

if the Australian provider does not do as directed by the ACCC, the agreement it has with the international telecommunications operator becomes unenforceable. This means that there are no pecuniary penalties for breach of the rules.

This is an incorrect conclusion. The *Telecommunications Act 1997* includes in the standard licence conditions that a carrier must comply with the Telecommunications Act.⁷ Section 570 of the Telecommunications Act imposes pecuniary penalties for a breach of a licence condition. Section 571 authorises the Minister or ACCC (but not the ACA) to bring an action for pecuniary penalty where there has been a breach of the licence condition relating to Rules of Conduct.

The ACCC notes the Productivity Commission’s comments:⁸

The Government consider making the provisions of the Rules of Conduct for international telecommunications operators more explicit. This could include: ... extending the range of possible remedies against *established* unacceptable conduct by foreign monopoly providers to include the targeted and limited application of parallel accounting and proportionate return requirements.

⁶ Position Paper, at p.51.

⁷ See section 68 and Schedule 1 of the *Telecommunications Act 1997*.

⁸ Position paper, at p.86.

Two points need to be made in respect of this statement. First, the Rules of Conduct cannot directly regulate the behaviour of international telecommunications operators, as their activities are not within Australian jurisdiction.⁹

Second, the Minister has made Rules of Conduct which permits the ACCC to direct a carrier or carriage service provider in writing to:¹⁰

- make an agreement with an operator on specific charges for any international service dealt with under the agreement; or
- make an agreement with an operator in relation to allocating all or part of the operator's telecommunications traffic to carriers or carriage service providers in a particular manner; or
- act in its dealings with an operator in a particular manner to prevent, mitigate or remedy unacceptable conduct engaged in by the operator.

The Commission's view is that these rules already provide scope for the application of parallel accounting and proportionate return requirements if necessary. Accordingly, the Productivity Commission's suggestion (as quoted above) appears to be redundant.

4. Access to International Telecommunications Networks

This chapter summarises the ACCC's recent final decision on Telstra's PSTN undertaking, and addresses specific comments made in the Productivity Commission's Position Paper on estimating network costs (specifically, estimating Point of Interconnection costs, pricing of interconnection charges and treatment of the access deficit).

ACCC's final decision on Telstra's PSTN undertaking

On 24 June 1999, the ACCC issued a final decision on Telstra's PSTN originating and terminating access undertaking (ie for interconnecting to its network to provide international and national long distance calls). The ACCC's final decision is to reject the undertaking on the basis that the non-price terms and conditions are not reasonable. For example, the undertaking provides opportunities for Telstra to reject applications and to suspend services to access seekers on the basis of Telstra's reasonable opinion of matters such as credit worthiness. This would provide Telstra with significant

⁹ See the Explanatory Memorandum to the *Telecommunications Act 1997* and the Minister's Explanatory Statement to the *Rules of Conduct about dealings with international telecommunications operators No. 1 of 1997*.

¹⁰ Paragraph 8 of the *Rules of Conduct about dealings with international telecommunications operators No. 1 of 1997*.

discretion and create uncertainty for access seekers. The undertaking also imposes obligations on access seekers that are not imposed on Telstra's own operations.

The ACCC's preliminary view (in its draft decision) was that the cost of providing the services was 2.02 cents per minute. As a consequence of further analysis by the ACCC and consideration of industry comment on the draft decision, the ACCC now estimates that the efficient cost of providing these services in 1998/1999 is between 1.73 to 2.53 cents per minute. The major reasons for this change are new estimates of Telstra's trench lengths, revised assumptions regarding the level of trench sharing with other utilities and changes in the estimates for operating and maintenance costs of the Customer Access Network. The range in the cost estimate is largely due to varying estimates of Telstra's trench lengths.

While it is not necessary for the ACCC to specify an exact price that it considers reasonable for the purposes of assessing the undertaking, it is establishing a consultancy to provide an independent estimate of Telstra's trench lengths. This will reduce current uncertainty and be a significant input into the ACCC's consideration of any future undertaking, or relevant arbitration.

The costs calculated by the ACCC in the final PSTN undertaking decision include a contribution to Telstra's access deficit; that is, the shortfall that Telstra incurs because of line rentals being less than line costs. The Government recently announced changes to the retail price control arrangements, which apply from 1 July 1999. While the ACCC could not determine the likely magnitude of any reduction in the access deficit because of the limited time from the decision on the retail price control arrangements to the final decision on Telstra's undertaking, the ACCC's preliminary view is that Telstra now has considerably greater freedom to rebalance its line and call charges, and therefore the decision is likely to have a not insignificant effect on the size of the access deficit.

The ACCC is undertaking further work on the effect of the retail price control arrangements applying from 1 July 1999, which is discussed further below.

Point of Interconnection costs

The ACCC notes the inclusion of Cable & Wireless Optus' comments in the Position Paper that interconnection pricing does not reflect Point of Interconnection (POI) costs, as a carrier with a smaller number of POIs will pay the same interconnection charge as carriers with more POIs, despite an apparently higher cost of interconnection.¹¹

Telstra's undertaking only covers interconnection for services terminating or originating on a POI within the same call collection area (CCA) as that POI. That is, if a call is to terminate or originate in a different CCA to that in which the access seeker has a POI, the undertaking charges won't apply. Calls originating or terminating in a different CCA require an additional transmission component which results in a higher charge than standard interconnection rates for calls originating or terminating in a CCA

¹¹ Position Paper, at page 53.

where the access seeker has a POI. Accordingly, an access seeker with only one POI is likely to face larger access charges than one that has a POI in all 66 CCAs.

Level of estimated interconnection charges

With regard to Cable & Wireless Optus' comments that the interconnection charges are overly generous, the ACCC notes that Cable & Wireless Optus base their comments on an estimate of the world's ten best practice carriers pricing interconnect at around 1.2 cents per minute. The ACCC believes, however, that there are a number of problems with the Cable & Wireless Optus comparison.

Firstly, the ACCC is cautious in interpreting any international comparisons because of the need to take account of Australian specific factors such as population density and population size. Further, the costing methodology used as a basis for these estimates can vary between countries.

Secondly, the ACCC believes there are flaws in the adjustment Cable & Wireless Optus make to take account of the different indirect taxation arrangements in different countries. That is, Cable & Wireless Optus have converted the charges in each country on a Purchasing Power Parity (PPP) basis *and* has adjusted for Value Added Taxes (VAT) for overseas countries. The effect of differences in VAT rates between countries is already taken into account in the PPP conversion (for example a country with a higher VAT rate would have a higher general price level) so to adjust for VAT effectively double counts for VAT differences.

Finally, most of the carriers in overseas countries have already significantly rebalanced their line and call charges, whereas retail price restrictions have restricted Telstra's ability to rebalance which, as noted above, leads to an access deficit. In the United States where an access deficit remains, the access deficit contribution may only be included in the call **origination** rates. Therefore, Cable and Wireless Optus' analysis, which appears to consider United States' call **termination** rates, does not always include the access deficit contribution where it exists.

If access deficit contributions are taken out of the interconnection charge, estimates of the range fall to between 1.32 and 1.42 cents per minute (from ACCC estimates that the cost of such access should lie somewhere in the range of 1.73 to 2.53 cents per minute).

Treatment of access deficit

In Box 4.2, the Productivity Commission discusses the ACCC's approach to assessing telecommunications prices.¹² In the middle paragraph of this box, the Productivity Commission comments on the ACCC's treatment of access deficit issues. The ACCC considers that the last sentence of this paragraph would better express the ACCC's view if it were reworded as follows:

The ACCC recognised it would be more efficient for the access deficit to be eliminated by rebalancing line rentals to costs rather than funded through call charges. However, given the

¹² *Ibid*, at page 39.

price controls existing at the time, the ACCC considered an access deficit contribution was needed to allow Telstra to recover its costs of the customer access network.

With regard to Global One's comments that inbound settlement payments should not be used to recover the costs of the CAN, some comment should be made on the appropriate way to recover costs.¹³

Ideally prices should be rebalanced such that non-call related costs (such as line costs) are recovered directly from non-call related revenues (such as line rentals). Where this is not possible because of the existence of price controls, Telstra needs to recover these costs from its call charges. A number of arguments have been put forward on how to incorporate an access deficit contribution in call charges. These arguments may still imply that inbound settlement payments should include an access deficit contribution.

Some parties have argued that as Telstra is enjoying monopoly rents on its local call pricing, these should be used to fund an access deficit. That is, any excess profits being made on services supplied over the customer access network should be used to offset any deficit on line rentals on the network. Only if these excess profits are less than the access deficit should Telstra be able to receive an access deficit contribution from access seekers.

Alternatively, a form of Ramsey pricing may be appropriate whereby a greater access deficit contribution is levied from those services with a lower price elasticity of final demand. In this instance, access charges for international calls would include a lower access deficit due to the relatively higher price elasticity of final demand. However, this approach may be difficult in practice due to the need to measure price elasticities of demand.

Another alternative is to adopt a broad based approach whereby all services operating across the customer access network make the same per unit access deficit contribution. An advantage of this approach is that all users contribute to the access deficit, and therefore the contribution from any particular service is minimised. In this case, the access deficit would be calculated on a per call or per minute basis.

As noted above, the ACCC is currently considering how it treats the access deficit, and is yet to reach a final view on its preferred approach to the access deficit contribution.

¹³ *Ibid.*

5. Definition of Internet peering

The ACCC notes the Productivity Commission's definition of Internet peering in section 3.5 of the Position Paper:¹⁴

Under peering, providers agree to accept all Internet traffic addressed to their network without any charge. Such agreements are based on a 'sender keeps all' (SKA) settlement.

However, Internet peering arrangements can take place within a variety of models, of which sender keep all (SKA) is only one possible method of peering.¹⁵ There are three widely recognised forms of peering. These are:

- **Sender keep all:** where traffic is exchanged between networks at no cost.
- **Bilateral settlement:** where two networks share the cost of interconnection, negotiate a settlement rate and make payments based on the nett volume of traffic. The settlement rate may be different depending on which network carries the most exchanged traffic. This model is similar to existing international interconnection arrangements for voice and other data telephony.
- **Multilateral settlement:** where ISPs pay their own interconnection costs to an Internet Exchange point (IX) and exchange traffic on either SKA or a bilateral basis.

¹⁴ *Ibid*, at page 33.

¹⁵ See G Huston (1994) 'Internet Service Provider Peering', at URL: <http://iepg.org> under Work in Progress, Peering Models for ISPs.