Australian Competition & Consumer Commission (ACCC) Discussion Paper – Mobile Services Review 2003

Submission by PowerTel Limited

Introduction

PowerTel welcomes the opportunity to provide comments on the “Mobile Services Review” discussion paper 2003 issued by the ACCC.

PowerTel supports the review and in this submission will emphasise in particular the declared mobile termination service, which is most critical for a sustainable, competitive telephony market.

Fixed network providers, like PowerTel are captured by the ‘Bottleneck’ nature of termination. The consequences of monopoly facility providers without effective regulation are well documented and their effect identified readily in the Australian marketplace. Corrective action is needed.

Fixed line service providers who are not vertically integrated are not able to avail themselves of monopoly rents on mobile termination. Those that are vertically integrated can after collecting these monopoly rents, use them to cross subsidise into competitive and substitutable products (wireline services, with cost-based regulated access pricing). Those bottleneck owners who are not vertically integrated reap even higher rewards because they have no need to pass on this profit to competitive products.

These monopoly rents have enabled Vodafone and Telstra to become the 1st and 11th most valuable telecom operators in the world[1].

With the regulatory controls in place since 1997 the ability of the mobile network providers to extract bottleneck, monopoly rents from all others has not been interrupted, and at the same time created a misallocation of economic resources, transferring value from fixed line services to mobile network owners.

PowerTel believes the Commission has complicated the issue by asking the question on the need to regulate the service in the first instance. The fervent interest shown by particular mobile carriers in arguing the case for ‘no regulation’, combined with the bottleneck characteristics displayed in the mobile access market, actually highlights the absolute need for continued and more appropriate regulatory control.

1.1 Domestic GSM and CDMA Terminating Access Service

Continuing the declaration

PowerTel believes that the domestic GSM and CDMA terminating access service should remain a declared service and that the supply of the service must be regulated as a cost-based service to interconnecting carriers.

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[1] Findings of *Telecom Week Global 25,Telecom Week,* 13-19 June 2003

To satisfy the long term interest of end-users (LTIE), the Commission must conclude that a cost-based approach such as total service long-run incremental cost (TSLRIC) is the appropriate pricing methodology.

To suggest forbearance (no regulation) or continuance of the current retail benchmarking approach denies the unfair advantage that the mobile carriers hold over a bottleneck facility and further denies the anti-competitive pricing that exists in the market today.

"Retail benchmarking approach"

The retail benchmarking approach, ie the glide path model, has not delivered a desirable outcome, nor has it provided the tool anticipated by the ACCC in the form of cogent data to allow the Commission to assess the status of ongoing competitive behavior by the mobile carriers.

The adoption of the retail benchmarking approach is inconsistent with the Commission's view on the appropriate pricing principles for the Originating and Terminating Public Switch Telephone Network (PSTN) Access Services and the access price for the Unbundled Local Loop Service (ULLS). PowerTel has continued to reiterate the need for a cost-based pricing model, which reduces the opportunities for anti-competitive pricing and improves allocative efficiency. PowerTel has repeatedly raised its concerns to the Commission regarding the problems in adopting this model in particular the opportunity for artificial distortions of the retail price movements.

The Chairman of the ACCC, Professor Allan Fels admitted the Commission "implemented a novel benchmarking approach for determining mobile termination prices"[2] during his address on "Competition in Telecommunications" at the Australian Telecommunications Users Group (ATUG) annual conference in Sydney. Subsequently, the ACCC has conceded[3]:

> *"The results of this monitoring to date are concerning in that the carriers are reporting large increases in the retail price of mobile telephony service. That said, close examination of the data provided by carriers has led to the Commission to hold concerns about the data provided to the Commission by carriers and the application of the appropriate methodology."*

PowerTel notes that the ACCC discussion paper[4] indicates that the UK regulator Oftel does not endorse the Australian retail benchmarking pricing principle.

A lack of valid data available to the industry in general and the uncertainty on the basis of a decision in case of an arbitration on access pricing has stopped progress towards 'fair' access pricing to mobile networks since the decision to adopt the retail benchmarking approach.

Pricing Methodology

In order to promote competition, and encourage efficient investment in infrastructure, the Commission adopted a TLSRIC cost-model for the Originating and Terminating PSTN Access Services and the access price for the ULLS.

With some argument this methodology has proven effective and has helped in developing a competitive, sustainable market in wireline services. This success indicates a conclusion that in the LTIE the pricing

[2] Professor Allan Fels address to ATUG on "Competition in Telecommunications", Sydney, 6 March 2003.
[3] See ACCC, *Mobile Services Review 2003 – a Discussion paper,* April 2003, p.33.
[4] See ACCC, *Mobile Services Review 2003 – a Discussion paper,* April 2003, p.49.

methodology for GSM and CDMA Originating and Terminating Access Service should also be cost-based.

PowerTel agrees with the Commission[5] that a cost-based approach would be a better benchmark and would provide limited opportunities for anti-competitive behaviour by integrated carriers.

PowerTel believes the Commission's previous conclusion that the cost of implementing such a pricing methodology outweighed its benefits was not correct. Indeed PowerTel strongly suggests that the modernity of structure, the elemental simplicity (ie less elements in the mobile network compared with the PSTN) and far more generic nature of mobile networks would allow a more simple model to be developed compared to the multi faceted technologies and sometimes dated PSTN infrastructure.

Cost of providing mobile termination services

PowerTel estimates that the true cost for mobile termination is in the region of 5-6cpm. As outlined in a previous letter[6] to the Commission, under normal market conditions (and where there is no difference in interconnect pricing between mobile carriers) the net settlement between mobile carriers is zero. For a mobile-to-mobile call, the cost to each mobile carrier is its internal cost for termination, which is significantly less than what is offered to carriers on a wholesale/interconnect basis.

PowerTel believes that an analysis of retail mobile-to-mobile pricing provides an accurate estimate of the true cost of mobile termination. This negates the need to depend on data supplied by the mobile network operators.

PowerTel has in the past drawn the Commission's attention to such retail pricing[7] (detailed below):

Carrier	Retail mobile-to-mobile charge (per minute)	Retail POI-to-mobile charge (per minute)
Telstra	16.13c	8.06c
Optus[8]	21.64c	10.82c

Table 1-1: Retail mobile-to-mobile "On-net" pricing

The above figures highlight that a retail mobile-to-mobile call is charged at approximately 16c (by Telstra). A mobile-to-mobile call consists of mobile origination and mobile termination. Therefore retail mobile termination is charged at approximately 8c (50% of a mobile-to-mobile call). This analysis is consistent with PowerTel's estimates that the true cost (ie the appropriate wholesale cost) for mobile termination is in the region of 5-6cpm.

PowerTel's analysis[9] indicates there is significant differential pricing for mobile-to-mobile "on-net" calls compared with "off-net" calls. This is a strong indication of the differential between costs and pricing

[5] See ACCC, *Mobile Services Review 2003 – a Discussion paper,* April 2003, p.50.
[6] PowerTel letter to ACCC, 20 March 2002
[7] PowerTel letter to ACCC, 24 August 2000, figures were derived from the retail prices offered to customers, including flagfall, GST and assuming a period split of 60% Peak:40% Off-Peak and bonus plan features. Calls were averaged over a five minute period.
[8] At the time of the analysis, Optus was under the control of Cable & Wireless
[9] PowerTel letter to ACCC, 24 August 2000

extracted from monopoly rents and necessitates a close review of the reason for the discrepancy in originating and terminating pricing.

It is imperative that the Commission release indicative pricing for GSM and CDMA Originating and Terminating Access Services at the conclusion of the review until such time a TSLRIC model or other appropriate cost-based model is developed. PowerTel suggests the Commission should consider the use of Regulatory Accounting Framework (RAF or other) data to calculate interim prices, or follow the approach taken by regulators abroad like the UK regulator Oftel that proposed a reduction of inflation minus 13 percent. The Competition Commission increased this figure to inflation minus 15 percent from July 2003.

Market failure

Industry groups including ATUG, International Users Group (INTUG), consumers and consultants share the views of fixed network operators that the mobile operators are benefiting from monopoly rents.

Notably, INTUG reports that:

> *"There are increasing problems with the rising prices of domestic and international call termination to mobile networks. These constitute an ever growing burden on individual consumers and especially on businesses.. Thus, where APEC economies are WTO signatories they are obliged to ensure that interconnection to all mobile networks complies with their commitments, including cost oriented interconnection."*

Similarly, the ATUG supports the view maintained by PowerTel. In its submission[10] to the ACCC, ATUG reported that a recent survey completed of 30 of the Top 100 companies by market capitalisation on the ASX revealed the following:

> *"These companies do not regard mobiles as a competitive market.. They think there is too little price and product differentiation. They specifically mention fixed to mobile and international roaming charges are problem areas"*

Furthermore,

> *"Nonetheless, ATUG feels that the margin being made on termination services, in the absence of market pressure or regulatory supervision, is such that this matter needs to be addressed".*

ATUG reiterated its view on excessive GSM termination through its column in the Voice and Data Magazine[11]:

> *"The high price of domestic call termination on mobile networks has worked so well in domestic markets, without any signs of competitive pressures to drive the prices down, that it has now extended to fixed calls to international mobiles. The recent removal of mobile prices from Telstra's Price Control Determination means there is no telecommunications specific legislative regulation of mobile retail pricing"*

According to Ovum[12], mobile termination rates account for approximately 30% of most operators' revenues and that Ovum's research suggests that these rates "are perhaps twice as high as they should be". Ovum proposes to assist mobile (and vertically integrated) operators prepare for the impending

[10] Submission by ATUG to ACCC, "Comments on the ACCC Draft Report on Pricing Methodology for the GSM and CDMA Termination Services", August 2002
[11] Voice and Data Magazine, October 2002
[12] Ovum Research Alert, 31 January 2003

reduction in mobile termination revenue as regulators globally adopt a more pro-active approach towards mobile termination regulation.

Level of fixed-to-mobile pass through

To assess the flow on effect of any reductions in the price of mobile termination services through to end-users, PowerTel believes that the Commission should consider two different markets, those being, residential and corporate/business.

PowerTel supports the theory of market forces leading to access cost savings being passed through to end-users.

Corporate Market
In the current market place the distortion of bottleneck pricing and cross-subsidisation has in some instances, led to the corporate customer achieving lower access prices than interconnecting carriers. PowerTel believes that there are corporate customers offered retail fixed-to-mobile calls (ie end-to-end call) at rates 25% lower than what PowerTel is charged for wholesale mobile termination (ie Point of Interconnect (POI)-to-mobile).

Residential Market.
In the residential market, there has been little reduction in charges for mobile termination, or perhaps even price increases. This is consistent with the view of Professor Allan Fels, Chairman of the ACCC in his address[13] to the industry at the recent ATUG annual conference:

> *"Unlike the market for other fixed line services – such as national and international long distance – there has been relatively little reduction in the final prices paid by consumers in recent years for fixed-to-mobile services. Further, and perhaps relatedly, there appears to be limited competition in terms of wholesale mobile termination"*

Similar to the introduction of the Customer Service Guarantee (CSG), (aimed at residential and small business customers to provide a level of assurance regarding installation and fault restoration) there is room for some legislative support to ensure cost reduction flow-through.

PowerTel reiterates that through the adoption of a TSLRIC model for wholesale mobile termination/origination the operation of market forces will *inter alia* result in more competitive offerings, and appropriate reduction in cost to the residential customer.

1.2 Domestic GSM and CDMA Originating Access Service

The GSM and CDMA Originating Access Service is identical to the GSM and CDMA Terminating Access Service, therefore the cost for providing either is the same. The Originating and Terminating Access Service utilizes the same network elements and therefore attracts the same cost. Justification of terminating mobile calls costs in excess of originating mobile call costs is illogical.

There is signficant difference surrounding the declaration of the GSM and CDMA Terminating and Originating Access Services. Unlike the GSM termination service, which declared GSM termination irrespective of the originating carrier, the GSM Originating Access service is limited in scope and applies only to calls made to Freephone and Local Rate Numbers (FLRNs) from mobile phones, ie calls from mobile phones to 13/1300 or 1800 numbers.

[13] Professor Allan Fels address to ATUG on "Competition in Telecommunications", Sydney, 6 March 2003.

Mobile carriers offer the Originating Access Service at wholesale rates far less than Terminating Access. PowerTel reiterates that this cannot be supported as the same network elements are used as for terminating situations. Hence the mobile carriers should offer the same rates for terminating access as for originating access.

In light of the reasons outlined above, the Commission should continue the declaration for GSM and CDMA Originating Access Service.

1.3 Domestic intercarrier roaming

To avoid duplication or triplication of network infrastructure, PowerTel believes that domestic intercarrier roaming should be encouraged and the possibility of a declaration should be considered. This has the benefits of reducing industry costs (which invariably would be passed on to mobile subscribers and/or cross subsidized to fixed network customers calling mobile subscribers) and redirecting capital and operating expenditure to improving network black spots or expanding the reach of the networks.

PowerTel believes that there may be commercial reasons as to why the GSM mobile network operators have deployed separate networks. However, in the interests of efficiency and reducing industry capital expenditure, PowerTel believes the Commission should encourage the mobile carriers to share infrastructure and enter into roaming agreements.

PowerTel considers that the subject of domestic intercarrier roaming should be subject to further review and that this review be conducted immediately following the release of the final pricing methodology for the mobile terminating and originating service.

1.4 3G Mobile Services

PowerTel notes that Hutchison launched 3G Mobile Services[14] recently and considers that 3G market is still in its infancy both locally and internationally. PowerTel believes that it may be too early to attempt a definition of the range of mobile services in order to introduce an appropriate commercial interconnection. For the meantime, voice termination and origination for 3G services should most likely follow any pricing methodology for CDMA (and GSM as the declarations are technology neutral).

PowerTel suggests that for the remaining 3G services, the Commission should engage in regulatory forbearance until such time as the 3G services industry is more mature.

Summary

The ACCC discussion paper has attempted to address the many issues of concern regarding the competitiveness of the mobile services market. The difficultly with such a broad scope is that it may fail to address the fundamental issues for non-mobile service providers and the LTIE. These issues stem from the appropriate pricing principles for the GSM and CDMA Originating and Terminating Access Services.

PowerTel believes it is important for the Commission to release indicative pricing at the conclusion of this review to provide guidance to access seekers with negotiations with the mobile operators.

[14] Hutchison launched 3G services in Australia on 15 April 2003, www.three.com.au Media release

The Commission should be concerned that:

i. Anti-competitive pricing clearly exists given that resellers and corporate customers are able to purchase retail fixed-to-mobile calls less (~25%) than what is offered to PowerTel for wholesale mobile interconnection;
ii. Competition is significantly affected whilst mobile carriers are able to charge access fees that bear no resemblance to cost; and
iii. Australia is possibly in breach of World Trade Organisation commitments[15] due to excessively high mobile termination charges as tabled by INTUG.

The Commission must adopt a TSLRIC cost-based pricing methodology for the GSM and CDMA Originating and Terminating Access Services. This will be consistent with the Commission's views on PSTN and ULLS access services and will provide for a more competitive mobile services market, which will be in the LTIE.

[15] Submission by INTUG to APEC Telecom working group, 19-23 August 2002, Moskva