TELSTRA CORPORATION LIMITED

Response to the Submissions of other Interested Parties on the Commission's Discussion Paper on the Review of the declaration of the Domestic Mobile Terminating Access Service

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CONTENTS

IT'S HOW WE CONNECT

01 EXECUTIVE SUMMARY

1. Telstra is pleased to provide this supplementary submission to the Australian Competition and Consumer Commission (**the Commission**) for consideration as part of its Mobile Terminating Access Service (**MTAS**) re-declaration inquiry process. The purpose of this submission is to address some of the key issues raised by other interested parties in their responses to the Commission's *Review of the declaration of the Domestic Mobile Terminating Access Service Discussion Paper* (**Discussion Paper**), where Telstra believes that those responses contain factual inaccuracies and/or are potentially misleading.

2. Before responding to some of the issues raised by other parties in their responses, Telstra reiterates the view articulated in its original submission to this Inquiry that the MTAS declaration should be continued and that this would be in the Long Term Interest of End Users (LTIE). Telstra believes that consumers in Australia are benefiting from a thriving and dynamic mobiles market, with continuing high levels of investment and improvements in the customer experience. This environment and the benefits that have accrued to consumers, Telstra believes that the Commission should consider very carefully before making any changes to current regulatory settings given the success of the retail mobiles market.

3. The issues that Telstra is responding to are set out below:

    - Section 2 addresses the arguments around the declaration of SMS termination. Telstra strongly believes that there is no need to declare SMS termination in Australia. Telstra believes that the facts that have been presented to support SMS termination declaration are misleading and in particular:

        - There is no evidence to suggest that there is a failure in the retail market. Consumers have benefited – and continue to benefit – from thriving competition in the market for mobile services. Customers buy their mobile services as a bundle and SMS is an integral part of that bundle. SMS usage continues to grow and while that growth may be slowing, in and of itself, this is not indicative of a need for regulatory intervention.

        - Furthermore, the increasing prevalence of alternatives to SMS means that SMS termination should not be regarded as a bottleneck. Customers with smartphones have a choice of messaging applications and even if this is impacting upon the rate of growth of SMS that should not be regarded as a problem rather, that is simply market forces at work. Regulatory intervention, therefore, has the potential to distort what is currently a well functioning market.

        - Unlike in the small number of other countries where SMS termination has been regulated, SMS traffic in Australia is relatively balanced between the Mobile Network Operators (**MNOs**). Customers have a wide choice of mobile plans and many of those plans do not differentiate between on-net and off-net SMSs. This contrasts with the market in New Zealand, for example, prior to the regulation of the MTAS and SMS, where the differential on-net and off-net pricing (and the relative high proportion of on-net versus off-net traffic of the two major mobile network operators) was contributing to structural problems in the retail mobiles market.

- As a further consequence of SMS traffic being relatively balanced between the MNOs, the net effect of any changes in the price of SMS termination would be very small. It is therefore questionable whether the regulation of SMS termination would be in the LTIE because in the case where there would be likely to be little benefit flowing to customers from a change in price, it could be that the costs of regulation would actually outweigh the benefits.

- Given the above, it would be preferable to leave the MNOs to commercially negotiate SMS termination pricing, a process that has worked successfully for the past decade. ***C-i-C*** [redacted]. ***C-i-C***

- Section 3 addresses the arguments put forward that the MTAS service description should be changed. Telstra disagrees with these arguments and strongly believes that maintaining the MTAS service description in its current form is in the LTIE. At least one of the proposed changes to the service description – which would have the effect of allowing access seekers to request the handover of mobile calls at any Point of Interconnection (POI) outside of the five capital cities – would have flow on impacts to the MTAS price as the MNOs would incur additional costs in the carriage of calls to the gateways associated with the Mobile Switching Centres (MSCs) in the capital cities. Telstra strongly recommends that the Commission carefully consider the potential impacts of any changes to the current service description.

- Section 4 addresses the claims around pass-through of reductions in the MTAS to the price of Fixed to Mobile (**FTM**) calls. Whilst not relevant to the issue of whether or not the MTAS declaration should continue – which is the subject of the current inquiry – Telstra strongly believes that it has more than passed through the reductions in the MTAS to customers. Telstra has calculated and the Commission's own figures confirm that its FTM yield has fallen by 10.4c since June 2004, yet over the same period the effective MTAS rate has fallen by only 7.5c. Therefore Australian consumers have clearly benefited from price competition in fixed services and the reductions in the MTAS.

02 There are no economic problems in SMS markets that require regulation

4. Interested parties have put forward that the Commission should consider declaration of SMS services. In particular Optus has suggested in its 5 July submission that the retail SMS market has significantly changed in recent years and that the case for declaration of the wholesale SMS market should be considered because: market growth has slowed; MNOs are exercising market power over SMS termination; and termination rates are in excess of cost based levels and significantly above the MTAS rate.

5. Telstra disagrees with each of these points. As discussed in its 5 July submission, Telstra considers that there is no cause to declare or include the SMS service in the MTAS service description, as there is no market failure in the provision of the SMS services in either the upstream or downstream markets, nor are bottleneck characteristics evident in relation to the provision of SMS.

6. This is particularly evident when the reasons given by regulators for setting SMS termination rates globally are surveyed and compared to Australia.

7. The main economic issues of concern raised by regulators that have led to the decision in a small number of countries to regulate SMS termination [1] include:

    a. traffic imbalances;

    b. retail pricing differentials particularly between “on-net” and “off-net” traffic; and,

    c. Commercial negotiations consistently failed.

8. Using the evidence presented in the below sections, it is clear that the Australian SMS market does not display any of the economic issues raised by global regulators as a justification for regulation of SMS termination. To the contrary, the market continues to grow, prices decline, quality improve, choice increase with numerous substitutes and large technological change, with the development of such products as ‘iMessage’, ‘Skype’, ‘Viber’ and ‘WhatsApp’, plus social media channels through which to communicate including, ‘Snapchat’, ‘Vine’, ‘Facebook’, ‘Line’, ‘Twitter’, ‘Meebo’, ‘Seesmic’, etc.

9. With such a highly evolving SMS market, if the Commission did choose at this time to set SMS termination rates, the risk and cost of regulatory error may be significant.

10. The risk of error would be high as a changing market (technology and demand) makes the correct assessment of efficient cost and demand difficult; increasing the probability of setting SMS termination rates incorrectly. At the same time, the costs of errors are likely to be greater at this time relative to when the market matures, as they will likely be influential on the rate and pattern of innovation (current or planned) directly through getting prices wrong and by adding regulatory risk to investment decisions. Reduced or distorted investment is likely to have pricing and technology impacts on retail markets, which will not be in the LTIE.

11. Each of the three broad categories is discussed below.

2.1. SMS traffic volumes are balanced

[1] A survey of 55 finds that only a small number (9 countries) have set regulated rates for SMS termination; see Appendix 1.

12. The volume of SMS traffic terminating on Telstra's network from MNO's is approximately balanced to the volume of traffic that Telstra terminates on other MNO's networks. The below figure illustrates the volume of SMS traffic since financial year 2010-11.

C-i-C

[redacted]

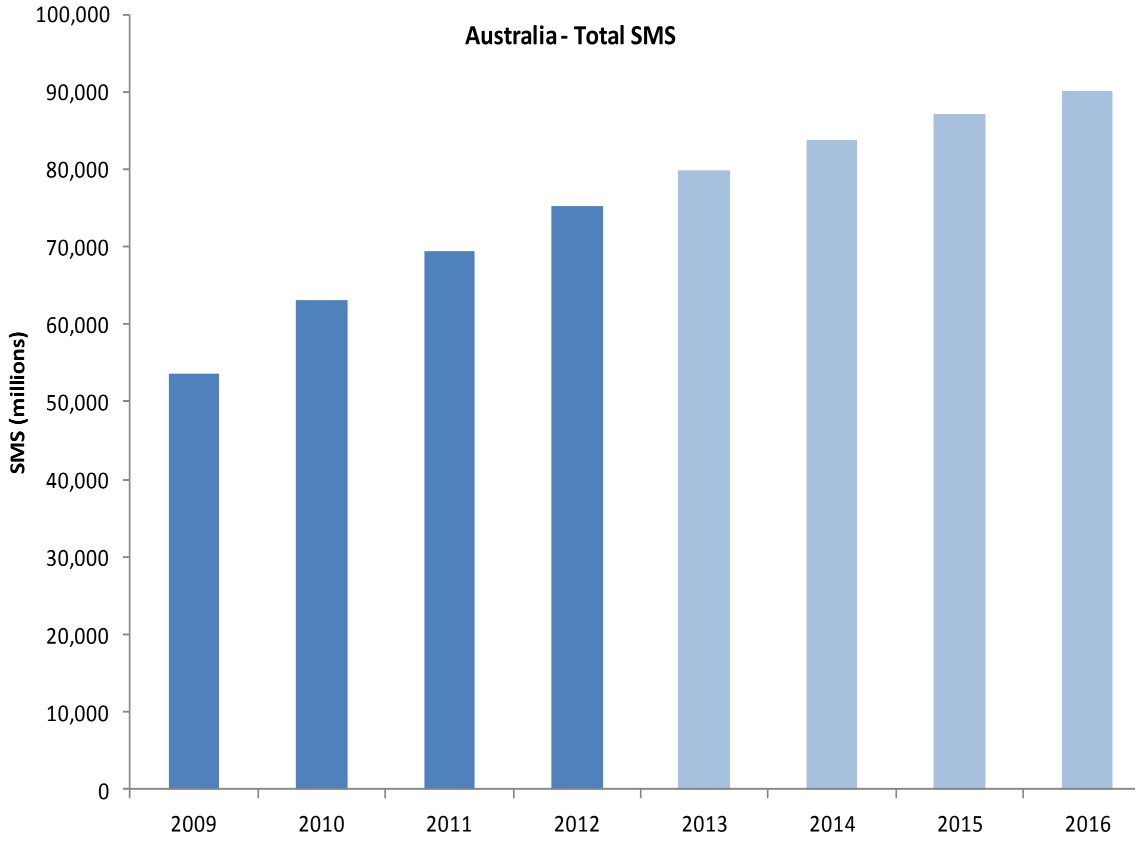
C-i-C

13. The historic and forecast volumes show that this balanced traffic has a historical consistency and is predicted to continue going forward, irrespective of any differences in the market shares of MNO's currently or in the recent-past.

14. Therefore, the issues cited globally for regulation of SMS termination: low cross-network traffic; and high concentration of market share or a dominant retail market player (for example 67+% market share) are clearly not relevant or evident within the Australian SMS market. More specifically, any structural issues that may have been present in other global jurisdictions i.e. large pricing differentials between on-net, off-net and pre-paid are simply not evident in the Australian market (see section 2.2).

15. As a further consequence of SMS traffic being relatively balanced between the MNOs, the net effect of any changes in the price of SMS termination would be very small. It is therefore questionable whether the regulation of SMS termination would be in the LTIE because in the case where there would be likely to be little benefit flowing to customers from a change in price, it could be that the costs of regulation would actually outweigh the benefits.

16. In addition to the balanced SMS traffic, it is important to note that the SMS market is still continuing to grow strongly and is forecast to continue growing as evidenced in the below figure.



Source: Ovum, Mobile Messaging Traffic and Revenues Forecast: 2011-16, 29 March 2012

17. What is important to note about the above figure is that not only are consumers continuing to send SMS' at present, but the amount of SMS' sent is projected to grow beyond 2016. This trend highlights that the current commercially negotiated SMS interconnection rates are both appropriate and working. In Telstra's perspective and in light of the above evidence, setting SMS termination rates in such a market is unnecessary, and is not in the LTIE.

2.2. No retail pricing differentials exist

18. Telstra has conducted a desktop survey of advertised pre-paid and post-paid mobile plans for consumer and business customers that are currently available in the retail market. Overall the survey shows that the majority of advertised mobile plans have no SMS pricing differentials between:

    a. On-net versus off-net; or,

    b. Pre-paid versus post-paid.

19. As such these two potential structural issues, cited globally as reasons to consider whether to regulate SMS termination, are neither present nor relevant within the Australian SMS market. In fact the desktop survey of mobile plans of MNO's Optus[2], Telstra[3] and Vodafone Hutchison

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[2] See https://smb.optus.com.au/opfiles/Shop/All/cis/Cis%20Documents/1390049_CIS_Optus_Prepaid_Social_0113.pdf https://smb.optus.com.au/opfiles/Shop/All/cis/Cis%20Documents/1390049_CIS_Optus_Prepaid_Social_0113.pdf

Australia (VHA)[4] illustrates not only that there are no retail pricing differentials, but also that the value per unit of consumption for SMS (and voice, MMS and data) has increased in recent years substantially.

20. All MNOs provide post-paid mobile pricing in 'bucket plans'. Within post-paid bucket plans, SMS is available to the consumer on an 'unlimited' basis, meaning that the notional average retail price per SMS decreases with each SMS sent, highlighting the strong retail demand for SMS.

21. Pre-paid plans, for all MNOs surveyed, advertise an allotted value for SMS. These plans are structured to provide the greatest value to customers in parts (voice, SMS, MMS or data) of each plan that are valued the most. Customers that value SMS more than voice calls, data or MMS can choose a pre-paid plan that has a low or lower SMS price per message.

    The above analysis shows that the retail market in Australia is not impacted or constrained by the existence of commercially agreed SMS interconnection rates. On the contrary it shows that markets are flourishing and clearly serving the LTIE in the presence of current regulatory forbearance. This contrasts in particular with the market in New Zealand, for example, prior to the regulation of the MTAS and SMS, where the differential on-net and off-net pricing (and the relative high proportion of on-net versus off-net traffic of the two major mobile network operators) was considered likely to be contributing to structural problems in the retail mobiles market.

2.3. Commercial negotiations have not failed

22. ***C-i-C*** [redacted]. ***C-i-C***

23. Given all of preceding analysis, it would be preferable to leave the MNOs to commercially negotiate SMS termination pricing, a process that has worked successfully for the past decade, without the need for regulatory intervention.

03 Changing the MTAS service description will not achieve any improvements for retail customers

24. Telstra notes that a number of other parties suggested that the MTAS service description needs to be changed.[5] Telstra disagrees with those views and maintains the view set out in its July submission that the existing service description is already technology neutral and will remain appropriate for the foreseeable future. Importantly, at present there are no plans to change the current interconnection arrangements for voice calls away from the well understood and robust CCS7 standard to any, as yet undeveloped, IP-based interworking standards. Therefore, changing the service description at this stage would be premature and is unnecessary.

https://smb.optus.com.au/opfiles/Shop/All/cis/Cis%20Documents/1390391_CIS_Optus_Crew_Cap_Recharge_Options_0113.pdf
https://smb.optus.com.au/opfiles/Shop/All/cis/Cis%20Documents/1390392_CIS_Optus_Long_Expiry_Cap_Recharge_Options_0113.pdf
https://smb.optus.com.au/opfiles/Shop/All/cis/Cis%20Documents/1390053_CIS_Optus_Connect_4_Less_0113.pdf
https://www.optus.com.au/shop/mobilephones/SimBYO
https://www.optusbusiness.com.au/shop/mobilephones/SimBYO

3 See for example http://www.telstra.com.au/mobile-phones/plans-rates/every-day-connect-plans/#tab-plan-60; http://www.telstra.com.au/help/download/document/personal-critical-information-summary-tpp-mobile-summary.pdf; http://www.telstra.com.au/business-enterprise/business-products/mobiles/mobile-plans/business-performance/index.htm

4 See http://www.vodafone.com.au/personal/sim-cards/sim-cards/sim-only-plans; http://www.vodafone.com.au/personal/plans/pricingplans; http://www.vodafone.com.au/business/products-and-services/business-plans/single; and, http://www.vodafone.com.au/personal/criticalinformationsummary?planCategory=Prepaid

5 See for example, AAPT, Macquarie etc.

25. With respect to the specific amendment to the service description that was proposed by AAPT6, Telstra believes that this amendment would not be in the LTIE. The proposed amendment (which also appears to be supported by Macquarie Telecom7) is to delete part (b) of the definition of the Point of Interconnection (POI):

> *"b) is associated with (but not necessarily co-located with) one or more gateway exchanges of the access seeker's network and the access provider's digital mobile network."*

26. However, the current MTAS service description – and by definition the MTAS price in the FAD – relies upon the handover of calls to the access provider's mobile network at a gateway exchange established at a point associated with (and typically co-located with) the Access Provider's Mobile Switching Centres (MSCs). This is a long established handover principle to facilitate the efficient interconnection of calls to and from mobile networks and the MTAS pricing is based on these accepted arrangements. If this principle is broken, then an access seeker could handover MTAS calls at any POI and the mobile access provider would incur additional costs in the carriage of these calls to the gateways associated with Telstra's MSCs in each of the 5 mainland capital cities. Those additional costs would need to be included in the MTAS price and Telstra considers that this would not be in the LTIE.

04 Consumers are the winners of fixed-to-mobile pass-through

27. Telstra notes that three[8] parties raised the issue of the pass-through of reductions in the MTAS to the price of fixed to mobile (**FTM**) calls.[9] Some of the other parties' submissions purported to show that Telstra has had a windfall gain from the reduction in the MTAS rate from 21 cents per minute down to the current level of 4.8 cents per minute, by not passing through that reduction to the price of FTM calls. Such claims are erroneous and misleading.

28. Telstra considers that the question of FTM pass-through is irrelevant to the issues that are currently under consideration; that is, whether or not the MTAS should continue to be declared and if so, whether that declaration should be varied. For the avoidance of doubt – and as noted by Telstra in this submission and in its July submission – Telstra believes that customers have benefited (and continue to benefit) from the regulation of the MTAS and that regulation should continue.

29. Telstra's analysis of the same, publicly available information as that used by other parties shows that from June 2004 to March 2013, Telstra's FTM yield has fallen by 10.4 cents per minute. Over the same time period, the effective MTAS rate paid by Telstra[10] has reduced by only 7.5 cents per minute.[11] In other words, Telstra has <u>more than</u> passed through the reductions in the MTAS rate to FTM pricing.

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6 AAPT, *Submission by AAPT Limited to Australian Competition and Consumer Commission, Review of the declaration of the Domestic Mobile Terminating Access Service Discussion Paper*, July 2013, p6

7 Macquarie Telecom, p16.

8 ACCAN, Optus and VHA.

9 See for example, VHA, *Declaration of the Domestic Mobile Terminating Access Service: Response to the* Australian Competition and Consumer Commission, 5 July 2013; ACCAN, Review of the Declaration of the Mobile Terminating Access Service, Submission by the Australian Communications Consumer Action Network to the Australian Competition and Consumer Commission, July 2013; and Optus, Submission in response to ACCC Discussion Paper: Review of the declaration of the domestic mobile terminating access service (MTAS), July 2013.

10 Of all the FTM minutes Telstra's fixed telephony customers consume, only a proportion of these are off-net and therefore trigger MTAS payments. As such if MTAS prices fall by one cent per minute, the cost saving for each FTM minute is proportionately less than one cent.

11 The effective MTAS rate is calculated by multiplying the prevailing MTAS headline rate by the proportion of off-net FTM calls.

30. Consumers have clearly benefited from this pass-through of the reduction in the MTAS rate.

31. Telstra further notes that the Commission itself has commented that FTM prices have fallen significantly. In its 2011-12 Annual Telecommunications Report, the Commission commented that *"Figure 4.5 shows price falls across every PSTN service components for residential consumers since 2007−08. Price reductions for international calls and fixed−to−mobile calls are particularly notable over the past three years, falling by over 10 per cent each year."*[12] The Commission's analysis is based on data from across the Australian telecommunications industry (i.e. it is not solely focussed upon Telstra), but as the other parties themselves argued in their submissions, Telstra remains the largest carrier in the fixed line market.[13] As such, the reductions in the FTM prices that the Commission has observed reflect reductions in the FTM prices of Telstra.

32. Further, VHA incorrectly reports that Telstra revenue is 280% of the cost of providing FTM calls.[14] This is incorrect as the figure for cost used by VHA comprises only network costs and not any of the other costs of supplying FTM calls, for example, product, market, sales and customer support.

33. Telstra reiterates that Australian consumers have benefited significantly, including over the long term, from the pass-through of reductions in the MTAS to the price of FTM calls and the Commission should disregard the false arguments presented by some other parties to the contrary. In addition, such arguments are not relevant to the Commission's considerations in the current re-declaration inquiry.

[12] ACCC, p81.
[13] See for example, Optus p17 and AAPT p3.
[14] VHA, 5 July 2013, p7.

APPENDIX 1: Global Regulation of SMS Termination

Country	SMS termination	Source
Bahrain	Regulated	Ovum. See also http://www.tra.org.bh/en/pdf/FinalPositionPaper_onMTRsPublic.pdf
Colombia	Regulated	Ovum. See also http://www.telegeography.com/products/commsupdate/articles/2011/10/04/crc-to-drop-interconnection-rates/
Denmark	Regulated	Ovum. See also http://www.t-regs.com/index.php/2010/07/28/2010-summer-of-sms-regulation-frdkpl-and-ec-already-considering-the-sunset-2/
France	Regulated	Ovum. See also http://www.arcep.fr/index.php?id=8571&L=1&tx_gsactualite_pi1%5Buid%5D=866&tx_gsactualite_pi1%5BbackID%5D=26&cHash=d22d6ab92d http://www.t-regs.com/index.php/2010/07/28/2010-summer-of-sms-regulation-frdkpl-and-ec-already-considering-the-sunset-2/
India	Regulated	Ovum. See also http://gadgets.ndtv.com/telecom/news/trai-recommends-levy-of-sms-termination-charge-to-curb-spam-messages-371896
Israel	Regulated	Ovum. See also http://www.moc.gov.il/new/documents/about/analisis_10.2.05.pdf http://www.telegeography.com/products/commsupdate/articles/2010/11/18/cellcom-set-to-raise-mobile-tariffs-in-response-to-lower-interconnect-fees/
Kenya	Regulated	Ovum
New Zealand	Regulated	Ovum
Oman	Regulated	Ovum
Pakistan	Regulated	Ovum
Poland	Regulated	Ovum
Argentina	Not regulated	Ovum
Australia	Not regulated	Ovum
Austria	Not regulated	Ovum
Belgium	Not regulated	Ovum
Brazil	Not regulated	Ovum
Bulgaria	Not regulated	Ovum
Chile	Not regulated	Ovum
Cyprus	Not regulated	Ovum
Czech Republic	Not regulated	Ovum
Egypt	Not regulated	Ovum
Estonia	Not regulated	Ovum
Finland	Not regulated	Ovum
Germany	Not regulated	Ovum
Greece	Not regulated	Ovum
Hong Kong	Not regulated	Ovum
Hungary	Not regulated	Ovum
Indonesia	Not regulated	Ovum
Ireland	Not regulated	Ovum
Italy	Not regulated	Ovum
Japan	Not regulated	Ovum
Jordan	Not regulated	Ovum
Latvia	Not regulated	Ovum
Lithuania	Not regulated	Ovum
Luxembourg	Not regulated	Ovum
Malaysia	Not regulated	Ovum
Malta	Not regulated	Ovum
Mexico	Not regulated	Ovum
Netherlands	Not regulated	Ovum
Norway	Not regulated	Ovum
Peru	Not regulated	Ovum
Portugal	Not regulated	Ovum
Romania	Not regulated	Ovum
Saudi Arabia	Not regulated	Ovum
Singapore	Not regulated	Ovum
Slovakia	Not regulated	Ovum
Slovenia	Not regulated	Ovum
South Africa	Not regulated	Ovum
South Korea	Not regulated	Ovum
Spain	Not regulated	Ovum
Sweden	Not regulated	Ovum
Switzerland	Not regulated	Ovum
Taiwan	Not regulated	Ovum
Turkey	Not regulated	Ovum
UK	Not regulated	Ovum