‘yes’ OPTUS

**Optus Submission to**

**the Productivity Commission’s**

**Annual Review of Regulatory Burdens on Business: Social and Economic Infrastructure Services**

**Response to Issues Paper**

**Public version**

**February 2009**

# Table of Contents


**1. Executive Summary ..... 3**

**2. The Part XIC Telecommunications Access Regime ..... 6**

A sector-specific access regime ..... 6
Objectives of the access regime ..... 6
Improving the operation of the access regime ..... 21

**3. The Part XIB Telecommunications Anticompetitive Conduct Provisions ..... 34**

A sector-specific anticompetitive conduct regime ..... 34
Improving the operation of the anticompetitive conduct regime ..... 34

**4. Customer Service Guarantee ..... 36**

**5. Law Enforcement: Prepaid Identity Checks ..... 40**

**6. Information provision to customers ..... 41**

**7. Standard Form of Agreement & other consumer contracts ..... 45**

**8. Universal Service Obligation ..... 46**

**9. Telecommunications Industry Information-gathering Powers ..... 47**

Retention of information-gathering powers ..... 47
Information powers should apply in cases of significant market power ..... 47
Information powers should apply in respect of a declared service ..... 48
Burdensome information-gathering regulations ..... 48

**Appendix A: Process for a Final Price Ruling on ULLS ..... 52**

**Appendix B: Competition Proceeding: WLR 'Price Squeeze' Conduct ..... 53**

**Appendix C: *Telecommunications Performance Monitoring Report (No.63)* ..... 55**

## 1. Executive Summary

1.1 The Productivity Commission has been tasked with identifying areas of regulation that are unnecessarily burdensome, complex, redundant or duplicative, and has invited interested parties to submit their views.

1.2 The telecommunications sector is one of the most highly regulated business sectors in Australia. It is subject to both generic business regulation as well as significant industry-specific regulation, encompassing government legislation and self-regulatory processes across competition policy, consumer protection, technical and operational regulations.

1.3 Optus is a leading integrated national telecommunications provider, delivering cutting-edge communications, information technology and entertainment services throughout Australia. Our services are used by consumers, businesses, corporate entities and government agencies. As such, we operate in a regulatory environment which encompasses national, state and territory laws and regulations, both generic and industry-specific.

1.4 In many respects the telecommunications industry operates under a complex and onerous regulatory burden. Optus therefore welcomes the opportunity to outline some key issues to the Commission's review. Our submission contains comments with respect to a number of specific pieces of regulation which we consider inappropriate, burdensome, unnecessary and/or poorly targeted.

1.5 Notwithstanding the level of detailed regulation, the Part XIC access regime has failed to deliver the primary objective underlying its introduction in 1997 – that is, to rein in the market power of Telstra and create a genuinely level playing field in the provision of fixed line services. It has failed because a conflict of interest has been allowed to go largely unchecked in the way Telstra, as the monopoly fixed line provider, has been structured. Optus will submit that the Productivity Commission should consider certain reforms to make the regime more effective, and to eliminate certain redundant aspects. In particular, Optus will propose that:

- the Operational Separation scheme set out in Part 8 Schedule 1 of the *Telecommunications Act 1997* is wholly ineffective and should be strengthened through the introduction of structural separation;
- Declaration under Part XIC should apply only to operators with significant market power;
- Part XIC should be streamlined such that parties be prevented from:
  - i) applying for merits-based review of the ACCC's decisions;
  - ii) applying for exemptions from access obligations; and
  - iii) submitting access undertakings materially similar to those previously rejected.

1.6 Further, the Commission should consider certain reforms to make the Part XIB anticompetitive conduct regime more effective including strengthening the ACCC's enforcement powers and eliminating draft notices.

1.7 Optus will assert that the Customer Service Guarantee, which imposes on Carriage Service Providers (CSPs) specific performance standards and compensation payment requirements with respect to the connection, fault rectification and making of appointments for the supply of standard fixed telephony services to consumers is highly burdensome, unevenly applied and outdated.

1.8 We will assert that the regulations requiring CSPs with mobile networks to collect, verify, store and, on lawful request, retrieve identity and address information about the purchaser and/or user of prepaid mobile phone services are poorly designed, impractical, costly and unreasonably applied.

1.9 We will also highlight the vast amount of information that CSPs are required to provide to their customers to the detriment of both CSPs and consumers themselves. This is because the regulations governing these requirements are poorly developed and inflexible; are in many cases increasingly irrelevant to consumers yet remain in force; and due to their industry-specific nature impose a greater regulatory burden on the telecommunications industry than is applied to other sectors.

1.10 Optus notes in this submission the highly complex and burdensome regulations governing standard forms of agreement and consumer contracts. Optus is subject to general national consumer laws, the various fair trading and unfair contracts laws of each state and territory; and various telecommunications-specific regulations. We are therefore pleased to hear the recent announcement about the development of a national consumer law.

1.11 Optus will submit that the Commission should consider funding the Universal Service Obligation (USO) from general taxation and that it should recommend abolition of the industry fund. It is inappropriate for Telstra to be subsidised by its rivals, given the significant advantages enjoyed by Telstra as the incumbent and the negative impact on competition resulting from the industry subsidy.

1.12 Finally, Optus will submit that the record-keeping rules (RKRs) and other information-gathering powers set out in Part XIB of the Act should be retained, but should be applied only to operators with significant market power and should be applied only where necessary to support the ACCC's regulation of an existing declared service.

1.13 Nevertheless we must not throw the baby out with the bathwater: targeted and balanced regulation is important to promote competition and constrain the abuse of market power. Accordingly, this submission also anticipates some of the more obvious arguments which might be made by the incumbent telecommunications player against specific pieces of regulation and attempts to address these so that the Productivity Commission is not presented with a one sided argument.

1.14 In this regard Optus will submit that the telecommunications access regime set out in Part XIC of the *Trade Practices Act 1974* (the Act) and the

telecommunications anticompetitive conduct provisions set out in Part XIB of the Act should be retained as sector-specific regulation.

1.15 Further, Optus will contend that it would be inappropriate to alter the objectives of the Part XIC access regime in order to bring it into line with the interests of Telstra shareholders, for example by introducing a bias towards the duplication of infrastructure. The access regime already allows Telstra to fully recover its cost of investment and stimulates all carriers to make significant infrastructure investments. Part XIC plays an important role in encouraging efficient investment in infrastructure. It aims to allow the ACCC to provide pricing certainty and a level playing field for all carriers. Optus will provide evidence of the successes of Part XIC in promoting competition and to expose the fallacy that access regulation discourages investment. It should always be borne in mind that Telstra was privatised subject to the access regime. Any argument by Telstra that the regime should be rolled back is an attempt to 'renege on the deal' with the Australian public by tilting the terms of the access regime in favour of Telstra shareholders.

1.16 Optus also commends to the Commission the submissions lodged with respect to this review by the Australian Mobile Telecommunications Association and by Communications Alliance. Optus is a member of each of these industry associations.

## 2. The Part XIC Telecommunications Access Regime

### A sector-specific access regime

2.1 The Productivity Commission has been tasked with identifying where regulations are unnecessarily duplicative. There may be an argument that Part XIC duplicates the effect of the general access regime in Part IIIA. Optus considers that this argument would be misplaced.

2.2 Optus submits that Part XIC should be retained as a sector-specific access regime. Optus has made specific submissions to the Productivity Commission on this issue in the context of the Productivity Commission's 2000-2001 review of the Telecommunications Access Regime, noting the critical features of the telecommunications industry which justify sector-specific access regulation. Optus refers the Productivity Commission to its previous submission, which is attached to this paper.

2.3 Optus also notes the Productivity Commission's recommendation on this issue in its final report in respect of that inquiry, which was as follows:

Recommendation 8.1

"*The Commission recommends the retention of provisions for a telecommunications-specific access regime. However, its objectives, principles and processes should adopt those in Part IIIA wherever possible*"[1]

### Objectives of the access regime

2.4 In response to its discussion paper the Productivity Commission may receive submissions from Telstra contending that the objectives of the access regime and the legislative criteria in Part XIC should be adjusted in order to bring the regime closer in line with the interests of Telstra shareholders, for example, biasing the access regime towards the stimulation of additional capital investment in telecommunications network infrastructure.

2.5 Optus considers that such an adjustment would be inappropriate, for the reasons set out in the following pages.

*Investment must be efficient*

2.6 Part XIC is explicitly intended to advance the long term interests of end users (LTIE) through promoting *efficient* investment in infrastructure. Optus submits that it is wrong to assume as an unqualified proposition that facilities based competition (through infrastructure duplication) is a goal to be pursued at any cost. Facilities based competition should be encouraged only where it involves efficient use of and investment in infrastructure. In particular, as the ACCC has concluded, facilities based competition is more likely to promote

[1] Productivity Commission, Telecommunications Competition Regulation Inquiry Report, Report No 16, 20 September 2001, Recommendations XXXVIII

the LTIE "[w]here it does not result in the economically inefficient duplication of infrastructure".[2] In the same paper the ACCC noted: [3]

> *The Commission's position has consistently been that it will only seek to promote facilities based (full or quasi) competition where it is likely to be economically efficient, and therefore in the LTIE.*

2.7 In the footnote to this passage the ACCC elaborated on the meaning of inefficient duplication of infrastructure, noting that:

> *... it would not be appropriate to encourage facilities based competition where the demand for services in a market can be satisfied at a lower cost by one facility than two or more facilities. In these circumstances, the LTIE would be best served by an effective access regime*

2.8 Optus submits that inefficient infrastructure duplication is a waste of society's resources, and the terms of the legislative criteria in Part XIC (and indeed the terms of Part IIIA) are intended to guard against this waste. Any suggestion that the access regime should be biased in favour of investment in infrastructure that is not efficient should be strongly resisted.

*The access regime allows Telstra to fully recover its cost of investment*

2.9 The ACCC crafts its pricing principles for regulated services in order to meet the legislative criteria in Part XIC including the promotion of efficient investment in and use of infrastructure. The ACCC sets the cost of regulated access to key services such as the unconditioned local loop service (ULLS) by reference to the access provider's efficient costs of supplying the service (inclusive of a normal return on investment). In doing so it pays careful attention to Telstra's ability to recover its costs. For example, the ACCC noted in its final determination of the ULLS access dispute between Optus and Telstra that: [4]

> *"the ACCC considers it is a legitimate interest for an access provider to earn a normal commercial return on its investment"; and*
>
> *"The ACCC is satisfied that the ULLS monthly charges it has determined in this access dispute do not impact on Telstra's capacity to earn a normal commercial return on its investments."*

2.10 The Trade Practices Act specifically requires the ACCC to set prices for regulated services with the objective of "encouraging the economically efficient use of and economically efficient investment in ... infrastructure". The ACCC is careful to ensure that this objective is satisfied by setting access charges that reflect the efficient, forward looking costs of service provision. In its final determination of the ULLS access dispute between Optus and Telstra it made the following statement on the matter: [5]

---

[2] ACCC, 'Fixed Services Review, A second position paper ', April 2007, p 15

[3] Ibid, p.21

[4] ACCC, March 2008, ULLS Access Dispute between Telstra and Optus, Statement of Reasons for Final Determination, pp.28, 29

[5] ACCC, ACCC, March 2008, ULLS Access Dispute between Telstra and Optus, Statement of Reasons for Final Determination, p.27

> *Again, the ACCC considers that access charges that reflect the efficient, forward looking costs best meet these considerations. Such charges are consistent with the access provider's legitimate commercial interests and, in particular, enable access providers to exploit economies of scale and scope. These charges also provide correct incentives for the access provider and access seekers to make efficient investments in infrastructure used to supply the ULLS and downstream services. By promoting competition, these charges also encourage dynamic efficiency.*

2.11 Given that the ACCC sets charges at the level of efficient cost, Telstra's insistence that it allows access seekers to obtain services at 'below cost' rates is puzzling. One explanation is that costs in excess of efficient costs are not recoverable. For example, the ACCC noted in its final determination of the ULLS access dispute between Optus and Telstra that: [6]

> *It is the ACCC's view that the term "legitimate business interests" does not necessarily extend to include costs associated with all investments, as on occasion there will be the potential for the access provider to make investments that were not efficient. The ACCC further notes that an access price should not be inflated to recover any profits the access provider (or any other party) may lose in a dependent market as a result of the provision of access.*

2.12 Optus submits that it is quite consistent with dynamic efficiency and encouragement of efficient investment incentives that such inefficient costs (gold-plating) and lost profits be excluded.

2.13 Another potential explanation is that Telstra believes that the ACCC has miscalculated the level of efficient cost. However the ACCC has devoted considerable time and effort to obtaining an accurate assessment of efficient cost. Optus submits that any suggestion by Telstra that the Productivity Commission should proceed upon the assumption that there has been regulatory error in the determination of access charges should be categorically rejected. This is not the forum for an attack on access prices.

2.14 The ACCC's approach to pricing key access services such as the ULLS under the access regime will compensate an access provider for its efficiently incurred costs. However, when this approach is applied to Telstra in the real world, it is apparent that in fact the ACCC's approach *overcompensates* Telstra for its incurred costs. This is because Telstra has already received compensation for much of its historic capital expenditure on construction of the copper customer access network (CAN). Evidence for this proposition may be deduced via an examination of the age and economic lifetimes of the relevant CAN assets.

2.15 Whilst a proportion of the CAN was constructed inside the last two decades, it is clear from historical records that a very high proportion of the CAN is much older. This view of the age of the network is supported by public statements from Telstra. For example, in 2001 Telstra reported the following information on the age of the CAN:

---

[6] ACCC, ACCC, March 2008, ULLS Access Dispute between Telstra and Optus, Statement of Reasons for Final Determination, pp.28, 29

*"…more than 50 per cent of the copper pairs in the Australian CAN are over 20 years old, more than 30 per cent are over 30 years old and nearly 10 per cent predate 1950".* [7]

2.16 This means that conservatively, at least 50 per cent of Telstra's current CAN was built before 1980 and 30 per cent before 1970. A significant proportion of the CAN was in place by 1960.[8]

2.17 The age of assets in the CAN is important as the ACCC's 'TSLRIC' approach to access pricing prices network assets on a modern equivalent asset (MEA) replacement cost basis which values the asset according to replacement value, year after year. That is, it compensates Telstra for its investment costs *as if the network assets were new* – it does *not* reduce the level of compensation to take account of depreciation in the value of assets. This has the effect of compensating Telstra for the cost of that asset many times over and well beyond the asset's economic life.

2.18 This issue of overcompensation can be illustrated using a simple example. The main assets that account for approximately 90% of the costs in the CAN are main cabling and ducting.[9] The table below lists the asset lives for these key assets and their contribution to the total annual cost.

**Table 1 – Significant assets in the CAN and contribution to the total annual cost in the TEA model** [10]

| Asset category | Asset life | % contribution to total annual cost |
|---|---|---|
| Main cable | 10 years | 20.27% |
| Distribution cable | 20 years | 15.10% |
| Main ducts and pipes | 40 years | 11.78% |
| Distribution ducts and pipes | 30 years | 43.19% |
| **Total** | | **90.34%** |

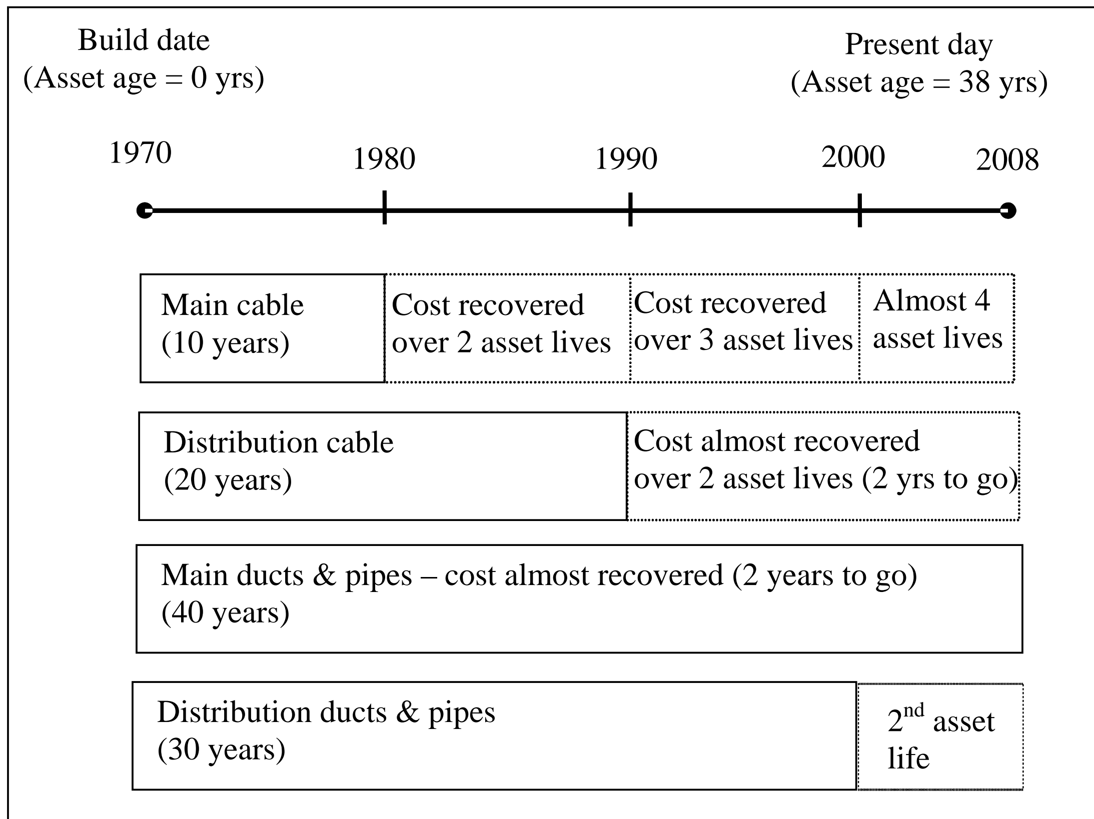
[7] Telstra, *Productivity Commission's draft report on Telecommunications Competition Regulation – Final Submission*, July 2001, p.21

[8] By 1960 the network owner (at that time the Postmaster General) had provided copper lines to the majority of serviceable addresses. After 1960, growth in the network was mainly for the purpose of servicing new addresses (in response to population growth).

[9] ACCC, *Telstra's Access Undertaking for the Unconditioned Local Loop Service - Discussion Paper*, June 2008 p.24

[10] Asset lives sourced from TEA model version 1.2.1

**Figure 1 – Relationship between build date, asset lives and Telstra's capital cost recovery**




2.19 The diagram above (Figure 1) shows that the approach historically applied by the Commission has allowed Telstra to recover its capital costs many times over. Making the very conservation assumption that only 30 per cent of the cabling and ducting was built by the end of 1970 and still exists in the current CAN, this means that for at least 30 per cent of this asset (which represents 90 per cent of the CAN cost), Telstra has recovered the capital cost almost 2 times over. It is foreseeable that for the (approximately) 10 per cent of the CAN that was built before 1950, Telstra has recovered its initial capital outlay over 5 times. Even in regards to an asset with a longer life (e.g. ducting), Telstra has been able to recover its cost approximately twice.

2.20 The current approach thus provides Telstra with a windfall gain in that it 'recovers' costs that have already fully recovered, in respect of assets that were already fully depreciated. The double recovery issue which arises with TSLRIC+ and with similar pricing approaches (also termed LRAIC)[11] has also been recognised in other jurisdictions. For example, in its 2004 paper on pricing approaches to unbundled local loops in the EU, Europe Economics stated: [12]

*Indeed, where LRAIC is applied to networks whose assets include an important element — such as duct — that was installed long ago and may*

[11] TSLRIC has been called LRAIC (Long Run Average Incremental Cost) by the European Commission however both terms have exactly the same meanings.
[12] Europe Economics, 2004, *Pricing Methodologies for Unbundled Access to the Local Loop,* Final Report, p.48

*have been fully depreciated, and charges are calculated so as to recover the LRAIC, this amounts to asking customers to "pay twice" for the assets, which may be very unlikely to be — or to need to be — replaced.*

*This is quite likely to be the case for ULL when a LRAIC methodology is used. As shown in the case study on Italy in Chapter 5, the relative weight of trench and duct costs in access networks — and the positive price trend of those assets — means that a ULL charge based on LRAIC will be expected to exceed a charge based on historic costs.*

2.21 Optus submits that by allowing double recovery of capital expenditure the TSLRIC+ approach to pricing the ULLS under Part XIC systematically over-compensates Telstra. Hence any suggestion by Telstra that the Part XIC access regime allows access seekers to obtain services at 'below cost' rates is disingenuous and misleading and should be rejected by the Commission.

*Non-Telstra carriers have made significant infrastructure investments*

2.22 The Productivity Commission may receive submissions implying that non-Telstra carriers do not make substantial investments in telecommunications infrastructure (and that this situation is attributable to the access regime). Such an implication would be inaccurate.

2.23 First, Non-Telstra carriers have made extensive investments in fixed line infrastructure. These investments have been made in response to the pricing certainty provided by the ACCC's pricing principles laid down under the Part XIC access regime. By the start of 2008 some 1084 competitor DSLAMs have been deployed across metropolitan Australia in some 387 exchanges.[13]

2.24 The table below shows the number of DSLAM installed by ISPs in recent years. It shows that the DSLAM footprint of access seekers including Optus and TPG have almost tripled over a period of 2 years. As at January 2007, there was a total 3,768 DSLAMs installed. [14] As at November 2008, there was a total 4,775 DSLAMs installed.

**Table: Number of DSL-enabled exchanges by carrier [5] [6]**

| Service providers with own DSLAM infrastructure | DSL-enabled exchanges | | | |
|---|---|---|---|---|
| | Jun 2006 | Jan 2007 | Nov 2008 | |
| AAPT | 22 | 22 | n/a | |
| Adam Internet | 25 | 29 | 33 | |
| Amcom | 34 | 34 | 37 | |
| EFTel | n/a | n/a | 58 | additional 29 listed as planned/in build |
| iiNet | 245 | 266 | 308 | additional 31 listed as proposed/in progress |
| Internode/Agile | 47 | 73 | 115 | additional 55 listed as planned/in build |
| MySoul | n/a | 22 | 27 | additional 1 listed as in build |
| Netspace Networks | n/a | 20 | 413 [7] | additional 19 listed as proposed/soon |
| Nextep | n/a | 95 | n/a | |
| Onthenet | 8 | 8 | 8 | |
| Optus | 100 | 304 | 366 | additional 2 listed as soon |
| PowerTel | 126 | 130 | 130 [8] | |
| Primus | 182 | 182 | 212 | additional 26 listed as soon |
| Regional Internet Aust | 6 | 6 | n/a | |
| Telstra | 2,109 | 2,432 | 2,754 [9] | |

[13] Telstra "Local Carriage Service and Wholesale Line Rental Exemption Applications" – Supporting submission, 12 October 2007, page 2

[14] ACMA, *Communications Infrastructure and Services Availability in Australia 2006-07*, 2007, p.5

2.25 Second, there has been an extensive roll out of 3G infrastructure by all mobile network operators (MNOs) in recent years, as the ACCC has observed.[15] Optus has recently incurred significant costs in the course of carrying out its plant to roll out its 3G mobile network to 98% population coverage, and will continue to do so for some years.

2.26 Since 2004 all four MNOs have entered into network sharing arrangements to build and deploy 3G networks, particularly in forward-looking 3G technology and not reinvestment in GSM networks. [16] The following list summarises the major mobile infrastructure developments since 2004:

- Since 2004 Hutchison has entered a 50/50 network ownership arrangement with Telstra to offer 3G services to Hutchinson's customers over the 3GSM 2100MHz network which operates in Adelaide, Brisbane, Canberra, the Gold Coast, Melbourne, Perth and Sydney; [17]
- In November 2005 Telstra announced its plans for the deployment of its 'Next G' 850MHz network, to replace its CDMA network;
- Since 2004 Vodafone and Optus have also entered into a joint venture arrangement for the deployment of 3G services, covering metropolitan areas in Adelaide, Brisbane, Canberra, the Gold Coast, Melbourne, Perth and Sydney; [18] and
- In January 2007 Optus announced its plans to build a new 3G mobile communications network to extend its 3G coverage, in addition to the network already co-owned with Vodafone in metropolitan areas.

2.27 To support these infrastructure developments, operators accumulate large capital expenditure to fund the deployment of new networks and network upgrades. The following table summarises the investment outlay for mobile infrastructure made by MNOs since 2004.

---

[15] ACCC, Nov 2008, Draft MTAS Pricing Principles Determination, p.14

[16] ACCC, *MTAS Pricing Principles Determination 1 July 2007 to 31 December 2008*, Final report, November 2007, p.28

[17] ACMA/ACCC, *Communications infrastructure and services availability in Australia 2008*, December 2008, p.20; ACCC, *MTAS Pricing Principles Determination 1 July 2007 to 31 December 2008*, Final report, November 2007, pp.28-30

[18] ACMA/ACCC, *Communications infrastructure and services availability in Australia 2008*, December 2008, p.20; ACCC, *MTAS Pricing Principles Determination 1 July 2007 to 31 December 2008*, Final report, November 2007, pp.28-30

**Table 1: Investment outlay on capital expenditure by MNOs since 2004** [19]

| | Telstra | Optus | Vodafone | Hutchison |
|---|---|---|---|---|
| **2004/05** | | $226 million [20] | | $207.1 million [21] |
| **2005/06** | $1.043 billion | $390 million [22] | $350.7 million | $203.8 million [23] |
| **2006/07** | $1.036 billion | $300 million [24] | $246.6 million | $268 million [25] |
| **2007/08** | | $302 million [26] | | $78.6 million [27] |
| **TOTAL** | ***$2.079 billion*** | ***$1.218 billion*** | ***$597.3 billion*** | ***$757.5 million*** |

2.28 Optus submits that, contrary to any suggestion that the existing legislation might have failed, Part XIC has succeeded in promoting significant investment in infrastructure by non-Telstra carriers.

*Part XIC promotes competition*

2.29 Part XIC advances the long term interests of end users not only through promoting efficient investment in infrastructure, but also through promoting competition.

2.30 The significant investments in infrastructure by non-Telstra players noted above are being used to by Telstra's competitors to serve a significant customer base. There has been a strong positive trend in ULLS uptake since 2005. As indicated in the following figure there has been an increased take up of unconditioned local loop (ULL) and line sharing service (LSS), which grew in the order of 100 per cent in 2006.[28] There are now over a million unbundled services currently in operation.[29]

---

[19] Unless otherwise stated, the following investment outlay values are from ACCC, *MTAS Pricing Principles Determination 1 July 2007 to 31 December 2008*, Final report, November 2007, pp.28-30

[20] Cash capital expenditure for mobile division for full year period to 31 March 2005. Singtel, *Singapore Telecommunications Limited and subsidiary companies management discussion and analysis of financial condition, results of operations and cash flows for the fourth quarter and financial year ended 31 Mar 2006*, May 2006, p.55

[21] Cash capital expenditure for full year period to 31 December 2005. Hutchinson, *Hutchison Telecommunications (Australia) Limited, Annual report 2007*, February 2008

[22] Cash capital expenditure for mobile division for full year period to 31 March 2006. Singtel, *Singapore Telecommunications Limited and subsidiary companies management discussion and analysis of financial condition, results of operations and cash flows for the fourth quarter and financial year ended 31 Mar 2006*, May 2006, p.55

[23] Cash capital expenditure for full year period to 31 December 2006. Hutchinson, *Hutchison Telecommunications (Australia) Limited, Annual report 2007*, February 2008

[24] Cash capital expenditure for mobile division for full year period to 31 March 2007. Singtel, *Singapore Telecommunications Limited and subsidiary companies management discussion and analysis of financial condition, results of operations and cash flows for the fourth quarter and financial year ended 31 Mar 2008*, May 2008, p.56

[25] Cash capital expenditure for full year period to 31 December 2007. Hutchinson, *Hutchison Telecommunications (Australia) Limited, Annual report 2007*, February 2008

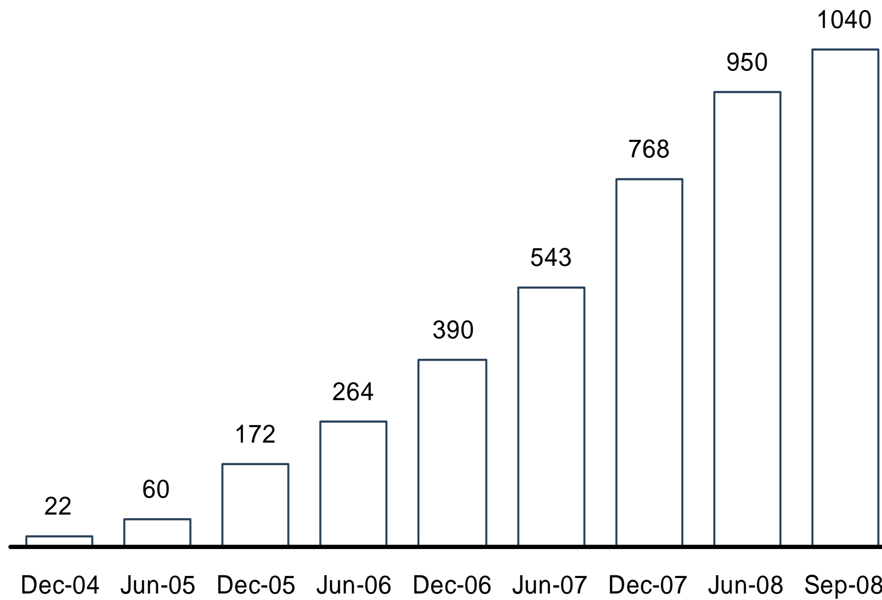
[26] Cash capital expenditure for mobile division for full year period to 31 March 2008. Singtel, *Singapore Telecommunications Limited and subsidiary companies management discussion and analysis of financial condition, results of operations and cash flows for the fourth quarter and financial year ended 31 Mar 2008*, May 2008, p.56

[27] Cash capital expenditure for half year period to 30 June 2008. Hutchinson, *Hutchison Telecommunications (Australia) Limited, Half year report – 30 June 2008*, August 2008

[28] ACCC, *Fixed Services Review – A second position paper*, April 2007, p.3

[29] ACMA, *Communications Infrastructure and Services Availability in Australia 2008*, 2008, p.3

**Figure 1: Australian unbundled lines - migrated customers (000s)** [30] [31]

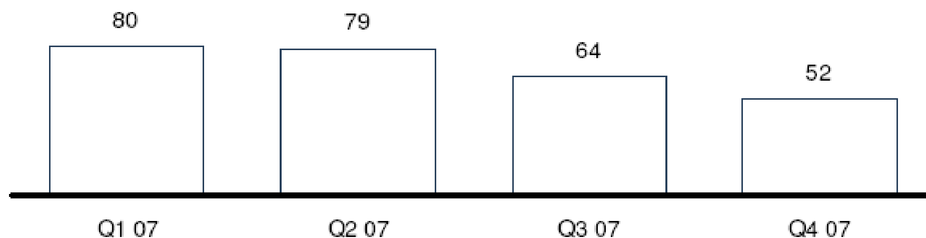



2.31 The significant investment in infrastructure by non-Telstra players noted above, which is premised upon effective access regulation by the ACCC, has driven important benefits to consumers – through lower prices, improved quality of service and greater innovation.

2.32 Competitors are using their own infrastructure to deliver innovative services such as Optus' Fusion product ($79/month for broadband plus telephony with unlimited local, long distance and calls to Optus Mobile) and iiNet's Naked DSL ($49.95 for broadband – without the requirement to pay for line rental).

2.33 The improvements in pricing have been tangible and are demonstrated by the following chart, which shows how consumers have benefited from aggressive marketing of Broadband services, in particular through capped plans.

**Average cost of data for standalone plans surveyed, if whole cap used ($/GB)**




2.34 The above chart is taken from a report for the Internet Industry Association by Spectrum Value Partners. Spectrum conclude that:

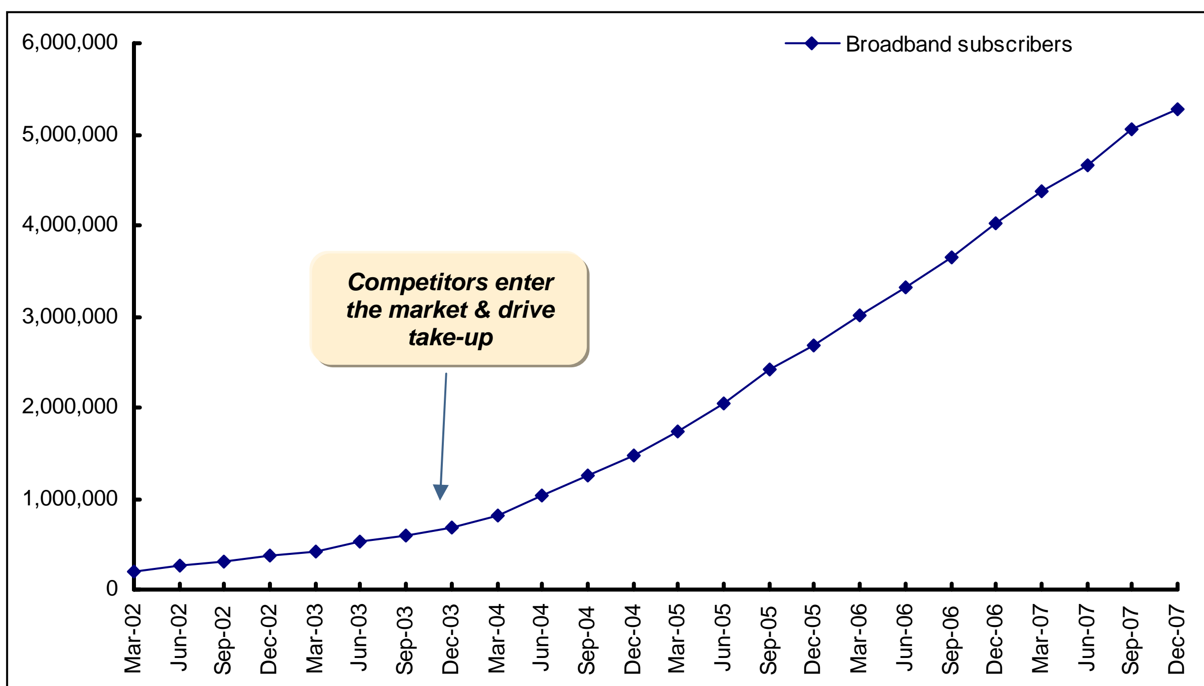
[30] These customer migration figures represent ULL migration by both ULL and LSS unbundling methods. JP Morgan, *Australian broadband market in 2007*, 17 March 2008, p.14

[31] ACMA, *Communications Infrastructure and Services Availability in Australia 2008*, 2008, p.5

*"As noted above, the other area where competition is manifesting itself is the cost of data. Operators are increasing data caps allowances without a corresponding increasing in price. For example, Optus has doubled the cap of their low end plans to 0.4GB and 2 GB without increasing the monthly charge."*[32]

2.35 The strengthening of competition is helping Australia's broadband market to catch up with the world, recovering from a delayed and sluggish start. The chart below shows how growth jumped sharply once competitors such as Optus entered the DSL market.

**Exhibit: Australian broadband uptake**[33]




2.36 The clear competitive benefits of unbundling have been recognised by the Chairman of the ACCC, Graeme Samuel, in a speech to the Australian Telecommunications Users Group:[34]

*"Increased competition in the provision of broadband services has seen progressively lower broadband prices, increased data caps, better speeds and new innovation and products (such as naked DSL). This increased competition in broadband by other ISPs and carriers owes a significant debt to being able to obtain access to Telstra's copper loop. Competitors have this access through the declaration of the unconditioned local loop service (ULLS) and the line sharing service (LSS)"*

2.37 Optus submits that access regulation has undeniably promoted competition, and that a change to the access regime aimed at biasing it towards the

---

[32] Spectrum/IIA Broadband Index – Fifth Edition (Q4 2008), 14 January 2008.
[33] Spectrum Value Partners analysis, ACCC Snapshot of broadband deployment (30-09-06), JP Morgan (17-03-08)
[34] ATUG 2008 Annual Conference, Graeme Samuel – 13 March 2008

stimulation of additional capital investment would undoubtedly lead to a deterioration in competition.

*Optus makes efficient use of declared services*

2.38 Telstra often uses Optus as its chief example to illustrate its attacks on the Part XIC access regime. It makes the claim that as a result of the access regime Optus purchases access to Telstra's network where it could be using its own HFC cable network in Sydney, Melbourne and Brisbane. Typically these attacks are supported by references to overseas cable operators.

2.39 Optus considers that this line of argument by Telstra is demonstrably wrong, for the reasons set out below.

2.40 The proposition that the Optus HFC Network effectively duplicates the Telstra copper customer access network (CAN) within its footprint is inaccurate. The Optus HFC Network is not a complete substitute for the Telstra CAN; it cannot be employed for the delivery of the relevant services to all premises within its footprint. A critical distinction exists between those premises that are serviceable by the Optus HFC network and those premises which are not serviceable. For a variety of reasons, a significant proportion of premises within the Exemption Area (approximately 36%) are not serviceable by the Optus HFC Network.

2.41 For premises which are serviceable, Optus already uses its HFC Network, in preference to accessing the declared services, to provide such services to residential end-users at serviceable premises. Optus also makes such investments in its HFC Network as are necessary and efficient for the continued operation of the network to service serviceable premises. In order to provide telecommunications services to those premises which are considered unserviceable by the Optus HFC Network, Optus makes use of regulated access to several declared services through Part XIC. Through accessing these services, Optus has been able to have a significant pro-competitive impact on market outcomes.[35]

2.42 Optus submits that the Optus HFC Network is already efficiently used to provide telecommunications services to premises which are serviceable by the network. It would not be efficient for Optus to make the required investments to duplicate last half-mile infrastructure where existing networks (including Telstra’s own HFC network as well as its copper access network) are already in place with capacity to service downstream markets.

2.43 Further, there are serious doubts about whether investment in HFC cable infrastructure would be an efficient investment, which has been highlighted in a recent paper by the consultancy CEG. CEG recently carried out a review of the performance of HFC cable infrastructure compared with DSL infrastructure in overseas jurisdictions (at Optus’ request, in the context of Telstra’s HFC exemption application). CEG found that despite attempts to promote facilities-based competition in overseas markets through roll-back of access regulation, cable is losing market share to DSL internationally:[36]

---

[35] See attached CEG Report October 2008

[36] CEG, *Assessing the Likely Effects of Asymmetric Access Regulation in Australia: Telstra's Proposed HFC Exemption*, October 2008, p.24

*"The overall picture that emerges from the international evidence is that while cable was initially strong in a number of markets, it has been losing ground in recent years in both the key revenue sources of pay TV and broadband."*

2.44 CEG concluded that:

*Cable's loss of market share internationally supports the view that DSL is a more efficient (lower cost) means of service delivery compared to cable, particularly for new connections where copper legacy infrastructure is in place and equivalent cable infrastructure is not."*

2.45 In support of its thesis, Telstra often points to the success of cable companies in other jurisdictions. Optus submits that such comparison with cable companies in other jurisdictions is misleading, since there are fundamental differences between the competitive conditions facing HFC network operators in Australia and those facing cable competitors overseas. These include:

- While pay TV has been a key driver for demand on HFC networks and an important part of expected revenues for cable operators overseas, Australian operators (and Optus in particular) have lower expected revenues from pay TV when compared with overseas operators. This is because:

  i) pay TV penetration in Australia is low by international standards, at approximately 27 to 29 per cent of households passed, as compared to 62 per cent in the United States and 65 per cent in Canada; and

  ii) pay TV operators in Australia pay some of highest prices in the world for content.

- Australia is one of only two OECD countries (the other being Portugal) where there is significant overlap between cable networks (where there are overbuilders in the United States, they are marginal players). Telstra's deliberate overbuild of Optus' HFC network with its own network (which Telstra undertook in order to protect its existing fixed line profits from platform competition) has had the impact of significantly harming the commercial prospects of Optus' HFC network, as evidenced by the write-downs that have occurred on the value of both networks.

- In Canada, the United States, the United Kingdom and the Netherlands, there is no or minimal incumbent local exchange carrier ownership in HFC networks.

2.46 These factors are conveniently overlooked by Telstra because they highlight the unprecedented advantage it has enjoyed over its international peers.

2.47 Telstra has recently run this argument in an application to the ACCC to bar Optus from access to regulated services to all premises within the HFC network footprint (whether serviceable or unserviceable). After extensive investigation, on 11 November 2008 the ACCC issued a Final Decision that which found that Telstra's proposed exemption order would not promote

competition or efficient investment in infrastructure, and accordingly was not in the long term interests of end users. In the course of its investigation the ACCC revealed many of Telstra's arguments and supporting evidence to be misleading. In order to give proper context to any claims Telstra may make in the course of the current review, Optus refers the Productivity Commission to the ACCC's final decision on the 'HFC exemption' matter (attached).

2.48 Optus submits that the Productivity Commission should reject any suggestion that Optus' use of declared services amounts to evidence that Part XIC has failed. The evidence submitted to support any such claim should be scrutinised very closely. To the contrary, Optus' use of declared services amounts to evidence that Part XIC is successful in promoting facilities-based competition where it is efficient to do so.

*International evidence confirms access regulation does not discourage investment*

2.49 An argument frequently made by Telstra and other incumbents is that regulated access leads to lessened investment in the telecommunications industry. However, this claim has been refuted in empirical research. On the contrary, there have been a number of studies which demonstrate the positive effects of unbundling on investment. For example:

- Willig et al. (2002) confirmed the alternative 'competitive stimulus hypothesis': they found that low unbundling rates induce competition and stimulate investment by incumbents, such that "a one percent decrease in the UNE-P rate[37] generated between a 2,1 and 2.9 percent increase in ILEC investment." [38]

- Willig (2003) noted that "the Competitive Stimulus Hypothesis follows naturally from basic economic theory and its understanding of competitive markets. Increased competition enabled by UNEs can be expected to result in lower retail prices both because of efficiency improvements induced by competition and because of the pressure competition places on above-cost pricing. .. Additionally, in a competitive environment, both the incumbent and the entrant will face enhanced incentives to improve quality and innovate with respect to services, leading to further investment."[39]

- Hassett and Kotlikoff (2002) raise a number of interesting results in their study of market dynamics under a variety of potential industry structures. "First, telecom investment and output generally increase significantly and telecom prices decrease significantly when new firms enter a market. This is true whether or not the entry occurs because of normal economic forces or as a result of wholesaling arrangements under which competitors rent access to customers from incumbents. … Second, *unbundling* (forcing the ILECs to rent to the CLECs all or part of their network elements) can dramatically increase CLEC entry by

37 UNE: unbundled network elements (US). UNE-P: a combination of UNEs including the local loop and switching that allow end-to-end service delivery by an access seeker in the US.

38 Based on Makova (2006) in Heinacher and Preissl, *Fibre-optic networks: On investment, regulation and competition*, CESifo DICE Report 3/2006, p.24.

39 Willig, *Investment is appropriately stimulated by TELRIC,* unpublished manuscript, October 2003. Available from URL: http://psc.ky.gov/pscecf/2003-00379/5200700_efs/04132004/MCI_ST_MTB_EX_14_04%2013%2004.pdf

lowering their costs of doing so. Third, competition raises consumer welfare relative to having a regulated monopoly in local voice and unregulated duopoly in broadband." [40]

- Ford and Spiwak (2004) conducted an econometric analysis to test the 'unbundling deters investment' hypothesis, in terms of the relationship between broadband deployment and local loop prices. The study found the opposite to be true, that "unbundled loop prices based on Total Element Long Run Incremental Cost ("TELRIC") actually lead to *increased availability* of broadband services and increased availability of *competitive* broadband services defined as area with at least four broadband providers."[41] The authors conclude that "this study adds to the mounting work showing that wholesale network access requirements (like unbundling) do not dampen broadband availability or investment incentives more generally." [42]

2.50 Further, the Ford and Spiwak (2004) study also cites a number of studies in support of their empirical findings: [43]

- Research has already conclusively proved that the competition produced by the market opening provisions of the 1996 Act increased the incumbent Bell companies' average net CapEx investment by $759 per year, or about 6.4% per year in the aggregate, for each UNE-P access line. PHOENIX CENTER POLICY BULLETIN NO. 5, *Competition and Bell Company Investment in Telecommunications Plant: The Effects of UNE-P* (17 September 2003) (http://www.phoenixcenter.org/PolicyBulletin/PolicyBulletin5.pdf ). *See also*:

- PHOENIX CENTER POLICY BULLETIN NO. 6: *UNE-P Drives* Bell *Investment - A Synthesis Model* (17 September 2003) (available at: http://www.phoenix-center.org/PolicyBulletin/PolicyBulletin6Final.pdf);

- G. S. Ford and M. D. Pelcovits, *Unbundling and Facilities-Based Entry by CLECs: Two Empirical Tests* (July 2002): www.telepolicy.com;

- T. R. Beard, R. B. Ekelund Jr., and G.S. Ford, *Pursuing Competition in Local Telephony: The Law and Economics of Unbundling and Impairment* (November 2002)(www.telepolicy.com);

- T. R. Beard, G. S. Ford, and T.M. Koutsky, *Mandated Access and the Make-or-Buy Decision: The Case of Local Telecommunications Competition* (December 2002) (www.telepolicy.com);

- R. D. Willig, W. H. Lehr, J. P. Bigelow, and S. B. Levinson, *Stimulating Investment and the Telecommunications Act of 1996*, Unpublished Manuscript (October 2002);

---

[40] Hassett and Kotlikoff, *The role of competition in stimulating telecom investment*, October 2002, p.3
[41] Ford and Spiwak, *The positive effects of unbundling on broadband deployment*, Phoenix Center Policy Paper No. 19, September 2004, p.4
[42] Ford and Spiwak, *The positive effects of unbundling on broadband deployment*, Phoenix Center Policy Paper No. 19, September 2004, p.12
[43] Ford and Spiwak, *The positive effects of unbundling on broadband deployment*, Phoenix Center Policy Paper No. 19, September 2004, p.2

- K A. Hassett and L. J. Kotlikoff, *The Role of Competition in Stimulating Telecom Investment*, AEI PUBLICATION (October 2, 2002) (www.aei.org/publications/pubID.14873/pub_detail.asp). Hassett *et al.* (2002) perform a simulation rather than using actual data. *See also, Does Unbundling Really Discourage Facilities-Based Entry? An Econometric Examination of the Unbundled Local Switching Restriction*, Z-TEL POLICY PAPER NO. 4 (February 2002)(www.telepolicy.com);

- Competition *at the Crossroads: Can Public Utility Commissions Save Local Telephone Competition?*, Consumer Federation of America (October 2003) (http://www.consumerfed.org/pr10.07.03.html).

2.51 Optus submits that effective access regulation does not discourage efficient investment in infrastructure, and roll-back of access regulation does not encourage such investment.

*Telstra was privatised subject to the access regime*

2.52 Finally, the Productivity Commission should keep in mind that the privatisation of Telstra was quite explicitly made subject to the continuation of the access regime; this was part of the deal that was struck with the Australian public.

2.53 On 6 March 2008 the High Court of Australia unanimously ruled against Telstra's claim that the telecommunications access regime involved the acquisition of its assets on less than 'just terms' as required under the Australian Constitution. The court found that: [44]

> *"what is now important is that the rights in the assets vested in Telstra were rights to use the assets in conjunction with the provision of telecommunications services but those rights were always subject to a statutory access regime which permitted other carriers to use the assets in question."*

2.54 A key element of the High Court's 2008 decision in *Telstra Corporation Limited v The Commonwealth* was to recognise the importance of history in the context of assessments of the regulatory regime, as economic commentators CEG have recognised:[45]

> *In effect, the High Court ruled that the PSTN assets which were vested in Telstra were already subject to an access regime at the time of privatisation and hence Telstra (and its shareholders) never held the property rights they claimed were being 'acquired' by the access regime. In making this decision the court emphasised the need to appropriately recognise the context and history of Telstra's interest in the PSTN.*
>
> *This reflection on history from the High Court has potentially broader significance than merely upholding the constitutional validity of the*

[44] Telstra Corporation Limited v The Commonwealth [2008] HCA 7 (6 March 2008) at 53

[45] CEG, Wednesday, 12 March 2008, High Court: History is important

*telecommunications access regime. It may be a salutatory lesson to those assessing other claims by Telstra under the access regime and telecommunications regulation which are related to Telstra's ownership of the PSTN. To ignore history risks granting rights to Telstra that it never actually held and also risks giving returns to Telstra's shareholder that are inconsistent with their reasonable entitlements.*

*Since Telstra (and its predecessors Telecom/OTC and AOTC) was incorporated and certainly prior to its privatisations (in 1997, 1999 and 2006) it has been subject to laws that impact on the value of its assets. These include controls on its retail prices which began as far back as 1989, regulation of the funding it receives from providing universal service at least as far back as the Telecommunications Act of 1991 and rules setting access prices under 1991 Act's regime and as amended in the Telecommunications Act 1997.*

2.55 A change to the access regime aimed at biasing it towards the stimulation of additional capital investment would amount to a partial roll-back of that access regime. Optus submits that if Telstra makes such an argument, this would represent an attempt to 'renege on the deal' with the Australian public by tilting the terms of the access regime in favour of Telstra shareholders.

**Improving the operation of the access regime**

2.56 The current regulatory framework has been in place since 1997 and most objective commentators would accept that this framework has been less than effective in both controlling Telstra and stimulating competition, especially in respect of the provision of fixed line services. Consideration of the problems arising from the current system will actually help inform us of the changes that must be made to the regulatory framework, changes that as especially critical as the industry moves to an NBN environment.

2.57 In framing the current telecommunications regulatory regime which took effect in 1997, policy makers rejected took the view that level playing field in the provision of telecommunication services could be achieved by a combination of general competition law principles coupled with telecommunications specific access regulation. Hence, under the current regime, introduced in 1997, Telstra remains vertically integrated but subject to specific regulation of the Trade Practices Act (TPA). Part XI B of the TPA deals with abuse of market power and anti-competitive conduct whilst Part XIC regulates the terms of access to services.

2.58 However experience has shown that Telstra has both the incentive and means to game the system to its advantage. Telstra has a well rehearsed game plan to frustrate the decision making processes: It employs a take it or leave it approach to commercial negotiations, which are treated merely as a stalling device. It rarely engages on issues and blatantly uses information asymmetries to undermine the negotiating process.

2.59 Given that Part XIC as it stands is both ineffective and burdensome, Optus proposes a number of potential improvements in the following sections.

*The current Operational Separation regime is ineffective*

2.60 Telstra's position is somewhat unique amongst its peers since it has been permitted to participate and take a strong position in almost all sectors of the market. It is, for example;

(a) the owner of the copper loop access network;

(b) both the largest retail and wholesale provider of fixed line voice and broadband services through its control of the local copper loop;

(c) the owner of an HFC cable network – the second largest fixed access network in Australia after Telstra's own copper loop network;

(d) the dominant provider of pay-tv services in Australia through its 50% ownership in Foxtel, which is provided over its HFC cable network;

(e) the dominant provider of directory information services; and

(f) the largest mobile player in Australia.

2.61 Typically incumbent telecommunication providers have been restricted from providing certain services and this decision to leave Telstra intact as a fully integrated provider of services has overhung the telecommunications market.

2.62 Telstra's integration into so many related businesses has been a major obstacle to competition, since it gives Telstra both the opportunity to use its control of one asset (eg the pay TV business) to impede competition in a separate market (eg broadband). Telstra's structure has proved to a significant source of recurring problems and has been instrumental in raising barriers to the effective emergence of competition in the provision of fixed line services. As indicated in the table below this has manifested itself in significant price and non-price discrimination.

2.63 Telstra was notionally required to implement "operational separation" under the Telecommunications Amendment (Competition and Consumer Issues) Act 2005, which resulted in the Operational Separation Plan (OSP) scheme set out in Part 8 Schedule 1 of the Telecommunications Act 1997. However, the changes this brought about are cosmetic and have had no impact on Telstra's behaviour.

2.64 Commenting on the arrangements that apply in Australia Professor Martin Cave concludes that;

*"This approach seems singularly ill-equipped to achieve any kind of equivalence in the services offered by [sic] to internal and external customers, as it exaggerates the differences in institutional arrangements between them".*

2.65 Similarly, Dr Chris Doyle notes that the current arrangements in Australia are "weak" and that;

*"Notably there is nothing in the operation separation plan that would appear to prevent Telstra from changing prices that resulted in a price squeeze or require Telstra to rectify its conduct by offering prices that would alleviate the price squeeze".*

2.66 The chairman of the ACCC, Mr Graeme Samuel had in June 2008 told a Senate Committee that the current operational separation regime that applies to Telstra is not an effective mechanism for promoting equivalency between Telstra and its competitors:

*"… We continue to receive complaints of conduct that suggest that the objective of equivalence, which was the objective of the regime, is not being achieved. … I guess, in summary, we would have to say that the regime is fundamentally unduly complex. There is a lot of discretion left to Telstra. There are limited self-regulatory mechanisms and unduly convoluted processes to implement any corrective action if a problem is identified".*[6]

2.67 The Senate Committee further heard that the ACCC had investigated and reported three breaches of the operational separation rules yet no action was taken against Telstra. It is quite clear that these arrangements offer no constraint over Telstra.

2.68 Given that the current Operational Separation Plan arrangements are ineffective, Optus considers that in order to achieve the objectives of the OSP regime, the Productivity Commission should recommend structural separation as a more effective and less burdensome tool.

2.69 Structural separation would address many of the problems which today arise from Telstra's dominant market position since it would change the incentives of the entity that owns and manages the network. Structural separation deters the risks of a vertically integrated entity from exercising its discretion to harm competition by settling inefficient access prices, which may send signals that lead to the inefficient use of, and investment in, infrastructure which would not be in the interests of access seekers nor be in the long term interest of end users.

2.70 Structural separation involves separating an entity that owns and manages the bottleneck infrastructure from any downstream affiliated retail entities. What this means in practice is that the critical component of the bottleneck infrastructure must be owned by a company (the owning entity) which is distinct from –and does not have shared ownership beyond a specified level – with any retail telecommunications provider.

2.71 Structural separation would also require that the network owning entity would have separate facilities, systems, staff and separate ownership from any retail operator. As a standalone business the incentives of the network owning entity would differ markedly from those of Telstra today. The network owning Entity would be legally separated from any retail entity. It would be required to have its own board of directors and management team and it would have a fiduciary duty to operate the network in its best interests and not those of any related retail entity. Compared to the vertically integrated Telstra of today, it would have a significantly reduced incentive to discriminate in favour of one particular purchaser of wholesale services (namely, Telstra Retail) against all others.

2.72 Structural separation would therefore assist in addressing the core problems associated with a vertically integrated Telstra today that have so blighted the industry. The network owning entity would give first priority to its own interests and financial performance. It would have very strong incentives to maximise use of the network. By contrast, today Telstra Wholesale gives priority to the interests and financial performance of the overall Telstra business.

2.73 Structural separation would mean that the network owning entity should;

- Engage in efficient pricing and ensure that all access seekers face the true economic wholesale prices;
- Respond favourably to requests by access seekers to develop innovative services.
- Offer differentiated levels of access to the network – although these would be offered to all on a non-discriminatory basis.
- Have no incentive to engage in price or non-price sabotage against a particular access seeker;
- Provide all access seekers with equal access to information important to their planning processes; and
- Have a lower cost of capital revealed in financial markets reflecting its lower risks as a standalone network owner.

2.74 This change in incentives for the network owner could be expected to flow through to a more competitive and diverse market. This in turn is likely to deliver very tangible benefits to customers in the form of lower prices and more innovative services. This is why the case for structural separation is a strong one. These benefits have been recognised by the ACCC:

*"a vertically separated ownership model could reduce incentives for the access provider to discriminate between downstream users of the access service and, therefore, facilitate strong and effective competition between access seekers in retail markets."* [46]

2.75 To ensure that separation can operate effectively and is not subject to gaming, especially where there is common ownership between a separated access provider and any downstream retail entity, additional ring-fencing rules would need to be adopted. These ring-fencing provisions should include measures designed to achieve equivalence, on an equivalence of inputs basis, for both price and non-price terms of access thereby ensuring that any entity with a common ownership could not abuse its position to discriminate against other access seekers.

2.76 The key elements to effective ring-fencing arrangements would include rules that require the access provider to:

[46] ATUG 2008 Annual Conference, Graeme Samuel – 13 March 2008

- Implement strict separation of its business from any jointly owned entity, including separate offices and IT systems, accounting and reporting;
- Implement strict separation of any directors, managers and employees of its business and any jointly owned entity;
- Ensure that the salaries and incentives of the managers and directors of its business are not influenced by the performance of any related entity;
- Separate strategy, marketing and service development functions between network and jointly owned downstream businesses;
- Provide wholesale access to all services provided by the network to all access seekers;
- Have identical non-price terms and conditions for all services provided on the network (or quality adjusted prices) for all access seekers;
- Undertake genuine arm's length transactions (codified by contract) by allowing all access seekers (including any jointly owned downstream operations) to access the same platform for ordering, provisioning, invoicing, billing, fault rectification and reporting;
- Commit to provide access pricing on an equivalent and non-discriminatory basis and subject itself to detailed price imputation testing to ensure that such rules are adhered to;
- Prohibit information sharing between the its business and jointly owned downstream businesses (both retail and wholesale) by separating IT systems, prevent staff sharing and prohibiting management overlaps;
- Ensure confidential information provided by an access seekers should only be used for the purpose for which it was provided and should not be disclosed to any person without the access seekers express consent;
- Have independent oversight over controls between the its business and any jointly owned downstream businesses; and
- Provide a report to the ACCC on compliance with the ring-fencing provisions.

2.77 In summary, Optus submits that the Operational Separation scheme set out in Part 8 Schedule 1 of the Telecommunications Act 1997 is ineffective, and should either be replaced by a form of structural separation or functional separation backed up by a strong equivalence obligation.

*Reducing the burden: Declaration in cases of significant market power only*

2.78 Part XIC s151AL states that the ACCC may, by written instrument declare that a specified eligible service is a "declared service". Once a service is declared the access provider must, if requested to do so by a service provider, supply the service according to the terms and conditions accompanying the Declaration.

2.79 It is important to note that a declared service may be supplied by a number of access providers. For example, consider three telecommunications services – the wholesale line rental service (WLR), local carriage service (LCS) and mobile terminating access service (MTAS). Both Optus and Telstra and supply the WLR and LCS, and all four mobile network operators (Optus, Telstra, Vodafone and Hutchison) supply the MTAS. The key issue is that regardless of the nature of the service being declared, or the service providers, declaration applies universally to all entities that chose to supply the service.

2.80 Optus considers that level of regulation should adhere to the general principle of being the minimum necessary to achieve the desired objective. In the case of telecommunications services, the most effective method of promoting the LTIE is to focus regulation on the precise source of inefficiencies or bottlenecks in the market. In this context, declaration should apply only to carrier(s) which possess significant market power (SMP) in the supply of a particular service.

2.81 The classic definition of market power from Queensland Wire is the ability of a firm to raise prices above supply cost without rivals taking away customers in due time, supply cost being the minimum cost an efficient firm would incur in producing the product. Gleeson CJ and Callinan J in Boral clarified when such power would be found to exist:

*"The essence of power is the absence of constraint. Market power in a supplier is absence of constraint from the conduct of competitors or customers… Matters of degree are involved, but when a question of the degree of market power enjoyed by a supplier arises, the statute directs attention to the extent to which the conduct of the firm is constrained by the conduct of its competitors or its customers."*[47]

2.82 There is a clear consensus that regulation should, as far as possible, only be targeted at an incumbent operator with significant market power. European regulators have targeted ex ante rules at the following areas:

- requirements on network and facilities operators with significant market power to ensure that they offer interconnection on a non-discriminatory basis, publish prices and set out the terms on which they provide interconnection;
- requirements to prevent vertical margin squeezing by network and facilities operators with significant market power including separate regulatory accounts;
- rules against unfair cross-subsidies by network operators with significant market power;
- rules on network and facilities operators with significant market power prohibiting undue discrimination and undue preference.

2.83 This approach is currently adopted by the European Commission. Regulation is only imposed on carrier(s) which designated as possessing SMP in the

[47] Para 121

relevant market.[48] The European Commission further stated that ex ante obligations:

*"should only be imposed on those electronic communications markets whose characteristics may be such as to justify sector specific regulation in which the relevant NRA has determined that one or more operators have SMP"*.[49]

2.84 The definition of SMP is laid down in Article 14 of the Framework Directive:

"*an undertaking shall be deemed to have significant market power if, either individually or jointly with others, it enjoys a position equivalent to dominance, that is to say a position of economic strength affording it the power to behave to an appreciable extent independently of competitors, customers and ultimately consumers*."

2.85 These rules are implemented by regulators (NRAs) of the EU member states.[50] E.g. The Austrian regulator defines a carrier has SMP if it is:

- Exposed to little or no competition;
- Has an overwhelming position on the market by comparison with its competitors because of its ability to influence market conditions, its turnover in proportion to the size of the market, its control over access to end users, its access to financial resources and its experience in providing products and services.[51]

2.86 As the European recommendations make clear there is little need for similar rules for operators without significant market power, because they necessarily have no ability or incentive to distort competition.

2.87 The scope of the Telecommunications access regime has been inappropriately extended by the ACCC into two areas:

- Declaration of services that are supplied where there is effective competition such as the mobile sector, where there are multiple competing infrastructure players and keen competition; and
- Declaration of services (such as local calling) supplied by new entrants where there is no market power.

2.88 Optus has made specific submissions to the Productivity Commission on this issue in the context of the Productivity Commission's 2000-2001 review of the Telecommunications Access Regime. Optus refers the Productivity Commission to its previous submission, which is attached to this paper.

---

[48] Official Journal of the European Communities, Commission guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and services 2002/C 165/03, 11 July 2002

[49] Official Journal of the European Communities, Commission guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and services 2002/C 165/03, 11 July 2002.

[50] Article 7 of the Framework Directive states that NRAs of the EU members to notify to the EC draft regulatory measures including (i) define the relevant markets for ex ante regulation (ii) designate (or fail to designate) operators as having SMP; and/or (iii) impose on the designated SMP ex ante obligation to constrain their market power, which must be 'appropriate' and 'proportionate'.

[51] Freund, Telekom Austria, " The proposed SMP concept of the European Commission and its implications on regulation in the Member States", paper for the regional ITS conference 2001 in Dublin, September 1st -3rd , 33 The Austrian Telecommunication Act -TKG

2.89 Optus also refers the Commission to its conclusion on this issue in that review, which was as follows:

Recommendation 9.3

*"The Commission recommends the adoption of stringent new declaration criteria, crafted to achieve the following intention:*

*The ACCC may not declare the telecommunications service of a carrier or carriage service provider unless it is satisfied of all of the following matters:*

*…(b) that there is enduring market power in the service;…"* [52]

2.90 Optus submits that Declaration should apply only to services provided by operators with operators with significant market power. Regulation of operators other than the incumbent is unnecessary and unduly burdensome.

*Appeals and legal challenges*

2.91 The tools available to the ACCC to regulate Telstra's behaviour have been blunted by Telstra's increasing use of the appeals processes and legal challenges. Given the competitive opportunity ULLS has opened up, Telstra has subjected the ULLS regulations to the full blast of its legal armoury. This includes using the Australian Competition Tribunal, the Federal Court and even the High Court to challenge the ACCC. It is disturbing but not surprising (given Telstra's clear use of legal processes to delay the ACCC's decision-making) that it took nine years to issue a final ruling on access prices – and that ruling expired shortly after. The debate and uncertainty continues since Telstra has lodged a further ambit claim[53]. This process has resulted in significant uncertainty for access seekers and has arguably held back investment.

2.92 Under Part XIC:

- The ACCC's decision on an access undertaking can be challenged to the ACT (merit review). The ACT's decision can further be challenged through appeal to the Full Federal Court (judicial review);
- The ACCC's final determination on an access dispute can be challenged to the Federal Court (judicial review); and
- The ACCC's decision on an exemption application can be challenged to the ACT (merit review) if an application is made within 21 days after the ACCC made the decision[54]. The ACT's decision can further be challenged via appeal to the Full Federal Court (judicial review).

2.93 The legal strait jacket within which the ACCC has to operate is demonstrated by the ACCC's revelation that in March 2008 it was involved in 48 legal actions initiated by Telstra:

---

[52] Productivity Commission, Telecommunications Competition Regulation Inquiry Report, Report No 16, 20 September 2001, Recommendations XXXIX

[53] Telstra is claiming a ULLS Band 2 price of $30 – notwithstanding the fact that its claim for a nationally averaged ULLS price of $30 across all bands was comprehensively rejected by both the ACCC and the Australian Competition Tribunal.

[54] s151AV

"*…it is unsurprising that Telstra –while complaining about the burden of telecommunications regulation and the decisions of the competition regulator, the ACCC –currently has 48 regulatory decisions under appeal. Even if Telstra fails in all these appeals, the appeal process itself slows down the progress of competition in the telecommunications sector, benefiting Telstra as the incumbent owner of the public switched telephone network.*" [55]

2.94 Similarly, Optus counted 47 legal actions initiated by Telstra in June 2008. This includes:

- 1 appeal to the Full Federal Court;
- 12 ADJR actions in the Federal Court;
- 1 Federal court ADJR action regarding administration of retail price controls; and
- 33 applications to the Administrative Appeals Tribunal for review of ACCC decisions on Freedom of Information requests (a clear abuse of the FOI provisions).

2.95 The use of legal means to block or challenge decisions by the regulator therefore provides a useful means for Telstra to slow down the progress of competition in the telecommunications sector. It leads to a degree of paralysis within the regulatory process whereby the ACCC is unable to fulfil its statutory decision making function with any degree of timeliness. Telstra has one of the largest legal practices within Australia and it ultimately has the means to out spend the regulator on litigation.

2.96 Optus' past experience indicates that the cost of running regulatory proceedings (exclude internal staff costs) includes legal costs of:

**CiC**

2.97 Smaller access seekers are left to the mercy of Telstra since they do not have the means to fund the litigation required to achieve a regulatory outcome. Those that do challenge Telstra face lengthy delays and the inevitable uncertainty that any decision may not be enforceable. Ultimately it is consumers who lose through this behaviour since competition is harmed.

2.98 In recent months the level of litigation from Telstra has increased. Recent action initiated by Telstra includes:

- Telstra brought a judicial review action against the ACCC on the *ACCC Final Determination on the ULLS access dispute of March 2008* to the Federal Court;

---

[55] ACCC, Commissioner Dr Stephen King, "Dealing with the regulatory burden: the participants and their incentives", 28 March 2008, Melbourne

- Telstra brought a judicial review action to the Federal Court against the ACCC on its Final Determination of November 2007 on a dispute over ULLS provisioning processes for multi-dwelling units;
- Telstra challenged the ACCC's decision in rejecting its exemption application with respect to Optus' HFC area to the ACT;
- Telstra appealed the ACT's decision to the Federal Court in rejecting its exemption application with respect to Wholesale Line Rental (WLR) and Local Carriage Service (LCS).

2.99 It was anticipated by policy makers that Telstra could behave in the ways described above to undermine competition. For this reason, the 1997 reforms equipped the regulator with specific powers to promote competition and address anti-competitive conduct (in the provisions of Part XIC and Part XIB Trade Practices Act). With over eleven years experience, we now know that these provisions have proved inadequate to control Telstra and to provide a genuine level playing field for competitors seeking to compete with Telstra in the provision of fixed line services.

2.100 Optus submits that the ability for interested parties to apply for merits-based review of the ACCC's decisions should be removed, since for the reasons described above it is burdensome and frustrates the aims of the regime.

2.101 Optus submits that ACCC rulings on prices should have immediate binding application across the market. This would avoid problems with the negotiate/arbitrate/appeal model that currently blights the industry. This model is consistent with the current provisions for setting prices under the Gas Code. It is also consistent with the powers of telecommunication regulators in many other jurisdictions. Implementation of this proposal will necessarily require changes to the current provisions of Part XIC.

*Exemption applications*

2.102 Under s152AR, a carrier or a carriage service provider is obliged to supply an active declared service to its access seekers if requested to do so. This standard access obligation is subject however to 'exemption' orders under s152AT. Section 152AT states that a carrier may apply to the ACCC for a written order exempting itself from all or any of the obligations referred to in s152AR if the ACCC is satisfied that the exemption will promote the long term interests of end users.

2.103 In 2007 Telstra lodged the following applications for exemption from its standard access obligations:

- On 24 August 2007, Telstra lodged an exemption application for domestic transmission capacity service (DTCS);
- On 8 October 2007, Telstra lodged an exemption application for domestic PSTN OA services;
- In July and October 2007, Telstra lodged exemption applications for Wholesale Line Rental (WLR) and Local Carriage Service (LCS):

- On 18 December 2007, Telstra lodged an exemption application for all fixed line services in Optus hybrid fibre cable (HFC) areas; and
- On 21 December 2007, Telstra lodged another exemption application for DTCS.

2.104 The ACCC's final decisions on all of these exemption applications (with the exception of the DTCS applications) were appealed to the Australian Competition Tribunal (ACT). Following the ACT's decision to overturn the WLR and LCS exemption, Telstra then in turn appealed that decision to the Full Federal Court.

2.105 With the exception of the exemption applications on DTCS, all the other applications are still subject to review by the ACT and the Full Federal Court. It has been 17 months since Telstra first lodged its exemption application to the ACCC on PSTN OA and WLR and LCS, however Optus and other access seekers of Telstra are still uncertain when to expect a final resolution of these matters since they are still subject to further appeal.

2.106 The regulatory burden placed on the parties involved in these proceedings is substantial. As mentioned elsewhere, the legal costs involved are significant, as are the demands on internal staff time and costs involved in preparing submissions and/or evidence to the ACCC and the ACT.

2.107 Further, the demands on time and resources required to participate in these processes are likely to be felt more heavily by access seekers due to the imbalance of resources between the incumbent and access seekers. Well resourced parties, primarily the incumbent, are better able to afford this time and resources than are less resourced parties, that is access seekers. This imbalance of resources provides Telstra with the ability and incentive to engage in regulatory gaming. Telstra is able to create uncertainty for access seekers' business models by casting doubt on their ability to get access at reasonable regulated rates, and it is able to outspend access seekers and divert their limited time and resources into resisting its legal manoeuvres.

2.108 It is critical to note that the ACCC is required to periodically review the basis for declaration of regulated services. Under s152ALA, the ACCC must specify an expiry date for the declaration and that expiry date must occur within the 5-year period beginning when the declaration was made. The ACCC therefore has to conduct regular reviews to consider whether it should extend, vary or revoke the declaration using the same statutory test as an exemption application, i.e. whether the declaration is in the long term interests of end users. Indeed, the ACCC has now begun a review of the declaration of fixed line services which canvasses all the issues raised by the applications for exemption lodged by Telstra in 2007.

2.109 It follows that applications for exemption relating to current declared services are entirely unnecessary. Moreover, the ACCC's decisions on declaration are not appealable. Optus submits that the rights for a carrier to apply to the ACCC an exemption order under s152AT should be removed. Allowing the ACCC to determine which services should be declared unhindered by the threat of appeal or exemption applications would immeasurably improve business certainty for access seekers and remove a key source of regulatory gaming and burdensome legalistic gaming by the incumbent.

*Undertakings*

2.110 The undertaking process is used by Telstra as a means to undermine the ACCC's price signalling processes and delay arbitral decisions. The arbitral process is stymied by constant questioning of due process and issues of jurisdiction. This has resulted in a merry-go-round of regulatory disputes and delay, legal challenges and rule changes to reinforce the powers of the regulatory. The cause of fixed line competition and consumer interests has been very poorly served by the system.

2.111 Evidence of the problem is provided by the table in Appendix A which shows the tortuous process for arriving at a final price ruling on ULLS – an essential building block of competition in the fixed line network.

2.112 For example, in response to the ACCC's draft decision on its ULLS undertaking of 2006 Telstra lodged in excess of fifty submissions, spread across a period dating from the deadline of the submission to the release of the final decision.[56] Optus considers this but one example from a raft of many, and synonymous with Telstra's general disdain for the regulatory process

2.113 The late submissions hinder the ACCC's ability to seek comments from interested parties while at the same time discreetly benefit Telstra by ensuring the information is before the ACT should Telstra wish to appeal the ACCC's decision.

2.114 Telstra has a well rehearsed game plan to frustrate the decision making processes of the Part XIC negotiate/arbitrate model at every stage. The system provides both the incentive and the opportunity for one of the most powerful and dominant incumbents in the world to game the system. Telstra has benefited richly from this state of affairs, and in doing so has subjected its competitors to significant regulatory burden.

2.115 In order to address the issues of delay and gaming identified above in respect of ULLS undertakings, Optus submits that the Commission should recommend that a party should not be able to submit an undertaking with terms of access including price that are materially the same – or indeed, which proposes a higher price – as those of a previous undertaking for the same service which has been rejected. Such a reform would improve certainty for business and thereby promote investment and competition.

2.116 In summary, Optus submits that whilst the telecommunications access regime set out in Part XIC of the Trade Practices Act 1974 (the Act) should be retained as sector-specific regulation and should not be biased towards duplication of infrastructure, the Productivity Commission should consider certain key limited reforms to make the regime less burdensome and more effective, and to eliminate certain redundant aspects. In particular, Optus proposes that the Operational Separation scheme set out in Part 8 Schedule 1 of the *Telecommunications Act 1997* is ineffective and should be strengthened through the introduction of structural separation, that Declaration under Part XIC should apply only to operators with significant market power and that parties be prevented from a) applying for merits-based

[56] ACCC, Assessment of Telstra's ULLS monthly charge undertaking, Final Decision, August 2006, p26

review of the ACCC's decisions,  b) applying for exemptions from the SAOs and c) submitting materially similar access undertakings.

## 3. The Part XIB Telecommunications Anticompetitive Conduct Provisions

### A sector-specific anticompetitive conduct regime

3.1 The Productivity Commission has been tasked with identifying where regulations are unnecessarily duplicative. There may be an argument that Part XIB duplicates the effect of the general anticompetitive conduct provisions in Part IV.

3.2 However, Optus submits that Part XIB should be retained as a sector-specific anticompetitive conduct regime. Optus has made specific submissions to the Productivity Commission on this issue in the context of the Productivity Commission's 2000-2001 review of the Telecommunications Access Regime, noting the critical features of the telecommunications industry which justify sector-specific regulation of anti-competitive conduct. Optus refers the Productivity Commission to its previous submission, which is attached to this paper.

3.3 Optus also notes the Productivity Commission's recommendation on this issue in its final report in respect of that inquiry, which was as follows:

Recommendation 5.1

*"The Commission recommends that the anti-competitive conduct provisions of Part XIB of the TPA be retained..."*

### Improving the operation of the anticompetitive conduct regime

3.4 Part XIB was intended to provide an alternate mechanism for the ACCC to take rapid enforcement action to address anti-competitive conduct. However under Part XIB taking action is very time-consuming and expensive.

3.5 Further, Part XIB requires complainants to discharge a burden of proof that is not achievable given asymmetries of information. In a dynamic industry like telecommunication, Telstra can enjoy months and even years of benefit from anti-competitive conduct before a matter is investigated and sanctions imposed.

3.6 Although five actions having been commenced by the ACCC –all against Telstra –no enforcement action has resulted. The table below provides a summary of the notices issued against Telstra.

| Competition Notices issued against Telstra | |
|---|---|
| **May 98** | • ACCC issues competition notice against Telstra, regarding Telstra's anti-competitive conduct in the internet market – in place until June 1999. No action taken. |
| **Aug 98** | • ACCC issues competition notice against Telstra regarding Telstra's customer transfer process ('commercial churn'). Three subsequent notices were issued and the ACCC commenced Federal Court action before the ACCC and Telstra reached a settlement agreement in February 2000. |
| **Sep 01** | • ACCC issues competition notice against Telstra regarding its supply of wholesale and retail ADSL services to its wholesale and retail customers – in place until May 2002. No action taken. |
| **Mar 04** | • ACCC issues a Competition Notice to Telstra with respect to the pricing of Telstra's broadband internet service - revoked in February 2005 following agreement between Telstra and the ACCC. |
| **Dec 05** | • ACCC issues a Consultation Notice to Telstra with respect to wholesale line rental price increase – revoked in February 2007 following successful Telstra ADJR challenge against the notice. |

3.7 This lack of action does not mean these cases were ill-founded. It is directly a result of the difficulty in the ACCC obtaining sufficient evidence (reliant as it is on Telstra for evidence) to take enforcement action. As a result the ACCC has all but signalled its unwillingness to continue to use its powers under Part XIB to control Telstra given the high evidentiary hurdles and the difficulties of enforcement.

3.8 Further difficulties with Part XIB are illustrated in Appendix B, which discusses a competition proceeding brought by Optus against Telstra based on claims that Telstra's pricing and other conduct in relation to the provision of wholesale line rental (WLR) services.

3.9 Optus submits that aspects of the Part XIB anticompetitive conduct regime could be considered ineffective, and that Part XIB should be reformed in order to reduce the burden on the victims of anticompetitive conduct. The process should be streamlined, timeframes and the evidentiary hurdles should be reduced, and the direct enforcement powers of the ACCC strengthened to give it the ability to effectively discipline anticompetitive conduct without reliance on the court system. In particular, the ACCC should be given powers to determine whether a contravention has occurred and to determine pecuniary penalties directly and expeditiously.

3.10 S151AKA of the Act restricts the ACCC from issuing a competition notice unless the ACCC has first given the carrier or provider a written notice stating that the ACCC proposes to issue a Part A competition notice, describes in summary form the instance of anti-competitive conduct, invites the carrier or provider to make submission and considers any submission received. Optus submits that the time required for the ACCC to receive submission(s) from Telstra in response to such notices and consider them allows Telstra many further months in which to continue engaging in anti-competitive conduct, thereby damaging competition in the market. The "Consultation notice" requirements are unnecessary and should be removed.

## 4. Customer Service Guarantee

4.1 The Customer Service Guarantee (CSG) operates under the *Telecommunications (Customer Service Guarantee) Standard 2000 (No.2)* (CSG Standard) and has been in place since the late 1990s (under a previous Determination). It imposes on Carriage Service Providers (CSPs) specific performance standards and compensation payment requirements with respect to the connection, fault rectification and making of appointments for the supply of standard fixed telephone services to consumers and small businesses customers. Optus believes that the CSG is a highly burdensome regulation that:

- has, from its outset, been applied unreasonably to CSPs seeking to enter the Australian telecommunications market and compete with the incumbent universal service provider, Telstra;
- imposes unreasonable costs on CSPs, both direct financial costs as well as significant distortionary costs associated with resource allocation and product and service development;
- consumes significant regulator resources at a cost to taxpayers, which could be put to more effective use elsewhere;
- unjustifiably remains in place after more than a decade of operation, during which there has been an explosive growth of alternative mobile and internet-based products and services; and
- in addition to the above points, is administered onerously by the Australian Communications and Media Authority (ACMA) via a highly prescriptive regime of quarterly reporting.

*CSG should apply only to universal service provider*

4.2 In a competitive marketplace, consumers are able to choose the service they desire and are able to trade off one particular service standard in return for another one which better meets their needs. In such an environment, providers will lose customers and become less viable if they do not offer customers the services they demand. This threat stimulates providers to be response in order to survive.

4.3 With respect to the CSG, Optus believes that it is reasonable that Telstra face regulated service standards because as the incumbent operator it continues to be overwhelmingly dominant in the provision of fixed telephony services (at the retail and wholesale levels); and because it is the fallback provider bearing the universal service obligation to serve all consumers in Australia with standard fixed telephony services regardless of where they reside or carry out their business.

4.4 That is, it would be both reasonable and beneficial for only Telstra to be subject to CSG regulations because it would ensure that where consumers have no choice of provider they are guaranteed a minimum level of service; and that where these benchmark standards exist in areas of competition, it

would set a service level floor that competing providers would need to improve upon in order to acquire and retain customers.

4.5 Under such a scenario, non-incumbent providers such as Optus would be able to divert resources to developing more innovative ways of offering service levels that are better than the regulated minimum standards and away from monitoring, reporting and maintaining automated penalty payment systems.

4.6 An important point to note is that when a consumer becomes a customer of a provider such as Optus, they are exercising an active choice to do so. That is, if Optus or another non-incumbent provider does not meet the customer's needs, the customer has the clear alternative of taking service from the universal service provider, Telstra.

*Direct financial costs of CSG compliance*

4.7 The costs of complying with the CSG are significant, consisting of costs to maintain complex IT systems; develop processes and procedures to ensure that all new fixed telephony services (including ordering, scheduling and billing systems) are integrated with these systems; training installations, customer service, marketing and sales staff; funding compensation payments; reporting on a quarterly basis to the regulator, ACMA; and employing staff to engage with ACMA and the Telecommunications Industry Ombudsman (TIO).

4.8 These costs are not within the control of the provider, but are determined by regulation. Providers such as Optus cannot limit the economic impact of these costs on their operations because they cannot change the underlying requirement to comply with the Standard.

4.9 For example, Optus estimates that during 2007-08 we spent **CiC**. This figure excludes costs associated with regulatory staff, training and product development overhead – and the approximately **CiC** spent by Optus in initially setting up our CSG IT infrastructure.

*Resource allocation distortion costs of CSG compliance*

4.10 The impact of the CSG on Optus and other non-incumbent providers also distorts resource allocation by requiring us to devote resources to satisfy a regulatory standard that does not meet our customers' needs and constrains our ability to design more suitable offerings. It also puts us and other non-incumbent providers in a "straightjacket" that is designed around the less efficient configuration of Telstra's network.

4.11 That is, requiring compliance with the CSG diverts resources away from opportunities to deliver more innovative products and services. It is costly and inefficient for a provider to divert resources into both complying with the regulated minimum standards imposed by the CSG while also seeking to develop more flexible services levels to meet consumers' needs. Consequently, more responsive standards are not developed and energy is focused on meeting the inflexible CSG service levels instead.

4.12 Moreover, the CSG performance standards have been designed around Telstra's Universal Service Obligation (USO) plan and network structure. Imposing the CSG on providers such as Optus requires us to mimic the operational characteristics of Telstra's processes and methods, developed over many years to support Telstra's more dated network and operations, rather than being more innovative and flexible.

4.13 A further point is that the telecommunications regulator, ACMA, employs a number of staff in its "Industry Monitoring" section, which administers the CSG. Optus believes that these people and the tax dollars that fund them could be more effectively and usefully utilised elsewhere.

*Onerous reporting compliance burden*

4.14 In addition to the imposition of the CSG policy itself on providers such as Optus, ACMA continues to take a micromanagement approach to its oversight of the policy's implementation and impose onerous reporting burdens on those providers subject to the CSG.

4.15 ACMA has significant discretion regarding monitoring and reporting on the CSG and is certainly under no obligation to require from non-incumbent providers such as Optus a level of reporting that is anywhere near what is currently required – that is, highly detailed quarterly reporting. A copy of a recent quarterly *Telecommunications Performance Monitoring Report* provided to ACMA by Optus has been attached to this submission as Appendix C for the PC's reference.

4.16 The key piece of legislation cited by ACMA to justify its CSG reporting regime in section 105 of the *Telecommunications Act 1997* and, in particular, section 105(3)(ea). We note that sections 105(1) and 105(3) of the Act place general requirements only on ACMA to monitor and report annually on "all significant matters" related to carriers' and Carriage Service Providers' (CSPs') performance, especially regarding consumers.

4.17 With respect to the CSG specifically, section 105(3)(ea) states that ACMA "must set out details of…the operation of [Part] 5 of the *Telecommunications (Consumer Protection and Service Standards) Act 1999* [the TCPSS Act]…" and section 105(4) states that "ACMA must monitor, and report each financial year to the Minister on, the appropriateness and adequacy of the approaches taken by the carriage service providers in carrying out their obligations, and discharging their liabilities, under Part 5 of the [TCPSS Act]."

4.18 With respect to guiding interpretation, the TCPSS Act's Explanatory Memorandum (EM) states that "…the ACA [is] to look proactively into systemic problems (eg consistent faults in a particular geographic area) and direct a carriage service provider about the things it should do to ensure those problems do not recur…The CSG is intended to guard against poor service in certain problem areas and provide a streamlined means for compensating consumers where standards in those areas are not met."

4.19 With respect to the CSG itself, this regulation has been in place for around a decade and is fully embedded within CSPs' systems and processes. Both the CSG itself and its related reporting requirements have been for many years

subject to intense scrutiny by ACMA. That is, Optus' compliance with this regulation has been well and truly demonstrated over many years and has been "institutionalised" (at significant set-up and ongoing costs) in our systems and processes. As such, we believe that – quite apart from the complete lack of merit we believe exists for Optus to be subject to the CSG at all, as outlined above – it is well part time for ACMA to end the current across the board micro-level reporting on the CSG.

## 5. Law Enforcement: Prepaid Identity Checks

5.1 Mobile prepaid identity checks in Australia operates under the *Telecommunications (Service Provider Identity Checks for Prepaid Mobile Telecommunications Services) Determination 2000* (the Prepaid Determination), which requires the telecommunications industry to collect, verify, store and, on lawful request, retrieve identity and address information about the purchaser and/or user of prepaid mobile phone services. The Prepaid Determination's primary purpose is to eliminate "anonymous" prepaid services in support of Australian national security policies.

5.2 Optus would contend that from its inception the Prepaid Determination has been a poor piece of regulation which provides for neither a balanced or cost-effective policy outcome. Since 2006, the Australian Communications and Media Authority (ACMA) has been seeking to improve compliance levels with the Prepaid Determination, with respect to identity check processes. However, this has brought about a regulatory regime which is inefficient, costly, unreasonably onerous and impractical and, of perhaps greatest concern, will perversely raise access barriers for disadvantaged consumers while not providing any inhibition to criminals – which is the point of the regulation.

5.3 The Australian Mobile Telecommunications Association (AMTA), of which Optus is a member, has provided a detailed overview of this matter in its own submission to this PC review. AMTA's submission fully represents Optus' views on this issue and, as such, Optus would refer to the PC to AMTA's submission when giving consideration on this matter.

## 6. Information provision to customers

6.1 The telecommunications industry is required to provide an incredibly vast amount of information to its customers at several different points in the customer lifecycle. Optus does not dispute that its customers should be well informed, however we find ourselves in a position where:

(a) we know that the provision of information in its required format is not effective in educating consumers, yet the legislation does not allow for alternate options;

(b) there is no sunset clause built into the legislation, which means that we are still required to send out information on an issue that was relevant some years ago, but is no longer of concern to consumers; and

(c) the telecommunications industry is required to provide information to consumers on issues that are broader than our sector – placing us at a disadvantage and having to expend additional resources when compared to other industries.

6.2 Both research and anecdotal feedback from customers and consumer advocates have shown that customers are confused and overwhelmed by the amount of information they are provided with, and yet – even though they are provided with the required information – they are unaware of their rights and the consumer safeguards that exist in the telecommunications industry.

6.3 Many pieces of telecommunications legislation and regulation require providers to mail certain information to their customers upon connection (or as soon as practicable after that), and every two years subsequently. As an example, Optus' welcome packs to its residential customers contain the following information:

(a) the Summary Standard Agreement for that product or service;

(b) Optus' Privacy Policy;

(c) information on Premium Services;

(d) information on Calling Number Display;

(e) information on Customer Service Guarantee;

(f) information on the Optus Special Assistance Program;

(g) information on the use of 112 as an alternate emergency service number from mobile phones;

(h) information on any other customer 'guarantees'; and

(i) a summary of the Optus Complaint Handling Policy.

All of this information is in addition to information on the actual product or service the customer has purchased or contracted to receive. Optus estimates that it spends approximately **CiC** per year in

meeting these information provision obligations, and this does not take into account its other information provision requirements which are not done via mail-out.

6.4 Even though research shows that the provision of this information in its current format is not effective, new regulations in the telecommunications sector continue to be brought into force containing additional customer information requirements, adding to the pile of material provided to customers and adding to the impost on business – without any assessment of the effectiveness or cost-benefit of providing such information to customers in such a format.

6.5 There does not seem to be any co-ordination in terms of how and why information must be provided to customers. Every new piece of legislation or regulation seems to include customer information provision requirements, without a clear analysis of:

(a) whether this information is provided elsewhere;

(b) whether the information will actually benefit the majority of customers;

(c) whether it would be sufficient to simply make it available upon request, or make it available online, rather than send it to customers at regular intervals;

(d) whether a sunset clause would be appropriate, so that the information stops being sent after a certain timeframe (for example, when it is clear that customers are now more aware and better educated about that particular issue); and

(e) whether the issue is one that crosses all industries or is specific to telecommunications.

6.6 This last point relates to the fact that the telecommunications industry has quite specific legislation that deals with issues pertinent beyond the telecommunications sector. The question arises as to why telecommunications providers are bearing the onus of informing their customers about issues that are not specific to their industry. A non-exhaustive list of legislative and regulatory instruments that contain customer information provision obligations follows.

| **Regulation of non-telecommunications-specific matters** | **Telecommunications-specific regulation** |
|---|---|
| Trade Practices Act 1974 | Telecommunications Act 1997 |
| State and Territory Fair Trading Acts | Telecommunications (Standard Form of Agreement Information) Determination 2003 |
| Complaint Handling chapter of the Telecommunications Consumer Protections Code (CA C628:2007) | Telecommunications (Customer Service Guarantee) Standard 2000 |

| | |
|---|---|
| Consumer Contracts chapter of the Telecommunications Consumer Protections Code (CA C628:2007) | Telecommunications (Consumer Protection and Service Standards) Act 1999 |
| Credit Management chapter of the Telecommunications Consumer Protections Code (CA C628:2007) | Priority Assistance for Life Threatening Medical Conditions Code (ACIF C609:2007) |
| Billing chapter of the Telecommunications Consumer Protections Code (CA C628:2007) | Telecommunications Service Provider (Premium Services) Determination 2004 No. 1 |
| Privacy Act 1988 | Telecommunications Service Provider (Premium Services) Determination 2004 No. 2 |
| Information on Accessibility Features for Telephone Equipment Code (ACIF C625:2005) | Calling Number Display Code (ACIF C522:2007) |
| | IIA Content Codes of Practice 2005 |
| | Customer Information on Prices, Terms and Conditions chapter of the Telecommunications Consumer Protections Code (CA C628:2007) |
| | Preselection Code (ACIF C515:2005) |
| | Local Number Portability Code (ACIF C540:2007) |
| | Mobile Number Portability Code (ACIF C570:2005) |
| | Customer Transfer Code (ACIF C546:2001) |
| | Handling of Life Threatening & Unwelcome Calls Code (ACIF C525:2006) |
| | Commercial Churn Code (ACIF C531: 2005) |
| | Emergency Call Services Requirements (ACIF C536:2003) |
| | Integrated Public Number Database (IPND) Code (ACIF C555:2008) |
| | Rights of Use of Numbers Code (ACIF C566:2005) |
| | Unconditioned Local Loop Service (ULLS) Ordering, Provisioning & Customer Transfer Code (ACIF C569:2005) |
| | Connect Outstanding Code (ACIF C617:2005) |

6.7 Optus therefore recommends that a review be undertaken of the customer information provision requirements in telecommunications legislation and regulation, with the aim of:

(a) identifying whether the requirement is still relevant; and

(b) if so, identifying whether:

   (i) the information could be made available to customers in an alternate format (e.g. online, or upon request);

   (ii) a sunset clause should be added, containing an end date for when this obligation will expire; and

   (iii) it is an issue particular to the telecommunications industry, and therefore requires the telecommunications supplier to provide it to their customers, or whether it is a broader issue that applies to consumers across all industries and is therefore best dealt with via national consumer legislation (for example).

## 7. Standard Form of Agreement & other consumer contracts

7.1 Optus is pleased to hear the recent announcements about the development of a national consumer law. This may well obviate the need for the Commission to consider the issue of contractual obligations within the telecommunications industry, however we believe that it remains relevant to discuss in this submission as an example of the rules under which we have operated for the past decade.

7.2 Telecommunications providers are afforded the right to contract with their customers on a general, non-individual basis via Part 23 of the *Telecommunications Act 1997* and the *Telecommunications (Standard Form of Agreement Information) Determination 2003*, which set out the rules with which any Standard Forms of Agreement must comply.

7.3 In addition, our contracts are subject to:

(a) the overarching rules in the *Trade Practices Act 1974*;

(b) the rules in the Consumer Contracts chapter of the *Telecommunications Consumer Protections Code*;

(c) the rules in the Customer Information on Prices, Terms and Conditions chapter of the *Telecommunications Consumer Protections Code*; and

(d) the varying requirements in each State and Territory's fair trading and unfair contracts laws.

7.4 Optus is a national telecommunications provider, offering fixed and wireless landline telephony, mobile telephony, internet, satellite and subscription television products across the residential, small business and corporate and government markets. As we operate in each Australian State and Territory, we must ensure that our customer contracts meet the requirements imposed in no less than nine different pieces of legislation and regulation. This is a ridiculous situation and untenable without huge costs to the organisation for legal advice to ensure all contracts comply.

7.5 We are pleased there is to be a national consumer law developed, and trust that contractual obligations and unfair terms legislation will form part of this.

## 8. Universal Service Obligation

8.1 The Universal Service Obligation (USO) framework set out in the Telecommunications (Consumer Protection and Service Standards) Act 1999 is funded through an industry levy on telecommunications operators' 'eligible revenue", which is essentially revenues less inter-carrier payments.

8.2 Optus submits that the Commission should consider funding the USO from general taxation. This would have strong public policy merit. In terms of the impact on efficiency, administration costs, equity considerations and transparency, funding the USO from general taxation is likely to be superior to an industry fund. For example, well-established taxation theory finds that the welfare loss of raising a given amount of revenue is substantially reduced by collecting that revenue over as wide a base as possible. The deadweight cost of general taxation is generally estimated to be in the range of 10% to 30% of the amount collected, while an empirical estimate of the deadweight cost of industry levies suggest that they may be three times or more as costly.

8.3 Even if this submission is not accepted, Optus submits that the Commission should recommend abolition of the industry fund, which is burdensome for smaller operators. It is inappropriate for Telstra to be subsidised by its rivals, given the significant advantages enjoyed by Telstra as the incumbent and the negative impact on competition resulting from the industry subsidy.

8.4 Arguments have been espoused in the past that USO compensation to Telstra is justified on the grounds of competitive neutrality. The main flaw in this argument, however, is that it ignores the fact that Telstra experiences significant cost advantages from being both the historical monopoly operator and therefore beneficiary of the wide range of structural advantages, primarily economies of scale. These factors provide Telstra with a clear competitive advantage over the rest of the market. Seen in this light, any claims that being the universal service provider (USP) diminishes Telstra's ability to compete appear unconvincing. Further, whilst Telstra acquires intangible benefits from being the USP, competing carriers who are required to contribute to its upkeep get nothing in return. Optus submits that competitive neutrality does not justify levying fees on the remainder of the industry given Telstra's continued dominance and profitability, and it would be appropriate for Telstra to self-fund its USO responsibilities.

8.5 Optus submits that – contrary to Telstra's typical position – the USO does not impose any cost burden on Telstra.[57] These points are discussed in Optus' submission to the Government's 2007 review of the USO regime (attached).

[57] In particular, Telstra as the USP does not incur losses or net costs in serving existing connections in rural and remote areas – and so should not be subsidised for doing so – since:

- existing methods for calculating the cost of the USO are flawed and result in significantly inflated cost estimates;
- a significant proportion of the "costs" Telstra typically claims in respect of existing connections are not in reality costs faced by Telstra at all – the cost of serving existing connections should be estimated on the basis of ongoing operations and maintenance expenditure only;
- Telstra's typical analysis is incomplete, since it receives revenues from customers in rural areas besides retail and wholesale line rental charges – hence the cost of connections in rural and remote areas is likely to be outweighed by revenues received by Telstra (including indirect revenue and intangible benefits of universal service); and
- even if there were any net cost of providing the USO, which is unlikely, Telstra remains highly profitable and is more than capable of continuing its traditional internal cross-subsidy of rural lines.

## 9. Telecommunications Industry Information-gathering Powers

9.1 Under Part XIB s151BU of the Act, the ACCC may make record keeping rules (RKR) requiring one or more service providers to prepare reports consisting of information that is relevant to the operation of Part XIB and XIC. The ACCC made a number of RKRs including the Telecommunications Industry Regulatory Accounting Framework (RAF), infrastructure Audit RKR, Division 12 reporting, Telstra CAN RKR, Access to Telstra Exchange Facilities, Bundling RKR and Accounting separation RKR.

### Retention of information-gathering powers

9.2 Optus submits that the record-keeping rules (RKRs) and information-gathering powers set out in Part XIB of the Act should be retained, since they are essential to address the information asymmetries which characterise the telecommunications industry and reinforce the incumbent's market power.

9.3 Optus has made specific submissions to the Productivity Commission on this issue in the context of the Productivity Commission's 2000-2001 review of the Telecommunications Access Regime. Optus refers the Productivity Commission to its previous submission, which is attached to this paper.

### Information powers should apply in cases of significant market power

9.4 Whilst Optus considers that aspects of the ACCC's information-gathering powers should be retained, certain elements are clearly redundant, in particular their application to operators without significant market power.

9.5 A number of these RKRs apply to Optus including the RAF, infrastructure audit RKR and Division 12 reporting. Whilst Optus acknowledges that the rationale in introducing RKR is to create greater certainty in the ACCC's decision making process, it is equally important that the RKR should also achieve the regulatory objective of efficiency, proportionality and rationality. Optus has in the past raised concerns to the ACCC that the regulatory burden in preparing these reports outweighs the value in introducing these RKRs at the first place. In fact it is seldom clear whether the reports provided by non-Telstra carriers are actually reviewed by the ACCC. Optus' concerns on each of these RKR will be discussed below.

9.6 Optus submits that the RKR should be imposed only on carrier(s) which has/have significant market power (SMP) (in particular the incumbent) as it promotes the objective of efficiency, proportionality and rationality. Very often the regulatory burden in complying with RKR is substantial and that it places a disproportionate burden on smaller carriers as they do not have the same financial strength as the incumbent but are required to spend the same amount of resources in compliance.

9.7 Optus refers the Commission to the discussion earlier in this document in the section relating to the Part XIC access regime, in which Optus contends that regulation of operators other than the incumbent is unnecessary and unduly burdensome. Optus has made submissions to the Productivity Commission

on this issue in the context of the Productivity Commission's 2000-2001 review of the Telecommunications Access Regime. Optus refers the Productivity Commission to its previous submission, which is attached to this paper.

9.8 Information provided by carrier(s) which has/have SMP should be sufficient in allowing the regulator to understand the state of the competition in the market and thus assist it in its decision making process. The information the incumbent can provide should give a clear indication if there is sufficient competition in the market. The value of information which smaller carriers can add on to information provided by the incumbent is going to be minimal and that would be onerous for smaller carriers as they have to spend the same amount of compliance cost as the incumbent when its size and financial strength is so much smaller than the incumbent.

9.9 Optus submits that the ACCC's information-gathering powers should apply only to operators with significant market power. Application of the powers to participants other than the incumbent is unduly burdensome, costly, and is not clear that it has served public good.

**Information powers should apply in respect of a declared service**

9.10 Optus considers that aspects of the ACCC's information-gathering powers could be considered redundant, in particular their application to cases where there is no declared service.

9.11 The ACCC in 2008 proposed to make further amendment to the RAF including a proposal for new reporting requirements for international mobile roaming services – a service which is not regulated by the ACCC.

9.12 Part XIB s151BU(4) states that the ACCC can only exercise its power to issue RKR if it is relevant to Part XIC. However, if the service is not a declared service, it will not be subject to regulation i.e. the standard access obligation under Part XIC. .

9.13 Optus submits that the ACCC's information-gathering powers should apply in respect of a declared service only.

**Burdensome information-gathering regulations**

9.14 Optus considers that aspects of the ACCC's information-gathering powers could be considered burdensome. These are discussed below.

*The RAF*

9.15 The ACCC introduced the RAF in 2001 and was later amended in 2003. It captures information such as revenue and cost information for wholesale and retail services, service usage information on the number of local calls and the number of national long distance minutes. The RAF applies to Optus, Telstra and Vodafone and that the reporting carriers must lodge their reports to the ACCC twice per year including a half year report (covers the first half year of the financial year) and a full year annual report (covers the full financial year).

9.16 It is estimated that the ongoing costs for Optus to comply with the report requires approximately **CiC**

9.17 Optus submits that the government should impose further conditions before the ACCC can exercise its information-gathering power. Section 151BU of the Act states that the ACCC may exercise its information-gathering power so long as it is relevant to the operation of Part XIC. It provides the ACCC with wide information-gathering power without the need to assess the value and the compliance cost imposed on carriers.

9.18 The ACCC has in 2008 proposed to make further amendment to the RAF, including the proposal for separate reporting of the declared Mobile Terminating Access Service (MTAS), 2G and 3G service, new reporting requirements for international mobile roaming services, mobile data and proposed allocation methods for customer support, billing and bad debt expenses, etc.

9.19 Optus considers that some of the amendment is unlikely to be feasible and appears likely to cause very substantial compliance costs. It is expected that the proposed amendment would further impose a substantial burden upon Optus, estimated at **CiC**.

9.20 Further information regarding the costs and the practicality of the proposed amendment are outlined in *Optus' submission to the ACCC on the proposed amendments to the RAF RKR of November 2008* (Attachment 1).

*Infrastructure RKR*

9.21 The infrastructure RKR was introduced in December 2007 to 22 carriers. Optus is required to provide coverage maps to the ACCC on a number of access media including HFC, radio (fixed), radio (mobile) and DSL.

9.22 Optus continues to express considerable concern regarding the compliance burden the proposed infrastructure audit will impose on the telecommunication industry as well as questioning the benefit to be derived from it. It is questionable the existence of an alternative piece of infrastructure is determinative in itself the nature of competition.

This view is supported by the decision of the Australian Competition Tribunal (ACT) in the case of *Application by Chime Communications Pty Ltd*. The ACCC adopted as a rule of thumb that an exemption from regulation will be granted for an exchange that had three or more infrastructure competitors (excluding Telstra) with installed DSLAMs. The ACT rejected the approach of a rule of thumb for regulation based upon the existence of a number of infrastructure players.

9.23 The infrastructure RKR therefore only provides the ACCC with large amount of data of limited utility, yet the compliance costs imposed on carriers are substantial. To date Optus has been complying with this RKR on an ad-hoc basis only; nevertheless, excluding staff costs, additional hardware or

software licensing required, it has incurred a cost of **CiC** each year.

9.24 Should Optus 'systemise' the process, it is anticipated that it would need to create a new reporting tool to capture the information. It is estimated it will cost **CiC** to develop new and/or upgraded system to record and report this data but the ongoing cost will be reduced to **CiC**.

9.25 Optus refers the Productivity Commission to *Optus' submission in response to the ACCC on Proposed Audit of Telecommunications Infrastructure Assets of April 2007* and *December 2007.*

*Division 12 reporting*

9.26 Under s151CM, the ACCC must monitor and report each financial year to the Minister charges paid by consumers for listed carriage services and goods and services for use in connection with a listed carriage service. The ACCC had as a result imposed the Division 12 RKR on 9 carriers including Optus, Virgin, AAPT, Hutchison, Vodafone, Telstra, Primus, iiNet Limited, MCI Worldcom Australia and their Australian subsidiaries.

9.27 The Division 12 report captures the following information:

- PSTN, mobile and internet services information. E.g. Call revenue, number of calls, call minutes.
- Information relating to changes to the prices and terms and conditions of supply of the relevant services during the financial year, including details of discounts and specials that were offered;
- For the 2005/06 financial year and every third financial year thereafter, Optus is required to provide a random sample of 385 bills to its customers for 3G/WCDMA mobile services;
- For the 2006/07 financial year and every third financial year thereafter, Optus is required to provide a random sample of 385 bills to its customers for GSM service; and
- For the 2007/08 financial year and every third financial year thereafter, Optus is required to provide a random sample of 385 bills to its customers for internet services.

9.28 **CiC**

9.29 Again, the amount of resources spent on complying with this RKR is substantial. **CiC**

9.30 In summary, Optus submits that the record-keeping rules (RKRs) and other information-gathering powers set out in Part XIB of the Act should be retained, but should be applied only to operators with significant market power and should be applied only where necessary to support the ACCC's regulation of an existing declared service. Further, the information-gathering powers discussed in this section must be eliminated in respect of non-incumbent carriers, or at the very least streamlined in order to reduce undue regulatory burden.

## Appendix A: Process for a Final Price Ruling on ULLS

| 1999 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 |
|---|---|---|---|---|---|---|---|
| **Aug**<br><br>ULLS declared | **Apr**<br><br>ACCC Pricing Principles set Band 2 Price 35 | **Jan**<br><br>Telstra AU lodged – Band 2 price $40 | **Dec**<br><br>Telstra revised<br>AU – Band 2 $22 | **Aug**<br><br>ACCC draft decision to reject Telstra's AU | **Jun**<br><br>ACCC draft decision to reject Telstra $30 AU | **Feb**<br><br>Telstra commences constitutional challenge to ULLS declaration in High Court | **Jan**<br><br>ACCC final access dispute ruling – Band 2 price of $14.30 |
| | | | | | | | |
| | | **Oct**<br><br>ACCC model prices<br>Band 2 - $22 | | **Nov**<br><br>Optus lodges access dispute | **July**<br><br>ULLS declared for a further 3 years | **May**<br><br>ACT rejects Telstra appeal and supports ACCC ruling to reject $30 ULLS | **Mar**<br><br>Telstra replaces Dec 07 AU with a new AU - $30 for Band 2 |
| | | | | | | | |
| | | **Nov**<br><br>Telstra revised AU – Band 2 $22 | | **Dec**<br><br>Telstra withdraws Dec 04 AU and submits 2 new Aus for the period to Jun 08 - $30 averaged national price | **Aug**<br><br>ACCC interim determination – sets Band 2 price at $17.70 dispute with Telstra | **Dec**<br><br>Telstra lodges undertaking for Band 2 ULLS only, at $30 | **Mar**<br><br>High Court rejects Telstra challenge |
| | | | | | | | |
| | | | | | **Aug**<br><br>Telstra appeals ACCC decision to reject AU to ACT | **Dec**<br><br>Telstra informs carriers that it will charge $30 for ULLS when interim determination | **Apr**<br><br>ACCC draft pricing principles for 2009 – Band 2 $15.20 |
| | | | | | | | |
| | | | | | | | **May**<br><br>Telstra indicates it will charge $30 from 1 July |

## Appendix B: Competition Proceeding: WLR 'Price Squeeze' Conduct

9.31 Optus began a competition proceeding against Telstra based on claims that Telstra's pricing and other conduct in relation to the provision of wholesale line rental (WLR) services. In summary, Optus submits that this case study highlights the following issues:

- The weight of evidence required in competition proceeding may mean that convictions are unlikely;
- Declarations, or the threat or declaration, may not necessarily constrain pricing of the incumbent; and
- There can be a significant time lag between the filing of regulation proceeding and decisions by the regulator.

9.32 The background to the proceeding was that Telstra made a 15% increases in wholesale price increase but did not pass-through a similar increase to Telstra retail customers. Optus considered that this increase essentially created a 'price-squeeze' for wholesale customers (such as Optus) as they would be unable to make an adequate margin when they resold the product to their own retail customers.

9.33 This action was filed based upon two specific sections of Part XIC, namely:

(a) s46 - taking advantage of substantial market power for a proscribed purpose; and

(b) s51AJ - taking advantage of substantial power in a telecommunications market with the effect or likely effect of substantially lessening competition.

9.34 An essential element of Optus' claim was that Telstra has a 'substantial degree of power in a market' and that Telstra was not materially constrained by regulation. At the time the WLR was not a Declared service, but the service was Declared whilst the dispute was in progress and hence the question became "what was the extent to which declaration of the wholesale line rental service improved the ability of Telstra's wholesale customers – such as Optus – to constrain Telstra".

9.35 Importantly, in the period prior to declaration of the WLR service, Telstra claimed that it was constrained by the 'threat' of declaration. The key to that claim was the extent to which Telstra could show that it actually 'felt' constrained by the threat that its wholesale customers might be able to seek arbitration of term of access. That is, unless Telstra could show that its pricing decisions in relation to the wholesale supply of line rental to Optus and retail supply of line rental to end-users have been modified or controlled in some way by a perceived threat of declaration, there would be little merit in Telstra's purely theoretical claim.

9.36 However, a significant problem for Optus was that unless it could see 'decision' documents from Telstra, any discriminatory evidence would be difficult to prove. This was despite prima facie evidence showing that threat

of declaration did not constrain Telstra as it made a 15% wholesale price increase that was sustained for a significant period of time.

9.37 As a result of these complications with evidence the case was settled without further hearing. However, the issues that arose from the case are important in the consideration of the effectiveness of the current regulations.

9.38 Firstly, given the type of evidence that is required to prove ‘discriminatory’ type actions it is difficult for claimants (and the regulator) to pursue strong cases. In the same way it is therefore relatively easy for defendants to delay discovery and therefore create delay costs for claimants such as legal fees and costs relating to uncertainty in the market.

9.39 Secondly, Optus highlights that even the 'threat' of regulation, supposedly an action that would be viewed as a restrictive force, may have created an additional incentive for Telstra to use its market power. The ACCC's Local Services Review Discussion Paper in April 2005 discussed the possibility of declaration of a wholesale line rental service, and the then 'threat' of declaration may have led to a perverse incentive for a period. For example, if Telstra believed that declaration was reasonably likely it may have had a greater incentive to benefit from higher prices while it could. In other words, if Telstra believed that declaration was likely then it may have wanted to secure any benefit of higher charges, even if transitory. Furthermore, the fact that declaration had no immediate effect to 'constrain' Telstra was evidenced by the observation that the conduct complained of by Optus continued unchanged.

9.40 Thirdly, a key issue highlight by this case is the time taken for a decision to be reached. The progress from lodgement of an access dispute to final determination by the ACCC is often quite slow. For example, Optus notified an access dispute in respect of ULLS on 22 September 2005 and understand that an interim determination was not made until October 2006. Similarly, it took well over a year for the ACCC to make a final determination.

## Appendix C: *Telecommunications Performance Monitoring Report (No.63)*

9.41 *Please see attached.*