Australian Consumers' Association

comment on the

Productivity Commission Draft Report

March 2001

Telecommunications Specific Competition Regulation[1]

Introduction

The Australian Consumers' Association (ACA) welcomes the finding by the Productivity Commission that telecommunications market is not yet approaching competitive maturity as consistent with the view we expressed in our submission to the Inquiry. We are pleased with the arguments to retain the Part XIC access regime, and agree with some of the suggestions to expedite outcomes under this regime. We are puzzled by the arguments to repeal the XIB anti-competitive provisions and are vigorously opposed to any suggestion to derogate from the long-term interests of end-users (LTIE) as the object of the telecommunications access regime.

LTIE

The ACA considers the place of the LTIE at the heart of telecommunications regulation is essential. This is not because it represents some kind of consumer nirvana. It is quite possible to critique the phrase "long-term interests of end-users". It can be taken apart and analysed in terms of whose interests it might operate. Long term is generally a frightfully convenient place. After all, it very seldom arrives, and if it does, it is hardly ever what anybody expected. 'End Users' is another fascinating term. The technology-based industries constantly refer to 'Users', and hardly ever in complimentary terms. Users are passive, and as such their interests have to be looked after for them. So from this perspective, the LTIE apparently refers to managing the interests of passive people for them in time frame so far from them that it is of little relevance. However, as recognised by the Commission, a specific regulatory regime is required, to give consumers of telecommunications services a market place where they are not passive users of a telecommunications network, but active customers of telecommunications service providers.

Any critique of the LTIE test tends to underestimate the *long-term* nature of the test. So it is not just about providing consumers with the latest fashionable technology or device. But it is not just about treating them as a proxy for the economy as a whole. Some play is made in the draft report of the desirability of maintaining consistency of the provisions of Part XIB with Part IIIA. While neatness is commendable, it is important that the legislation reflect the special characteristics of network industries. We feel an essential and taken for granted (but not guaranteed) element of telecommunications is the notion of any-to-any connectivity, as recognized in the

[1] ACA File Reference 000434

Draft Report. This may or may not be arguable from the standpoint of overall economic efficiency – ideal competition theory (with the emphasis on *theory*) may well decide that competing networks should be able distinguish themselves to the point of non-interoperation, or at leas raise barriers to navigation. But the test of the interests of end-users means that the excesses of economic purism can be contained by an imperative to meet the needs of consumers. Access regimes are essential to maintain this connectivity and in our opinion giving primacy to the role of the consumer (albeit imperfectly expressed as the LTIE) is an important part of this.

XIB anti-competitive provisions

There is a considerable emphasis in the Draft Report on the risk of regulatory error and on limiting the discretion of the Regulator. However, the overwhelming evidence from the marketplace is that the regulatory error (supposing that there has been one) has not been doing too much, but rather doing too little. The system has been slow and ineffective in application, not withstanding suggestions that the system has had some effects simply by its existence rather than by its actions. The Draft Report comments that regulatory creep should be avoided, but it would seem that the risk of the some of the recommendations is in fact regulatory retreat. The anti-competitive provisions particularly have been slow, cumbersome and at least explicitly ineffective. But rather than recommend ways to make them more effective, the proposal is to roll them back to the general Part IIIA provisions, which commentators do not applaud as speedy and effective.

Rather than a constant refrain that generic provisions will suffice as a starting assumption, we would rather see an analysis that started from what is required to make the telecommunications market place work for consumers as rapidly and effectively as possible. On the other hand, perhaps the general provisions would benefit from the insertion of an object to maximise the long-term interests of consumers, since without them competition as an end in itself has little point. At this point we should indicate that we agree with the recommendation to retain the ACCC as the telecommunications competition regulator as argued in our original submission, primarily because of the embedded C for Consumer in their remit as generalist regulator.

Part XIC access regime

This is more the approach taken to the Part XIC access regime. We agree the TAF as a self-regulatory mechanism seems to push the limits of the possible and should be abolished. Perhaps part of the regulatory error has been the premature aspiration to the ‘light touch’.

We agree that sunset provisions in access arrangements could be useful, but suggest that these should be couched in terms of measurable outcomes, rather than an arbitrary time limit. These goals should be related to the long-term interests of end-users, and obviously reflect the reason for the declaration. When these conditions are met, then the sunset clause could operate. If there is one thing the current regime has proven it is that simple effluxion of time usually favours the powerful and incumbent.

As noted, there are enduring disputes over details of costing methodologies. One key areas of disagreement has been over the access deficit. The Draft Report adopts a

dismissive tone towards 'social regulations'. We have serious reservations about the ACCC recommendations on removing price caps and on Telstra rebalancing local call costs. We fear the end of virtually universal access to the phone system as people drop out off the network because of poverty traps or gaps. Social regulation is important and large profitable industries have their part to play. It would be a great shame that just as the banking sector is waking up to this fact, the telecommunications industry should start to let its excellent record in this regard slip.

We note with concern the consistent theme from industry that regulatory adjustment is required to protect certainty for the investor, while all the while declaring that competition is sufficient to protect the consumer, and the various regulatory controls here can be relaxed. We find this at odds with the headline finding that competition is not mature, and suggest that potential investors probably benefit from this in risk assessments for proposed investments.

Convergence

The Commissioners at hearings requested further input on the issue of convergence and the impact of this phenomenon on telecommunications regulation. Our position was expressed in our initial submission to this inquiry, which in summary is that to the extent that convergence exists, we regard it as a tide which lifts all network ships to meet the special competition requirements provided for telecommunications markets, rather than as driver to reduce telecommunications to the level of generic competition regulation. Further discussion of the convergence issue is contained in the article 'How big is the Con in Digital Convergence?' (attached), originally published in the Spring 2000 edition the ACA policy journal Consuming Interest. The proposition is that there are two potential big cons in convergence. Firstly that government will be persuaded that convergence has 'arrived' prematurely. On the other hand, if regulation is left as-is or is just dumped as obsolete, the ability of government to respond to new forms of market failure could be compromised. Regulation in an internationalising context is essential to achieve these consumer benefits. We must not be conned into removing it by convergence rhetoric.

Attachment 1

How big is the Con in Digital Convergence?

The creation, transmission, and storage of information are obviously important to the changes consumers are starting to see around them. Critical to these is the move from analogue methods of information handling to digital methods. Rather than being coded as a waveform directly reflecting the source material, all content is reduced to a string of zeroes and ones, 'On' or 'Off', the binary heartbeat of digital processing. The change is rippling not just throughout the economy, but also into the cultural infrastructure of our society. These effects emerge at the level of the humble information devices consumers have in their homes, in the enterprises which make these devices and supply the information content which they receive, display, store or process. The industries that these enterprises constitute are changing with technology and associated shifts in consumer and enterprise behaviour. As the tectonic plates of the industry segments shift, governments and their regulators have to adapt. The moves made by these guardians of the public interest then have a material impact on the options, opportunities and threats that emerge from digital change to confront consumers.

The digital changes are often termed 'convergence'. 'Convergence' as a word has actually become a convenient word for players to use to mean whatever they like. For the purposes of this article, convergence has been used to describe the impact on economic and social systems of the essential indifference of digital bits to what they represent (content) and how they are conveyed (carriage). This creates the potential for a landscape for the communication of information devoid of the traditional features that business (and governments and consumers) used to navigate. Some players say that such a flat landscape means the end of regulation – we have the fabled level playing field. More astute observers note that it is the features (for example supply bottlenecks, spectrum scarcity) which have been used to extract additional value in the marketplace, and that where these have been removed, industry will try to create features from which to derive value (for example through control of interconnect to networks, domination of standards, restricted access to facilities and product bundling for consumers).

It is only recently that we have come to view some types of content as information as such. In the predictable lounge room of the analogue era, the form of the information dictated how it was used. The postal system delivered written and printed material. The telephone provided voice communications. The newspaper delivered textual information with some illustration. Magazines and books provided a more durable (and expensive form of such text). Radio, vinyl record players and cassette tape machines provided sound and music. The television delivered its own version of analogue convergence, since it delivered images with sound and some brief textual information in graphics and teletext. Everything was in its place and there was a place for everything.

The initial home invasion of digital processing was by CD players, the personal computer (which came home from work) and the computer games machine (that came

in from the amusement arcade). As they originally appeared, each did a discrete task in an orderly analogue kind of a way. PCs did words and numbers; CDs played music; games machines did primitive graphics in no way comparable to the TV. Over time, the digital potential has become apparent. PCs morphed into multi-media machines. CDs betrayed their digital heritage by carrying lots of information besides music – pictures, software, and documents. These appeared on the PC, and images started to gain quality the TV could not match. The PC started to use the telephone line to communicate digital data with the Internet, and the multi-media material began to arrive, albeit slowly, by that route.

These developments have set people to thinking. Perhaps the TV and the PC will combine to become a single digital display device, dispensing information and entertainment. The digital TV will become interactive, and maybe the PC as such will disappear. Or the reverse might apply, and people will stop watching their TVs and become glued to their PC night after night. Perhaps the telephone and the PC will merge – videophones may become a reality, and the TV will become one with the phone. Many people use the Internet for things they might have used either the mail, fax or telephone for in the past. Maybe the morning newspaper will arrive on the computer and newsprint will become a thing of the past.

However, it is important not to get too carried away with this consumer level convergence thinking. Important social, architectural and ergonomic consumer realities will continue to apply even though the fundamental technologies may be changing. Households will come together for some content, other content is better suited to single person viewing, and still other works better on the move. An important differentiator is between content which creates a 'lean forward' engaged response, and that which creates a 'lean back' entertainment response. Function will dictate how content is consumed. In many ways it is an extension of analogue thinking to insist that devices will converge and become one. Digital technology will mean that eventually devices can more exactly fit a given purpose.

At the enterprise level, the same displacement of analogue thinking into the digital domain in the name of convergence can take place. Companies are hypnotised by the changes wrought by digital change. Business plans are created and torn up at a rapid rate as technology creates one fashion after another – video on demand, interactivity, portals, customer profiling, mass customisation, .com, WAP, datacasting. Start-up companies make it big. Established companies fear for the future, and cast around for opportunities so they do not get left behind.

Convergence can often mean old-fashioned mergers where the larger corporations buy what they feel they cannot grow. Before 'convergence' these manoeuvrings were often in pursuit of 'synergy'. So telephone carriers decide they might need content to add value to their old-fashioned information carrying business – they talk to Internet producers, software makers and perhaps even eye a TV station. Meanwhile, broadcasters talk to Web developers. Newspaper groups look for opportunities in digital broadcasting. Cable companies merge with ISPs.

However, companies have a core competency - that is, a job they do well. As digital change continues, they will have to adapt their skills and mission to a changed environment. But feeling they must take on new forms of doing business because of

this digital change is to misunderstand the nature of the change and to see it through analogue style lenses. The business model they have been working with will need to adapt to the impact of digital change. However it is not likely to happily assimilate an entirely different culture and set of business objectives simply on the basis that the underlying technologies have become similar. Enterprises that concentrate on function over form, on what they do and why, are most likely to adapt successfully. Those who do not will have large bills for the acquisition of incompatible and indigestible businesses – bills that the consumer ultimately pays.

However, this caution about interpreting convergence at the enterprise level is not to say that the structures of industry are not changing with digital innovation. What *is* changing is vertical integration between ownerships of the means of delivery (infrastructure) and production or at least presentation, of content. In the analogue world, a radio broadcaster is distinguished by its use of a radio transmitter. A TV broadcaster uses a different transmitter. A newspaper needs to have printing presses; a voice telephone company needs copper wires, phone towers and fibre links and an ISP needs routers and modems.

In a fully digital world, these associations break down. A newspaper masthead can migrate to the Net – no printing press there. Voice can be carried over data channels over pay-TV cables, bypassing traditional exchanges. The Internet could deliver TV over the copper pair cables in homes currently used for voice – no need for radio frequency transmission. On the other hand mobile telephone data spectrum could be used for digital TV.

Convergence can be used to justify changes which will not benefit consumers, and which do not necessarily flow from the nature of the phenomenon of digital change. There is the additional challenge of timing any move on regulatory systems. Move too early, and convergence has become the tail that wags the dog. Incumbent interests can achieve long treasured and wholly analogue goals in digital disguise. On the other hand, delay the adaptation of the regulatory apparatus and the new choke points can generate their own class of robber barons. These dilemmas emerge particularly in the realms of media ownership rules, regimes that govern access by content providers to infrastructure resources at reasonable prices, technical standards and consumer protection rules.

Media barons declare that digital convergence means regulations seeking to preserve diversity in media ownership are obsolete and therefore they should be tossed aside. Their economic acolytes often declare that ordinary competition rules will suffice to stop market dominance. However it is unpersuasive to argue that controlled dominance gives diversity. The goal remains, but the processes of convergence are dissolving the convenient markers used in regulation – the broadcaster – transmitter, phone company – copper wires couplings have been useful in the past, but will become increasingly unhelpful into the future. Therefore the challenge is to devise systems of regulatory encouragement to ensure the required diversity of media content ownership – notions of share of voice and other measures will need to be explored.

Access regimes to ensure that content can span and interconnect across the increasing number of digital networks are critical. There is currently a Productivity Commission

inquiry into the need for telecommunications specific regulation in Australia. One important aspect of this regulation relates to ensuring access to infrastructure by entrant carriers and consumer portability of connectivity. It is important that the telecommunications market continues to grow and that it remains interconnected and interoperable. These imperatives will undoubtedly emerge in other digital markets. There will probably be access seekers to digital television spectrum, to cable, microwave and satellite systems for digital purposes, not all of which will be traditionally telephonic. Therefore, it may be that there will be a requirement to beef up general competition regulation with improved access guarantees or perhaps specific digital provisions to competition regulation. It is important that in the meantime that telephone system access regulation not be abandoned prematurely.

Standards take on a particularly pivotal position in the digitally convergent world. As noted above, interconnection is essential. How things interconnect and continue to provide a seamless consumer experience (interoperate) is defined at a technical level by agreed standards. In the analogue world, standards are a rather boring technical arena where boffins argue intricate wiring issues. In the digital world, control of technical standards is one of the key choke points, the place at which to levy the road tolls of the digital data highway, and that is not boring at all, as Microsoft has comprehensively demonstrated. For the consumer however, the options available are diminished or made more expensive. Standards become the place for bitter tussles, as illustrated by the corporate turf war that erupted over the definition of digital television standards for Australia. The interests of the consumer were of marginal interest to most players. Standards processes are typically voluntary, consensus oriented and co-operative. As they come to represent the competitive commercial high ground in the digital world, it is likely that regulators, probably on a worldwide basis are going to have to take an interest and stake in the development of digital standards to preserve the interests of consumers.

Consumer protection cannot be taken for granted in the digital marketplace any more than in other marketplaces. Digitalisation offers many potential benefits to consumers; innovative services, greater convenience, better prices, more options and greater choice among them. However, as with other aspects of the convergence phenomenon, there are countervailing trends which demand attention if the consumer experience is to be positive. Particular areas of concern are bundling of services and the erosion of universal service concepts. In their search for competitive replacements for the structures previously imposed by the analogue environment, business will often seek to manufacture new structures that suit their purposes and channel consumer decisions and options into predictable channels. One way of achieving this is via bundling; that is forcing or enticing consumers to buy a suite of services rather than just the one they might want. So pay TV may be cheaper if you take the local call services of the cable company. Cable modems may only be available if you are connected for voice. At best these deals mean consumers have to assess the total bundle value, at worst it means they have to buy extra services they don't want or need, or are locked out because they can't afford the bundle.

As the tide of digital change washes across the communications and media landscape, the notion of universal service is periodically challenged. Critics note that the notion of universal voice telephone access has been extended to data. "Where will it end?" they ask despairingly, "Will it get ratcheted up with each technological innovation?"

And of course, the answer is 'Yes'. And so it should be. Universal service is needed not just because it is about equity and something the people at the margins of our society need (although that is true). It is critical because it mirrors at a social level the digital need for interconnection and access at the technical level. It matters to all the users of the system that other people can access and use the various networks. The more people there are on the networks, the greater the potential utility of the network to all. Excluding people from the networks on bases like poverty or geographic location reduces the value of the network, not only to those who cannot get on, but also to those who are on but cannot access their absent friends (or potential customers, partners, relatives, or community members).

Convergence is mirrored in our personal lives. Where many decisions were made for us by our environment, digital technology means and will increasingly mean that we have to make those decisions ourselves. Just as the rules which govern the regulation of industries like broadcasting and telecommunications are changing because the physical cues are merging and mutating, the rules of everyday life are under technological challenge by questions like: when are you at work; should you be available by phone, message or email 24 by 7; is the weekend obsolete; what is entertainment; what is the value of your personal information? These questions are not reasons to throw away the notion of having a rule book, but it means that the rules will relate more to what we want to achieve and what we value, rather than what the technological landscape dictates. That means we have to identify, both at a personal and a social level what matters, what we are prepared to trade-off to get it.

We need to nail the potential big cons in convergence. Consumers need resolution of the paradox that there is a potential for *both* greater diversity and new entrants *and* greater concentration of ownership and control of key aspects of the digital economy, just as consumers' homes may come to have a vast array of new devices, but these will probably be connected to a single home server mediating their information interactions with the world. Consumers should have access to the full range of the diversity, in a market environment that mitigates the concentration effects. There is not always enough competition, and competition is not always enough to supply non-price outcomes such as diversity, innovation, quality of service, universal service. Regulation (including effective self regulation) sensitive to an internationalising context is essential to achieve these consumer benefits. We must not be conned into removing it by convergence rhetoric. If we attempt to coast we will get a default option driven by technology and the interests of the powerful. By confronting the need for values and making decisions based on them, we have the opportunity to get closer to what we really want.