



**TRANSCRIPT
OF PROCEEDINGS**

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PRODUCTIVITY COMMISSION

**REVIEW OF TELECOMMUNICATIONS SPECIFIC COMPETITION
REGULATION**

**PROF R.H. SNAPE, Deputy Chairman
PROF M.C. WOODS, Associate Commissioner**

TRANSCRIPT OF PROCEEDINGS

AT SYDNEY ON TUESDAY, 15 MAY 2001, AT 9.11 AM

Continued from 14/5/01

PROF WOODS: Welcome to the second day of the draft report hearings for the Productivity Commission inquiry into telecommunications specific competition regulation. I'm Mike Woods and I'm the presiding commissioner for this inquiry. I'm assisted in this inquiry by Richard Snape, deputy chairman of the commission. The draft report was released on 29 March this year. It covers Part XIB and XIC of the Trade Practices Act and various parts of the Telecommunications Act. The commission is requested to aim to improve the overall economic performance of the Australian economy in its considerations. A copy of our full terms of reference is available outside the room.

I'd like to reinforce a point that we have made consistently through the inquiry, that this is not just a stocktake of the here and now; it is about setting the regulatory framework for the medium-term future of telecommunications in Australia. I'd like to express our thanks to those people and organisations who have contributed to the inquiry to this point, including those who have responded to our draft report. These hearings represent the next stage and will be a valuable input into the finalisation of our report. The final report will be provided to government by or before 22 September this year.

I would like these hearings to be conducted in a reasonably informal manner but I remind participants that a full transcript is being taken and will be made available to all interested parties. It will be posted to our Web site within three days of each of the days of hearing. At the end of the scheduled hearings for the day I will provide an opportunity for any persons present to make a brief oral presentation should they wish to do so. I'd like to welcome to today's hearing our first participant from Paul Budde Communication Pty Ltd. Mr Budde, could you please for the record state your name and your position.

MR BUDDE: My name is Paul Budde. I am the managing director of Paul Budde Communication.

PROF WOODS: Thank you very much and welcome. Do you have an opening statement that you'd like to make?

MR BUDDE: Yes. What I would like to state up-front is that I was disappointed with the draft report when it came out, because I think telecommunications is becoming a very important part of our society and of our economy. The reason why we have this inquiry, the reason why we have regulations, the reason why the government is involved, the reason why the rural community is in uproar, is a clear indication that telecommunications is more than having a chocolate factory or something like that. It's critical to our society.

In order to put things into perspective, what's happening within the industry and the various players and the various markets and various products that are regulated or not regulated - we'll actually have to see why on earth we are doing this.

Now, we are doing this because if you go back, let's say 40 to 50 years to the time of our parents after World War II, et cetera, then you see an enormous effort from all the countries around the world to put a lot of effort into education. Our parents suffered quite a lot to make sure that their kids could go to school and universities and high schools and what have you. Education was seen by our previous generation as a key sort of element in our society.

We have over the last 40 to 50 years created a society of people who are different than the society of our parents and the society before them, who were struck by the Great Depression and what have you. Education has formed us more than anything else over the last 40 to 50 years and therefore we have a different look at the world. We have a different look at ourselves. We see ourselves differently. We are no longer a society that's only interested, as individual people, in money. We are more interested in learning things. We are interested in enjoying life. We are interested in communicating with different people and different communities and different countries. We travel and things like that. That's all part, because of the fact that we've put a hell of a lot of resources in education and getting people beyond just looking for a shelter above their head and getting some food on the table.

As this has been progressing through the 60s, 70s, 80s, 90s, et cetera, we are now seeing that we as people have different values - well, not different values; our values have changed and we are looking at lifestyle, we are looking at culture, we are looking at emotional values, we are looking at family values and things like that. I think the Sydney Morning Herald produced a report about the problems that women face when they have all these double jobs and they actually want different things out of life than what you get. There's really a cry-out for all the things in life. That's where I think telecommunications can play a key role.

Telecommunications can assist us in enhancing our lifestyle, in creating a better society, in exchanging information with other peoples, having access to people who have similar views that we can exchange - that we like to talk to but also that we like to trade with. That makes it easier for us to find markets around the world. Through this sort of situation we can make more contacts. Actually, with telecommunications it can be quite personal, despite the fact that you don't see people. Quite often emails between people are far more revealing than a plain conversation. People dare to be a little bit more emotional and a little more personal in that sort of information.

We see an increase in value that we put on an infrastructure that facilitates what I call an e-society. It's a knowledge based society where we can have access to information wherever it's published - in Moscow, in Los Angeles or in Beijing, in Canberra, or whatever. We can have access to information and we can use that information ourselves and make decisions ourselves, rather than in the past where we had to rely on the media or on politicians or on the ministers in the church to make the decisions for us, because they were actually the only people who had a bit of an overview, however biased these people were.

Now we can take control of our own lives, our own minds, and I think that's where telecommunications fits in very well. The fact that people like S11 and M1 sort of protestors are around is also an indication that this - it's similar to the sort of student revolts that we saw in the 1960s, et cetera, where young people get on the streets. We might not always agree with their violence but a lot of the things that they express specifically five or 10 years later on people start to realise, "Gee, you know, the hippies in the 1960s were right," or "These students in Paris in the 1970s were right," et cetera. I think with S11 and M1 we also will see things like that.

We will have to start learning that there is more in life than just money and wealth, as in the sense of monetary wealth. There's other wealth that we've gathered over these years and that is as valuable, if not more valuable, and I think that's where we have to see telecommunications going. What I would like to see, if we can establish it, is that we would like to use telecommunications as a conduit, as an infrastructure to get a better lifestyle, to get a better economy, and things like that.

That's what our vision should be, in how to look backwards. If you say, "Okay, this is what we want. How are we going to get there?" quite often a lot of the day-to-day problems are standing in the way of having this broader sort of vision and saying, "Okay, let's now - if we can establish that Telstra and Optus and the government and everybody else - that they all believe that we should have this sort of a facility where people have the choice, can use the infrastructure, how can we then work our way back and get the right sort of things in place?"

If you go back to some of the decisions that are discussed as we speak - you know, we saw the datacasting issue that has now been withdrawn - if the government had shown vision in 1996, and particularly the ABA with Peter Webb; if they had shown vision when they advised the government I think in 1996 to look at the broader picture rather than cutting all the little bits of pieces, then of course we would have a totally different outcome. If we had in 1994 - and once again, in 1996 there were people like myself who said, "Hey, guys, what are we doing?"

In 1994 people like myself and Mark Armstrong and other people, were standing there and saying, with the pay television regime, "Why on earth are you going to give these exclusive rights to the same people who own the telecommunications infrastructure?" The government in its wisdom said, "It's nothing to do with each other. Telecommunication is totally different from pay television. So yes, the same people who own the telecommunications infrastructure can own the pay television infrastructure. It's no problem whatsoever, if you look in the paper, you talk to Telstra, whatever." Now we've got a problem because now they're saying, "If we can't have exclusive rights to this, blah blah blah." They blackmail you again.

Again and again and again we fall in the trap that we forget to have a picture of where we are in four, five or six years' time. The picture now is very, very clear that

there is no absolutely no difference between broadcasting as an access technology, cable television as an access technology, satellite based technology as an access technology and telecommunications as an access technology. Who cares about the fact, if you are going to deliver high-speed Internet access via a wheelbarrow, via the broadcasting signal, via the telecommunications signal, via the electricity wire - who on earth cares? People want high-speed access to the Internet. People want video based documentaries or movies or entertainment or whatever. That's what people want. How it gets delivered is totally irrelevant to the users. If that's the case, why on earth do we have then different regimes that operate differently and have different rules and regulations for the whole thing? So that is a key in that respect.

If we then narrow it down, so I'm going down from the division, the infrastructure sort of freeways, highways, superhighways that we have as access technologies - let's now focus then on the telecommunications sort of area. It has become very, very clear, despite the best efforts of ministers and politicians and the industry itself, that there's no way in the world that we will have a second telecommunications network in Australia. There's absolutely no way in the world that that will ever, ever happen. It's too costly, it doesn't make sense, so we have to scrap the idea that has been brought forward by ministers, politicians and Telstra in particular that we have to keep prices high on the current telecommunications infrastructure because that would stimulate others to actually start putting infrastructure in place.

Now, that's not going to happen and the people who are going to suffer most from it are the rural and regional people in Australia. We already know that. It's very visible. It's very, very clear. If that's the case and we know that there's no more infrastructure coming, why on earth aren't we then saying, "We have a broadcasting signal, we have cable television services in certain areas, we have mobile systems. Let's make sure that all of these systems can compete with each other in order to bring the right sort of services to people." If a broadcasting company can deliver Internet to people cheaper or better - or better quality or whatever - then it can compete with Internet delivery via a telecommunications network or via a cable television network because the end product for the user is exactly the same. There might be differences in quality, there might be difference in money, there might be difference - but that is exactly what we want in a competitive environment.

So if we can't use the telecommunications network in isolation to create competition, then we have to finally open up our minds and say, "Listen, we have to look at access technologies. Which are the access technologies that will lead us to this e-society, to this e-economy and things like that?" and then make our way forwards in that particular area. Once again we are the odd one out in the world because the rest of the world is making sure there is competition in Europe and the United States between the cable television networks and between the telecommunications network. If we would have that situation in Australia then we wouldn't have Telstra complaining about the fact that they didn't want to upgrade the digital network because, if they're not going to upgrade the digital cable telephone

network, then their competitors on the other side would actually have an advantage in the market.

But here Telstra can do what it wants because it owns everything, and the government in its infinite wisdom is going to treat these two access technologies as totally different technologies. Therefore, you don't get any competition out in areas specifically outside metropolitan Australia because there is no competition in access network. So unless we start creating competition in access networks, we will always run behind in this country and we will not be able to give our citizens the same sort of services to this e-society and e-economy. I don't want to go into details with that because everybody can fill in what that means. It means telemedicine. I saw this morning on television a fantastic program about what you can do with telemedicine.

These are all real advantages. I'm not just talking about money, I'm talking about real advantages for our society that you can start creating once you have true competition available in that access regime. These access networks, of course, need to be regulated in one way or another because the owners of these networks are so powerful and have such a monopoly that they have not the best of society or the best of the economy at heart but they have their own purses at heart. I'm not saying that that's wrong but that's the reality. If that is the case, then we as a society will have to find out if having a communications network is more important than having a chocolate factory. If we think that is the case, then we want to have a say as a society in what sort of networks there should be in order to advance our society in the way I described before.

We will have to make sure that there should be open networks. That is, these networks are available to organisations and people who want to put content and services on the network, and that is eventually where the real competition will starting taking place. As I indicated before, people are not interested to know how you're going to deliver services. You might want to do it in a wheelbarrow, as I mentioned before. The access technology, from an end user's point of view, is totally irrelevant in the decision-making process.

The end user is making a decision based on the service that's provided on top of the network, so if you create competition on top of the network, then people can make a choice and can say, "I like this education program better than I like that education program," rather than that you have the access provider who says, "No. We have an exclusive deal with this educational organisation and this is the educational organisation who's going to provide all the education over this network." I think that's totally wrong in the society that we at this moment have and that we are increasingly going to develop further. We do need to have rules and regulations to make sure that we've got plenty of services over the network, make them available over the network.

Eventually this will happen automatically. If you look at BT in the United Kingdom, they've made such an enormous amount of stupid mistakes. They've spent

£30 billion in spectrum and, of course, the whole thing is worth approximately 1 or 2 billion. So they've got a financial problem and this company now will have to find ways of actually getting back into shape, and one of the options that they then have is opening up the network, because if you get more wholesale companies on it, you get more money in, et cetera. You lose your control but you get more services on it. That might happen automatically if Telstra were to collapse, but I would not like to see that sort of a situation.

It's too important, for a reasonably small country populationwise, for Australia to make sure that we have a strong and powerful Telstra - I would be very much in favour of that - but it should be in the role of being the infrastructure provider and let other people use their networks. It doesn't really matter if it's a cable television network or if it's a telecommunications network. Of course there will be tension. There's no doubt whatsoever that the monetary pressure - the shareholders' value as they like to call it within Telstra - to protect the network can clash with the sort of needs that we as a country want, but I would very much like to propose that they follow the European model - they only started deregulation in 1998 and they are now roughly two or three years ahead of us; we started two or three years before them - by very simply saying that if we as a society, through the ACCC, through the government, through reports such as the Productivity Commission, come to a conclusion that certain things are necessary in the telecommunications world to progress to this e-society and we therefore put certain regulations and conditions on networks, then they should be implemented immediately.

So if after exhausting discussions and whatever the ACCC comes to a conclusion that a particular service will have to be declared or a network has to be opened, then it should be implemented straightaway. That's happening in Germany, that's happening in Holland, that's happening in Denmark; that's happening in most European countries. The company that's then affected by it - as, for example, Telstra - would then get the opportunity to appeal that in two years' time. So you get a two-year period of time when the company can come back and say, "Listen, the decision you made was wrong," and then you can have certain regulations on how to solve that.

I can tell you from the 80 bigger decisions that have been made in the European Union, according to my understanding, none of them has been challenged after two years by the incumbent. After a year there were some doubts about certain things, but what happened, for example, was that certain prices were set in 1998. Then there was a lot of uproar, similar to what we have here in Australia. By the year 2000, the prices that were set by their regulator in 1998 were actually too high for the situation in the year 2000.

The changes are happening so rapidly in telecommunications that if you have a two-year grace, then you immediately find that most of the issues that were very very hotly debated at the time had gone away over a two-year period. The countries in charge of course then had the advantage of having that early start with the new prices

or the new open networks or whatever the decision that was made by the regulator. That is the major stumbling block in Australia - that none of the decisions - we are still working on the Labour government's regulatory environment for 1992. We are not working on the 1996 Telecommunications Act because none of that stuff was implemented. None of the important stuff has been implemented dating back from that situation.

I personally am very strongly opposed to the 1996 legislation because I indicated self-regulation is not going to work and I compare that with this one big fat elephant and 50 mice running around. Guess who wins in the self-regulatory debate. A half-year ago, something like that, I repeated that and it drew a very very strong personal attack from the minister on myself, and it clearly indicates how wrong we have been by thinking that self-regulation is going to make it. We had the datacasting situation; we lost four years. We had the Telecommunications Act; we are losing five years. How much further do we want to go as a country when we have these four or five-year delays with every decision that we are going to make in the telecommunications area?

We have to speed up the sort of processes that this government and the bureaucrats have put in place, because otherwise we are always running four or five years behind in our society. Things are changing so rapidly that we cannot afford to have four or five-year delays. If you look at broadband, Korea of all places, 57 per cent broadband penetration; America, 12 to 13 per cent broadband penetration; Hong Kong, Singapore, close to 10 per cent broadband penetration; Europe, 6-7 per cent broadband penetration; Australia, 1.5 per cent broadband penetration. That's the picture that we have and if you are always running behind then we're doing a disservice to our e-society and to our e-economy.

I really would like to see a speed-up of the process. You can only do that if you know what the vision is. Where do you want to go? If you know where you want to go, then you can put strategies in place, like regulations and whatever, and you can start doing things like that. But what we are doing now in this country, we look at the rules of the situation. Today there will be another announcement - \$5 million here, \$10 million there, \$50 million there. That's not a vision. That's not working from a strategy. That is bushfire brigade work. What I would like to see is a visionary sort of situation: where do we want to go as a country, put strategies in place, and then once you've put strategies in place have them backed up with proper regulations and execution straightaway, rather than five, six years down the line. That's where I will stop.

PROF WOODS: Thank you, Mr Budde. We appreciate your contribution to our inquiry and our thinking. We've read other of your works, where you identify that broadband would be your crusade for the year 2001, and other writings of yours we have taken note of as part of the background to this inquiry. I would commend to you the transcript of the evidence that we've been receiving during these hearings into our draft report, where we have been asking others - and I should acknowledge,

at your prompting in large part - to expand on their vision as to how they see regulation of telecommunications fitting into achieving a broader telecommunications environment for Australia to achieve some of those matters that you raised in your presentation.

So I commend those transcripts to you, and also our overview of the draft report, which also brings together a number of the threads that come out of this inquiry. As you'd appreciate, there is the necessity to deal with the detail and to ensure that the detail supports the vision and, therefore, naturally the body of the report addresses those matters of detail, but our overview is the vehicle by which we can demonstrate how they collectively work to achieve the sorts of outcomes that are appropriate. Thank you for that contribution to our inquiry.

I'd appreciate some views, as a participant in this industry, of material that was put forward by Telstra. When we had them at our first round of hearings last year, they made considerable mention of accounting and operational separation that was taking place. We asked them for an update at these hearings, and they didn't seem to have made a lot of progress - is my judgment of it. The transcript stands, and you can - as all can - read what Telstra said and our questioning of it. What would be your impression? If you look at Telstra wholesale and Telstra retail, do you see that the operation of I think you used the phrase "elephant" in its current format it can contribute to achieving the outcomes that you were setting out in your introductory comments?

Before you do answer, I'd draw your attention to our terms of reference which require that the review not encompass the structural separation of Telstra in line with government policy on this issue, but of course that doesn't extend to accounting and operational separation.

MR BUDDE: What you see happening is that Telstra, and most of the other incumbent carriers around the world, are based on the so-called vertical-integrated business model, and that means that they want to be everything to everybody. That vertical-integrated model, of course, is based on the fact that you've got a monopoly, because if you've got a monopoly you can push 15 things down people's throats very easily based on the monopoly. If you had to compete on every one of these 15 issues, then across the world you will see that 50 to 70 per cent of the customers are actually walking away from the incumbent once you get a choice. So there is a desperate need for an incumbent who obviously is not able to maintain its market presence or its market share through normal competitive customer service or whatever. The only way for them to actually maintain the high level of penetration in the market, apparently here, is through this vertical-integrated model, where you can push as many products as possible down people's throats - basically by forcing them.

The vertical-integrated model is crumbling in a number of cases. I've already alluded to the BT model which is crumbling because of financial pressure. In more

competitive markets, what you see is that automatically the market forces you to change. The reason why is that normal consumer behaviour would be that you want a particular product. You then actually look for a product based on your personal specifications. The specifications might be, "I want the best quality," "I want the lowest price," or whatever, but you put in the parameters on what you base your decision to buy a product of service.

Once you are able to do that in the telecommunications environment, then obviously a lot of people will actually look for specialists. If you are a Vietnamese immigrant here in Australia, it's quite possible that you are going to make a lot of calls to Vietnam. If there is a service provider who is specialising in that area, it's highly likely that you would like to use the service of that company if they provide the right sort of services, so you would go to a specialist. If you are a medical organisation and you would like to become involved in telemedicine and link hospitals and doctors and whatever together, most likely you are going to look for a specialist who can help you in that sort of area.

Currently Telstra wants to do all of that and be a vertical-integrated company. If your goal in life is to be a vertical-integrated company, then of course it becomes very very difficult to have these separate sort of issues of wholesale and retail. For example, I was talking to the Country Wide people of Telstra, who I respect very highly, and they are coming across a lot of problems, and the wholesale division is in a similar sort of situation whereby they said, "We need to be separate. We can't run our show. We're constantly running against this brick wall. We would like to move forward," and these are people within Telstra themselves who are coming across these sort of problems that you see happening within the organisation.

PROF WOODS: Did you say the same applies to wholesale?

MR BUDDE: Absolutely. The same wall applies to wholesale. Of course the people within Telstra, they would not publicly say things like that because they would be sacked the next day. So you have to be very careful as a Telstra employee what you tell a person like myself. But at the same time I've got the distinct impression that that is holding back several of the groups within Telstra, because what happens in a vertical-integrated company? Yes, there is a nicely separate wholesale division and there is a separate Country Wide division and a separate this division and what have you. In the end, all decisions are coming back from the top level and they are saying, "Oh, my god. We want a vertical-integrated company. Sorry, what you want not possible," because it clashes with what happens with the overriding goal that the company has, being a vertical-integrated company.

So while they might pay lip service to the fact that, "Yes, there is a nice division and a very nice manager in charge," who is doing the right job - and I'm not saying that a Rosemary Howard or a Doug Campbell is not doing the right things. They're excellent people, they're fantastic people, but they have to live within the limitations of the Telstra structure. What's a vertical-integrated company? As long

as you stand by your vertical-integrated company, it will never ever be possible to have really separate divisions because the ultimate thing of having separate divisions is that there are separate companies.

Everybody knows that if you really want to grow a market, and what do people do, is split up companies. We've done it for the last five years. I don't know how many hundreds of thousands of companies have been split up from large organisations because that gives them the opportunity to grow in that market and do something for themselves. That should be happening within Telstra as well, if you want to do things like that.

Ultimately, the changes that you see happening with BT - I've mentioned AT&T; KPN in the Netherlands is exactly the same situation; Telefonica in Spain; Telecom Portugal - all of these companies are now looking at splitting themselves up and hiving off areas because of that reason. If you are in the mobile market where there is competition, you will have to make the decisions on your own. You can't constantly go back to the board because otherwise your competitors are going to kill you.

PROF WOODS: Thank you very much. My next line of questioning heads into digitisation and access pricing and the like. Professor Snape, do you want to ask something more - - -

PROF SNAPE: Yes. Thank you very much for that. I'd like to pick up a line which was put by AAPT yesterday and just bounce it off you, if I may. In our draft report we have been speaking about the risks of access pricing being too high or being too low and, not only in this draft report but also in the position paper on Part IIIA of the Trade Practices Act, we refer to those risks as being rather greater for pricing too low than for pricing too high, the idea being that you're worse off if the investment doesn't occur. It means you never get the facility. AAPT were emphasising the other way: the risk of the access prices being too high, that you would get duplication of investment. You'd get overinvestment.

They were saying that that would be in fact a greater risk. As I understand their reasoning, it would be non-viable. The facility would then be sold or whatever and it would be on the second-hand market and the price would be low and it would in fact make the other non-viable. They were making that sort of point. Have you given thought to the risks and where you would come out in that? I'm linking this to your comments before; that you were saying that in your opinion there would only be one telecommunications network. I might also ask, following up, what precisely you mean by that, but perhaps we'll follow up that one.

MR BUDDE: Yes, I'll do that. To clarify that first, I'm talking about the copper cable telephone network that we've got now across the country that's connecting basically every village and community in Australia.

PROF SNAPE: It's the local loop that you're talking about.

MR BUDDE: The current local loop and that is copper based.

PROF SNAPE: Sorry. What you meant by that is that there won't be a duplication of copper based local networks?

MR BUDDE: Absolutely, yes. I'll elaborate a little bit further on that. I'll explain to you the way it's going. Let's go back to your first question regarding prices. What you see happening in the telecommunications market so far has been two things. If you lower the prices, you bump up demand, so you see an increase in usage. If you look at data communication, this has been around since the 1960s and has been exclusively in the domain of only the top 500 corporate companies in Australia because the prices were so high that nobody else could afford that sort of situation. That changed through the Internet when suddenly prices were so low that everybody was using the Internet. If you now start looking at the data communications market, a \$3 billion market, the Internet market is going to surpass this this year. So within five years we are having a bigger market than we've built up over 30 years.

The fact is that if you can bump up demand, even at the very low price of the Internet - I mean you can't go lower than the Internet price - you are creating a market within a very short period of time that is equal to, if not bigger than, the market that you've been protecting for the last 30 years. What I'm saying is, why on earth is everybody - the broadcasters, the telco companies - sitting there on their own little pie trying to protect it? Everybody forgets there's a huge big pie around it. If they share this with all of us, we can grow from the small pie - the \$3 billion broadcasting pie or the \$30 billion telecommunications pie- and we can move to a \$90 billion pie and everybody gets a much better share of the whole thing.

But we have to look at the bigger picture, and as long as everybody is trying to protect their own little turf, then of course nothing is going to happen. What I am saying is, if access prices are coming down, we stimulate demand. If we stimulate demand, then what will happen - and we see it happening in Korea, in America, and countries like that - is that if you open up the market, the first thing is access. The only thing that people want in a lot of countries is high-speed Internet access; the only thing they want. They don't buy anything else. Suddenly they're using high-speed Internet access and they find out, "Wow, I can download a movie. It only takes me five minutes to download. It costs me \$5. I'll do that." "Hey, I can now tap into this particular program" - education, documentary, whatever - and suddenly you start seeing that you create demand for other services that people initially didn't necessarily ask for but are going to buy.

So the access is a lever that you open the door with to generate more money, because once people have paid for their access, which should be low, then the next step is to buy a service. I come back to the statement I made before that eventually the competition will be on services, not on access. If you create low-price access, a

couple of things will happen. First of all, you start increasing demand. If you're going away from the telephone services - I hope that this inquiry is not talking about telephone services, because that's totally gone; we are talking about broadband nowadays.

If you start looking at broadband services, if you start opening up that particular market, people are going to download. If you just look at the Internet use after two and three years, most of these people are totally frustrated with the low dial-up access. They want more, they're educated, they know what they want, they move forward, et cetera, and they're frustrated. They can't get any further in Australia because there's no broadband facility available. Once you take that first step, after two or three years these same people will be the leaders in new services, et cetera.

If the telcos were clever they would understand that if you have low access you might suffer a little bit now with your profits, true, but you are opening the road, because our society that I've painted before is educated, is looking for lifestyle, et cetera. This society is ready to start buying services from your network and you start growing the pie and you can make more money. True, that won't be a vertical-integrated model. Telstra will not be able to dominate the \$90 billion market. It would be a crime if that were the case. It would be a disaster for this country if Telstra was the only company that could run the \$90 billion pie in the year 2010. We need to open it up, we need competition, we need that sort of a situation. So by having low access prices, the first thing that will happen will be more people going online. I predict that from 2005 onwards fibre to the home is back on the agenda.

PROF SNAPE: It is in Canberra already.

MR BUDDE: Exactly. You get examples already around the world - pockets where it's happening earlier - because the demand is going to be on the network to download specifically entertainment - and that's what the majority of us would like. We love entertainment. We like movies, we like theatre, we like all that sort of stuff. If it becomes available at affordable prices, we will use it. The reason why we're not using it is either it's not available, it's not affordable, or it takes forever to do things with. It's very user unfriendly. Once we've got that right, then demand will increase.

I'm not saying that in 2005 we've got fibre to the home; that might be a 10 or 15-year plan that will then start to evolve. But what you will see happening is that new infrastructure will have to be built. The current copper telephone network is totally inadequate. The cable television network is totally inadequate for these sorts of new services that we need for the next decade; perhaps not for this decade but for the next decade. So automatically, by creating demand, by having low access prices now, we do a couple of things. First of all, we finally unlock a lot of knowledge, a lot of services, a lot of activities, for our current society, for the people who are living in Australia now. We give them the services now.

At the same time we create a business model for the telecommunications industry where they will say, "Wow, there is demand. We can actually offer more services." Lots of companies would like to develop services - what I call a permission based service - over the network and start utilising the network. Therefore, by 2005 fibre to the home is back on the agenda and the first leading telcos will start looking at how they can implement that. I'm already talking to some of the electricity companies who are very seriously looking at fibre to the home in Sydney and in Melbourne, based on that plan of five years out from now. A lot of these companies are slow movers.

What you see happening is, you do an enormous favour to the society now by opening it up now, and at the same time indirectly you do the industry a favour because you start creating demand for new infrastructure, for new networks, for new investments in 2005. If you keep the lid on the access now, then the telcos will keep on telling us, "There is no business model for it. Nobody wants it." That's what they did for 30 years in the data communications market - "There's no business model for it" - until the Internet came around and the Internet clearly showed lower access will in the end mean higher revenues back to the people who invest in it.

PROF WOODS: It's certainly a very strong issue that we want to pursue - of how to provide a regulatory framework that encourages investment in facilities. That is a very high priority. Is it possible, however, that if prices are very low for the copper network, that a couple of things may occur? One is that it doesn't therefore allow viable business models for alternative communications networks, such as wireless, satellite, regional roll-outs by small players and the like, and that it's not generating sufficient cash to enable the copper itself to go through the progressive maintenance and upgrade processes that need to happen. I'm not talking about some middle pricing debate. I'm talking about very low pricing. Is there a danger at that bottom end of pricing that those could be some of the consequences?

MR BUDDE: No, absolutely not. The reason is that a couple of things will happen. At the moment we have a network that you can compare with the T-Ford model. If you only have a T-Ford model you can argue about price and what have you, but that's it. If you start using a T-Ford model and you're driving it mad, and at a certain stage people will say, "My god, this car is not good enough for me any more. I want a better car. I need the next model up." Then the market will come back, "Sorry. This is for \$5, but this is my product for \$10." If you start creating differentiation, people will say, "Listen, I've had this T-Ford model now and it did its job, but thank you very much, I will now move on. I'm more than happy to pay the \$10 now for access because I want high speed, I want security, I want this, I want that."

So you automatically - but if they're even on the \$5 model, nobody can experience and nobody will actually ask for this model because they're not even allowed to drive in this model. If you don't start somewhere, then you will never

ever get the next model. Look how many car models there are in the world. There must be thousands of them and why not one? There are thousands of different car models and somebody pays 500,000 for a car and another pays \$500 for a car. The same will have to apply to the access networks.

There might be clever entrepreneurs who come up with a network after you start developing this market and say, "Listen, there is a lot of demand for movies," or whatever, "I've got very nice specialised infrastructure that can deliver it for half the price that Telstra is doing over the fixed network." Fine, there's an opportunity. This guy will set up this particular network because he knows there is demand for this particular application. Go for it. So there will be a large number of new access technologies developed because it's totally impossible to even do - if you look at the year 2010, the current networks that we have can't handle more than 20 per cent of what we need in 2010. The current networks that we have - cable, satellite, telephone, whatever - can't handle anything like what we actually need in 2010.

That's why the NextGens of this world are pumping billions of dollars into infrastructure. They're not stupid. They know that things like that are going to happen and they are not going to concentrate on the local market, but they know that you need the freeways around the country that actually start collecting all the traffic that comes from these communities. You see that sort of investment going on, despite the fact that everybody is talking about bandwidth glut in the Pacific Ocean or whatever. New cables are rolled out, new cables are planned every day. These companies are not stupid. They know that we are going to get this enormous demand.

But we have to start somewhere, and we have to start at the \$5 model because you cannot go to people who don't anything about it - "No, sorry, we're going to start with the \$100 model" - because nobody is going to use it.

PROF SNAPE: So it wouldn't worry you if the access to the copper cable was regulated at a price of zero?

MR BUDDE: No. What I would say: no. I'll tell you why.

PROF SNAPE: No, it wouldn't worry you?

MR BUDDE: It would not worry me at all, and I think it might actually be going to happen. The reason is that I would love to have as many people as possible access the network. I want to sell the services. In the end the services that people are going to pay for - - -

PROF SNAPE: There would be no maintenance at all if it was priced at zero.

MR BUDDE: No, what will happen is what I call the business model - we are looking at business models. If I look about the markets, that we don't have enough

capacity, we only have 10 per cent of the capacity that we need in 2010, obviously the business models that we are having now are also totally inadequate - the business model we already alluded to, the vertical integrated system.

Let me paint you the picture of what's happening in 2005. I'm not going to 2010. We are building a telecommunications network that doesn't look like a telecommunications network any more. It looks like an IT network. So the telecoms of 2005 and 2010 are going to look more like the IBMs and the Hewlett Packards than they look like the current Telstras and AT&Ts, et cetera. We are building this gigantic local area network through Australia, so all of Australia will be one big computer network. On that computer network there will be gigantic data centres where all sorts of IT activities are going to take place. These are linked to CRMs, customer relation management systems.

Now, I'm the customer of Coles. I walk into Coles, do my shopping, and get out of the shop. Coles wouldn't have a clue that I went in. Coles wouldn't have a clue where I live, what I do, what my patterns are, or whatever. If Coles would know what I was buying, how my pattern would be, they could actually start providing me with some advice on making a shopping list, et cetera. But it's quite possible to say, "I don't want that." I give permission to certain companies and say, "Listen, to help me do my shopping, here is my list." I can tell the system that in a month's time I'm in the market for a new car and I want to spend X thousand dollars and the car has to be the colour red, or whatever. This goes into the system and I allow Ford and Holden and Toyota to come back to me and say - but after I bought the car, the last thing that I want is getting information from people, "I want to sell you my car." So I am in control and I switched off and said, "No, I've bought a car. Now I don't want any information."

PROF SNAPE: How are these networks all connected to each other?

MR BUDDE: These networks will initially start on the copper cable network. They will quickly move to the broadband network because what the Coles Myers, the Fords, Holdens and Commonwealth Banks of this world would like to do is establish one-to-one communication with me. We're going away from this broadcasting one-size-fit-all advertisement that absolutely nobody wants. We all go to the toilet and make coffees and whatever when the ads appear, so obviously we don't want it, but that's not to say that we don't want to have any information from all these companies who advertise, but we want the information that we are interested in. I'm interested in particular car tyres, then I'll let them know and they can come back to me; not that blurb in the air, you know, they've got car tyres. I'm not interested at that time.

So if you can establish a relationship between customers and suppliers and you create a marketplace in between, not a messaging system where advertisements are messaged to you without any - you know, you're not interested - no, a marketplace like we had 1000 years ago, where people came by to sell, feel and touch. That's

what you create. Based on that you build trust. Based on that you can start working on one-to-one marketing in communication with your customers. In a situation like that, by the end of this decade 65 per cent of all telecommunications costs in the residential market will be paid for by the companies, not by the users.

Only 35 per cent of the cost of telecommunications will be paid for by the users; 65 per cent by the market. The 65 per cent are Telstra's customers. Telstra should make the money from them. They shouldn't charge me for access. All these Commonwealth Banks of this world are more than happy to subsidise the access in order to make the communication sort of situation with me. The business model will change from that access model that we've got now. It will be that Telstra, AAPT and Optus will start talking to the Commonwealth Bank and to the thousands of companies around Australia: "How can you use our total infrastructure of which the telephone network will be less than 20 per cent of cost and 80 per cent will be the IT and T information, the data centres, the software, the whole sort of environment that surrounds that sort of a situation. The access will be a very minute part of the actual cost in the year 2010.

You will get exactly the same as you see in magazines and newspapers. When you buy a magazine for \$5 the actual cost might be \$10. You're not charged per page; you always get that particular magazine. The same will happen in a situation like that. People who don't want to participate in the permission based model, who say, "Listen, I don't trust any of these bastards out there. I don't want to give my information to anybody" - no problems whatsoever. It's a permission based system. I pay my \$50 or \$60 access fee and I still can get the service the way I want it. We put the user in control; we don't put the supplier in control of that sort of a situation. I can see the cost of access going down to zero in situations where the business model is no longer based on access.

PROF WOODS: Thank you very much. Can we look at some of the current constraints to the development of the infrastructure that you've been portraying? We have in Australia two major HFC cable networks, and Optus was saying that theirs passes 40 per cent of homes, and of course you've got Telstra as well.

PROF SNAPE: Passing the same 40 per cent of homes.

PROF WOODS: Yes, indeed. Neither of them are digitised. Telstra was saying that one of the major constraints to their digitisation was the regulatory uncertainty of access and pricing that would follow from that. How, in your vision of the new environment, would you overcome those sorts of constraints? Here's a network that's actually physically in existence that requires some adjustment, but the potential consequences of that are very significant, and yet it's not happening. How do you - - -

MR BUDDE: Blackmail, ransom. Blackmail because they want a monopoly; ransom is because of the stupidity of the government of not allowing competition

between telecommunications network, cable television network, digital television. If you offer monopolies in all of the different sort of things that everybody invents, of course why on earth should these people open up? Why on earth would you do it? It's up to the government to say, "Listen, we are talking telecommunications, not this stupid copper cable." Telecommunications is a whole area of activities - access technologies. If the government bites the bullet and is saying, "Listen, these are all access technologies. We allow them to be developed for our e-society and our e-economy," then that issue is gone overnight.

The second thing of course is that, as I mentioned before, we are the only country in the Western world that allows a telco to both operate in a monopolistic way the copper cable network and the cable television network. It doesn't happen in Europe and it doesn't happen in the United States. It doesn't happen in Canada. We're the only country where we allow Telstra or Optus to hold us at ransom and to blackmail us with situations like that. If there would be competition then Telstra and Optus would be more than happy to invest because, if they don't invest, the other party who has a better network and can deliver the same sort of services would be the flavour of the month by the consumers, and the consumers would go to that network, and they wouldn't use the other network.

But if we don't allow competition to happen between these networks, then of course we can sit here for another three, four or five years and have exactly the same discussion as we have now. If we don't start with a vision of where we are, if we start looking at all these little things in isolation, we can sit here forever. It will never ever change. They will always hold us at ransom. Today it's the cable network, tomorrow it's digital television, the other day it will be a local network and another day it will a satellite, whatever. If we move on to the next step and say, "Listen, this is telecommunication, not just this or this or this," then we have a chance to start addressing these issues. Then we actually say, "All right, fine, we've got these networks. Guys, if you don't do it we open it up and we let competition happen on this network."

The reality, of course, is that we are not here but what we should do is work our way up. If we have to do something for Telstra and Optus to save their skin, then we would say, in my opinion, "Okay, fine, we want to move to this vision. We've made mistakes in the past. We can't just throw you out straightaway, so we're going to build an interim period over the next two years where we say you get exclusivity. We don't do anything with you. We allow you to do whatever you have to do, but in two years' time there will be open access on your network." Then they can do what they want and they know that if they are not going to do it, somebody else is going to do it for them, because they lose their monopoly.

But now, if they delay and delay and delay and delay, they can keep this monopoly for four, five, six, seven, eight years - 10 years perhaps, if we are not firm in that respect. We might have to compromise a little bit in that particular area by giving the incumbents something in order to move forward. What is very important

is that we end the current regime, that we start coming back with the vision and say, "This is telecommunications. This is where we are moving to. This is how we are going." Okay, it's not an ideal world that we live in. We might have to compromise between here and there.

PROF SNAPE: Could I just pick that up? What you're saying here, if I may put it another way, is that you're looking for competition between platforms, rather than competition on the existing telecoms platform.

MR BUDDE: Correct.

PROF SNAPE: So we're looking for competition between platforms. You would say you would need, in fact, differentiated ownership, so breaks of ownership between platforms so that they are competing against each other, and yet on the other hand we hear the Optus's of the world, for example, saying that we need to have packaging of various services so that we can make a business case from these various services. Is there any conflict between that? You would argue that there isn't, I guess.

MR BUDDE: I have to be careful here, what I'm saying. The situation is that if we start trusting them - we've been doing that now for 10 years - I mean, the cable network was started in 1994, six years ago. It's only now that we start talking about opening up the network. Why suddenly now? In America they started in 1996 to upgrade the networks and in Europe in 1998. Why didn't Telstra and Optus do it in 1996 and 1998? They keep this as a very nice tool, and I know that on 16 June Foxtel is going to switch on part of its digital network. They're not stupid. They will have to do certain things. They also know that whatever they have to do, they cannot delay it forever because the value of their asset declines. It doesn't really matter a great deal what the regulatory issues are. They will have to move forward - they know that - in one way or another.

We have to be very careful. Is what they are saying also really what they are doing? We have relied on Optus as being the duopolist, since 1992. Now it's sold off to Singapore and what have you. We have to wait and see what happens now. If we start trusting these companies, then I would feel very uncomfortable about things like that. The new word is "packaging". In two years' time they'll come up with another word for why they will delay it.

PROF SNAPE: Perhaps I could put it in another way. I'm not sure if you can recall the recommendations of the broadcasting report on cross-media ownership. It was very much in a convergent world, and it was thinking of new ways of delivering services in the way that you've been talking about. It put certain conditions on it, including opening up broadcasting for more competition, relaxation of the foreign ownership rules, et cetera; that there should be a new public interest section inserted into the Trade Practices Act where it should be assessed on a public interest base - whether there should be cross-media ownership.

MR BUDDE: Yes.

PROF SNAPE: What I think you're arguing is that it is not the media that is of concern or what is in fact being carried on the platform, but it's the platform itself.

MR BUDDE: Yes.

PROF SNAPE: And what you would worry about is cross-platform ownership rather than cross-service ownership. Is that correct?

MR BUDDE: Yes, because why do you have cross-media ownership? Because you have these platforms that are the monopolies. The platforms are the monopolies. The content over these platforms are not necessarily a monopoly but the fact that you've got a monopoly on the platform automatically makes the content a monopoly because it's linked to that particular sort of platform. So the combination of it becomes a double monopoly rather than a single sort of monopoly.

PROF SNAPE: That's because there's regulation of what you can do on the various platforms.

MR BUDDE: Exactly. That's what I'm saying. You've got different regulations for different platforms. In the end, once again, in our broadband society that we're talking about now, it's totally irrelevant what sort of platform you have to deliver the service.

PROF SNAPE: If you get rid of those regulations as to what could be done on the various platforms, then what you would be looking for is competition between the platforms and then, therefore, some sort of public interest restriction on the ownership of the platforms themselves.

MR BUDDE: Yes.

PROF SNAPE: Rather than saying free-to-air broadcasting versus - this versus that.

MR BUDDE: Correct, yes. We are already seeing the situation on the digital television system where there's a new platform called MHP - multimedia home platform. It's a new technology specifically developed for digital television with Australia in mind, because what it allows you to do is to broadcast. A broadcaster can broadcast any of its programs, but the funny thing is it is then actually pumped into a computer and the computer is pumping it out into an Internet site and you can watch exactly the same sporting match or exactly the same movie on the Internet, but then it's called video streaming and you bypass the regulations of broadcasting. It's not broadcasting.

So you start creating this incredibly stupid situation - that the technology nowadays can bypass all of that. So why not pre-empt that and say, "Okay, we don't want to have the bushfire brigade out every time"? What are you going to do? Are you then going to regulate video streaming on the Internet? Then they come back with a new technology. Are you going to regulate whatever they find out? Are you going on as a government forever regulating, trying to catch up with technology? We know it's futile, but unfortunately these governments in Australia go to MMDS, go to digital satellite back in the 1980s, et cetera. It's a constant repeat of trying to regulate technologies.

If you don't regulate technologies, you open up the platforms. If the government says, "We don't want pornography on broadcasting," I haven't got any problems with that. Regulate content because we as a society don't want pornography on broadcasting, fine, so be it. But to say, "You can have pornography on the Internet but you can't have it here. You can have it there," that's stupid, of course. You should have platform totally technology neutral from a regulatory point of view, open them up. Let people do what they want to do, and then you as a society can say certain rules on the content that you want, but based on the content not on the delivery of the content.

PROF WOODS: You created a little image there of the regulator constantly chasing the ripples in the pond as they move out. Would you agree with the vision as we express it in the document here that the regulations should focus on the core disturbance, the local loop, as being the primary bottleneck, and that that's where the regulatory focus should remain?

MR BUDDE: Yes. What I would like to see is, once again, okay, the vision is here. This is the strategies. One of the strategies we'll have to address. We start at the bottom. It's nice talking about 2010. The reality is that we live in 2001. So the reality of 2001 is that the most critical sort of element is access to the local loop. What I can't understand is that back in 1995 and 1996 when we discussed it, we were discussing the problems of access technology, and this goes to both platforms. With cable television, I spoke to Michael Lee in 1994 and he said, "No, there's no problems. The cable television networks are open." It took seven years to then go from the fact that he said, "No, they are open," and to actually execute the whole thing. The same applies to the local loop. We discussed that with Austel back in 1992 and 93 and 94.

At a certain stage we will have to get the local loop open if you want to move from the T-Ford model. If we want to move further, we start with the T-Ford model, being the local loop, and we have to start working on that. What I can't understand is that every single year since 1996 - it started in 97 when it has been introduced - the minister has either given the ACCC more powers, have promised them more powers, and the ACCC is either not using the powers or - I don't know what's happening, but we are not going to open it up. I was talking to somebody else the other day and he was telling me that the ACCC does have currently the powers to implement access to

the local loop. If that's the case, then I would like to see the Productivity Commission make a clear statement that there are sufficient powers in place now to do what we have to do now, what we've been discussing for the last 10 years - open up the local loop and set prices and do things like that.

If that's not the case, then what is going wrong in this country, where every year the minister stands up and gives the ACCC more powers and nothing is happening. What is going wrong in this country in that situation? How much longer do we want? We need local access loop now in 2001, not in 2002, not in 2003, 2004; we need it now if we want to progress our society towards the sort of e-society that I've been talking about. We are already running behind the rest of the world by two years. Why is that? Why do we as Australians have to run behind the rest of the world?

PROF WOODS: Thank you for your views on those matters. Have you got other matters that you'd like to bring before the commission before we bring this part of the hearing to a close?

MR BUDDE: Yes. I'm worried about the fact that we go through all sorts of processes in this country. I run my own business. I've got a small business and we do well. I'm quite happy with it. As an individual I don't have a regulatory department at Paul Budde Communication. I'm putting quite a lot of effort into making submissions to you guys, to the ACCC and to others. What frustrates me totally is that in the end we as a country come up with a good report - the Productivity Commission reports in the past have been extremely good - and then in a totally undemocratic way they don't get used. You are genuine people who are putting a lot of effort into it and then in one way or another the government is able to totally ignore what we as a society - and it's not just this industry.

With the broadcasting report we had every man and his dog involved in it - the unions and the consumer associations; everybody was involved in it. Here we have another sort of situation and already the minister is saying, "Oh, forget it. It's too late. September we're going to do" - it becomes very disheartening for people like myself to put in a lot of effort if in the end you already know the minister is going to totally ignore it. That is a very frustrating sort of feeling, and it's not only me. I talk to people in the industry, because in the end the regulators in the industry are also people, and if I talk to them they get exactly the same feeling - "Yes, okay. My boss tells me I have to do it, but it's a total waste of time because in the end the government is not listening to what we as a country want."

I just want to express that and get it on the record. I speak for many people in the industry. We are very disheartened by the lack of political will to move in the direction that we as a country want to move into.

PROF SNAPE: I don't think I will pursue that too much in this context. I would say that certainly with the Productivity Commission's predecessors - the Industry

Commission, for example - sometimes the reports are not adopted, the recommendations are not adopted, sometimes they are adopted immediately. If one goes to international air services, for example, you'll find that virtually all the recommendations there were adopted and are being implemented. Sometimes they lie low for a while. In health insurance, for example, several years afterwards the recommendations of lifetime cover are picked up and implemented. In other cases, they just fester away for a while and maybe they'll be picked up later on. I think one can get disheartened, as you are suggesting, but I wouldn't give up.

MR BUDDE: No, we won't.

PROF WOODS: Thank you very much, Mr Budde, for your evidence this morning. Our next witness is the Institute of Public Affairs, but I suggest that we take a five-minute break in between. Thank you.

PROF WOODS: We'll resume the hearings, and welcome the Institute of Public Affairs, who have provided a submission to this round of hearings, and also of course to our previous hearings. Please indicate your name and the position that you hold.

MR HOGGETT: Jim Hoggett, director of economic policy, Institute of Public Affairs.

PROF WOODS: Thank you, Mr Hoggett; always a pleasure to have you before the commission. You have provided us with a submission but do you have an opening statement that you would like to make?

MR HOGGETT: Yes, thank you for the opportunity to appear. I have provided you with a submission in which I've commended the draft report which I think is very detailed, with good analysis and very fair. I don't want to say any more about that but I know how difficult it is to produce such reports and I think it's a very good effort indeed. I won't rehearse the submission that I made. I don't see any point in that. Generally speaking, I agree with the findings of the commission's draft report and also with most of the recommendations.

Looking at it broadly, I think that with all that's happened in the industry in the past few years there would have been something wrong if you had produced a report that recommends more regulation, or even retention of the existing level of regulation, although I recognise there are quite a lot of participants in the inquiry who are asking for more regulation or more detailed regulation of various kinds. I think it would have been the wrong direction and it would have been a very bad signal to come from the commission.

There has been a lot of talk about visions and more this morning. I have to say I don't think it's up to the commission to produce a detailed vision and I don't think you're probably going to try to do that. It's not the role of public agencies to produce industry visions. The commission isn't George Gilder, who will produce a vision every year for you, and quite often different from last year's vision. That's up to the industry, and if the industry doesn't have a vision then they should be sacking their CEOs and their planning departments because that is part of their job. It was encouraging to hear the commissioners encouraging industry to produce something of that kind. Even if they're conflicting, that would be, I think, instructive.

One of the difficulties we have here now may be that so much of our telecommunications sector is now overseas owned that the production of the vision is part of a global vision and the Australian end of it is just a segment of that. Nevertheless, I think we do have a right to know where the gigantic corporations that now participate in our telecommunications sector are going, or think they're going. One thing I'll also say about a vision: it's easy from the outside to produce one. It's easy to speculate and it's easy to speculate in terms of years hence, but the people engaged in the industry actually have to put their money, or somebody else's money

for which they're responsible, on a vision, and they have to be able to make a profit out of it. They can't ignore the risks that are entailed in that and they can't ignore the history that's gone before it. It's easy to sweep away objections and say, "Let's do this, let's have a zero access price," and things of that kind. But if you're sitting on a cable network which you've painfully constructed over 40 or 50 years, or even over six or seven years, with all its technical and financial history, you're not able to take sweeping decisions of that kind.

There was some discussion of the cable network which supports the pay television system and the lack of digitisation of that. I can clearly recall when that cable system was set up in a great hurry to meet a new entrant, of which I was then an officer, and it just wasn't possible for those who were engaged in that activity to digitise that network as they rolled it out. They couldn't do everything at once. They rolled it out at great expense. Two entities did that. They did it in analog form for the most part, and I tell you it still hasn't paid for itself. Even though it was the cheapest alternative, it still hasn't paid for itself and it's not showing real signs of doing so yet. So it's not a simple matter of getting from A to B by seeing B and going for it. You've got a heck of a lot of history in A and I think it would be unwise of the commission to ignore that depth of history.

There's been a little bit of discussion about price too high, price too low for investment, which has been engaged in by various participants here. What we're talking about is not decisions that are made independently by the corporations to price at certain levels in the expectation of certain increases in demand, but a regulated price imposed by government on corporations. If you price too high - you're probably not going to price much too high, although you may do that. If you price too high you'll generally get some competition that will bring the actual price down, and you will get the investment that you require. If you get two networks set up, which is actually what's happened, you will get some competition but you won't get the destruction of both networks as an outcome of that. You might get the financial destruction of certain corporations engaged in that activity but the infrastructure will remain. Somebody will take it over and somebody will make a profit out of it - probably Kerry Packer if he lives to see the day, because he's very good at that. I'm joking of course.

If you price too low in a regulated fashion, I think you'll get California; you don't get infrastructure built. We've got examples of it in energy and I don't think this is too different from that. In that respect I do sympathise with the industry representatives here who have been asked to quantify the effect of regulation on investment, because investment decisions are based on numerous parameters that are all uncertain: customer reaction, rate of take-up, costings, margins, quality control, competitor reaction. All of these are uncertain and each time a business plan is drawn up, each of those parameters will have probability ranges. The worst-case scenario is usually way down in the red, and the best case is way up in the black. The range is often quite enormous, particularly when you're dealing with new technology. So you have to make a stab somewhere in the middle and hope that at

least half of the parameters are within the optimistic range.

In these circumstances regulatory uncertainty can be the final straw, partly because it's just another risk and partly because it's a risk of a special kind. You get a "no" delivered as a "maybe" or a "maybe" delivered ultimately as a "no". What you do know is that there will be a bias towards the unpredictable and a bias towards the generally negative if you're talking about access and matters of that kind, things that will generally affect the value of the asset that you're proposing to build. Regulatory uncertainty deserves examination as a special kind of risk.

For all of these reasons our submission, of course, was generally pro-deregulation and we strongly supported the repeal of XIB, partly influenced by what we regard as some of its egregious characteristics. We think that regulations of this kind with these sorts of powers in them should be clearly seen to be essential, and the experience with this regulation doesn't suggest that it is essential. It's not been a really active measure and I take the point made by Optus that it is perhaps a deterrent. It's hard to measure that deterrent effect and in the end, as we said in our first submission, it comes down to making a judgment. We believe if it were repealed the sky would not fall in. It's a regulation of a kind that should be under continuous review, with a view to repealing. We think now is the time.

I was encouraged by the shift in the debate that's occurred during the progress of this commission. The submission by Vodafone I think is one example of a corporation that's looking ahead, obviously, to its own interests but also to the broader public interest and looking for lighter-handed regulation. The speakers from Optus all focused very closely on perhaps the real regulatory distortion, which is the price controls. Incidentally, there's a typo in my submission where I'm talking about access price controls. It's actually retail price controls I'm talking about. It's in the highlighted section.

PROF SNAPE: That's page 6, is it?

MR HOGGETT: Yes. It's interesting that there's a sort of growing consensus that the action, of course, is very much in this area, but it's also very much in another area that the commission is only partially focused on, and on which the ACCC has produced a report which the government has conveniently buried. We won't see it in public, I don't believe, before the election; a report which presumably - although we don't know this - recommends, on the basis of the earlier indications, removal of retail price controls of various kinds. That is a large distortion.

Looking at XIB and the regulations generally, what I would say is that if we look for perfect regulation, which seems to me the drift of a lot of the submissions, even those submissions like that of the previous speaker, which are looking for a better functioning market - a much future-looking market - if we look for perfect regulation we will simply get more regulation and more detailed regulation. Our record in producing it isn't very good and it's unwanted side effects are the cause of

this activity that we're engaged in now. We think less regulation may well do the trick, with all the risks that are involved in the existence of the elephants and the rhinoceroses. I don't think they're mice. I think there are a lot of very strong competitors out there.

We're still of the opinion, and this is where we disagree with the commission, that XIC ought to be repealed. We still believe that a revised IIIA and the rest of the act would be sufficient. We're not talking about no-access regime, we're not talking about the abolition of competition law or even its substantial weakening, but we still believe that XIC could be repealed and the sky would not fall in. In fact it might help matters. With the indulgence of the competition I'd like to make a general comment following on something that was said by the previous speaker. This review doesn't take place in a vacuum. People do participate in it on the basis that it will complete its work and will not be pre-empted. That's the whole point of the Productivity Commission. It's an entity that you put a problem to and you go away and wait until they produce at least their answer, which you may not agree with. That's why people put a huge amount of time into contributing to the work of this body.

So it was very disappointing to hear the minister speculating on matters that the government has remitted to the commission, saying that it wouldn't wait for the final report and promising early action on some of the crucial issues that are being discussed by the commission. It's especially disappointing after they had remitted a couple of extra terms of reference to the commission in the wake of the Besley report on the recommendation of Tim Besley. I think this is a sign, I guess, of a government that's too impatient to wait for the final and full review, and it does affect the attitude of the parties and it's a shame. It is a particularly a shame because basically the way that the minister is looking at the matter is for more intervention, more regulations, more regulators and less fairness. That seems to be the drift of what he said.

It seems strange to me that the industry is beginning to move one way and the minister seems to be moving the other. He should at least, I think, let the process be complete before making significant policy changes that will have effect probably for years. That's all I wish to say, thank you.

PROF WOODS: Thank you very much, Mr Hoggett. I appreciate your submission and your opening remarks. In the participants to date we've had specific companies involved in the industry and one commentator on it. You're our first in the category that the institute is in. Just for the purposes of transparency, do you receive any financial support or have any financial relationship with any of the major organisations involved in this industry?

MR HOGGETT: The institute is supported by a very wide range of companies and a very wide range of individuals. None of the contributions, as far as I'm aware - I'd have to check this - amount to more than 2 or 3 per cent of the total budget. We do

receive support from members of the industry, yes.

PROF WOODS: Thank you very much. An area you've identified is this question of whether telecommunications - - -

MR HOGGETT: Perhaps I should say one thing on top of that. Sorry to interrupt you.

PROF WOODS: Please.

MR HOGGETT: The purpose of the institute is to produce completely independent opinion, and we do not accept direction or anything of that kind from any of our subscribers. I should make that absolutely clear.

PROF WOODS: We understand the institute. Thank you. There is this issue of whether telecommunications is unique or whether it should be folded into generic regulatory framework. We have put forward the proposition that wherever possible the generic approach should apply across all of industry, but we have identified certain characteristics of telecommunications that in certain instances would warrant particular development; things such as the network effects leading to any connectivity, the speed of technological change, and those sorts of factors. You're aware of them in our draft report. Carrying that through to Part XIB we say the generic approach in the draft report is the preferred approach and recommend, as a draft at this point, the repeal of XIB. But that has attracted considerable opposition from a number of players in the industry. You've also touched on it, both in the submission and in your opening comments.

From your perspective, can you appreciate the views of those who oppose that draft recommendation, that it will unleash behaviours of Telstra that would be detrimental to development of competition in the industry? How would you respond to their concerns by drawing on section 46, for instance?

MR HOGGETT: There are several levels to this, I suppose. This review is a review of competition policy. If we are talking about the regulation of this industry for other purposes, then it's unique. Every industry is unique. I worked for a building materials company. They're unique. They have unique regulations relating to quarrying and things of that kind. But we're talking about competition, so there has to be something really special to enact a couple of large sections of an act of parliament to regulate competition in a particular industry. I have come to the conclusion, and we've come to the conclusion and written it into our submissions, that in competition terms this industry is not unique. Network effects are not unique to this industry. Almost any of the other aspects that you've highlighted in supporting the retention of XIC are not really unique. They're present in other industries. They may be more pronounced in this industry in some respects, but they're generically the same.

We concluded that what was left in the act after this was repealed was sufficient. That was one angle we looked at. We're talking about competition policy. The reactions of the participants in the inquiry are as you would expect. This inquiry is part of - if I may put it this way in its crudest form - regulation gaming inevitably, and you cannot criticise corporations for engaging in it because there's a set of rules by which they play. They would like to change the set of rules or keep the set of rules according to whether it affects the value of their corporation. It's quite normal behaviour. I don't know what the views of the individuals concerned would be if they were not working for those corporations or were working for other corporations, but they might well change. There's no profound point of principle there. People will protect a patch.

That gets back to whether repeal of XIB and, indeed, XIC would leave a sufficient regulatory structure in place to contain the Telstra - not monopoly, but to contain the Telstra market power, which is undoubted. It's absolutely undoubted. Nobody can deny that it exists. We think that you've done another job on IIIA and posed some changes to that which will, I think, strengthen it, make its purpose clearer and give people a better opportunity to use it. Section 46 is a very powerful section. It's been used by the ACCC, as you've said, in court cases but it's used regularly and extensively by the ACCC in discussions with organisations that come to them with propositions or organisations that are being called to account by complaints. I think there's a great deal of power in that section that doesn't involve litigation. Having experienced it, I can tell you it's pretty solid power.

The conclusion I reached was that there was sufficient power in those sections for the ACCC to supervise this area to the degree that it requires. It's not as detailed. It doesn't provide for the sort of schema that's in XIC, but the main elements are there and the main powers are there. I don't think there'd be any greater delays than there already are. We delude ourselves if we think that more regulation is going to reduce delays, particularly of the kind that the minister is proposing. That was the conclusion we reached. We've got a special remit here to look at competition law. We believe the industry's problems are generic and not unique, and we believe that the safeguards that remain are sufficiently strong.

PROF SNAPE: I think essentially what you're saying is take all the telecommunications-specific parts out of the Trade Practices Act and you take XIB and XIC, there's not much left.

MR HOGGETT: Yes. There's still a lot of regulation left, though.

PROF SNAPE: Yes. I said out of the Trade Practices Act.

MR HOGGETT: No. I mean within the Trade Practices Act. It's not specific, but there's still a lot of regulation of a general kind.

PROF SNAPE: Yes.

MR HOGGETT: Very powerful regulations.

PROF SNAPE: The thrust of the draft report is that eventually we would see that, too. It's more that we're saying that as we stand today there are historical circumstances and that is very powerful - the historical monopoly, the consequences of that, the local loop, et cetera. So I suppose the difference between you and our position on that is that you think we've already got to the situation that we think we might get to in the future.

MR HOGGETT: Yes. I think you could move faster.

PROF SNAPE: I don't think that your comments about it being not in a vacuum - an expectation of a response - I don't think we can respond to. It's not up to us to respond to that. You will note that on the draft report we have a couple of sentences there:

This is a draft report prepared for further public consultation and input. The commission will finalise its report to the government after these processes have taken place.

That's our position.

MR HOGGETT: I wouldn't expect anything else.

PROF SNAPE: Very good.

PROF WOODS: Anything more on XIB?

PROF SNAPE: No.

PROF WOODS: You draw attention to our views on XIC and, as we've just discussed, perhaps it's more a question of timing, and you encourage us to take a more urgent approach to its long-term repeal. You make a comment at the final dot point on page 5:

The expectation of greater competition in the local loop has been disappointing, even though Optus has had every opportunity and protection to compete and has an extensive network.

Then you say:

We believe that the rigorous application of XIC may have had a part in this.

Could you elaborate on that thinking for me?

MR HOGGETT: What I had in mind here was, I recall the pay TV years and the previous speaker said, "The network was rolled out then. It was rolled out very quickly," and indeed it was. It was rolled out extremely quickly. That doesn't mean that connections were able to be rolled out as quickly, but connections were available, and I clearly recall in conversation with the ACCC that the intention was to protect the second player and allow them room to develop very quickly. The front line activity at that stage in both cases was pay TV, but it was always known that there was a much bigger gain - and the previous speaker has referred to that - than just pay television involved here, and that it was the telecommunications applications more generally that would in the end finance those cable roll-outs and make them profitable and maybe absorb all the capacity, or the overcapacity which was then seen, in other product.

So the network was rolled out very quickly, but actual connections in relation to Optus, other than for pay television, came much more slowly. I'd take the points that were made yesterday - that, in fact, substantial progress has been made in the last couple of years. The point I had in mind there, I guess, is that if you have an access regime where the pricing is determined by a regulator and the regulator's purpose is to create a second network, there's going to be a tendency for the pricing of access to be kept very tight. We've all talked about too low, too high.

PROF WOODS: Are you talking tight high, tight low?

MR HOGGETT: Tight low.

PROF WOODS: Does that help the second provider of infrastructure?

MR HOGGETT: No. I think in the long term it probably doesn't, but the short-term temptation is to use the existing network. It's an imperative. If the regulation gives you a better price than you can get by investing, then you take the regulation. There were severe pressures on Optus, severe financial pressures, for several years. Again, we have to think about the history here. They were very strapped financially and in a very tight corner, and they had to take some tough decisions, and I believe that one of them was probably that they decided that they would use, wherever possible, the Telstra network, if they could get the right price, because the investment in other things that they had to do - they had a satellite. They had a whole bunch of other things going on that they were frantically trying to put into commission. "Well, we can lease instead of buying" was a very sensible decision at the time. If the pricing had been more realistic, less constrained - - -

PROF WOODS: As in higher?

MR HOGGETT: Yes, higher, less constrained by the need of the regulator to get a second contender up, Optus might well have been encouraged by the higher prices, I guess, to go into their own investment, and then there would have been a clear

indication through the whole process to retail that you needed higher prices at the retail end to finance this as well. The structure of competition might have been raised a bit and we might have had that network that the previous speaker was talking about.

PROF WOODS: I'm trying to work my way through that. If the regulated price for access to the duplicated cables was higher and that caused Optus to have to pay a higher price to Telstra or use its own cable, I don't understand how that would alleviate its, as you described it, cash-strapped position.

MR HOGGETT: We're into the realm of speculation here. What I think would have happened is that the structure of retail prices would have risen. People keep saying we've had fantastic advances in prices. We have, but it's not always true that the lower price is a good price. It can arise for a number of reasons and it can arise from regulation. We've had a structure of prices partly imposed by a regulatory structure that is quite low. We've all benefited from that and it looks great, and it is good, but the issue that you're trying to determine here, in part at least, is what price will finance a future investment group that we need? If we cast our mind back we might consider what price would have given us a different pattern of investment from the one that we now have. That was the question that I was trying to address, obviously with very limited resources to do it and very little data to work on.

I suppose the question that occurred to me and the answer that I arrived at was that a higher structure of prices might have benefited people all around, including the consumer ultimately, because it's simply a backward projection of what you're saying forward. If you've seen people now desperately trying to hang onto these access regimes in the expectation of low access prices, you might say to yourself that there are a number of competitors around at the moment who will not survive when the price gets to a realistic level, and that's okay. Competitors are out there to kill each other. They're basically out there to put each other out of business. They've got to do it by fair means and not foul, but the competitive process is the heart of our system and some people will die. Some people have been taken over for the very reasons that they are not financially strong enough to stand on their own feet.

If you interfere in the pricing structure you probably accelerate some of those processes and you probably also end up with a price structure that's not appropriate. The conclusion I reached was probably that through this period some prices, particularly retail prices, had gone to low. People have got wonderful discount plans on the basis of it, and they offer people stuff that they couldn't sustain.

PROF WOODS: I take that point. I guess this is the really critical difference between you and Mr Budde, who was speaking before you. I think it ties back a little bit to what you said at the beginning of your remarks when you referred to the Californian situation as you interpret it, and energy infrastructure and the lack of investment that occurred there. The question, I suppose, is: is telecommunications the same? Or is the technology moving so fast, and the possibilities

moving so fast that the crucial factor is to drive demand and the technologies will follow? Whereas in energy, energy is a pretty stable technology. So is railways and a lot of the other areas in which the access provisions may apply. Here you've got an extraordinarily dynamic industry. You've got a convergence of various technologies, all the things that Mr Budde was talking about, and competition between platforms emerging all the time.

What is important here, it could be argued, is not to establish prices that will ensure that another power station is built, or that a railway is maintained, but rather to establish prices which will drive demand in the explosive manner in which it has occurred in some of these areas, and the technologies and the platforms will follow. That, I think, is the essence of the difference between what you're putting forward here which, if I was to put on Mr Budde's hat for a moment, I might say was a view that is appropriate - guessing what he might say, is appropriate to old and established technologies but not appropriate to the dynamism of this industry.

MR HOGGETT: I think there are vast areas of agreement between myself and Mr Budde. I wouldn't disagree on the dynamism of the industry, its capacity to move at a tremendous rate, its capacity to reduce the price of services that are now fairly heavily priced, to bring them down within the range of people who previously bought televisions and were led to buy monitors, presumably. What we're talking partly about is, "Where are we?" and what we're talking partly about also is, "How do we get to that point out in the future?" which will not be nirvana but will be some other stage on the way to somewhere else. That's where the profound philosophical difference probably arises. Do you do it by more regulation or do you do it by less regulation? We're arguing that you do it by as little regulation as you can so that the decisions are made not by governments, who are very poorly placed to make those sorts of decisions, but by the corporations themselves.

You can take account of all the aspects, technological and financial - because no service is free; there is no free lunch. Even in telecommunications there is no free lunch. You let them make the decisions and you fall back, and you leave in place those minimal protections you require to prevent abuse of market power, which is potentially considerable in this sector. That's all very generalised but, to come back perhaps to the specific, would I have government regulate a very low price? I wouldn't have them regulate any price. If there's an opportunity there for somebody to work through to a lower price, I think they will. I think they will.

PROF WOODS: We're referring to access prices. You do in fact contemplate the retention of Part IIIA.

MR HOGGETT: Yes. There's an area where I would agree you have to regulate for access, but not to the point of saying everybody has free access. That's just too simplistic. You just can't say everybody should be let on, because that completely begs the whole crucial question that we've been talking about in this inquiry: at what price?

PROF WOODS: But it's the bias here between too high a price or too low a price. Perfection is impossible, even for the Productivity Commission.

MR HOGGETT: That's precisely the point. There is no such thing as regulatory perfection, which means you will not get the right price at the time, whatever that is, whoever is regulating it. If you interfere, then you interfere without responsibility for the consequences of getting the wrong price, which is what's been happening over the last several years. I guess the point is that we're not really talking about access here. To my mind we've never really been talking about access because, as Mr Budde says, we've got an access regime. It's there. The powers have been there for ages. We're talking about the access price. The whole thing hinges around what price you pay.

PROF SNAPE: That's, I think, the essence of this difference here with the access price. In our position paper on IIIA, as well as in this, we've been talking about the risk of setting the price too high, and thereby discouraging investment, as being rather greater than setting the price too - I'm sorry, the other way round - as being less than setting the price too low. Setting the price too low would discourage the investment and one would never get the new power station or whatever you're referring. The question is, does that comment apply to telecoms? I think an interpretation of what Mr Budde was saying, as well as AAPT yesterday - they were saying that the risk here is the other way round, and that in fact what you need is to drive the demand, and therefore you will in fact - the risk of setting the price too high is greater than the risk of setting the price too low.

PROF WOODS: If I can develop that one point further, in your earlier evidence you were, in relation to the HCF cable, suggesting that the retail price had been too low, partly because of the setting of the access price too low. So that would lend further weight to the view that I certainly have received from your evidence, that you would go the other way; you would continue with the high price bias.

MR HOGGETT: I think we probably need to separate a couple of things out. Firstly, as you said, Prof Snape, none of us are talking about getting rid of an access regime of one kind or another. Even we aren't advocating that, although if we had a bit more time we might work on that one too. We're talking about having an access regime of some kind and I'm talking about a lighter access regime, rather than a heavier one. There's a degree of difference there. It's a difference of degree, rather than anything else.

Setting aside whether there should or should not be an access regime, because we agree for the moment that there should, and returning to the point about the level of the price, how in practice does one set a price if one is a regulator? I guess if you set the access price too high you're allowing the monopolist to charge more than they ought to charge, and that is a severe problem. You may well discourage competition of various kinds. But I think you will have automatic flow-on effects through into

retail prices and you will tend to have a different price structure. If you set it too high you will certainly get the investment that you want. Well, you'll get some investment.

PROF SNAPE: You might get too much.

MR HOGGETT: You may well get too much. You're always going to get too much anyway because people will miscalculate about how much of the market they want to get. As I said in a previous submission, you're always going to get too much investment in a new and exciting area, and some of it will waste away and be taken over, so you may well get too much. That's okay. If you set it too low it's almost a Laffer Curve analysis. If you set it low everybody rushes in for the product. You find that your delivery costs are a lot lower than you thought they were, and you get the revenue that then generates the profits.

I guess what I'm saying is that that's a huge gamble on the part of the regulator and that's not the gamble that they're making. The gamble that they're making is a cost-base gamble and this is what it costs. The gamble they're taking is a commercial one; they're making a commercial decision for the participants in the market. If there were some demand that might help, but you can't rely on that. The people who put the money up really need to determine the prices. If you've got an access regime, I guess you've got to listen to the people on both sides. If you're a regulator, what I'm saying is the bias will be to low, and to low will not, to my mind, necessarily drive that demand. You don't know it will. It's a big gamble to make with other people's money, including mine. I should declare an interest: I have shares in Telstra.

PROF WOODS: You and a few others.

MR HOGGETT: Everybody in the populace.

PROF SNAPE: Not us.

PROF WOODS: No, not everybody.

MR HOGGETT: Well, there you go.

PROF WOODS: If so, we would have so declared it.

MR HOGGETT: I don't have a lot of shares in Telstra.

PROF WOODS: Thank you for that though. You have an interesting proposition to further refine the object to look at economic welfare, rather than economic efficiency. I find some attraction to that but do you want to develop that just a little further?

MR HOGGETT: Yes. I suppose this goes back almost to my university days

when there was a subject called welfare economics, which was part of economics and not part of sociology or anything else, and it was all based on the old-fashioned utility theory which everybody did - indifference curves and things of that kind - but it was a well-refined theory at the time, and a good one, and it embraced within economics a whole concept of broad wellbeing. In other words, how did your economic decisions affect you in the broad utility sense? It seemed to me that if one were to incorporate that rather old-fashioned but I think still valid economic welfare definition into the act, you might bring together the two concepts of efficiency, which is incorporated in welfare economics, and the welfare of the consumer, whilst constraining it, as the section does, with the words "promoting the efficient use of an investment in telecommunication services" and the word "economic" remains in there. So you have still got a restrained definition but it's a more attractive and broader definition that seemed to me to merge the sociological and economic side without losing the efficiency concept.

I must add though that I am not in the least suggesting - in fact I would strongly object to any notion that these provisions ought to be used as making the ACCC into a quasi-welfare agency or trying to equalise outcomes or anything of that kind. It would simply be to incorporate a broader definition in. I made reference earlier to uncompensated side effects that take place in some rural legislation, and if you examine some of that, you can see fairly profound infringements of basic property rights going on through environmental legislation, water legislation and parks legislation. Those forms of legislation can affect people's welfare quite considerably, so it was really trying to think more broadly about what the section was intended to achieve.

PROF WOODS: Yes, certainly being a distinction between the broad issue of welfare and the role of the regulator who is not to encompass that but to have a very clear view on the efficient operation of the industry, and that government has other vehicles by which it can pursue its other social or equity policies.

MR HOGGETT: I had in mind, I suppose, that the Trade Practices Act does have a consumer ring to it very much, a very strong consumer - so in that sense the welfare of the consumer is incorporated in there.

PROF SNAPE: The lawyers of Telstra were yesterday reminding us about what courts do to interpretations, and established interpretations, et cetera, so while you and I might understand very well what we mean by economic welfare, we can't be quite sure that the judge would have attended the same course.

MR HOGGETT: No, but at the moment what you've got is long-term interest of consumers, and in getting from A to B again, if a judge looks at that, then he is likely to ignore the long-term interests of the producers of whom there were a number represented yesterday, and this perhaps is a halfway house. You're right, they wouldn't accept that refinement but the words of the act in promoting efficient use of and investment in telecommunication services and the defining word "economic"

would

remain in the definition that I'm suggesting.

PROF WOODS: Thank you very much. That brings to an end the particular questions we have of you in relation to your submission and your evidence. Are there any other matters that you wish to bring before the commission?

MR HOGGETT: No. Thank you, very much.

PROF WOODS: We very much appreciate the evidence you have provided today. We will have a one-minute break and bring forward our next participants.

PROF WOODS: Our next participants are from Fox Sports. Welcome. If you could please identify your name and the position that you hold?

MR MARQUARD: John Marquard, director of business and corporate affairs.

MS ALLEN: Christina Allen, corporate counsel.

PROF WOODS: Thank you very much and welcome to this hearing. We have two submissions from you. Do you have an opening comment that you wish to make?

MR MARQUARD: Yes. As you probably know, we have only recently submitted those to you, and I'm not sure if you've had much chance to digest them. However, we would like to confine ourselves to one chapter of your draft report. We initially wrote a submission in response to the issues paper, but due to some timing issues we were just finalising that when the draft report came out, so we thought it best just to put that on the table, and then as well comment or probably elaborate on some other points that had been made in the draft report.

I think it is fair to say that the overall thrust of what we would like to discuss today is in general terms a concern with some of the perhaps assumptions that seem to have been made in relation to the preliminary views that have been formed, in particular because we feel that this is an example of regulatory creep. The Telecommunications Competition Regulation draft report seems to have now just tacked on this issue of pay TV programming without really, we think, considering many of the issues.

We can only talk to you about sports rights and programming because that's really where our expertise is. But certainly in relation to those areas, we think there are a number of features which haven't really been adequately looked at and we would suggest that they need to be very closely considered before you would even countenance some regulation along the lines that have been suggested, because we believe there are some incredible costs and implications which flow on from that, not only in our area but certainly for sports bodies and for the community as a whole, which haven't actually been considered at all. As a result we think that this is the sort of area where there is certainly a need for some greater level of scrutiny, if that's what you think needs to occur. We would say, however, in response to that, that we don't think any evidence has been presented to you in relation to the competition which you have been asked to look at.

There are a number of reasons for that. The main one of those is that exclusivity certainly in the area of sports programming is used as a product differentiator. It's a feature of the media industry. It is something which I think one of the other submitters, I noticed yesterday, referred to as uncontroversial, and the prices that are paid reflect this. It's not something which is a feature only in the pay TV industry, it's a feature of free-to-air television, it's a feature of radio, it's a feature

of magazines. The fact of the matter is that the content is bargained for on a basis of exclusivity and there is product differentiation on that basis. It is, in that sense, a natural right. It's something which we noticed that the ACCC recognised in the submission as a feature of other markets, even where they say there should be further regulation.

Another reason that we'll come to talk about in a minute is anti-siphoning. I'll let Christina talk about that, but that is certainly an area which impacts very heavily on our industry in the sports area. It's something which the Productivity Commission has looked at itself and we endorse what you said, obviously, before. But we would like to point out that the regulations that you are suggesting may be appropriate here. I mean, you certainly haven't said that they are. It would only serve, in our view, to entrench the existing position of the free-to-air markets for the simple reason that when we look at sports rights, we're looking not only at the area of pay TV but also free-to-air. The free-to-air position on sports rights is that they will go out and try and obtain exclusivity, not only in relation to other free-to-air operators but as against pay TV in relation to those.

The other point we would like to make, which is a fairly obvious one, is that sports rights come up for renegotiation fairly regularly. It is open for anybody to acquire rights and there is a fair bit of jostling in relation to that. In relation to some existing sports rights in Australia that is fairly self-evident. We would also say that the overseas examples are not relevant in relation to this market, and the prescriptive mechanism that the ACCC proposes - I don't really want to go into that unless you do but we think there is some fundamental problem with that. I don't want to go into it because, as I say, the evidence is not there to show that we should have such a regime. Even if you had such a regime, the one suggested, we think, is full of holes, and for a number of reasons.

But in general we would also like to make two other final points. We have a new market here, a new industry here; the pay TV industry has only been around for six years. I think it's fair to say that is one that has attracted a fair degree of media attention, probably often for the wrong reasons in terms of where it sits sometimes. It is one which faces a fair degree of competition both within and without. It is very heavily regulated already and we say that costs to the industry as a whole of further regulation would certainly outweigh any potential problem that we were trying to address to the specific issue which you might identify.

At the end of the day, you know, pay TV programming should not be treated as a commodity, and that seems to underpin something in that particular chapter of the report. It is not like electricity or whatever. We don't see it in that way. Christina might just want to talk a little about the anti-siphoning issue, because it is something which is addressed and we're happy to answer appropriate questions from you.

MS ALLEN: The anti-siphoning: we've consistently argued that we're inhibited in buying programming and competing with the free-to-air networks, and we see that

unless the anti-siphoning scheme is reformed along the lines that we've suggested in our submission to the Productivity Commission in its broadcast inquiry - and also we've made a recent submission to the ABA - we think that this additional layer of regulation would not give pay TV operators incentives to invest in regional infrastructure for pay TV development.

We have undertaken some research and that shows that we have to compete with the free-to-air networks. A lot of programming is already locked up by the anti-siphoning scheme, and our research has shown that only 15 per cent of that programming, which is locked up by the anti-siphoning scheme, is actually shown by the free-to-air networks on a live basis. We actually endorse the Productivity Commission's recommendations that there should be a dual rights approach, that the free-to-air networks should not be entitled to acquire pay TV rights to sports programming and vice versa for the pay TV program suppliers.

PROF SNAPE: Our recommendation on that was that was only for major events, of course.

MS ALLEN: Of high cultural and public interest, yes.

PROF SNAPE: The other minor ones that wanted exclusive rights could in fact be achieved.

MR MARQUARD: Indeed. As you're aware, the ABA is conducting a review at the moment into that particular issue about the extent to which events have been consistently broadcast and what changes, if any, should occur to the anti-siphoning scheme.

PROF SNAPE: Our position stands on that as it was in the broadcasting report, as we have reiterated here.

MS ALLEN: I think that basically what we have said in both our submissions about anti-siphoning is a fairly general approach but we really think that the anti-siphoning scheme should be reformed before this other layer of regulation - well, we don't think that this other layer of regulation is required. Despite the anti-siphoning scheme, the pay TV industry has been able to provide regional Australia with access to a number of sports through Austar, the major regional supplier. I think we will leave it there.

PROF WOODS: Okay.

MR MARQUARD: Unless there is anything specific you would like to talk to us about.

PROF WOODS: Thank you very much. The note on which you were ending there was discussing the general availability of sport on Austar and you make the point in

your submission - can I say up-front thank you for your submissions, and despite the timing, yes, we have read them and gone carefully through them, and we do appreciate having them. Some of the matters that you raise in the submission that was to have come earlier pick up the points of detail in the draft. I don't intend to go through those. Had we had your submission, clearly we would have been in a better position to have reflected on those matters, and that is a timing issue. It was unfortunate that your submission was not before us at the time but they can be quickly and easily resolved. So I won't invest any further time in those.

Can I also say that I take it from your opening comments that you are supportive of more evidence being put to us and a greater level of scrutiny on these issues, and therefore following today's hearing we would welcome a further submission from you which sets out some detail. These are clearly matters of principle that you have put before us today. To the extent that you're able to support them with firm evidence of industry activity and behaviour and some of the pricing issues relating to that, as we will discuss this morning, that will put us in a better position to be able to more clearly see the force of your arguments. So if we can go from today, which will deal with some principles, if you can then support that subsequently with market behaviour, that would be greatly welcomed.

MR MARQUARD: That's fine to us in principle, but I'm not sure exactly which area you're seeking. If there's anything you'd like in specifics, we can certainly try to but it's a - - -

PROF WOODS: Let's discuss that as we go.

MR MARQUARD: Okay.

PROF WOODS: On your first page under the heading Pay TV and Regional Telecommunications, you say that you do not agree with submissions made to the Besley inquiry by the ACCC, calling for special pay TV programming access regime. Then you go onto say:

The first and most obvious reason for this view is that regional Australia is not, as a whole, being deprived of sports programming.

You talk about availability through Austar. I mean, yes, in that sense, but the terms of reference that are put before the commission don't deal with that issue as such. The issue that we're required to examine is the lack of availability of such programs to support business models of alternate delivery platforms. That's the key focus of our current inquiry in relation to these matters. It would help for the record if you could set out the terms and conditions on which you offer this product to those who are delivering alternate platforms, such as perhaps Neighbourhood Cable and Transact. Could you explain to the commission the nature of the terms and conditions on which you offer your product to those who are trying to develop alternate delivery platforms?

MR MARQUARD: We don't look at it from the perspective of whether or not people are looking at developing alternative delivery platforms.

PROF WOODS: No, but that's the matter before us.

MR MARQUARD: Yes, I understand that. But I think that comes to our point overall, in that yes, that is an area you looked at. We feel that you're looking at it from that perspective and then saying, "Well, this is potentially one area where we've been asked to focus on," and we don't think at this stage of your inquiry you have really managed to achieve that outcome, possibly because you haven't had enough submissions in front of you and possibly - - -

PROF WOODS: You are here now.

MR MARQUARD: We're here now - to concentrate on one area. We can only speak as a program provider and compiler.

PROF WOODS: Yes.

MR MARQUARD: We look at a number of issues, and I think we've actually addressed some of those in the submission. We consider a number of factors. We consider overall where a particular arrangement will take us in relation to our long-term future and in that sense the relative size of an operator and its model will be something which is important because of subscriber numbers overall and the cost to us of program acquisition and program compilation and distribution issues. Other issues are also important, such as ensuring that there's no unauthorised distribution of our signal, marketing, positioning of our brand. All of those sorts of things do become important and they are some things that we would take into account. We believe we've developed a brand which is a strong brand.

PROF WOODS: That's the Fox Sports brand.

MR MARQUARD: Correct.

PROF WOODS: Which is different from the delivery platform brands, whoever they may be.

MR MARQUARD: It is a different brand, yes. But we are promoted and we provide a fully produced channel, or channels. Those are, if you like, the main issues, and obviously the price that is paid for our content is an important component, both in what we can sustainably go out and acquire and compile on a medium and a long-term basis, and those are very relevant questions for us.

PROF WOODS: Yes. Perhaps I could break my question down into several and start with the very simple question of, do you offer your product to organisations

such as Neighbourhood Cable and Transact? Let's start at the basic factual - - -

MR MARQUARD: Do we offer? We're not in, if you like, a retail sense going out to people and saying, "Here is our channel." If somebody comes to us - if anybody comes to us - with a proposal which meets those criteria, we are happy to pursue that opportunity. However, in relation to those discussions which we have held, they haven't met those underlying criteria where we haven't pursued an arrangement.

PROF WOODS: All right. Do you have a commercial relationship with other than Austar in regional Australia?

MR MARQUARD: No.

PROF WOODS: Okay. Presumably it wouldn't be on grounds of technical degradation of signal or possible pirating or something for, say, an organisation such as Transact. They wouldn't be the sorts of factors on which you'd be dismissing them?

MR MARQUARD: To be quite frank with you, I don't even know how they ensure signals are encrypted. Can I just take that back one particular point. To the extent that there was sufficient quality issues to ensure that signal encryption would occur, that would not be a problem, but in all our relationships with all the people from whom we acquire sporting rights, we must ensure that there is sufficient signal - - -

PROF WOODS: I understand that. But presumably those who are setting up these businesses - - -

MR MARQUARD: Yes, I understand where you're coming from.

PROF WOODS: - - - understand that as well. So, no, you don't have a commercial relationship with others than Austar. Do you expect that Fox Sports will, in the foreseeable future, have a business relationship with other than Austar in regional Australia?

MR MARQUARD: That very much depends. As I say, if somebody does approach us with a business plan which we can see is a medium to long-term one, the answer is - - -

PROF WOODS: That remains open.

MR MARQUARD: Totally open, and that's an important point.

PROF WOODS: Absolutely.

PROF SNAPE: When you say it was medium to long term, you wouldn't require that the operator, a person, a group approaching you had already been established for

several years?

MR MARQUARD: I'm sorry, I'm not quite following.

PROF SNAPE: I'm thinking that the financial future of a new operator may itself be uncertain. You don't need five years' experience in the industry before you would entertain a proposal?

MR MARQUARD: I wouldn't say that of itself is a relevant criteria. However, I would say that obviously the ability of a customer to pay us is important because we're entering - - -

PROF SNAPE: I take that. But you would be prepared to take a risk that they may go out of business in 12 months or something? I was just picking up on the medium to long term to establish a - - -

MR MARQUARD: In the right circumstances, absolutely. Yes.

PROF SNAPE: To establish a medium to long-term contract is one thing; to be absolutely certain that the body is going to exist for the duration of that contract is another.

MR MARQUARD: Correct. One of the previous customers of Fox Sports did go out of business, as we know. That was Galaxy and Australis.

PROF WOODS: You identify a number of flaws in the suggested access model. Flaw 1 you talk about "increased regulation may stifle growth or competition".

MR MARQUARD: Yes.

PROF WOODS: Number 4, you talk about, "The market is not yet mature, too early to make claims about overall regional competition". Item 5 talks about:

A regulated access regime could substantially reduce the likelihood of continued investment decisions -

and item 6 talking about:

Freedom to make such arrangements may allow companies to invest in infrastructure and to innovate.

Those four all seem basically one issue. Perhaps you could assist me in differentiating each of those and elaborating on them.

MR MARQUARD: I think part of the problem is the way in which the access regime was suggested. It imposed various prohibitions on program suppliers and

operators which in our view assumed a very static market. I'll just give you one example of the sort of problem we're talking about, which then flows on. It prohibits supply contracts that cover territories which are not in a particular service area and then also prohibits sublicensing in unserved areas. If we entered into a program supply agreement with a pay TV operator who is not at the present time providing a service in a particular area, it would seem that you would thereby prevent that operator from providing additional products or services at a future time. There is a timing issue there in relation to the roll-out of those services and delivery of those.

That was a fairly obvious one, because of the way in which it said there's an absolute prohibition on those things. It is something which, by imposing hard and fast rules in relation to that, you're stifling the way in which anybody could make decisions about future services and future products and their availability. We think that is obviously not the way to go. The access regime also does not take into account the way in which sports rights are effectively sold. They're not sold on a segmented basis, if you like, in the way that they are in the United States. The United States have had a traditional series of regional monopolies. Here we don't have that.

It seems to us to be taking that model and trying to transplant it into Australia. We have a different set of circumstances here and a different set of criteria. Similarly, with the way in which we say the ACCC has looked at one other area, and that is the BSkyB in the United Kingdom and applied that here. Again, we have a very very different situation, both because of where the pay TV industry sits but also relative to the free-to-air industry as well. The free-to-air industry in some areas serves regional Australia, we say, very well. I know that's a specific area you've looked at. In other areas they don't. But the point is, when you lay the anti-siphoning over that and the product that must be available on free-to-air, it seems to us that the ACCC submission does not take account at all of the free-to-air issue at all; it just ignores it.

There are a number of those areas, that is right. That's probably one area where we've just looked at in broad principle terms, because we just say that this is so wrong and it just hasn't been thought through. We don't want to get into the nuts and bolts of it, partly because we didn't want to accept the underlying premise. We didn't want any suggestion that we were accepting the underlying premise that there should be some form of access regime, because we don't.

PROF WOODS: No. You talk about "increased regulation may stifle growth and competition". We're looking at potential deliverers of platform who need product. The evidence that we get is that the commercial drivers, the business models, for new roll-out rely on pay television content, whether it be movies, sport or some combination of the two - Internet, broadband access - and that telephony in itself is not a strong business driver and that it wouldn't sustain the promotion of alternate platforms. So there has to be reliance on those things, part of which you're a key market participant in, for new platforms to roll out to be in competition with Telstra.

Yet if they can't get access to the sort of content that you have, they can't develop business models that will sustain them for investment. And that's the very point that you've got here. You're saying that "increased regulation may stifle growth and competition", but maybe regulation is the only answer to actually allow growth and competition.

MR MARQUARD: I think you can look at that two ways, and one is to say that if people encourage growth - if it's at the level where it encourages growth and competition - if I can just go back a step point again and look at the sports area, we will buy, as other sports providers do, Australia-wide pay TV rights, okay? The price we pay for that is premised on that, if you like, being exclusive to us against other pay TV providers.

PROF WOODS: Pay TV are content providers.

MR MARQUARD: Content.

PROF WOODS: Not deliverers.

MR MARQUARD: Yes, I'm talking one level up here.

PROF WOODS: Yes.

MR MARQUARD: We will make a decision to invest in a particular product by producing and compiling the content in many cases. So, for example, we will go and cover Rugby Union matches or whatever. To the extent that that is a commodity and all that we are going to receive from our labours is, if you like, a price which is available on a basis which is non-exclusive and doesn't allow a particular customer of ours to use that as a market differentiator, it may not actually result in there being any - the economies of that may not result in us wanting to do that or being able to do that in the future.

PROF WOODS: I guess that is a point, and you've made that several times in here, that we need to test with some actual market knowledge and you'd be the best ones to have that market knowledge. If you could explain to us perhaps in a subsequent submission the pricing that you get on a per customer delivery basis by having an exclusive contract with say, Austar, versus the reduced price that they - but that others also would then be able to pay to have access to it, multiplied by the increase in the per customer base. I mean, it's a fairly simple mathematical process, once you have actually established your market pricing.

MR MARQUARD: Yes, it is. In general terms the price you are going to pay on a non-exclusive basis is much lower. I am happy to give you the - - -

PROF WOODS: It is the much lower where we need to understand it.

MR MARQUARD: Yes.

PROF WOODS: If you could elaborate on that in an additional submission that would give us great insight into this particular issue.

PROF SNAPE: Presumably the seller of that content. I mean, you are then describing the price that you would be prepared to pay.

MR MARQUARD: And the seller of the content would also be in a position to provide you with information of - - -

PROF SNAPE: What they would be prepared to offer to - - -

MR MARQUARD: - - - what they would expect, if that were, if you like, available non-exclusively. I'm not sure whether you've approached any of those to provide you with submissions.

PROF SNAPE: Who is getting the benefit of that higher price that might come, as you argued, from exclusive?

MR MARQUARD: That's right. I'm not sure whether any of the sports bodies are talking to you about this, or their international program providers, because the price you would - - -

PROF SNAPE: Not yet. Program provider, yes, but not the sports body.

MR MARQUARD: The price you would expect, yes, to receive as a sports body if content was available non-exclusively is much lower as well, with the result that there would be less money available to those sports bodies, and there would be some fairly significant flow-on effects from that. I don't know where.

PROF WOODS: The more you can elaborate on your understanding of market behaviour will greatly assist us in understanding that point.

MR MARQUARD: Sure.

PROF WOODS: To move on, your second factor you've identified in terms of flaws in the suggested access model - you say in part:

There are a number of reasons why these arrangements may be made inconsistent with other competition law principles. The onus should be on the regulator to show that they substantially lessen competition.

In fact, the regulator has come to the view that they substantially lessen competition and we quote on page 16.23 that "The ACCC's judgment is that on occasions vertical integration has been used to hinder or foreclose competition in

regional pay TV and related telecommunications markets." So the regulator has actually spoken, which seems to nullify - does it - your point 2?

MR MARQUARD: Not at all, and the regulator has remedies available to it, as does anybody else, in relation to the existing Trade Practices Act. They are saying there is a flaw in the legislation here and that is, if you like, a separate issue. I think they haven't actually identified the point they make. If you look at it they say, "On occasions vertical integration" - they haven't identified what vertical integration - "has hindered or foreclosed competition in regional pay TV and related markets." I mean, it's a fairly general statement they make there.

They do go on, as I've said, to say that they can't - they're not convinced that those requirements have yet been met. It is our view that that legislation is sufficient. If you go back and look at - I'm not sure who it was who talked about the UK experience where they said it was a problem but it was a similar regime, as I understood that submission to say, that they were then able to take action.

PROF WOODS: It's on your third page where you talk about the premium paid by operators for so-called exclusivity and you raise that again on the following page.

MR MARQUARD: Yes.

PROF WOODS: In that respect, further information would be gratefully received.

PROF SNAPE: On that issue, you might like to refer back to the chapter we had in sports on broadcasting and see whether we got it right in that, and if not - either way tell us, please. Otherwise we'll presume we did get it right there.

PROF WOODS: Yes, on the anti-siphoning, in fact on your fourth page at point 2, you talk about amendments to anti-siphoning and you're saying this would result in better pay TV programming, leading to a greater willingness to invest in regional areas and the development of more broadband services. I would be interested in your views then between broadband services and improved pay TV programming for regional areas. What is that nexus?

MR MARQUARD: Sorry, can you tell me exactly where you are?

PROF WOODS: I'm on your second point, last sentence on your fourth page. The second point is the one that starts, "If the anti-siphoning scheme is amended".

MR MARQUARD: Yes.

PROF WOODS: Your last point, if you could explain that nexus more fully for me.

MR MARQUARD: I think it was picking up on a point in your issues paper and

some submissions that had already been made, I think in particular drawing some inferences from others that had been made. If the anti-siphoning scheme was amended it would allow pay TV operators and pay TV program providers, such as Fox Sports and others, to more effectively compete for television sporting rights. It would therefore provide greater levels of content to operators and presumably where those models of existing or new operators were looking at more than one service - in other words, pay TV and other services - they would flow on from there. Yes, it's not our business. You know, it's not our model.

PROF WOODS: No, I understand, but you're an important player as an input to their business.

MR MARQUARD: Yes.

PROF WOODS: And you have drawn on that issue so I was interested in your views on it.

MR MARQUARD: Yes. We just think, further up the chain, where we are, that is an obvious point; that we are seekers of content. That is a current major impediment to our business, the anti-siphoning scheme.

PROF WOODS: For the record, could you just clarify the relationship between Fox Sports and Foxtel?

MR MARQUARD: Foxtel is a customer of Fox Sports. We provide them with two of the three channels we produce: Fox Sports and Fox Sports 2.

PROF SNAPE: And the ownership links?

MR MARQUARD: Fox Sports, as we've said in our submissions, is a fifty-fifty joint venture between a subsidiary of PBL and News Ltd. Foxtel, as I understand it, as everyone knows is 50 per cent owned by Telstra, 25 per cent by News and 25 per cent by PBL, ultimately.

PROF WOODS: In terms of access to Fox Sports product, you are identifying that for regional Australia that is only achieved at the moment through Austar.

MR MARQUARD: Correct.

PROF WOODS: In the Canberra market, presumably that's only achieved through Foxtel.

MR MARQUARD: Yes.

PROF WOODS: Foxtel are advising consumers in Canberra that they will not be making the products, such as yours that they have as part of their pay TV operations,

available through a cable being developed that's owned by a body called Transact but only by the means of individual satellite dishes and boxes which, in some respects, may prove to be a more expensive per household connection charge. As the owners of sporting products does that concern you; that you may be having limited customer reach by only having Foxtel as the supplier of your product to the Canberra market?

MR MARQUARD: I don't want to go into, in this forum, our business model. However, the - - -

PROF WOODS: It would help.

MR MARQUARD: I appreciate that, but I'm not at liberty currently to disclose it. I am going to say in general terms, however, that to the extent - and as I've said before - that we were approached and in relation to an offer which made sense to us, we would pursue that to see if there was some arrangement that could be achieved. However, the question of reach and availability of our channels is one factor which we consider and, as it happens, through Foxtel they are the largest provider of pay TV services in this country and that is obviously a relevant factor for us. If there was another operator who came to us with a particular model, that would be something - as I say - if it made economic sense to us on a medium to long-term basis we'd look at it.

PROF SNAPE: Your contract with Foxtel would not preclude that?

MR MARQUARD: I don't want to go into the specifics of any of our terms of our arrangements with any of our customers. Suffice to say, as I've said previously, if somebody approached us with a model that makes sense, that we think makes sense to us and our customers, we would actively look at it.

PROF WOODS: It has actually been very helpful having your material and we do look forward to some elaboration of those issues in follow-up submissions, so we thank you for the time that you've taken. Are there other matters that you want to mention?

MR MARQUARD: I think there is just one other matter. We were particularly concerned by some other submissions. I think we have set out in our submissions some points. We don't want you to be left with what we think is a mischaracterisation of the true picture in relation to some of those matters.

PROF WOODS: No, we've got that.

MR MARQUARD: You have all that and in particular - - -

PROF WOODS: As I say, we drafted this in the absence of the input from you.

MR MARQUARD: I understand that. As long as you can take those into account - - -

PROF WOODS: Yes. Now that we have your input we can go through and if we need any clarification from either yourself or those others who provided input, if there is a mismatch in material put to us we undertake to follow that through with you. Our staff will be in contact. I saw those as largely factual details and now that you've provided us with additional information and perspective, we can tidy those up. If you consider them of greater moment than factual clarification, please speak now and we will follow up in our submission. I don't see them falling into that category. Nothing else on anti-siphoning?

PROF SNAPE: I made the point before that it would be helpful if you went back and actually looked at that chapter and took it into consideration and tell us whether we've got it right or not.

MR MARQUARD: Sure. We'll certainly do that.

PROF WOODS: Thank you very much for the time you've taken and the effort you've gone to. We look forward to further, particularly market-based information. We will resume these hearings at 2 o'clock.

(Luncheon adjournment)

PROF WOODS: Thank you. We will resume the hearings into the Draft Report of the Productivity Commission into Telecommunication Specific Competition Regulation, and we have before us participants from PowerTel Ltd and support. Would you indicate your names and the organisations that you represent.

MR EMERY: Thank you, professor. My name is Russell Emery, from PowerTel Ltd.

MR CHRISTOPHER: My name is Andrew Christopher from Baker and McKenzie, solicitors, on behalf of PowerTel Ltd.

MR CONRADI: And my name is Mike Conradi, also Baker and McKenzie.

PROF WOODS: Thank you very much. Mr Emery, do you have an opening statement you wish to make?

MR EMERY: A fairly short one, professor, and then I might just have a couple of comments from each of my colleagues.

PROF WOODS: Please.

MR EMERY: Thank you. Once again, PowerTel thanks the commission for the opportunity to continue to participate in this process. As a lot of other submitters have noted, your report covers a lot of territory and there are a number of issues with which we entirely agree with the commission's approach, and there are some issues that we don't agree. What this presentation will try to do is just talk to some of the major areas where we would like you to reconsider your views. We will be making a formal written submission which will have further information.

I think we first committed to participate in this process in August last year, which is nearly a year ago, and our submissions argued that the market hadn't reached a sufficient stage of competition to justify the end of industry-specific legislation, in particular Part XIB, and I think that we also argued that the industry and particularly the dominant incumbents, both in mobile and fixed, needed to demonstrate more of an approach to access dealings which was mature and showed that the industry could actually be relied on for solutions. We stated that while Part XIC had a number of deficiencies, we felt that these could actually be corrected and that if those improvements were adopted it would assist in developing long-term sustainable competition.

I think it's fair to say that in our view, in the 10 months that have passed, we have really seen nothing to change our minds, other than to say as a company we must have come of age because we've had our first arbitration with Telstra and not at our initiation, I might add. We continue to see Telstra's EBITDA as a percentage of revenue to continually exceed anyone else in the region. In Australia only Optus was

showing a positive EBITDA, and even at that earning rate it's been sold by its current owner. No-one else is actually EBITDA positive yet. The commission may have other information but that's what we have available to us.

I've noticed that in the course of the hearings the commission has asked people, "What's the vision for the future?" and our vision really we will try and articulate as we go along, but what we really feel is that the current debate that's going on about the competition legislation has really been focused on the level of legal structures and the appropriateness of those legal structures, and it hasn't really been at a level which talks about the technology, the developments in technology and the structures that are necessary to drive those benefits through to the community at large.

We also think that there's been a lot of discussion about the need for a common access regime but we keep coming back to the position that we've put to you before. Telecommunications is very different because it's interconnected. Other industries seem to use basic pipes to deliver homogenous products. The telecommunications industry seems to only need the pipes in order for very intelligent platforms and computer-driven services to be delivered across them. We'd like to see that somehow come to the front and try and help the commission in its considerations of those matters.

We've also felt that there's been a lot of discussion in this forum which really is a hangover of the voice based environment in which the first legislative scheme was set in place. We're really talking about dealing with things on a product-by-product, on a minute-by-minute and price on a minute-by-minute basis. We think that the emerging data and IP networks require a completely different approach to access and pricing. We give the example that in 2001 the domestic industry doesn't still have an agreed wholesale optic interconnection standard or network-to-network interfacing, whereby a whole host of different ATM and frame-type services can be delivered.

So I guess if you were to ask us what's our vision for the future that this industry should have, we would like to see a national network of interconnected networks owned by a large number of parties, each of whom delivers an efficient service at the level that it can operate at. The interconnection arrangements would encourage both services and facilities based competition and the charges would primarily be based on some efficient economic basis, and our view - and we've taken this position with the ACCC in all its considerations - is that it should be TSLRIC. We don't subscribe to the views that certain other carriers like mobile carriers put forward, that competition on the retail side of mobiles is sufficient. We actually see an imbalance developing where the wholesale charges for connection to mobile services actually will exceed the retail charges.

We believe that we really need to retain Part XIB at the moment, and I think there is an issue of timing in our submission again. We still believe that the industry is not ready to be let off the leash. We also believe that Part XIC - and I think we agree with a number of your recommendations to improve it, and we will try and

expand that a little bit now, and if you don't mind I will pass on to Andrew.

MR CHRISTOPHER: Thank you very much. Just as a preliminary point, PowerTel has had insufficient time to fully analyse and understand all the practical implications arising out of the report and what it would mean for its business, so the views we express today are conditioned on that caveat and should be taken to be preliminary views only.

PROF WOODS: We look forward to your further submission.

MR CHRISTOPHER: And the significance of that is that there are a number of changes that can't be looked at independently and as a package, of suggested changes in relationship between each element needs to be considered pretty closely. Having said that, PowerTel's approach in relation to its earlier submissions and in relation to its proposed response to the report is to look at the issues through the filter of its own commercial experience and its dealings with the industry and its customers and other participants, and we'd also consider that the commission before finalising any recommendations or suggesting legislative reform would also have a clear vision of what the regulatory framework means to the people who live through the cut and thrust of it daily, and PowerTel, though recognising that the commission had regard and gave critical analysis to the views of submitters, would like to see that same level of critical analysis continued in a consideration of these supplementary submissions or responses to the reports to ensure that everything is looked at through the filter of practical experience.

PROF SNAPE: We will of course be doing that but these hearings on the draft report are our last public hearings, and so there is no interchange beyond this.

PROF WOODS: We do post all subsequent submissions up onto the Web site, which allows rejoinder, so we urge you to maintain your vigilance on the other participants and assist us in our analysis as you see fit.

MR CHRISTOPHER: Thank you. As a general proposition, PowerTel considers that the regulatory framework should not feather the incumbents nor provide an unfair or undeserved advantage to new entrants, particularly those who might not be efficient or would seek to point to the regulatory framework as an apology or excuse for a lack of success, and obviously in analysing the positions of any of the submitters the commission would have to apply a healthy degree of scepticism to what was said by anyone. That's all by way of - - -

PROF WOODS: We apply that to all participants without limitation.

MR CHRISTOPHER: Some of the recommendations and most notably the suggested repeal of Part XIB appear, and I say appear, to be predicated on an assumption that the present state of competition is sufficiently strong to warrant fairly significant changes. PowerTel's experience and its perception of the reality is

that when one applies a different set of indices and perhaps a deeper analysis of financial performance, competition is still in a relative state of immaturity and one should not confuse the number of new entrants, the reduction in the price of certain telephony services and a growth in certain subsectors or parts of the industry as presenting a reliable demonstration of strong competition. Russell has made mention of the fact that EBITDA figures and share price performance return on capital and other measurements show Telstra overwhelmingly in front of the new entrants on those scores.

It follows from that proposition that any change in the present arrangements must necessarily imply cost benefit analysis or, to put it more simply, what will be gained from the change and what might be lost or what risks might there be of losing from the suggested changes, and it goes without saying that involves some element of speculation. From that PowerTel says there should be a presumption, albeit a rebuttable one, in favour of the status quo, unless there's a compelling reason to depart from it, and this is particularly the case as important investment decisions, medium and long-term planning and strategic decisions have been made by participants on the present regulatory framework, and as the regime has only been in place for a short number of years and indeed given there are certain amendments that are yet untested, for example, those to Part XIB, it would create significant uncertainty to implement wholesale changes in a short time frame, particularly some of the changes that are suggested by the report.

If significant change is warranted and a theme does emerge from the report that some areas do need revision, I must say that PowerTel doesn't necessarily concede that some elements of the regime do need those changes but remains open-minded about it, then the changes urged by the commission will be somewhat different to those that PowerTel would argue for, and those that are consistent with the vision, if I can call it that, that Russell Emery outlined a moment ago. PowerTel is of the view that its vision would be realised not by a drive towards homogenous or more generic style regulation but one that continues to recognise the unique features of telecommunications network and services, and recognise the fact that whilst technological convergence is inevitable it's still far enough away not to dictate the form of the present regulatory arrangements.

The other very critical element that needs to be borne in mind is that telecommunications networks are by definition interconnected and every element of those networks has a role to play in delivering efficient outcomes. Whilst it may be a desirable aim to have common or a move towards more common infrastructure regulation, at this stage most other network-dependent industries - for example, electricity, gas, rail, transport, airports - still maintain at least industry-specific access regimes and some degree of ex ante price regulation, at least in relation to prices oversight, and there are numerous examples to be found in the various gas and electricity access codes, airport undertakings and rail access regimes, which are built around the particularities of each industry.

One other possible difficulty with some of the recommendations made by the commission is that they don't tackle head-on the continued potential for a large number of bilateral interconnection disputes where a lack of transparency, potential timing issues or timing abuses and gaming possibilities arise. As a general remark, those problems tend to favour the incumbents, particularly Telstra, who in most cases is the central participant in bilateral disputes, given its preponderant network ownership and role in various service offerings.

In some respects certain recommendations have elements in inconsistency. For example, an argument that regulation should be confined to core cases where the case for intervention is strong but then apparently arguing for an application of access regulation uniformly, irrespective of the economic power of the service provider and network owner, may give rise to a particular tension, and Mike will expand on that in the context of the Part XIC recommendations.

There's also a general theme that PowerTel detects running through the report which suggests a departure from industry-specific regulation or at least a softening of industry-specific regulation and a move towards generic regimes or nonspecific regulations. PowerTel's experience since deregulation would suggest that a departure from the present stated specificity is not warranted, even if some of the current regulations are clearly not working.

Where the current regime has proven unworkable or problematic - for example, Part XIB - the reasons need to be examined before a conclusive view could be reached that the framework or the fundamental underpinnings are flawed, rather than there being an implementation or practical resourcing problem. PowerTel particularly holds that view in relation to Part XIB where it considers the theoretical underpinnings to be fundamentally sound and the structure of the legislation to be fundamentally directed towards the right type of sanctions and incentives, but the practical workings demonstrate some degree of failure, at least in timing, which leads into our specific comments on Part XIB.

In PowerTel's initial submission it raised the view that criticisms of Part XIB in some ways describe the problems or diagnose the symptoms without analysing their causes. PowerTel remains of the view that Part XIB, even in its present form - and PowerTel concedes it needs some revision - provides, at least in theory, a useful set of remedies and disciplines on conduct abuses, and for that reason alone should be maintained. There were only a couple of proponents who argued strongly for its abolition and the majority of submitters appeared to argue for its retention, and some argued for an enhancement rather than a diminution of the ACCC's powers.

The chief critic of Part XIB was Telstra, who not coincidentally was the chief recipient of complaints under the relevant provisions. The commission recommended the repeal on various bases, notwithstanding the strong calls for its retention. In some respects PowerTel considers that this requires further analysis.

PROF WOODS: We weren't guided just by the numbers of arguers on one side or the other but by the merits of the arguments.

MR CHRISTOPHER: The particular work that Part XIB does may not be at the hard edge of competition notices and adversarial procedures. It operates more as a guiding principle or discipline in negotiations, and to that extent a great deal of its work is done behind the scenes, rather than in any obviously transparent way. PowerTel is of the view that without Part XIB or some analogous set of provisions, many issues that had been resolved would be left unresolved.

Picking up the commission's point about the sheer number does not equate to the validity of the argument, Telstra's complaints about the draconian nature of Part XIB should also be carefully analysed in the same way as the smaller players' - if I can call them that - complaints about - or calls for the retention should be analysed. Empirical evidence has demonstrated that Telstra has not been the recipient of any harsh penalties. True it is that there have been compliance costs, opportunity costs and other management time devoted to resolving Part XIB disputes, but at least on the side of penal sanctions or pecuniary sanctions being issued, Telstra can't point to any history of that in the past couple of years.

Most industry participants that PowerTel is in contact with, at least anecdotally, will consider that Telstra has got the better of the complainants and the ACCC in the majority of Part XIB disputes. Further, there's no empirical evidence that's been available to PowerTel, or at least was apparent in the submissions made by the parties, that suggest that Part XIB inhibits investment or that the cost of compliance is overly burdensome. There are numerous assertions to this effect but no hard evidence. True it is that where people controlling companies have to make investment decisions they obviously take into account the regulatory framework, there's no obvious connection between the effect of Part XIB and the cost of compliance and investment decisions.

PROF SNAPE: Will you tell the commission how you would get that evidence?

MR CHRISTOPHER: It would be difficult to work out whether it operates on the controlling mind and will of corporations in a subtle way in decision-making, but at the lowest level the sort of evidence that would demonstrate would be the type of data that Russell Emery referred to earlier, namely historical EBITDA analyses, projections, reviewing capital investment and attempting sensitivity analyses and regression analyses might be one way. I concede that it's a difficult exercise and one that's inherently problematic, particularly where the silent effect of Part XIB on investment decisions is not transparent.

PROF SNAPE: Would not that data support the alternative hypothesis that any investment which was anticipated to have a moderately low return but high risk would not be undertaken, and so you only get the high return ones in?

MR CHRISTOPHER: One could draw that inference.

PROF SNAPE: Sir, I think that the evidence that was submitted could equally support the opposite hypothesis. If you go and ask firms what investment was not undertaken, you do risk gaining the answer. We'd be very interested to see what evidence you would think could in fact be secured that would, first of all, not be ambiguous; and secondly, would in fact support the proposition.

MR CONRADI: The evidence that Russell referred to at the beginning was Telstra's EBITDA figures as a percentage of their revenue. If it was the case that they were only looking at the very most profitable investments, they wouldn't have a high EBITDA as percentage of revenue, because the revenues are fixed for the purpose of this argument.

PROF SNAPE: I'm not sure about that.

MR EMERY: We take your point, professor.

PROF SNAPE: Thank you.

MR CHRISTOPHER: Turning to the structure of Part XIB, it's been suggested that Part IV may represent a suitable conduct-related sanctional remedy or legislative set of prohibitions in lieu of Part XIB. PowerTel's view is that Part IV, in its present form at least, is inadequate. Part IV came into effect in 1974 and that's not to say that it lacks currency. Clearly it still is current. There are numerous problems with Part IV but the two notable ones are, firstly, it's not sufficiently particular to the telecommunications industry and therefore suffers from certain practical and legal problems as a viable remedy. Some commentators have suggested that recent High Court authorities, such as Melway, have ameliorated some of the Part IV problems.

A careful analysis of Melway and the reasoning which underpins the judgment would suggest against Melway representing any opening up of purpose based requirements into that cause and effects based test. Although, in its implementation the difference between purpose based test and effects based test has proved problematic, it's not to say that again the theoretical distinction is not an important one, nor that it's not exercising the minds of those people engaged in disputes around Part XIB. Further, telecommunications is not unique in implement ex ante or conduct-related regulation. It is true that most other forms of network infrastructure don't have specific anticompetitive conduct prohibitions. Nonetheless, there are various prices oversight regulations and other sanctions that regulate the owners or operators of energy, transport and other network based industries. Some parallels for their continued justification in those industries can be drawn in relation to telecommunications.

Further, the rationale for the 1997 amendments remains current and until one could say with confidence that the market can produce outcomes that obviate the

need for conduct regulation, or unless Part XIB was shown to be fundamentally deficient, rather than practically problematic, the presumption should be in favour of its retention, not its repeal. There are certain forms of anticompetitive conduct - for example, bundling or price squeezing - which would be particularly difficult to prove under a purpose based test. That is not to say that they, as a matter of theoretical jurisprudence, could not be proved. It's just that it would add a heightened burden on the part of those moving for a remedy under those provisions. Further, Part IV in its present form is characterised by a distinct lack of speed, and those legal practitioners and clients that have had recourse to Part IV can testify to those practical and procedural difficulties.

In summary, in relation to Part XIB, PowerTel argues strongly for its retention. Having said this, there is room for improvement and some of the recommendations include the implementation of new time line procedures, sunset provisions or tighter procedural rules, and imbuing the ACCC with broader powers, for example strengthening record-keeping and tariff filing rules, and seeking to redress information asymmetry difficulties. There is a cost to participants by increasing the regulatory burden. The question is whether that additional cost is warranted by applying a cost benefit analysis and determining whether, at this stage of the market's maturity, and given the continuation of the conduct related problems, the repeal is justified.

The other important point that needs to be made is there is a relationship between Parts XIB and XIC and the present regime, and similarly under the proposed new regime, if the recommendations were adopted by the commission in their entirety, the relationship between the conduct-related rules and the access rules would need to be very carefully considered. On the very preliminary basis of PowerTel's understanding of the commission's recommendations on Part XIC, there would remain a need for conduct-related regulation under Part XIB, although it may be the case that if Part XIC took on a particular form, there might be reason to revisit a view that Part XIB needed to be maintained. On one view a more uniform or less discriminatory access regime that moves more towards a generic or homogenous regulation would serve to strengthen the argument for the maintenance of Part XIB, rather than support its repeal.

They're the general comments in relation to the recommendations affecting Part XIB. On Part XIC my colleague, Mike Conradi, will make some particular points. Just as an introduction, two principal points that PowerTel would like to make in relation to the proposed recommendations are these: firstly, to converge the principles in Parts IIIA and XIC as a long-term aim again is laudable and would ease the cost of compliance and bring more certainty to bear on the economy generally. To this extent it's a desirable outcome. However, at this stage, to merge the principles would present a particular legislative challenge, as Part IIIA in its present form does not adequately take into account critical industry-specific principles, such as any-to-any connectivity, which do not sit easily with the sort of declaration criteria suggested by the commission in its proposed new Part XIC, or certainly would not sit

with the sort of criteria applying in the national significance test that currently characterises Part IIIA.

Further, PowerTel considers there is justification for asymmetric or non-uniform access regulation and, whilst conceding there are possible dangers arising from a regime in terms of inhibiting investment and unduly prejudicing incumbents, those dangers can be accommodated by adopting an overall reasonable access obligation and a more rigorous application of TSLRIC principles. On those two points Michael Conradi will make some particular comments.

MR CONRADI: The basic principle that we're coming from, which I think the commission has endorsed pretty strongly in the draft report, is that the aim of regulation should be that it be reduced to the minimum necessary to achieve the aims, whatever those aims are; whether it's the long-term interests of end users or overall economic efficiency - whichever aim you choose. We want to go for the minimum necessary to achieve that and not go over the top. We submit then, with that point being agreed, that what's proposed on Part XIC, or rather the current - there's a much better way to regulate access which would involve much less regulation, and that is one inspired by - I think we should say - the European Union.

I'll describe that in a bit more detail in a moment but what I mean - the sort of things that we could avoid, we'd suggest, are some of the detailed and complex regulatory decisions like what are the declaration criteria? Is this particular asset of significance to the national economy? Should we have a sunset on the declaration of this service? How many years should it be? Should we have an access holiday for this particular investment? Would this investment happen anyway? All of those decisions are ones which it is extremely hard for a regulator to make, because they essentially involve the regulator going behind the market players and looking at their motivation and trying to second-guess their sort of business decisions.

You could avoid all of that by imposing much more regulation only on the dominant operators. When I say "dominant" there's obviously some room for discussion about exactly what the criteria should be. Perhaps you'll say significant market power but having some sort of test to do with the degree of market power and imposing extra access obligations on those carriers. As regards all the rest, you don't have no regulation. You have a simple statement that they must be reasonable in what they offer in the terms in which they offer access. As I said, I will describe that a bit further in a second.

But the main advantage of this system as we see it, is that the regulator is only making economic decisions and those are decisions which are much more suitable for a regulator to make, so the regulator is deciding what is the market. Does this operator have the ability, profitability, to raise prices for a non-transitory time? They don't have to look at business decisions. They don't have to look at whether or not investment will be made. They just have to look at economic questions.

To discuss our suggestion in more detail: to be clear, it is not the same as the European Union but it is based on that. What we suggest is that all carriers, whether dominant or not, should have an obligation to offer access on reasonable terms - and again I will return to what that means - but dominant carriers, and again that could be a different test, but the carriers with more market power will also have further obligations and three - I'm coming under three headings.

The first one is transparency: that means there should be publication of all of their technical information and all of their prices and all of their terms and conditions for their wholesale services, so that includes the terms and conditions that they offer to their own retail arm, but it also includes the terms and conditions offered to other market entrants. That is a reference interconnection offer, to use the European Union terminology. That's a publicly available list of all services which are available on standard terms and, moreover, that list would be added to in time as new services became available, as long as they were subject to the regulation.

In other words if the carrier was still dominant in the relevant market and that the market will change as new markets develop, then these obligations still apply. So the first extra obligation is transparency, which I have just discussed; the second one is non-discrimination. That again extends not just to prices but also to all terms and conditions - service levels, times a service will be switched on, even down to the details of how you get access to the switch, if necessary. There will not be any undue discrimination.

The third one is cost orientation and, as we have suggested, that should be on TSLRIC principles. More specifically, if I talk about some of the details of that. On the criteria for declaration, in the first instance we would just suggest you don't - if a proposal like the one we're suggesting is adopted then it becomes a sort of irrelevant question because you would say, "Is this service provided by an operator which is dominant in the relevant market?" If yes, then it's declared. If no, it's not. That's the only thing you need to look at. But assuming you don't adopt our proposal on that or examining it in the way that it is set out at the moment, the draft report suggests strengthening the criteria for recommendation and, in particular, it suggests there should be introduction of a test that elements could not be declared unless it was of significance to the national economy.

We would suggest that that is inappropriate because, as Andrew has said, what's really fundamentally different about telecoms is the absolute requirement for any-to-any connectivity, so that means if you just isolate any one network element - you know, connection between two small towns in rural Australia, they may well be taken by themselves to be of no significance to the national economy, but the principle that any operator should be able to ensure that its customers get access to any other point anywhere in the country is so fundamental that that means every element is of significance to the national economy taken on that broader view, so we don't think you need to introduce that principle and, to the extent it means anything, we think it is counterproductive.

MR CHRISTOPHER: The National Competition Council, when considering recommendations for declaration of services has grappled with the concept of national significance, as have submitters who have made submissions in relation to such applications for declaration. The application of that criteria is visited with particular difficulty in the context of less complex network facilities, such as rail networks and other forms of fixed infrastructure. When one adds the added complexity of telecoms networks which, by definition, require another level of analysis because of the requirement for any-to-any connectivity, the concept of national significance in its practical application would have some very real difficulties and it's easy to imagine that very few defined networks or parts of networks would ever satisfy that criteria. PowerTel has a concern that - - -

MR EMERY: On their own?

MR CHRISTOPHER: On their own when taken in isolation as a discrete network element, whereas when taken as part of a wider series of elements - if I can call it that - it may be capable of satisfying the national significance criteria. Of itself it will be extremely difficult. The other point that is relevant is there has been a trend towards de-declaration rather than further declaration in the present regime, so it's hard to imagine why there would be a particular concern that the present declaration criteria is overly burdensome in those circumstances where empirical evidence suggest a move away from further declaration towards de-declaration.

MR CONRADI: That was the first specific point which we wanted to discuss in more detail. The second one is, we think it would be helpful to have a very clear statement that the access prices or other operators of the access prices for dominant operators should be based on TSLRIC principles, and to make it crystal clear that that does not mean only that they're based on any one operator's actual costs but they're based on the cost of a notional efficient operator. That's very important because it seems from our experience that that principle isn't actually understood by all industry participants and it can lead to very significant difficulties.

Under the system as we see it the TSLRIC price would be agreed or, if it couldn't be agreed, it would be set by the regulator and then it would be published as part of the reference interconnection offer that I discussed earlier. That regulated price would then become, just through the ordinary operation of market forces, a benchmark of what was considered to be reasonable, because remember what we are suggesting is that non-dominant operators should only have an obligation to be reasonable in what they in the access terms offer, so that will help with the third point which I wanted to discuss, which is how you deal with two access disputes.

The draft report suggests as a justification for maintaining an access regime across the whole industry rather than on specific participants, that even non-dominant operators have the ability to abuse their bottleneck control over their own lines and therefore the draft report says you ought to have all of these

regulations which apply across the whole industry. We suggest there is a better way to deal with - or rather to prevent non-dominant operators from abusing their position in that way and, that is, if they only have an obligation to be reasonable in the terms that they offer access then when they are negotiating with Telstra or whoever - it doesn't have to be Telstra, it could be another non-dominant operator - if they don't offer reasonable terms the dispute gets referred to the regulator and the regulator will use the published TSLRIC prices as a benchmark. So they're not going to be able to ask for something outrageously expensive because the regulator is not going to agree to that. TSLRIC is the benchmark.

In practice you can expect - and European Union experience is - that similar networks end up with similar but not necessarily identical access prices, and the fact that they're not identical is itself a good thing because it means to the extent that a new operator provides something different - it provides a unique service or something special - remember I am not talking about - to the extent their network is different; just to the extent the services they provide are different - then they can charge and they can be reasonable when they try and charge a different access price. So it's perfectly reasonable for mobile operators to have a higher access price than fixed-line operators.

There are other examples of other services you might want to encourage. Just off the top of my head, Orange has a service, Orange 1, which combines elements of fixed and mobile. If you try another more interventionist approach which says, "You have to say your services (a) fixed or (b) mobile and charge an access price." You remove the incentives on that sort of innovation, so this is much more flexible but does have enough in it to prevent abuse of bottleneck power.

MR CHRISTOPHER: And should also operate to reduce the proliferation of 2A access disputes to the extent there's industry expectations as to particular service offerings having like prices, which is an important point.

MR CONRADI: Yes. That's all I really had to say on XIC.

PROF WOODS: Thank you, Mr Emery and colleagues. We appreciate PowerTel making the time to prepare submissions and to come before the inquiry, and we have welcomed your input on each occasion. As you remind us, it is 10 months since we started off on this process and had dialogue with you. Perhaps you could provide for our benefit just a little update of PowerTel's business and current activities, so that we can refresh our minds as to where you are currently.

MR EMERY: I think we identified ourselves as being primarily focused in the CBD business districts of Brisbane, Sydney, Melbourne. We had our own infrastructure in each of those cities and connected between each of those cities. We also have leased facilities to Perth and Adelaide and we are currently continuing our business plan to grow our data network. We're primarily a data-offering company. We also offer voice but our focus is data and wholesale services. We have increased

the number and the variety of our customers that are now connected. In the last period since we saw you we had just completed our network, so that is the thrust of our business case. So we're still not focused on the residential market.

PROF WOODS: Okay. I just wanted to make sure you were still largely in terms of business model as you were before us before, but you have been extending your customer base through buildings and the like.

MR EMERY: Yes.

PROF WOODS: I take it also from a comment you made that you're an access provider in terms of a dispute and that Telstra is the access seeker?

MR EMERY: Yes.

PROF WOODS: Is there anything you want to elaborate on in terms of that process? How you find yourself as the access provider?

MR EMERY: Unfortunately, as you know, these disputes have very strict confidentiality provisions.

PROF WOODS: Yes.

MR EMERY: We had actually sought making the dispute a bit more open, but that was opposed and we're still bound by it. But it is on the issue of PSTN terminating access, the charges to be paid by Telstra to terminate on our network.

PROF SNAPE: I am sorry, I missed the last bit.

MR EMERY: The charges to be paid by Telstra to terminate on PowerTel's network.

PROF SNAPE: You are unable to reach a commercial arrangement?

MR EMERY: That's correct, yes.

PROF WOODS: Does that make you dominant in that particular little submarket?

MR EMERY: If we were in a position to give you further confidential information about the various offers I am sure you would be interested. I will have to get some legal advice on what I can give you.

PROF WOODS: No, no. To the extent you can that would be very helpful, but I notice one of your colleagues in their comments cast some doubt on whether the commission had adequately dealt with the question of bilateral negotiations, but I do draw your attention to chapter 9 and, I think, some fairly extensive coverage there.

An improvement in transparency was one of the key themes that we were putting forward.

MR EMERY: Yes.

PROF WOODS: And I trust that actually has your support, in the directions to be taken.

MR EMERY: Yes, it certainly does.

PROF WOODS: Thank you, Mr Emery. I was fairly confident that that would be your view on that. You have spelt out now in some detail what was intended by the criteria of transparency costs orientation and non-discrimination, and we thank you for that.

PROF SNAPE: How do you define "dominance" in a market?

MR EMERY: I'm not an economist. I've got one year of university-level economics. I am not purporting to be in a better position than you to set that, but my understanding is that the usual test is the ability to profitably raise prices for a non-transitory period.

PROF SNAPE: That was, I think, not a test for dominance but for market power, significant market power. If you are relying on that test, then it would seem to me that a small participant, for whom termination was important on their network, might in fact have some significant market power, and that is one of the things that was considered in the draft report. In your terms, by your suggested definition, it would be dominant in that market, and so it doesn't seem to meet your criteria in that you're trying to get a dominance in general.

MR EMERY: If that was the result - I mean, we were careful not to try and set exactly what the economic test should be, but suppose that was the result. Then under our proposal the result would be that the non-dominant operator would have to be transparent, non-discriminatory and cost-orientated on the prices for access to its network, but not on anything else.

PROF WOODS: Not unreasonable.

PROF SNAPE: So you are allowing, then, for dominance within what you might call, if you were calling the whole thing the "telecommunications market", in a submarket within that general market.

MR CHRISTOPHER: Yes, one must be careful in segmenting the market in a too fine manner, because the reality is that some participants possess market power or dominance or a degree of influence, or whatever test one wants to adopt, in certain parts of the market, and the effects are felt in other parts of the market, and

ultimately dealings as between one functional level of the market, be it two carriers, for example, doesn't necessarily translate directly into the dealings that one would have with its customers. I think if you characterise an access provider being dominant or non-dominant or having market power or not having market power, you can't undertake that analysis just looking at a particular network element for which access is sought; one needs to take a more broad view of the markets and industries within which they participate, so that - - -

PROF SNAPE: Well, that's what I'm trying to get at to tie this down, because maybe what you are saying is that Telstra is the dominant party so it should only be Telstra. Now, if that's what's being said, I guess let's say it, because if one is going the other way into market power - I think it is that in a submarket if you've got these questions, which are well explored in a lot of the legal-cum-economic literature on these matters, but what you've suggested at the moment does not seem to give you the result, which I suspect is behind what you are saying - that it is Telstra only.

MR CONRADI: I don't think we would want to say that it's Telstra only. Of course in most cases in most markets it will be Telstra, but I think we're definitely prepared to acknowledge that there may well be markets where Telstra is not dominant. It may be the case - I'm not saying it is - that wholesale markets between Melbourne and Sydney, or mobile markets - certainly Telstra might not be, and other operators might be. So we're not trying to - this isn't all code for "regulate Telstra, don't regulate anything else".

PROF SNAPE: Well, it would I think be helpful if you could explore this further and tried to pin down more securely what you're getting at in this, because I think at the moment it's rather loose.

PROF WOODS: Certainly that question of what constitutes a submarket, the level to which you would go, is very relevant. I mean, presumably PowerTel actually wants to become a bit more dominant in some of its market areas, and that's the focus of its business case, but you could also see where an operator in a provincial city might roll out a particular form of network that is significantly higher capacity than Telstra's existing copper network. Now, do they become the dominant entity insofar that all others who want to connect would be wanting to connect into that new operator? So we need to understand at a practical level just what constitutes an acceptable degree of fine-graining without destroying the purpose of your proposition.

PROF SNAPE: And insofar as the Trade Practices Act moved away, in fact, from the dominance concept a number of years ago into a "significant market power" concept, we do need to - it would probably be better, if in fact this is what you are meaning in this context - if significant market power is what you are meaning, then it would be best to express it in those terms.

MR CHRISTOPHER: Yes.

PROF SNAPE: And I think that you were referring to the sort of criterion that was within the mergers guidelines - - -

MR CHRISTOPHER: Yes.

PROF SNAPE: - - - in which case, to tie it down more securely into that, if that's what you're drawing upon - - -

MR CHRISTOPHER: Yes.

PROF SNAPE: - - - so that - and make sure that simple-minded economists like us don't go astray.

MR CHRISTOPHER: Sure. I mean, those definitional issues that you quite rightly point to certainly in any transitional phase would be very important. Over time, the definitional issues or any sort of difference in treatment would become less relevant as a move towards transparency and a reference pricing regime and a more rigorous application TSLRIC would render some of those definitional issues less critical than they might be in any transitional phase.

PROF SNAPE: Could I pick up "non-discrimination" as well, since it's in that context there, and ask you what - and this is one of the three criteria that would be imposed upon what you call a dominant operator - and ask precisely what is meant by "non-discrimination". Just to illustrate it, does that mean that one would not be able to discriminate in a price manner, in what is often regarded as an efficient manner in Ramsey pricing? So that if you have to cover fixed costs you are in fact pricing those with the low elasticity of demand more highly than those with a low - sorry, low elasticity of demand more highly than those with a high elasticity of demand, so that you're pricing to market to cover your fixed costs?

Would it mean that you couldn't discriminate in that manner? Would it mean that you can't discriminate between large-volume or small-volume customers? Does it mean that you post up a very detailed menu on your front door that includes specification of the elasticity of demand so that, so long as you can fit into a particular category, you can go in the door and say, "Give me that"? What do we mean precisely - precisely - because this just has to be precise. What do we mean by "non-discrimination"?

MR CHRISTOPHER: Well, there's different conceptions of non-discrimination. At one extreme it would contemplate no tolerance for any forms of discrimination, including those you've just outlined, but that would - - -

PROF SNAPE: But would you advocate that? I mean, that seems to be a very - - -

MR CHRISTOPHER: No. No.

PROF SNAPE: - - - inefficient pricing policy.

MR CHRISTOPHER: Clearly not. That would have no justifiable basis on the application of any rationale. So some forms of discrimination would be tolerable. Precisely which ones - volume based, cost based, price elasticity based - it would be impossible, I think, for PowerTel to offer a concluded view on which forms of discrimination might be more acceptable than others immediately.

PROF SNAPE: So it's really the menu that you're - - -

MR CHRISTOPHER: Yes.

PROF SNAPE: A posted detailed menu is what you're calling for?

MR CHRISTOPHER: Yes. I mean, that would be a fairly sort of prescriptive regime, and it would be difficult to define exhaustively which forms of discrimination might be applicable in every circumstance, but it's do-able and - - -

MR CONRADI: What I think we might have in mind is every time a dominant operator with a degree of market power reaches an agreement with anyone else which is to do with interconnection or access or wholesale services, then the full details of that are publicly available, and anyone else who thinks that they don't differ from the position of that other party in any material way would be able to get access - would be able to have the benefit of exactly the same agreement. So, you know, if they have significantly different volumes then it may be that there's a justification for imposing a different price, but as long as that difference is justified on the real basis of difference in cost.

PROF SNAPE: So they wouldn't be able to Ramsey price?

MR CONRADI: I'm not too familiar with the concept of Ramsey pricing.

PROF SNAPE: Well, that's pricing according to the elasticity of demand for the product - - -

PROF WOODS: Elasticity of demand, yes.

PROF SNAPE: - - - which is generally regarded as an efficient form of pricing if in fact you're having to cover your costs, fixed costs, on the economies of scale and if - - -

MR CHRISTOPHER: Yes, I mean, it's generally regarded as efficient provided there's some reliability on the provision of a service to the seeker.

MR CONRADI: But we're talking about identical services here. To take the

example of Telstra - maybe I've just misunderstood what Ramsey pricing is, but we're talking about offering the same service to companies A, B and C, so that I assume that the elasticity will be very similar.

PROF SNAPE: That's not necessarily so.

PROF WOODS: Not necessarily.

PROF SNAPE: If A, B and C are in fact firms with different products.

MR CONRADI: I see.

MR CHRISTOPHER: I don't think, as a matter of principle, PowerTel would have a difficulty accepting the validity of Ramsey pricing, provided that in its application there was some rigour applied to the costs associated with the Ramsey pricing.

MR EMERY: Perhaps I could turn it around and say that this sort of recommendation is driven from perhaps the example of an arbitration with Telstra where we're not the first party on the same subject, and we're really proposing that, where you have a regulated service, that regulated service be done in such a way that there is non-discrimination and transparency, so if I'm buying the same type of thing from Telstra and it's a regulated thing for the purposes of any-to-any connectivity, then the scope for that regulatory gaming, confusion and everything should be eliminated. That's where I would come from.

MR CHRISTOPHER: I mean, one way of employing non-discriminatory pricing is to have (indistinct) parameters which tolerate Ramsey pricing within those parameters.

PROF SNAPE: Thank you.

PROF WOODS: Thank you. Perhaps to complete the trifecta, if we look at transparency, you're proposing there be full transparency for those who have dominance or market power, however you end up defining your proposition, which basically is posting the menu.

MR CONRADI: Yes.

MR CHRISTOPHER: Yes.

PROF WOODS: You suggest for those that don't fall into that criteria that they be required to have reasonableness, and where there are disputes they go to arbitration. Do I conclude from that, therefore, that those disputes are non-transparent, in which case, isn't that a little contrary to your proposition?

MR CONRADI: No. The results of them would be published. They would be

public hearings, if required.

PROF WOODS: So you would have transparency in dispute resolution relating to reasonableness - - -

MR CONRADI: Yes.

MR CHRISTOPHER: Yes.

PROF WOODS: - - - just not a front-end commitment and requirement to transparency in posting a menu of prices of non-dominant players?

MR CONRADI: That's right. I see. I'm sorry. We're talking about where there's a dispute in regard to someone that's not dominant?

PROF WOODS: I was just trying to extend your transparency and work out whether you in fact didn't want a transparent dispute resolution, which was contrary to where Mr Emery was heading before.

MR CHRISTOPHER: I don't think that's the position.

PROF WOODS: No.

MR CHRISTOPHER: There would be transparency. Indeed, if there was transparency in terms of adopting a menu of posted prices, one expected consequence would be for a drop-off in the amount of disputation, and if you made disputes transparent additional, you'd expect that over time there would be, in an ideal world, no disputation because there would be full transparency.

PROF SNAPE: We might pause for a moment to digest some of your comments.

PROF WOODS: Thank you. We were discussing the question of transparency and I think that completes the look at those three issues of transparency, cost orientation and non-discrimination.

MR CONRADI: We had the opportunity to have a quick chat. We would like to spell out that we're not necessarily trying to avoid the conclusion that non-dominant operators, which nevertheless have bottleneck control, should be obliged to be transparent, non-discriminatory and cost-orientated. We don't consider those three obligations are so onerous and terrible that we're doing everything we can to try and find an argument to avoid that. If the conclusion is that an operator like PowerTel, which has bottleneck control over some of its own access lines, must publish prices for access to those lines, must be non-discriminatory and those prices must be based on TSLRIC principles, we don't think that's such an outcome.

PROF WOODS: I appreciate your clarification of that point, but what it then does is reduce the differentiation between those who are dominant and those who are non-dominant and we come back, I would have thought, to an industry based regime.

MR CONRADI: The reason I don't think it does that is because, to take PowerTel's business again, when it's building a trunk link between two cities it's not dominant in that and we're suggesting it shouldn't have any obligations, other than to be reasonable - - -

PROF WOODS: Perhaps that shouldn't be declared. It's a separate question.

MR CONRADI: Right. Well, rather than having this whole system of declaring or not declaring it, we just say if it's not dominant it's not subject to access regulation, other than general obligation to be reasonable.

MR EMERY: We just need to go away and - - -

MR CHRISTOPHER: And refine the argument.

MR EMERY: - - - refine it a bit.

PROF WOODS: We look forward, Mr Emery, to your subsequent submission on that matter.

MR CHRISTOPHER: The draft report made it clear that even smaller operators have power over their own networks, and it might follow from that that there shouldn't be any difference in treatment so far as access obligations are concerned. If that ended up being the firm conclusion, subject to these comments that are made, that might be an acceptable outcome. But the price for that would be, in PowerTel's view, at least some maintenance of a conduct-related regime to check abuses, whoever may be perpetrating them, whether they be non-dominant, dominant, market power or less market powerful operators.

PROF WOODS: We'll look forward to Mr Emery's further submission. You put forward a number of considerations in relation to XIB. Should it be repealed? Can you outline for us some of the behaviours that you would expect to be confronted with upon its repeal that would be of great difficulty to PowerTel?

MR CHRISTOPHER: Obviously, as indicated by Mr Emery, PowerTel has recent experience in relation to Part XIB and would not want to disclose that experience in the context of this hearing. But one might imagine practices such as what are often described as bundling or price squeezing, or the application of whole-of-business discounts or conduct that relies by definition on being an integrated operator operating in different functional levels of the market, conduct that relies upon the ability to absorb long delays in the conclusion of commercial negotiations, conduct

that involves reliance on a lack of information on those seeking a particular commercial outcome. They all sound like proxy terms for Telstra, and to some extent they are. I don't think PowerTel is embarrassed to say that.

But one should not form the conclusion that there are not other persons equally capable of taking advantage of that type of conduct for commercial aims. If an examination is had of the section 46 cases since the enactment of the Trade Practices Act, one will see that it's not only monopolists or massive corporations that have had section 46 allegations against them. In any particular instance anyone can take advantage of a particular position or market power or dominance, as the case may be. But that's the sort of conduct that Part XIB, we think, is directed to you and if it was repealed, there's no ready substitute for it in section 46.

PROF WOODS: Is PowerTel able to assist the commission by indicating the number of times you've gone forward to the ACCC and advised them of behaviours that would warrant them calling upon XIB and that the process of discussion and, may I use this phrase, threat of application of XIB has caused a change in behaviour by the other party?

MR EMERY: I think we'd like to do that separately.

PROF WOODS: Okay. If it is being used actively to discourage anticompetitive behaviour, that's very helpful for us to understand - that even though that may then not necessarily proceed to overt action.

MR EMERY: Sure.

MR CHRISTOPHER: There are a few dimensions to it. As indicated, at the most extreme view of the spectrum, it's the commission causing a competition issue to be noticed, and there are gradations from that; letters of complaint, inquiries, it having an unseen silent hand on commercial negotiations. It's obviously hard to get a handle at the lower end of the gradations, whereas the issue of competition notice is obviously - - -

PROF WOODS: Yes, we can measure those.

MR CHRISTOPHER: I would anecdotally suggest that a significant amount of the work that it does is done at the lower end of the spectrum.

PROF WOODS: Perhaps some elaboration from PowerTel's perspective might help us to understand the dynamics that XIB creates in the marketplace. Are there other matters that you wish to bring before us, Mr Emery?

MR EMERY: No, thank you, commissioner.

PROF WOODS: Your colleagues?

MR CHRISTOPHER: No, thank you.

PROF WOODS: Thank you very much for that. Again, may I thank PowerTel for being a strong contributor to this inquiry and we appreciate the efforts you go to in that respect. Are there any others present who wish to make a statement to the commission this afternoon? That being the case, I'll adjourn today's hearing and we will recommence tomorrow morning at 9 am.

AT 3.14 PM THE INQUIRY WAS ADJOURNED UNTIL
WEDNESDAY, 16 MAY 2001

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