



TELSTRA CORPORATION LIMITED

Domestic Mobile Terminating Access Service

**Response to ACCC Discussion Paper on the Re-declaration of
the MTAS of December 2008**

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Overview

Telstra welcomes the opportunity to provide comment to the Commission on its review of the declaration of the Domestic Mobile Terminating Access Service (“**the MTAS**”).

Mobiles is the real commercial success story of this industry, as evidenced by the high level of investment and innovation that has occurred in mobiles technology over the last few years. Australians are now enjoying the benefits that competition from four network owners brings: an unprecedented level of infrastructure-based competition from four mobile carriers operating six mobile networks¹. For Telstra’s part, the Next G™ network offers customers superior speeds, unmatched coverage and unique content. Telstra’s Next G™ network provides greater network coverage than any of its mobile competitors, and it provides the fastest 3GSM speed of any telecommunication’s company in the world.² The Next G™ network has been enabled with Evolved High Speed Packet Access (eHSPA) technology delivering peak network downlink speeds of 21Mbps from the end of 2008 with plans to introduce 42 Mbps technology in late 2009 or early 2010³.

The advancements in the 3G networks deployed since 2004 have allowed consumers to experience the launch of new and exciting services now available from their mobile services, including broadband over mobile phones, Pay TV over mobiles, and video calling. These new services, together with continued intense price competition for mobile services more generally, has seen penetration of mobile networks in Australia achieve over 100%, with the number of mobile phone services in operation as at 30 June 2008 increasing by four percent from the previous year⁴.

However, in relation to the regulation of access services on mobile networks, it remains the case that the declared MTAS is still a bottleneck. Given the level of dispute that has occurred within the industry regarding the terms of supply of the service, the Commission should extend the declaration of the MTAS for at least a further 3 years.

In doing so however, Telstra remains concerned that the Commission appears to still have a blinkered approach to defining the relevant retail markets impacted by the MTAS, and has not acknowledged the problems that above-cost pricing of the MTAS has caused, and will continue to cause, for this industry. In particular:

- It is clear that there is increased convergence of fixed and mobile voice calls, as well increased substitution between voice calls more generally and alternative services such as SMS, VoIP and email. The Commission should no longer be approaching its analysis of the market on the basis of a separate “market within which FTM services are provided” and a separate “market for retail mobile services”⁵. When this level of convergence and substitution is coupled with the substantial increase in the level of competition experienced in the provision of fixed network services, it is now clear that calls made using the fixed network are part of a highly competitive and much broader market;

¹ *Communications Infrastructure and Services Availability in Australia 2008*, a joint release by the Australian Communications and Media Authority and the Australian Competition and Consumer Commission, p19

² Full-year Shareholder Update 2008, Telstra, at p2. Available on www.telstra.com.

³ *Telstra Bolsters Next G Backhaul, 21Mbps devices Coming* Communications Day, 30 January 2009,.

⁴ See the ACMA and ACCC Report, *Communications Infrastructure and Services Availability in Australia 2008*, at p21.

⁵ ACCC, *Domestic Mobile Terminating Access Service – An ACCC Discussion Paper Reviewing the Declaration for the Domestic Mobile Terminating Access Service*, December 2008, at p10.

- The Commission still appears to focus solely on Telstra's retail fixed to mobile (FTM) prices, expressing concerns about the level of FTM pricing in isolation of events occurring in the broader market. But this focus is misconceived, and its approach is based on a now out-dated view that fixed network services are not competitive. The Commission's position here reflects another inconsistency in its approach to regulation – an outcome which a regulator should be doing its utmost to avoid; and
- pricing the MTAS at above-cost prices, which has been allowed to occur to date, and which the Commission proposes to continue in its recent draft decision⁶, promotes inefficient investment decisions by access providers, for it discourages investment in technologies such as the PSTN and WiMAX, and instead encourages investment in mobile technologies. The adverse impact above-cost pricing of the MTAS is having on providers of services over other technologies was noted by Unwired in its recent submission to the Commission⁷. The Commission must seek to address the distortion that has occurred over previous years by applying a consistent approach to the regulation of the termination of voice calls across all regulated services. That is, it needs to price MTAS at the level of efficient costs.

Telstra therefore encourages the Commission to extend the declaration of the MTAS for a further period of 3-5 years, and to reduce the regulated price of the declared service to the level of efficient costs (ie 6cpm) as soon as possible.

This submission firstly gives a brief overview of recent developments in the provision of mobile services in Australia, and then outlines the major changes that have occurred in the last few years regarding voice telephony calls, including the increased convergence experienced across various technologies by which voice telephony calls and their substitutes are now delivered, and consequently the increased competitiveness experienced in the provision of fixed network services. It then concludes with Telstra's recommendation for the future regulation of the MTAS.

Telstra's answers to the specific questions raised by the Commission in its discussion paper are set out in Schedule 1.

A Mobiles Is an Australian Commercial Success Story

The provision of mobile services in Australia is a success story. With four mobile network operators, the industry is rich with investment and innovation: new and exciting services are being introduced regularly, and networks are being upgraded to provide more and more coverage and capability. With mobile penetration now at over 100% of the Australian population, demand for mobile services continues to grow as consumers continue to enjoy choice, the benefits of cheaper and more flexible pricing, as well as the new features and functionality that are on offer.

Competition has only intensified over the last few years. The Australian mobile networks enjoy a high level of investment which has led to continued innovation in the nature of the services offered and increased pricing competition.

⁶ ACCC, *Draft MTAS Pricing Principles Determination for the period 1 January 2009 to 30 June 2011*.

⁷ Unwired Australia Pty Ltd, *Submission in response to Assessment of Telstra's Unconditioned Local Loop Service Band 2 monthly charge undertaking – Draft Decision November 2008 and Draft MTAS Pricing Principles Determination November 2008*, undated, at p7.

High level of Investment

Since 2004, when the Commission last considered the declaration of the MTAS, the four mobile operators have continued to invest in their networks, and some have launched new mobile networks. A brief snapshot of the major investment that has taken place is set out below.

Telstra

In October 2006, Telstra launched the Next G™ network. This \$1.1 billion investment now provides geographic coverage of over 2 million square kilometres and population coverage of 99 per cent of the Australian population. The network uses 850MHz spectrum, which enables it to deliver superior rural and in-building coverage over similar networks⁸. Since its launch, Telstra has continued its investment to extend the coverage of the network, and further enhance its capabilities. Telstra's Next G™ network is now the "largest, fastest, national wireless broadband network in the world"⁹, providing a peak network speed of 21Mbps, with Telstra expecting to start deployment of 42Mbps technology in late 2009/early 2010.

Optus

In May 2008, Optus announced that it would invest \$315m in expanding its national mobile network to reach 98 per cent of the Australian population by December 2009¹⁰. This followed a \$500m investment announced in December 2007 to deliver a national 3G/high speed packet access (HSPA) network to reach 96 per cent of the Australian population at speeds of up to 3.6Mbps¹¹. Optus' 3G network during 2008 was being upgraded to deliver broadband speeds of up to 7.2Mbps, with plans in place to increase the speed of the network to up to 28 Mbps from late 2009¹².

Vodafone

Vodafone, too, continues the investment story in Australian mobile networks. In early 2008, Vodafone announced the appointment of Ericsson as the primary vendor to support its national mobile broadband rollout based on HSPA, which is now due for completion in April 2009. The network will see Vodafone's mobile broadband coverage reach 95 percent of the areas where Australians live and work¹³.

Hutchison

Hutchison's investment in the 3GIS joint venture that it shares with Telstra continued to provide improved service for its customers, with the joint venture increasing the number of mobile sites to 2,650 as at 30 June 2008. 3GIS is continuing to invest in its network, with proposals to bring the peak network downlink speed up to 7.2Mbps, up from 3.6Mbps, and to increase its coverage to 96 percent of the population, up from 56%¹⁴.

⁸ *Australian wireless broadband bet paying off for Telstra and customers*, Telstra media release, 12 February 2008.

⁹ *Telstra First and Singtel Optus last in Broadband, says independent report*, Telstra media release, 16 January 2009.

¹⁰ *Optus sets new milestone with the expansion of mobile network coverage to 98 per cent*, Optus media release, 7 May 2008.

¹¹ *Ibid.*

¹² *Ibid.*

¹³ *Vodafone selects Ericsson for national mobile broadband rollout*. Vodafone media release, 6 March 2008.

¹⁴ Hutchison Telecommunications (Australia) Limited, ASX Half Year Information – 30 June 2008, Appendix 4D, 19 August 2008, at pages 7 and 10.

Other Developments

Aside from the considerable investment occurring in mobile networks, a range of wireless broadband providers have entered the market, with many offering “mobile-like” voice services via Voice over the Internet Protocol (VoIP) with a mobile terminating component. There is now a range of fixed and mobile providers with VoIP offerings who provide for voice calls that terminate on mobile devices. While not as widespread yet as the more traditional mobile technologies, these alternatives demonstrate the continued level of innovation and new services offered by other providers.

Exciting Innovation

The investment that has been outlined above has resulted in the launch of many new and exciting services using the 3G technology, including mobile wireless broadband, mobile TV and video calling, as well as increasingly competitive and innovative pricing offers which make mobile services much more accessible to the average consumer than they were in 2004.

The rollout of 3G networks, which allow for both voice and data services to be available to end-users as they provide increased bandwidth, has promoted competition in the provision of new content and applications. The 3G technology deployed by each of the mobile carriers allows data and internet services to be accessed by a variety of means, including either directly over a mobile phone; via a mobile handset serving as a modem for a computer; or via a data card inserted directly into a computer¹⁵. Popular services over mobile phones now include SMS; ringtones, wallpapers and screensavers; email; news and weather; etc¹⁶.

As an example, Telstra’s Next G™ network allows consumers to enjoy numerous different data services including: using mobile data cards to enable remote access to the internet via a laptop service, Mobile TV using Telstra’s Mobile FOXTEL service, online mobile music, information, video calling, and location based services. In a survey conducted in January 2008 of Telstra’s Next G™ network subscribers who use their mobile service for more than voice and SMS, it was found that:

- 45 per cent of Next G™ subscribers using wireless data cards in their laptops purchased goods, services or tickets;
- 67 per cent used the wireless data cards for online banking and bill payments, and to work away from the office;
- 21 per cent of mobile users watched entertainment over their mobile phones; and
- 93 per cent sent photos via their mobile.¹⁷

While the range of new mobile services has increased, the nature and type of pricing plans available from the mobile operators has also increased, with a preponderance of capped plans and pricing options available to customers, leading to reduced retail prices¹⁸.

The increasing accessibility of mobile services, together with the emergence of other technologies, has significantly changed the options available to customers and the way in

¹⁵ See the ACMA and ACCC, *Communications Infrastructure and Services Availability in Australia 2008*, at p20.

¹⁶ *Ibid*, p23.

¹⁷ *Australian Wireless broadband bet paying off for Telstra and customers*, Telstra media release, 12 February 2008.

¹⁸ See for example Telstra’s Annual Report 2007, at p21, where it comments that while call minutes generally increased for each mobile technology, these benefits did not outweigh the reduced price due to capped plans.

which Australians now communicate with each other. As a result, the market is experiencing increased convergence amongst fixed and mobile services, as well as services delivered over other technologies. These developments mean the Commission's traditional approach to assessing the relevant retail markets based on the technology over which the call is delivered is no longer appropriate.

B Fixed and Mobile Convergence

With the increased penetration of mobile services, and the increased availability and take-up of alternative services such as VoIP, it is clear that consumers (business and residential) have a wide variety of choices available to them when considering how to communicate with others. They no longer automatically reach for the traditional fixed telephone to make a call. Instead, the market is undergoing change, with increased convergence of fixed, mobile and alternative services such as VoIP driven by behavioural and cultural changes in the market. This market development has emerged over the last few years, and should be recognised by the Commission in developing its understanding of the market in which voice calls are now provided. It is no longer appropriate to look at fixed voice calls in isolation, for they are not provided in an isolated market. Instead, they form part of a highly competitive environment that offers significant choice for consumers.

For instance, factors such as:

- The increasing take-up of mobile services (now at more than one mobile service for every individual in Australia) is leading to an evolution where phones are increasingly becoming personal communication devices that attach to individuals as opposed to location-specific communication devices attached to households;
- The reduction over time of the cost to the consumer of calls made from mobile phones, and the availability and popularity of alternatives to telephony calls such as SMS, has led to a substantial increase in usage of mobile services over time, reflecting the trend of fixed to mobile substitution¹⁹;
- The increasing substitution of email communication for voice calls; and
- The increasing take-up of low-cost alternatives such as VoIP²⁰, which is now offered by 268 providers, 106 of which provide PSTN and VoIP services²¹,

all demonstrate that, particularly when one is speaking of the market in which voice telephony calls are made, it is no longer correct to classify it as a "fixed voice" market, or a "retail mobile market". Instead, consumers now have available to them many different options in how to communicate with others, using many different technologies.

For example, in 2006, Vodafone commissioned a study of the level of mobile phone use by business customers. The study found that 74% of workers in the small office/home office and

¹⁹ For example, the number of local calls made from Telstra's PSTN declined by 13% during 2007-08, with the number of long distance, FTM and international minutes remaining relatively stable. During this time, mobile voice telephony minutes over Telstra's mobile networks increased by 17.5%, with the number of SMS sent increasing by 42.2%: *Annual Report 2008*, Telstra Corporation Limited, p13 and p16.

²⁰ In 2008, ACMA initiated a survey which indicated that 17% of broadband internet users already use a VoIP service at their home, with 23% proposing to take up VoIP services within 12 months: ACMA & ACCC, *Report, Communications Infrastructure and Services Availability in Australia 2008*, at p29.

²¹ *Ibid*, at p28.

small-to-medium enterprise segments regularly used a mobile phone to make voice calls in the office, with 35% admitting that at least 50% of their in-office phone time was spent on the mobile. This mobile phone usage occurred even though 96% of those surveyed said they had access to a fixed telephone. The study also found that staff in small businesses made on average approximately 10 business calls a day using their mobile phones while they are in the office, even though they are within easy reach of a fixed telephone.²² Given the increased penetration of mobile phone services since 2006, one can only assume that this level of substitution has continued to increase.

The level of competition for providing voice services over the fixed network has clearly increased since 2004. For example:

- As at 30 June 2004, there were 12 major carriage service providers offering fixed telephony services, with some of these providers offering fixed telephone services only to corporate customers²³. At that time, ACMA also provided an example of four providers who were offering VoIP services²⁴. In April 2007, there were 413 voice service providers, with 210 offering services over the PSTN, and 268 providing VoIP services²⁵; and
- Towards the end of 2003-04, some wholesale customers were in the process of installing their own DSL equipment inside Telstra's exchanges. This was expected to provide those ISPs with greater flexibility in the types and plans and quality of service they could offer to subscribers²⁶. By the end of 2007, at least one competitor to Telstra had installed DSLAM equipment in a Telstra exchange in 387 metropolitan exchanges, which does not include the five mainland CBD exchange areas²⁷, with some exchanges having eight competitors. ACMA reports that there are 533 exchanges with at least one installed competitor DSLAM to Telstra²⁸. The number of Unconditioned Local Loop (ULLS) services now stands at over 574,000²⁹.

In addition, in 2004, there were approximately 4.8 million more mobile phones than standard fixed lines³⁰. Now the number of mobile phones is more than twice that of fixed telephone lines³¹.

Following from this, there is no basis for anyone to now claim that the market in which fixed voice telephony services, and consequently fixed to mobile services is provided is not competitive. To do so would reflect a misunderstanding of how the market is currently operating, and how consumer behaviour continues to change as technologies change.

Telstra notes that the Commission itself recognised the increased competitiveness of the retail market in which voice telephony services are provided in its recent decision to grant

²² Vodafone, "Vodafone: Mobiles Muscle out Fixed Line – research reveals 74% of workers use their mobiles in the Office", News Release, 24 August 2006.

²³ ACMA, *Telecommunications Performance Report 2003-04*, at p59.

²⁴ *Ibid*, at p66.

²⁵ Market Clarity VoIP Database provided to ACMA, April 2007, as reported by ACMA and the ACCC in *Communications Infrastructure and Services Availability in Australia 2008*, at p28.

²⁶ ACMA, *Telecommunications Performance Report 2003-04*, at p85.

²⁷ See Telstra's Exemption Applications for the supply of the WLR and LCS of July 2007 and October 2007, available on the ACCC's website.

²⁸ ACMA and ACCC, *Communications Infrastructure and Services Availability in Australia 2008*, at p6.

²⁹ ACCC, *Snapshot of Telstra's CAN as at 30 September 2008*.

³⁰ ACMA, *Telecommunications Performance Report 2003-04*, at p72.

³¹ ACMA and ACCC, *Communications Infrastructure and Services Availability in Australia 2008*, at p21 and 29.

Telstra exemptions in the supply of the declared wholesale line rental and local calls services. In that decision, the Commission adopted a broader definition than previously, recognising retail fixed to mobile calls were provided as part of a broader bundle of services which included basic access, local calls, national and international long distance calls and FTM calls³². On the basis of this definition, the Commission concluded the market was competitive in 248 exchange services areas that were the subject of Telstra's exemption application.

While this was an important step in the Commission's analysis of the competition that has emerged over recent years, and establishes the Commission's acknowledgement that competition for fixed line services has emerged, it by no means goes far enough, since the Commission was focussing solely on substitution for PSTN-provided voice services by the Unconditioned Local Loop Service (ULLS). The Commission did not consider broader market developments such as those identified above, including fixed to mobile substitution, use of SMS and email instead of voice telephony services, the emergence of VoIP, etc. When this broader view is taken, there can be no doubt that the conclusion is clear: the market in which voice telephony services are provided is highly competitive, with not just alternative technologies now available on which to make a voice call, but also alternatives such as SMS and email.

C What does this Mean for Regulation of the MTAS?

The recent market developments outlined above provide an important backdrop to the Commission's decision to re-declare the MTAS, and how to price it, for several reasons.

First, nothing in the above picture affects the need for the Commission to continue to regulate the declared MTAS, which remains a bottleneck service. As each mobile operator has control over services that terminate on its network, and operators have no control over which networks are called by their end-users, regulation of the MTAS remains critical. Increased fixed to mobile substitution does not change this: the nature of the declared MTAS remains as it was in 2004. This is consistent with the views expressed by the Commission in 2004 in concluding that the MTAS is in a separate market to other mobile services (including retail services)³³. The Australian Competition Tribunal recently agreed with this analysis:

*"It is correct to identify a wholesale market for the supply of Optus' MTAS. There are no substitutable products and the relevant market transaction is a wholesale transaction provided by one network operator to another. To the extent to which there is substitutability of products or services it is the bundle of services which is substitutable; one of the services is not substitutable for another of the services."*³⁴

Accordingly, Telstra believes the Commission should re-declare the MTAS for a period of at least 3 years.

Second, the Commission does not need to consider broadening the scope of the declared MTAS to include other services, such as data termination or SMS. Regulation should only be contemplated where there is market failure. It is clear that there is no market failure in this instance, given the lack of any disputes regarding the terms of supply of the wholesale inputs

³² ACCC, *Telstra's Local Carriage Service and Wholesale Line Rental Exemption Applications, Final Decision and Class Exemption*, August 2008, at p42. Note that the Commission's decision has been overturned by the Australian Competition Tribunal, a decision which is currently under appeal to the Full Federal Court.

³³ *Mobile Services Review – Mobile Terminating Access Service – Final Decision ACCC*, June 2004.

³⁴ *Application by Optus Mobile Pty Limited and Optus Networks Pty Limited* [2006] ACompT 8 at para [80].

to these other services. Any attempt to broaden the scope of regulation at this time would simply risk harming the current competitive process that is being experienced in the marketplace today.

Third, the increasing substitutability between voice calls made over different technologies highlights the importance of the Commission taking a consistent approach to determining terminating access prices across those technologies. By proposing to price the MTAS at a level which remains above efficient cost, while pricing services such as PSTN terminating access in accordance with the TSRLIC of the service, the Commission is discouraging investment in the fixed network, and inciting over-investment in mobiles. This cannot promote efficient investment across the industry, and cannot be in the long-term interests of end-users. Requiring PSTN network owners, and providers of voice calls using alternative technologies such as WiMAX, to continue to subsidise investment in the mobiles industry through the setting of above-cost termination rates (which has already been occurring for many years at prices considerably higher than efficient cost), only serves to artificially promote investment in mobiles ahead of other technologies, and significantly distorts the competitive process – particularly when mobile operators such as Optus and Vodafone enjoy low cost-based termination rates when calling Telstra’s fixed line customers. This cannot be in the long-term interests of end-users.

Fourth, there is simply no basis for the Commission’s continued focus on the question of whether reductions of MTAS rates have been passed through to users of Telstra’s FTM service³⁵. Indeed, in questioning the level of pass-through of MTAS price reductions to Telstra’s retail FTM prices, the Commission is taking an inconsistent approach to regulation, on several different levels:

- In 2004, the Commission determined that FTM calls were provided in the same market as other calls in the pre-select basket of services³⁶. More recently, the Commission determined that fixed to mobile calls were provided as part of a broader bundle of services which included basic access, local calls as well as the pre-selected basket of services³⁷. It is completely inconsistent with these determinations for the Commission to then isolate one calling service only (FTM) in an attempt to determine whether pass-through of FTM calls has occurred;
- The reductions in MTAS prices that have occurred since 2004 have benefited all users of the MTAS: that is, all parties making voice calls that terminate on Australian mobile networks, irrespective of the platform or technology used in originating that call, benefit from lower costs of termination. Fixed to mobile calls (and indeed, FTM calls made only by Telstra’s retail customers), form a very small part of this set of customers. It is inconsistent and inappropriate for the Commission to isolate one small section of customers for regulatory attention;
- While the Commission is seeking evidence of any pass-through of reductions to retail pricing as a result of reductions in MTAS charges, it does not adopt this approach when considering the access price that should be payable by parties wishing to acquire access services over Telstra’s PSTN. This inconsistency remains unexplained.

³⁵ See for example the discussion by the Commission on FTM pricing at p16 of the discussion paper.

³⁶ See the discussion of this in the ACCC’s *Domestic Mobile Terminating Access Service, An ACCC Discussion Paper Reviewing the Declaration for the Domestic Mobile Terminating Access Service*, December 2008, at p10.

³⁷ ACCC, *Telstra’s Local Carriage Service and Wholesale Line Rental Exemption Applications, Final Decision and Class Exemption*, August 2008, at p42. Note that the Commission’s decision has been overturned by the Australian Competition Tribunal, a decision which is currently under appeal to the Full Federal Court.

The Commission's focus on Telstra's retail FTM prices reflects a view of a lack of competition in the provision of fixed network services (and in particular, FTM services) which is now outdated and unsustainable. The simple truth is that if Telstra's FTM prices are too high, then customers will not use the service: they will instead choose one of the other 210 providers of voice services over the fixed line; or they will pick up their mobile phone to make the call (noting that there is now more than one mobile phone for every head of Australian population); or they will send an SMS or an email; or they will use other technologies such as a VoIP service.

As a result of the above, it is clear that the Commission should re-declare the MTAS in its current form for a period of at least a further 3 years, and it should immediately reduce the regulated price of the MTAS to 6cpm, which reflects the Commission's current best estimate of the TSLRIC+ of the service, so as to promote competition and efficient investment within the industry for the provision of voice calling services.

Schedule 1: Answers to Questions in the ACCC Discussion Paper reviewing the domestic mobile terminating access service

4.1 Service description for the MTAS

Is the current MTAS service description adequate?

Yes.

Should data, the short message service (SMS) and multi-messaging system (MMS) be considered as part of the MTAS description?

No. Mobiles services are currently provided in an intensely competitive market, with all mobile operators continuing to invest in their networks, leading to increased capability, and new and innovative services. This, together with the current level of commercial agreement that exists in relation to the provision of other services (such as SMS, MMS or data services more generally), demonstrate that there is no need for expanded regulation. Any proposal to regulate these services would likely harm competition and lead to less optimal outcomes, and therefore would not be in the long-term interests of end users.

4.2 MTAS market definition

Does the MTAS continue to have bottleneck service features?

Is the market definition outlined in 2004 still appropriate?

Since 2004, have there been any changes in mobile telecommunications technology with the potential to change previous ACCC findings in relation to the nature of the MTAS market? In particular, are there any demand and supply-side substitutes for the MTAS?

The competitive nature of the mobiles industry does not affect the fact that the declared MTAS remains a bottleneck service. The nature of the declared MTAS has not changed since 2004. Telstra agrees with the conclusion the Commission reached in 2004 that the MTAS is in a separate market to other mobile services (including retail services)³⁸. This view is also consistent with the views expressed by the Australian Competition Tribunal, which commented that:

“It is correct to identify a wholesale market for the supply of Optus’ MTAS. There are no substitutable products and the relevant market transaction is a wholesale transaction provided by one network operator to another. To the extent to which there is substitutability of products or services it is the bundle of services which is substitutable; one of the services is not substitutable for another of the services.”³⁹

Accordingly, Telstra believes the Commission should re-declare the MTAS.

³⁸ Mobile Services Review – Mobile Terminating Access Service – Final Decision ACCC, June 2004.

³⁹ Application by Optus Mobile Pty Limited and Optus Networks Pty Limited [2006] ACompT 8 at para [80].

Should mobile phone network services deployed in aircraft operating within Australia fall under the MTAS service definition?

Telstra believes that the termination of a voice telephony call made from an aircraft on a mobile service in Australia would already be caught by the definition of the declared MTAS. Telstra therefore sees no reason to vary the definition.

4.3 Defining Other markets in which declaration may promote competition

Are there any new services or fully effective substitute services which could be considered to be in the same market as that within which FTM services are provided?

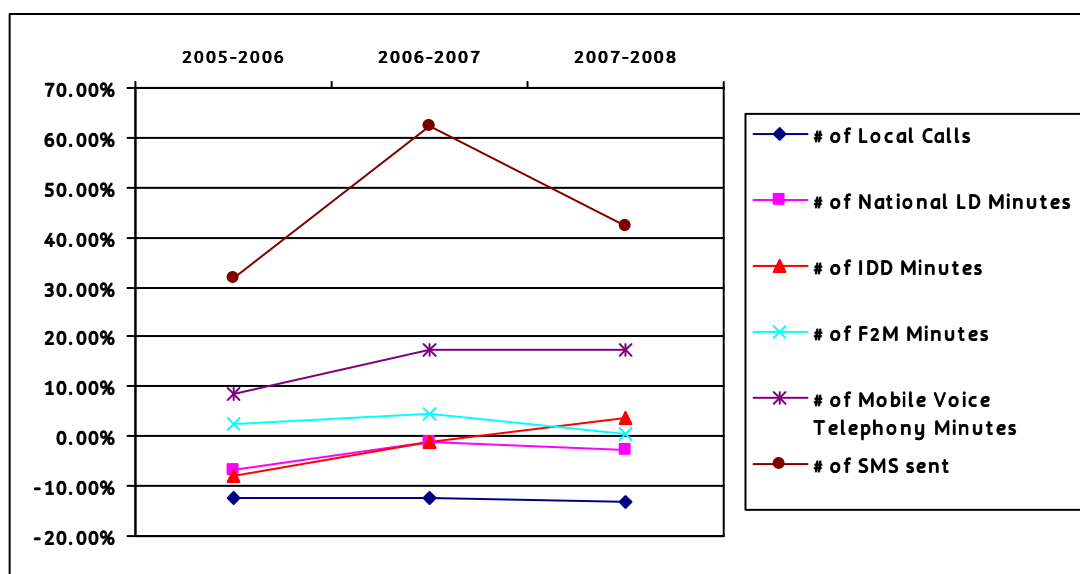
In 2004, the Commission found that FTM calls were provided in the same market as other calls in the pre-select basket⁴⁰. Only last year, the Commission broadened its market definition and considered that the importance of one bill for customers' fixed voice services meant that the appropriate bundle of services now included basic access and local calls, in addition to the services comprising the preselection basket.⁴¹

However, as mentioned earlier, this market definition was determined in the context of considering an exemption application that focussed solely on the question of whether the ULLS provided an effective substitute for Telstra's PSTN voice telephony services. Telstra believes this definition of the market is too conservative, given the increasing level of substitution now occurring between fixed and mobile services, particularly for voice calls, and the emergence of alternative technologies such as VoIP and other substitutes for voice calls such as SMS and email. For example, an analysis of Telstra's last three annual reports demonstrates the increasing convergence of fixed and mobile services:

⁴⁰ *Mobile Services Review – Mobile Terminating Access Service – Final Decision*, ACCC, June 2004.

⁴¹ ACCC, *Telstra's Local Carriage Service and Wholesale Line Rental Exemption Applications, Final Decision and Class Exemption*, August 2008, at p42.

Percentage Change in Call Usage of Telstra Services from Previous Year



Source: Telstra Annual Reports, 2006, 2007 and 2008.

During the period outlined above, the number of mobile services in operation in Australia increased by 2.4 million, from 19.7 million as at 30 June 2006, to 22.12 million at 30 June 2008⁴². Given this, it is interesting to note the substantial year on year increase of mobile voice telephony minutes and SMS sent, compared to the decline in local and other calls made on the fixed network, and the only slight increase in FTM minutes.

This picture does not include other technologies used for making voice calls, such as VoIP and WiMAX. In its 2008 Communications Infrastructure and Services Availability Report, ACMA and the ACCC noted that there were 268 operators offering VoIP services⁴³, with an ACMA-commissioned study indicating that 17% of broadband internet users used VoIP at home, with a further 23% of users planning to acquire VoIP within 12 months⁴⁴. In the same report, ACMA and the ACCC noted while the number of subscribers to VoIP services is unknown, Engin reported active subscriber numbers had increased 9% to 30 June 2008, and MyNetPhone reported an increase of 71% in subscribers over the same period.⁴⁵

Accordingly, Telstra believes the Commission's previous approach of isolating a market for calls made in the fixed network pre-select basket, or indeed in the broader basket of fixed network PSTN services, is no longer sustainable, as it fails to recognise the increasing substitution of calls across different technologies, including mobile services, VoIP and email. The Commission must now take a broader approach when considering the relevant retail market.

⁴² Communications Infrastructure and Services Availability in Australia 2006-07, and 2007-08, ACMA and ACCC joint release.

⁴³ At p28.

⁴⁴ Ibid, p29.

⁴⁵ Ibid, p30.

Even if the Commission takes a narrow view of considering only the fixed network basket of services as being the relevant market in which FTM services are provided, it is clear this market is now highly competitive, and indeed much more competitive than it was in 2004:

- There are currently 210 providers offering voice services over the PSTN⁴⁶. This demonstrates there are low barriers to entry to offering these services to consumers;
- The availability of the highly-regulated ULLS, providing Telstra's wholesale customers with increased opportunity to offer their own standard telephone service to end-users via access to the copper loop for a regulated price which is currently well below the efficient costs of supply. Wholesale customers use the ULLS to provide their own voice telephony and other services (including broadband) over their own network. The takeup of ULLS has substantially increased recently, with the number of ULLS SIOs more than doubling, to 527,000, in the 12 months to June 2008⁴⁷; This number had further increased to over 574,000 by the end of September 2008⁴⁸; and
- The availability of access to regulated services (such as Wholesale Line Rental (WLR), PSTN Originating Access and MTAS) which comprise all of the key inputs at the wholesale level to the provision of FTM services. In particular, Telstra notes WLR, which is a key input cost to providing FTM services, was declared by the Commission in 2006, after its 2004 inquiry into the MTAS. This can only serve to further lower any perceived barrier to entry to the retail market, thereby making the market in which FTM services are provided even more competitive than they were in 2004.

Telstra sees every justification, therefore, for the Commission to conclude that FTM services are provided in a highly competitive environment.

Are the markets in which FTM services and retail mobile services are provided still the only relevant downstream markets for the MTAS?

As noted above, the Commission's approach to defining the relevant markets should be much broader than determined previously, and should include not just voice and mobile telephony services, but also alternatives such as SMS and email.

Are there other markets which should be taken into account?

No.

⁴⁶ *Communications Infrastructure and Services Availability in Australia 2007-08*, ACMA and ACCC joint release, at p28.

⁴⁷ Telstra, "Financial Highlights Year Ended 30 June 2008", 13 August 2008, at p20.

⁴⁸ ACCC, *Snapshot of Telstra's CAN as at 30 September 2008*.

Are mobile data and messaging services offered in the same bundle as mobile voice services? If so, to what extent?

Yes. Customers of mobile services have services such as SMS automatically available to them. Customers of mobile services with appropriate equipment can also access the internet, email, GPS services, etc.

4.4 State of competition in the relevant markets

Are there any structural and behavioural changes in the MTAS markets which make them more competitive than they were in 2004?

Telstra believes the structure of the wholesale MTAS market identified by the Commission in 2004 remains appropriate today. As each mobile operator has control over services that terminate on its network, and operators have no control over which networks are called by their end-users, regulation of the MTAS remains critical.

This has also been evidenced by the high level of disputes over MTAS pricing in recent years: Telstra has generally found other mobile operators unwilling to reduce their prices, even though the regulated prices for the declared service have been (and remain) well above the efficient costs of providing the service. This reinforces the need to maintain regulation of the current declared service, and for the Commission to be vigilant in reducing prices to a level which matches the efficient costs of providing the service, which as acknowledged by the Commission, is well below the current draft indicative price of 9cpm⁴⁹. For this reason, Telstra believes the Commission should set an indicative price of 6cpm from 1 January 2009.

Are there any structural and behavioural changes in the retail mobile services market which make it more competitive than it was in 2004?

As mentioned earlier, there is intense competition in the provision of retail mobile services in Australia. The increased capability of the 3G networks that have been deployed has seen innovative new services being launched. This, together with the increasingly competitive pricing offered by all of the mobile operators has led to continued increased take-up of mobile services by Australian consumers.

However, given the increased convergence between fixed and mobile services, and the availability of alternatives such as email, it is no longer appropriate for the Commission to attempt to define separate markets based on the types of technology used to make a particular call.

⁴⁹ ACCC, *MTAS Pricing Principles Determination 1 July 2007 to 31 December 2008*, November 2007, p1 and Table A.3-1 in Annexure A.3.1.2 of the Report and page 47.

Are there any structural and behavioural changes in the market in which FTM services are provided which make it more competitive than it was in 2004?

The key change to emerge since 2004 is the market-wide move to communications convergence, including the use of portable devices as a platform for a variety of voice call substitutes (eg mobile devices such as the Blackberry which allows internet access, email, instant messaging and social networking applications, location-based services, voice to text and text to voice, etc).

As mentioned above, since 2004 fixed and mobile voice calls, and also voice calls made over alternative technologies such as VoIP, are increasingly being provided in the same market. However, irrespective of whether the market in which FTM services are supplied is accepted as including mobile services or not, it is clear the market in which FTM services are provided is competitive.

The main changes since 2004 in relation to the market in which FTM services are provided, include:

- The substantial number of providers offering voice services over the PSTN;
- The increasing substitution between fixed and mobile calls;
- The increasing use of SMS as a means of communication, again as an alternative to voice calls;
- The increasing use of email as a substitute for voice calls;
- The increased use of VoIP services, and other technologies such as WiMAX, as an alternative to the more traditional fixed line voice call;
- The availability of the regulated ULLS as a building block, enabling wholesale customers to provide a standard telephone service over their own network. As mentioned earlier, the takeup of the ULLS has increased substantially over recent years;
- The decision by the Commission to declare Wholesale Line Rental in 2006, thereby effectively allowing entrants to the market access to regulated rates for all of the key inputs to providing a FTM call to customers, further reducing any barriers to entry; and
- The recognition by the Commission of the increasing competitiveness of the wholesale market in which the fixed network inputs to FTM services are provided⁵⁰.

⁵⁰ ACCC, Telstra's Local Carriage Service and Wholesale Line Rental Exemption Applications, Final Decision and Class Exemption, August 2008 and ACCC, Telstra's PSTN Originating Access Exemption Applications – CBD and Metropolitan areas, Final Decision and Class Exemption, October 2008. Note however that the Australian Competition Tribunal has overturned the ACCC's decision in relation to the WLR and LCS exemptions (a decision which is currently under review), and the Tribunal is further considering an appeal in relation to the PSTN OA exemption decision.

4.5 The extent to which competition would be promoted by declaration

Are MTAS prices likely to be above the underlying costs of production if the service is not regulated?

Yes. The level of dispute within the industry in recent years concerning the pricing of the declared MTAS demonstrates that if the MTAS is not regulated, there is a significant risk that other operators will increase their prices.

Indeed, Telstra remains concerned that the Commission's draft indicative price of 9cpm from 1 January 2009 is well above the efficient costs of providing the service, as it has acknowledged in the past⁵¹. The Commission needs to further reduce MTAS prices to promote efficient investment, which in turn would be consistent with the long-term interests of end-users, as required by the legislation.

Telstra notes its concern has recently been echoed by Unwired Australia Pty Ltd, where it stated that:

“the Commission approach to not requiring the mobile operators to price MTAS at cost results in fixed line voice callers potentially subsidising the mobile operators' offerings of services that compete with Internets [sic] service connections operating through other technologies”.⁵²

The Commission needs to correct the distortion which is occurring within the marketplace, and which is incenting access providers to invest in mobile technologies over alternative platforms such as the PSTN, by ensuring that the declared MTAS is priced at the level of efficient cost.

What impact has the continued declaration of the MTAS had on competition within the market within which FTM services are provided since 2004?

The continued declaration of the MTAS has promoted competition for other services, including the services provided in the market within which FTM services are provided, leading to more vigorous competition in the retail and wholesale markets. There is intense competition for customers' voice telephony business, no matter which technology is considered. There is now increased substitution between fixed and mobile services, and increased competition is faced by providers of voice telephony services from providers of other services such as VoIP and WiMAX. The nature and variety of calling plans now available on the fixed network, including bundled offers and capped plans, reflects the increased competition faced by providers of these services.

Telstra notes the Commission has expressed doubts about whether the reduction in MTAS rates has improved competition by repeating its concern with the slower than expected

⁵¹ ACCC, *MTAS Pricing Principles Determination 1 July 2007 to 31 December 2008*, November 2007, p1 and Table A.3-1 in Annexure A.3.1.2 of the Report and page 47.

⁵² Unwired Australia Pty Ltd, “*Submission in response to Assessment of Telstra's Unconditioned Local Loop Service Band 2 Monthly Charge Undertaking – Draft Decision November 2008 and Draft MTAS Pricing Principles Determination November 2008*”, undated, at p6.

decline in FTM prices over time⁵³. However, as mentioned earlier, this approach is unsustainable, as it is based on an outdated view of the competitiveness of the market in which FTM services are provided, and is inconsistent with the Commission's approach to defining the market in which FTM services are provided, and is inconsistent with its determinations of access prices for other declared services. As a regulator, the Commission should be promoting consistency within its decision-making processes. If Telstra has incorrectly priced its FTM services, then Telstra will bear the consequences of that in the marketplace.

In any event, the Commission's concern in relation to FTM pricing is unfounded.

As Telstra has made clear previously⁵⁴, focussing on FTM prices alone does not provide the answer of whether pass-through of reductions in the MTAS price has occurred. This incorrectly implies the only way the benefits of lower MTAS prices can be realised by end-users is through lower FTM prices, that the only relevant form of competition is price competition and, even then, that price competition is an assumed isolated FTM submarket.

In the context where FTM services are provided in a broader bundle of services (which as the Commission itself has acknowledged, is at least the broader bundle of basic access, local calls, national and international long distance calls and FTM calls⁵⁵), then the Commission cannot determine whether pass-through has occurred simply by considering the price of one service in that bundle. Pass-through may have occurred in the form of price reductions in other services provided in the bundle. Or it may have occurred in the form of increased value in the form of additional value-added services, or new service initiatives.

Telstra's view is completely consistent with the views expressed by the Australian Competition Tribunal, which has previously stated its concerns about the inflexibility that would arise by requiring FTM pricing reductions on fixed network providers. In rejecting an undertaking by Vodafone which sought to impose such a requirement for pass-through on fixed to mobile pricing, the Tribunal said:

"We are also concerned that the Pass Through Safeguard is inflexible in relation to the opportunity for competition to be promoted as a result of any reduction in the price of the VMTAS. It limits the opportunity of access seekers to determine the form in which any reductions they may receive in the supply of the VMTAS may be passed through to the retail fixed services market.

*We consider that the pass through provisions in the undertaking deprive access seekers of the flexibility to determine competitively the individual price elements for services within the basket of services that are supplied within the fixed-to-mobile market, and the form in which pass through will take place. This approach retards allocative and dynamic efficiency, inhibits competition, is not in the long-term interests of end-users and, in our view, is not reasonable."*⁵⁶

In adopting this position, the Tribunal was accepting arguments made to it by the Commission, which was similarly concerned about the negative impacts that requiring pass-

⁵³ ACCC, *Domestic Mobile Terminating Access Service, An ACCC Discussion Paper Reviewing the Declaration for the Domestic Mobile Terminating Access Service*, December 2008, at pp16-17.

⁵⁴ Telstra Corporation Limited, *Response to the ACCC's Draft MTAS Pricing Principles Determination and Indicative Prices for the Period 1 January 2009 to 31 December 2001*, Public Version, 15 December 2008, at p15

⁵⁵ ACCC, *Telstra's Local Carriage Service and Wholesale Line Rental Exemption Applications, Final Decision and Class Exemption*, August 2008, at p42.

⁵⁶ *Re Vodafone Network Pty Ltd & Vodafone Australia Limited [2007] ACompT 1*, 11 January, 2007, at paras 289-290.

through of MTAS price reductions to FTM calls would have on competition⁵⁷. In light of all of these factors, how can the Commission now look only to FTM retail pricing calls as a means of saying whether or not pass-through of MTAS price reductions is occurring?

Telstra also reminds the Commission that the Australian Competition Tribunal has repeatedly emphasised that the objective of promoting competition involves the idea of creating the conditions or environment for improving competition, and it does not require demonstration that there will in fact be an actual advance in competition⁵⁸. Clearly, it is efficient, cost-based pricing of the MTAS that puts in place the necessary conditions for improving competition – which may occur across the price control basket of preselect calls, or in the form of price reductions elsewhere, or in forms other than price. Any proposal to propose a pass-through mechanism, or to seek direct reductions in FTM pricing, reflect a flawed understanding of the LTIE criterion and the ‘promotion of competition’ objective, and is completely inconsistent with the Commission’s approach to market definition and its determination of access prices for other declared services.

What impact has the continued declaration of the MTAS had on competition within the market within which retail mobile services are provided since 2004?

As mentioned earlier, it is imperative for the Commission to continue to reduce MTAS rates towards the efficient costs of supply of the service. By allowing MTAS prices to be set at levels which are above cost, the Commission is requiring owners of non-mobiles technology to continue to subsidise mobiles investment. It is also distorting the competitive environment by encouraging over-investment in mobiles at the expense of other technologies. This does not promote competition or efficient investment in infrastructure.

Could the market for retail mobile services be considered effectively competitive today?

Telstra believes the market in which retail mobile services, FTM, and other voice telephony services, are provided, is effectively competitive today.

4.6 The impact of declaration on any-to-any connectivity

Have circumstances changed since 2004 such that any-to-any connectivity would now be likely to be achieved in the absence of declaration?

No.

⁵⁷ Ibid, para 289, where the Tribunal summarises the Commission’s arguments.

⁵⁸ See, for example, *Re Review of Freight Handling Services at Sydney International Airport* (2000) ATPR 41-754 at (40,775); *re Duke Eastern Gas Pipeline Pty Ltd* (2001) ATPR 41-821 at (43,061); and *Application by Services Sydney Pty Limited* [2005] ACompT 7 at [130]- [179].

4.7 Economically efficient use of infrastructure

Has anything changed since 2004 in the pricing structure to encourage a more efficient use of infrastructure?

No. Telstra believes the continued declaration of the MTAS is required to encourage the efficient use of telecommunications infrastructure. However, as mentioned earlier, this needs to be coupled with the Commission continuing to reduce MTAS rates towards their efficient costs of supply. Failure to do so will simply require further subsidisation of mobiles services by customers of the fixed networks: an outcome which does not encourage efficient investment.

4.8 Economically efficient investment in infrastructure

What has the level of investment in mobile telephony infrastructure been since 2004?

As outlined above, investment in the mobiles industry has intensified since 2004.

Which type of infrastructure has the investment been put into?

The investment made by the industry has been largely focussed on the introduction of 3G networks, and their further expansion and enhancement.

On what basis has the investment been efficient investment?

Above-cost MTAS rates have prevailed in the market for several years. This has distorted the incentives for investment in telecommunications infrastructure away from networks such as the PSTN, in favour of mobile technologies. This has not led to efficient investment across the industry, as it does not promote competition and efficient investment across all platforms. It is imperative that the Commission corrects this by immediately reducing MTAS rates to efficient cost.