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Dear Ms O'Reilly

Preliminary View re declaration of SMS Termination Services – Telstra Response

I refer to your email of 23 May 2014 notifying stakeholders that the Commission has reached a preliminary view in relation to whether application-to-person (**A2P**) SMS should be excluded from the proposed declaration of SMS services. Specifically, the Commission has reached the preliminary view that a declared SMS termination service should not exclude termination of A2P SMS services. This letter provides Telstra's response to the Commission's preliminary view.

As the Commission is aware, Telstra does not support the Commission's preliminary view in the Draft Decision that the MTAS service description should be varied to include SMS termination services (whether such SMS messages originate on a handset or otherwise through some form of application). Telstra's position on this was outlined in our response to the Draft Decision and in our more recent response to a submission made by Thomson Geer on behalf of Message4U. As set out in more detail in our previous responses, Telstra maintains that there is compelling and growing evidence for the substitutability and competitive constraint upon SMS messaging from OTT messaging applications. The market for SMS services and OTT messaging applications continues to develop at a rapid pace and this, combined with the risks associated with over-regulation of access, suggest that it is not in the Long Term Interests of End-Users (**LTIE**) for SMS termination services to be declared.

In addition, Telstra has submitted that if the Commission was nevertheless minded to declare a termination service for handset originated SMS, the Commission should carve out A2P SMS from the service description – a position the New Zealand Commerce Commission has endorsed when regulating handset-based SMS termination in 2011.

The Commission has now set out a preliminary view that any declared SMS termination service should not exclude termination of A2P SMS services. This letter addresses some of the reasons provided by the Commission for this preliminary view below.

Is the Commission correct in suggesting exclusion should only occur if there are good reasons to do so?

The Commission does not consider that the termination of some SMS services should be distinguished from other services based on the origination of these services when they display similar characteristics. Specifically, the Commission considers that “[a] specific type of SMS service should only be excluded from declaration if there are good reasons to do so.”

Telstra does not agree with this approach, and considers it inconsistent with the statutory regime. The default option for declaration should not be inclusion of a distinct category of service unless there are good reasons to exclude. Rather, as required by the declaration provisions in Part XIC of the *Competition and Consumer Act 2010 (CCA)*, the declaration of new types of services should only occur if there is evidence that such a step will promote the long-term interests of end-users. An example is where there is an identified market failure relating to provision of the service (such as a bottleneck) which has demonstrably impacted on competition in the market or market segment, to the detriment of consumers.

Reflecting this, the declaration regime allows - and indeed Telstra would argue it requires - the ACCC to ensure the description of a declared service is not so broad as to have the effect of extending application of access regulation beyond what is required to address an identified market failure or other matter relating to the LTIE. Indeed, the Explanatory Memorandum for the *Trade Practices Amendment (Telecommunications) Bill 1996* noted that:

“In making a declaration of an eligible service, the ACCC will have a high level of flexibility to describe the service, whether it be in functional or any other terms. This will enable, where appropriate, the ACCC to target the access obligations (which are triggered by a declaration) to specific areas of bottleneck market power by describing the service in some detail, or to more broadly describe a service which is generally important (such as services necessary for any-to-any connectivity).”¹ (our emphasis)

In this context, Telstra’s position is that:

- A2P SMS services are distinct from person-to-person or peer-to-peer (**P2P**) SMS services and should therefore be treated as a separate segment of the market; and
- the characteristics of the A2P segment are such that Telstra believes there is no reason for these services to be included in any declaration of SMS termination services, and – as explained below- Telstra considers the ACCC has not in its published comments on the issue to date provided evidence to the contrary.

Do A2P SMS share the same bottleneck features as P2P SMS?

The Commission has found that the termination of A2P SMS shares the same bottleneck features as P2P SMS termination. Similarly, the Commission considers that A2P SMS messages only differ from other SMS in terms of their technical origin. This is technically correct. However, this finding ignores key characteristics of A2P SMS services which clearly distinguish them from P2P SMS services. Specifically:

¹ Explanatory Memorandum to the Trade Practices (Telecommunications) Amendment Bill (1996), item 6, proposed section 1.

- Wholesale service provision – SMS termination for P2P SMS is a separate component that is also invoiced between Mobile Network Operators (**MNOs**) separately where messages are sent off-net. By contrast A2P SMS services are end-to-end services. SMS termination will be included in the end-to-end service charge levied by the originating MNO, even if messages are sent off-net, but the way in which this is charged will depend on the specific nature of the service being provided (i.e. volume of messages, type of customer).
- End-user experience – P2P SMS messages are exchanged between individual end-users for (in most cases) personal reasons. A2P SMS messages are sent to individuals who are either end customers or prospective end customers of a service or business provided by the A2P service provider (who may send messages through an SMS aggregator or directly through an MNO). A2P messages generally do not require or enable a response. Further, A2P SMS messages are sent for commercial or business reasons. They are aimed at providing a value-add to end users and ultimately to the business or service provider. The value-add to the business or service provider may include, for example, increased revenue opportunities, decreased administrative costs or increased patronage. In determining how to generate this value-add, the business or service provider has a range of commercial options to reach customers or prospective customers, of which A2P SMS is but one.
- Cost – the cost of P2P SMS messages (including termination) is borne by the end user who sends and receives SMS messages and the charges are set either on a per SMS or bundled basis to end users who send SMS messages. The cost of A2P SMS messages are borne by the A2P provider only and the end user who receives A2P messages does not pay a charge for the service nor does the ability to receive A2P messages impact the value or choice of mobile plan chosen by end users. P2P SMS termination charges have been negotiated between MNOs on a per SMS basis that does not vary according to volume or the type of customer. As noted above, the cost of the A2P SMS message service will depend on the nature of the service; this is a commercially negotiated cost that may vary depending on the type of service, volume and type of customer. The A2P business or service provider will consider this cost in determining which of the range of commercial options available to reach customers or prospective customers it chooses to adopt.

The characteristics strongly suggest that A2P and P2P SMS messages should be considered as separate markets. To date, the MTAS inquiry has been focused on the more common P2P SMS messages and it is not sufficient to simply include niche A2P SMS messages by default this late in the process.

Would declaring A2P SMS promote competition for wholesale A2P services and in the downstream markets?

The Commission considers that including A2P SMS in any declaration of SMS termination services will promote competition in the relevant markets.

What the Commission does not take into account, however, is that the A2P SMS market is already effectively competitive. The market is comparatively small compared to P2P SMS although Telstra estimates that it is growing off a low base by an estimated 25 per cent per annum. There is already competition between MNOs for customers, such as banks and government agencies, where A2P services may be provided as part of a broader telecommunications package. Further, the ability of SMS aggregators to buy services from different MNOs means that they are already in a strong position to negotiate commercially attractive rates.

This position is strongly borne out in practice and the Commission has not been presented with any evidence as part of the current inquiry of any commercial failure between A2P operators in negotiating supply terms for A2P services nor any evidence of any likely adverse impacts on consumers from the existing arrangements. Further, no concerns have been raised about A2P SMS services in terms of the level of pricing or that MNOs are acting in any way to restrict or stifle access to A2P SMS services.

The consideration of whether or not to declare P2P SMS was effectively initiated in response to an issue raised by one mobile carrier which argued that the process of commercial negotiation of SMS termination rates was not working effectively. Even if the Commission considers that may be the case for P2P SMS, these circumstances have not occurred with respect to commercial arrangements between MNOs and A2P service providers and aggregators. Telstra's position is that it is inappropriate to include (by default) A2P SMS in any SMS declaration where there are no demonstrated barriers to entry and no evidence of market failure. No evidence has been presented that the declaration of A2P SMS termination will flow to provide enhanced levels of competition or services or prices for end users in what is already a highly competitive and contestable market segment.

Is it in the LTIE to include A2P SMS termination services in the MTAS declaration?

For a declaration to be in the LTIE, the CCA requires that the following objectives be achieved:

- Competition promoted in the relevant markets;
- Any-to-any connectivity; and
- Economically efficient use of, and economically efficient investment in, the infrastructure by which telecommunications service.

As noted above, Telstra considers that the market for A2P SMS services is already effectively competitive as demonstrated by the high growth of this currently niche market. There are no issues associated with any-to-any connectivity. With respect to the economically efficient use of, and investment in, infrastructure, Telstra does not believe that this will be encouraged by the declaration of A2P services. Rather, the declaration of A2P SMS is more likely to result in a "wealth transfer" from MNOs to A2P providers or SMS aggregators who are in most instances sending A2P messages for commercial benefit. This is likely to discourage additional investment and innovation in the provision of A2P SMS messages which is not in the LTIE.

As stated above and in other submissions, Telstra maintains its position that the declaration of SMS termination services is unwarranted, unnecessary and would not be in the LTIE. Telstra considers that the declaration of any service must be in the LTIE and a last resort where other regulation (including competition law) and competitive constraints in related markets are not likely to be effective over the regulatory period in question. This is not the case with SMS termination services, which show no sign of market failure and are subject to competition from OTT applications. However, if the Commission is minded to declare SMS termination the service description in the Draft Decision should be amended to expressly exclude A2P SMS messages rather than include these services by default. The A2P SMS market in Australia is competitive, thriving and there is no evidence of market failure requiring a regulatory response.

Please contact Justine Bond on (02) 8576 2736 should you have any queries in relation to the contents of this letter.

Yours sincerely,



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