SUBMISSION TO PRODUCTIVITY COMMISSION

by

AUSTRALIAN TELECOMMUNICATIONS USERS GROUP

1 Introduction

The Australian Telecommunications Users Group (ATUG) is pleased to respond to the Productivity Commission's invitation to respond to its March 2001 Draft Report on *Telecommunications Competition Regulation.*

As the Commission will be aware ATUG has made two previous submissions during this inquiry. ATUG apologises for the lateness of this current submission.

ATUG congratulates the PC on the scope and depth of analysis of its Draft Report but, perhaps not surprisingly, holds differing views in relation to a number of the recommendations the PC proposes to make to the Government. In this submission ATUG outlines these views and makes specific proposals on a number of them. ATUG would hope to have the opportunity to discuss these in detail with the Commission at a convenient time.

ATUG intends to be represented at the Public Hearing commencing in Sydney on Monday, 14 May 2001.

2 ATUG's Policy Perspective

In assessing the recommendations set out in the Draft Report, ATUG looks at their potential impact from two points of view. While it is aware of the need for good policy to drive the industry in the desired direction, nevertheless it also must consider the practical impact of policies on the industry in general and end users in particular.

ATUG believes that the major underlying principles in the *Telecommunications Act 1997* (TA) must be maintained in making any changes to that legislation. Specifically these are: the overarching requirement for any-to-any connectivity, an emphasis on services rather than facilities and the importance of the industry delivering long term benefits to end users.

The need for any-to-any connectivity between any and all networks providing services to the public is arguably unique to this industry and underpins the interdependence of all players at the infrastructure level. It is this requirement that demands an industry-specific approach to regulation of telecommunications.

In ATUG's view the PC's assessment of the current performance of the industry is based overly much on a view of what has happened in the industry rather than what could have been the case had all players accepted the concepts and intent of the legislation rather than participating in regulatory gaming. Most importantly, the time is now right to focus on the future and meet the needs of all end users particularly those Australian firms competing aggressively in what is an international marketplace.

The development of the industry, particularly since 1997, has led to an over emphasis on shareholder value, company profits and share price rather than end user service. As evidence of this, during the dot.com mania of 1H2000 the return to shareholders was driven by arbitraging stock prices rather than building value from increasing revenue streams and growth in the underlying core business of companies.

This experience cannot and should not be forgotten or worse ignored as an element of the context in which this current review by the PC is taking place especially as its recommendations are likely to have a profound impact on the way the industry develops and operates in the future.

3 Assessment of Competitiveness in the Industry

3.1 Current Status of the Market

Despite nearly four years of open competition operating under the TA , Telstra still retains a market share of over 95% of all access lines in the Customer Access Network (CAN). ATUG's view is that this indicates an urgent need for another mechanism to enable the ACCC to address the problems this huge imbalance causes, especially from an end user's perspective. ATUG and its members see the effect of Telstra's near monopoly control of the CAN as preventing them from obtaining the range of new services from competing carriers and service providers that they need to maintain their competitiveness in their individual markets.

While the situation in the mobile market appears to be more balanced, clearly Telstra is in a very strong position there also. Telstra Mobilenet has 46% of all customers as against Cable and Wireless Optus' (CWO) 33%. Another measure, that is revenue,

shows how considerable the imbalance really is – Telstra has 53% of mobile revenue while Optus has only 28%, a little over half of Telstra's.[1] Again, it is clear that Telstra's market power in mobiles is strong and growing.

In another area of the mobile market; the cost of calls to mobiles from fixed services, ATUG sees very high prices being charged by mobile carriers, especially compared with the price of calls within the fixed network. For example, the price of a call to the UK is now around 15 cents per min. while the price of the cheapest fixed to mobile call is around twice this. ATUG's view is that this is clear evidence of the failure of competition in the mobile market.

Looking at another aspect of the industry; the number and strength of competitors, while there are over 70 licensed carriers, most industry observers, including those in the Finance industry, believe we are going to see a period of consolidation in the near to mid term. This will likely result from the larger players getting very much stronger and smaller players selling their businesses to them. Thus the outlook is for less competitors rather than more therefore careful attention must be given to stimulating strong competition among the survivors.

Looking at future technological developments that are likely to lead to the offering of new services, it is not clear that, in the current environment, many are likely to emerge in the near future. VoIP, while it may reduce costs somewhat and as a consequence lower prices, is actually only a substitute for the existing circuit switched service. What Australian businesses really want are new services closely aligned to their business needs.

While , in the mobile field, 3G has been promoted by some as the next platform to bring about a breakthrough in applications development, others have doubts about its wide acceptance and hence its viability.

As far as ATUG can determine, new services development does not appear to be high on the agendas of the larger carriers who, ultimately, will decide if and when these are to be made widely available to users.

3.2 While the prices for many telecommunications services have undoubtedly fallen in Australia, ATUG has concerns about these vis-à-vis the prices of comparable services in countries which compete with Australian businesses. ATUG is concerned that the PC does not appear to have assessed Australian telecommunications prices, both wholesale and retail, against international benchmarks.

In addition, although call prices have fallen, similar reductions in other services

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[1] Deutsche Bank Weekly Report, 27 April 2001, p 14

upon which businesses also depend, have fallen little or in some cases not at all and provisioning times of these are very poor.

In summary, ATUG's view of the telecommunications industry is that there remains a lack of robust, effective and innovative competition in many parts of the market and users, in particular business users, are being adversely affected especially in their attempts to compete internationally.

4 Industry Regulation

4.1 Anti-competitive behaviour

ATUG submits that there is still evidence of serious anti-competitive behaviour in the industry, particularly by Telstra. An example is Telstra's pricing and availability of access to its CAN, the prices of business services, for example broadband, and its dealings with its competitors in a number of areas; for example, charges for PSTN interconnect and for termination of mobile calls from the fixed network.

ATUG has been, and continues to be, concerned at the slowness of the ACCC to act when prima facie evidence of anti-competitive behaviour is brought to its attention. While ATUG recognises that the ACCC must act within the limits of its powers, nevertheless, it believes that the ACCC should act more speedily and decisively to limit anti-competitive conduct and its adverse impact on other players. Ultimately, it is the users who suffer as a result and it is they who are forced to carry the cost of delays in redressing such conduct.

ATUG requests the PC to consider ways by which the ACCC could be given power and encouragement to address anti-competitive conduct more expeditiously and effectively. The timeliness of outcomes must be a key element of the PC's final recommendations.

4.2 Competitive attitude

The larger players in the industry continue to take a 'protect or perish' approach to competition from smaller competitors, rather than 'participate or perish'. Put in practical terms, large carriers are not taking a commercial approach to negotiations but are, instead, using their market power to delay outcomes and limit competition by taking a negative approach to negotiations and, when taken to arbitration, using regulatory gaming to delay final decisions.

4.3 Policy, Pricing, Process

While the Government has policies in place to enable a truly competitive marketplace to develop, pricing does not reflect strong effective competition in all

areas, nor has the ACCC the powers to enable it to implement promptly the Government's policy intentions. This inability is caused by the current legislation permitting large players to engage in regulatory gaming to the detriment of their competitors' businesses and, in the final result, end users.

ATUG believes that the experience of the past four years does not support the PC's view that there is regulatory overhang which should be redressed. ATUG submits that the contrary is the actual situation – the ACCC needs additional powers to enable it to carry out its responsibilities effectively and in a timely manner.

5 ATUG's Comments in Detail

5.1 Draft Recommendations 5.1, 8.1, and 8.2

Repeal of Part XIB

(a) ACCC's use of its powers

ATUG's experience of the ACCC's execution of its responsibilities is that it has used its powers sparingly and has chosen not to intervene when it is of the view that certain matters are best left to commercial negotiation and the operation of market forces.

In fact, there have been times when ATUG would have liked the ACCC to have acted more promptly and decisively but accepted the ACCC's view that it was unable to do so under the limited powers it currently has under the TPA.

ATUG would therefore support a strengthening of the relevant legislation rather than its repeal or even a weakening of it, particularly to ensure more speedy outcomes.

(b) Investment in infrastructure

ATUG has noted, and indeed Telstra has indicated publicly on a number of occasions, that the current anti-competitive provisions of Part XIB of the *Trade Practices Act 1974* (TPA) have led Telstra (and possible others) to make investment choices that will result in a reduction in investment in infrastructure in Australia in the future.

ATUG strongly questions the PC's acceptance of this view. ATUG believes that, if Telstra has made such a decision, it has done so for reasons unrelated to the problems it perceives arising from Part XIB of the TPA.

Telstra's CEO has stated on a number of public occasions that Telstra intends to decrease its dependence on the Australian market in favour of increased investment and activity in international ventures. Such a policy shift can only mean that Telstra is in the process of transferring capital from the Australian to the international market.

In ATUG's view Telstra's investment policy shift clearly demonstrates that it sees overseas markets as having greater potential for profit making than the Australian market. While ATUG does not take issue with Telstra's decision only the reasons it has stated to the PC for making it, nevertheless ATUG is surprised that Telstra has not focussed on growing its Australian business by promoting new uses and applications based on its existing infrastructure.

In fact, ATUG believes that the current policy framework has led to a greater emphasis on the provision of facilities, that is infrastructure, than on the provision of a wider range of cheaper, innovative services.

ATUG views this trend with concern as it believes that on-going facilities-based competition may not be sustainable in the Australian market in the longer term.

(c) PC's recommendations relating to anti-competitive behaviour

ATUG strongly opposes the recommendations relating to repeal of Part XIB.

In our July 2000 submission we advised that "the potential for instances of anti-competitive conduct to take place do not appear to have declined…". Furthermore, we said that, "In the telecommunications industry, the current size imbalance between industry players … suggests that the creation of a balanced or level playing field … is unlikely to develop without further regulatory support". Consequently, we strongly advocated enhancement of the *Trade Practices Act 1974* (TPA) specifically Parts XIB and XIC.

ATUG considers that the PC's arguments for anti-competitive conduct in the industry to be dealt with under the general provisions of section 46 are based on an overly optimistic interpretation of Part IV in general and section 46 in particular.

The PC has referred to the ability of the Courts to infer a prohibited purpose from the circumstances in which a firm's conduct takes place. In practice, it is extremely difficult to infer purpose in such situations. Furthermore, section 46 is not concerned with overall reduction in competition as a result of the behaviour in question.

In contrast, the effects test in section 152AJ of Part XIB allows the ACCC to act against an offending firm without the need to go through the very difficult process of identifying a proscribed purpose, thereby leading to the ACCC being in a position to act more expeditiously.

ATUG submits that a better approach to Part XIB would be to remove some of the legal obstacles that hinder the ACCC's attempts to act as quickly as it and many industry players believes it needs to curb unlawful conduct.

Another difficulty with the PC's proposal for Part XIB is its assumption that anti-competitive conduct could be addressed under Part XIC rather than Part XIB. This would not be practicable as anti-competitive conduct does not necessarily always occur in relation to declared services and Part XIC only relates to such services.

This would be aggravated if the PC's proposals for changing the test for declaration of services were accepted because the vast bulk of services would then not be declared.

The PC's proposal to retain the information-gathering powers in Part XIB would appear to be impractical and ineffective if the competition safeguards were to be repealed. In fact ATUG believes the current information-gathering powers need to be backed up with enforcement powers to be practically useful.

ATUG would argue, and it believes it would have the support of many industry players, that far from being ineffective, as the PC apparently believes, Part XIB has had a deterrent effect on the larger players in the industry. Although there is still evidence in the market of misuse of market power, nevertheless ATUG believes that there would have been even more serious problems had it not been for the industry-specific provisions of Part XIB.

For all these reasons, ATUG does not believe that repeal of the anti-competitive provisions of Part XIB is consistent with the Government's objectives in relation to competition in the industry nor experience of the market behaviour of competitors over the past four years.

5.2 Draft Recommendations 8.3, 8.4, 8.5, 9.1,

Amendments to Part XIC

(a) Negotiation versus Arbitration

In its first submission, ATUG expressed concern that commercial negotiations were not being used as the main avenue for obtaining access to declared services on reasonable terms and conditions, as the Government had intended. Industry experience is that access seekers have generally found it necessary or perhaps more expedient, to seek arbitration at an early juncture in their negotiations with access providers rather than continue with what has become normal industry practice: long drawn out negotiations that, more often than not, become deadlocked.

ATUG believes this to be contrary to the intention of the legislation which envisaged commercial negotiation as the primary method of gaining agreement between access providers and access seekers with arbitration acting as only a 'safety net'.

ATUG is very concerned that the trend to a legal solution , that is arbitration, to establish access arrangements, is causing a blow-out in the operating costs of both access seekers and access providers with consequent adverse impact on prices of services to end users.

There is also the matter of delay. Arbitration has been shown to be a long drawn-out process during which time the access seeker may or may not have the benefit of an interim determination.

For these reasons ATUG believes that end users' interests are better served by access providers and access seekers reaching agreement through commercial negotiation rather than through arbitration.

ATUG had hoped that the PC would have addressed this problem in its review - a number of industry players brought this to its attention in their submissions – as it seems to have become endemic in the industry and in dire need of resolution.

To assist the industry in restoring the primacy of negotiations ATUG, in its first submission, recommended that the Part XIC process include a requirement for the disputing parties to enter into mediation/conciliation before the ACCC agreed to arbitrate on a particular dispute. ATUG continues to support the concept of mandatory mediation as the first step in resolving differences between access seekers and access providers.

In this regard, ATUG would see a role for the Australian Communications Industry Forum (ACIF) in establishing and maintaining arrangements that enable industry players that are in dispute, to, either voluntarily or by direction from the ACCC, enter into mediation at an early stage to try to resolve their differences.

Another approach that could assist resolution of disputes would be for the ACCC to redress the information imbalance that currently exists between access seekers and access providers. In their negotiations with large access providers, in particular, access seekers are seriously disadvantaged by their lack of information about the access provider's cost structure. This means they are negotiating from a position of weakness and this can lead them to expect and demand unreasonably low prices.

If access providers were required to provide a reasonable level of information on the real cost of providing a particular service, it is likely that access seekers would respond positively and accept rather more readily access providers' pricing proposals.

(b) Speed and transparency of determinations

Interim determinations (IDs) provide the ACCC with a mechanism for providing relief to access seekers against access provider's excessive demands before it has completed its work on an arbitration leading to a final determination.

ATUG therefore supports the retention of IDs. However, ATUG's observation is that the ACCC has appeared to be reluctant to issue interim determinations in some arbitrations and has taken an excessive time before finally doing so. During this period, access seekers can be and usually are, seriously competitively disadvantaged.

ATUG would support legislation that would establish a deadline – possibly 45 days- by which time the ACCC must have issued either an interim or final determination.

The PC has recommended (R 9.7) that class arbitration be permitted. ATUG has been an advocate of this and believes it would be a positive step towards hastening arbitrated outcomes. ATUG therefore welcomes the PC's proposed change to the legislation.

ATUG is pleased to see that the PC has recommended greater transparency of arbitrations generally and supports this. ATUG has long been of the view that this will lead to better outcomes in the

industry and to an increased likelihood that access seekers and access providers will prefer to negotiate agreements rather than seek arbitration.

(c) Access undertakings

ATUG has been concerned for some time that the mechanism in the TPA for offering voluntary access undertakings to the ACCC has been not operated successfully. While acknowledging that Telstra has made two unsuccessful attempts to offer a PSTN interconnect undertaking, ATUG believes this may say more about the way in which Telstra has approached its formulation of the undertakings than the failure of the regulatory process.

In any event, the current legislation does not allow the ACCC to direct Telstra to amend the undertaking and to resubmit it within a certain time.

This leads ATUG to propose that the legislation be amended to give the ACCC the power to direct an access provider (or at least the dominant provider) to submit an access undertaking for each declared service that it offers and to do so within 60 days of declaration of the particular service.

(d) Industry resources 'pooling'

ATUG believes that, in the future, there should be much greater policy emphasis on the optimum utilisation of the resources of the industry in meeting the needs of end users.

While ATUG will continue to supports robust competition in the delivery of services and, to a lesser extent, in facilities, it considers that, in the future, there should be a greater emphasis on the sharing of network infrastructure. This would mean that access to the industry's 'facilities resource pool' should, in the future, be cooperative and transparent rather than aggressively competitive.

Simply put, ATUG wants the next wave of competition to be primarily at the 'service' level rather than at the 'resource' level. A good example of this from another industry, is the use by competing freight companies of the same roads even where these are provided by private companies.

(e) PC's recommendations relating to access

While ATUG is pleased that the Commission has recommended retention of Part XIC generally, it views with considerable alarm the proposal to re-orient the Objects clause in section 152AB(1). Specifically, ATUG strongly opposes the proposed change to the Objects clause to include "enhancing overall economic efficiency by promoting the efficient use of, and investment in, telecommunications services", rather than retaining the present focus on the long term interests of end-users (LTIE). Furthermore, ATUG strongly opposes the PC's recommendation (9.1) that the access regime "should be governed by objectives and principles convergent with those in Part IIIA".

ATUG's concerns extend to the corresponding proposed changes to section 152CR of the TPA and sections 3, 389, 384(5) and 485(5) of the *Telecommunications Act 1997* (TA).

ATUG believes the current LTIE test has served Australian telecommunications consumers well since 1997 and it does not believe the PC has put forward adequate or acceptable reasons for its replacement with a far broader test.

Likewise, the PC's proposal to broaden the specific criteria for declaration of services would unquestionably make the requirements for declaration more onerous – particularly the need to demonstrate that the service in question was of 'national significance'. This would undoubtedly result in many services presently declared not fulfilling this criterion. In fact, it would mean that, effectively, only services that were monopolies could be declared under the amended Part XIC.

With regard to the use of Part IIIA, ATUG understands that experience with this part, the generic access regime, has shown that the Part IIIA criteria make declaration a very difficult and time-consuming task.

As far as we are aware only two services have ever been declared under Part IIIA – a commentary on the task of obtaining service declaration under this part of the TPA.

ATUG believes that the current Part XIC access regime has been very effective in ensuring that smaller carriers and carriage service providers have guaranteed rights to essential inputs – those that are critical to effective competition and any-to-any connectivity.

5.3 Draft Recommendations 9.2 and 9.4

Roles of ACCC and TAF

(a) ACCC role

ATUG strongly supports the PC's recommendation that the ACCC continue to oversee telecommunications-specific regulation.

(b) Telecommunications Access Forum

ATUG supports the abolition of the Telecommunications Access forum (TAF). While the TAF played an important role in developing the Access Code, it has been unable to satisfactorily complete any other significant work since that time.

5.4 **Draft Recommendations 9.3, 10.1 and 10.3**

Access pricing

(a) Ministerial pricing powers

ATUG sees no particular value in removing the reserve power for the Minister to determine pricing principles. This is a reserve power and although it has not been exercised to date its presence in legislation is recognised by all players. ATUG believes this provides an important measure of support for the ACCC's Access Pricing Principles.

(b) Legislated pricing principles

ATUG is opposed to the inclusion of pricing principles in legislation. Pricing principles need to be capable of being varied over time to meet changing situations. ATUG see no value in creating inflexibility which would lead to long delays in amending the legislation to meet new circumstances.

(c) Public disclosure of costing methodologies

ATUG supports this recommendation.

5.5 **Draft Recommendation 11.1**

Industry Development Plans (IDPs)

ATUG continues to support the need for a strong research and development capability in the Australian telecommunications industry and it would be concerned if the abolition of IDPs, as a pre-requisite for receiving a carrier licence, led to a significant reduction in expenditure on this important activity.

5.6 **Draft Recommendation 17.1**

Determination of the USO

ATUG opposes this recommendation particularly in relation to the provision for a full merit review by the Australian Competition Tribunal (ACT).

ATUG believes that determination of the USO is a matter for Government and should be made against the backdrop of Government policy. This may change over time and between governments of differing persuasions.

The PC's proposal that determination be by the ACA with appeal to the ACT would inevitably result in delay and instability in the industry over the final level of the USO. This would cause business uncertainty with carriers not knowing either the quantum or the timing of the payments they would be required to make. This uncertainty would inevitably reflect in the prices that end users would pay for services from these carriers.