



MTAS DECLARATION INQUIRY

**SUPPLEMENTARY SUBMISSION TO THE
AUSTRALIAN COMPETITION AND
CONSUMER COMMISSION**

April 2014



Vodafone Hutchison Australia Pty Limited (**VHA**) welcomes the Australian Competition and Consumer Commission's (**ACCC**) invitation to comment on the issues raised in a submission by Thomson Geer on behalf of Message4U Pty Ltd (**Message4U**), which relate to the ACCC's Draft Decision on the Mobile Terminating Access Service (**Draft Decision**).

VHA remains opposed to the declaration of SMS termination. Declaration appears contrary to best regulatory practice that would first seek to find the least interventionist regulatory solution that would resolve any perceived competition concerns. In contrast the ACCC is proposing the most head-handed of the ACCC's regulatory armoury. We do not consider that the ACCC has demonstrated the existence of a market failure that has a detrimental impact on the long-term interests of end-users let alone justifying such a substantial increase in the ACCC's jurisdiction.

We urge the ACCC to examine other regulatory options to resolve the concern that have been identified. This will avoid a long-term regulatory burden at a time when there is a government focus on reducing high cost approaches to regulating the sector. If the ACCC has identified preliminary concerns (for example, the persistence of "high" SMS termination rates) then it should consider lighter touch forms of market intervention before resorting to such a heavy handed intervention to this service.

In our view the draft interim decision to declare SMS termination was based on insufficient information obtained from a limited set of information requests and an inadequate assessment of the issues (see **Table 1**). Given the ACCC is proposing a significant and substantial expansion of the ACCC's jurisdiction into the mobiles market we do not believe that it was appropriate to simply add this issue into the MTAS declaration inquiry. This did not allow interested parties to put forward the evidence that the ACCC would require to make a thorough assessment.

Table 1: Factual inaccuracies in relation to SMS termination in the ACCC's draft decision

ACCC assertion*	Comment	Recommendation
Assessment of substitutability of over-the-top messaging applications (pp 33-34)	The ACCC's assessment is characteristics-driven and has ignored empirical data on consumer behaviour from, for instance, markets where messaging applications are rapidly displacing SMS traffic. Further it has not assessed the substantial reduction in the SMS price to respond this new competitive pressure.	ACCC undertake an evidence-based assessment of consumer demand for messaging applications.
49% smartphone penetration (p34)	Reported ACMA figures are around two years of out-of-date and ignored the trend toward rapid adoption of smartphones by consumers. At the time of the Interim Determination there were a range of more up to date data that would have confirmed this.	Use updated ACMA figure of 64% smartphone penetration. By the time declaration would be in effect we would expect that smartphone penetration to be closer to 70%. This significantly changes the substitutability assessment and would confirm that there are a range of substitutes that will continue to driver competitive outcomes
Imbalance in SMS traffic (p39)	VHA maintains that SMS traffic between service providers is balanced. It appears that the ACCC may be relying on data between carriers that has not been reconciled.	ACCC should define thresholds for "balanced" and, if it believes there are imbalances identify the specific causes for that imbalance. VHA would be happy to participate in a data reconciliation exercise with the other MNOs.

* Page references refer to the ACCC's 2013 Draft Decision on the MTAS.



In our view a thorough assessment of the issue would determine that this issue does not raise such a significant market problems to require the onerous step of declaration. For example the Australian retail mobiles market has low SMS prices with most of VHA's post paid plans providing unlimited SMS. We recognise that the ACCC has identified some concerns regarding SMS termination services, primarily that commercial SMS termination rates might be "inefficiently high" relative to the cost of providing the service. VHA does not consider these concerns sufficient for the ACCC, as part of the MTAS declaration inquiry, to declare SMS termination services. Unlike mobile voice termination, mobile network operators do not have a clear incentive to set "high" SMS termination rates to the detriment of the rest of the market because traffic flows between MNOs is generally balanced. We therefore do not understand the basis on which the ACCC could consider that it has sufficient evidence to reach a conclusion, nor how a view could be reached that declaration is in the long term interests of end users (as the level of termination rate has not prevented rapid and dynamic movements in SMS retail prices. It is also unclear why the ACCC could come to a view that commercial negotiations could not be capable of delivering the desired outcome sought by the ACCC – that is, a significant reduction in SMS termination rates.

We agree that the industry's SMS termination pricing is a reasonable issue for the ACCC to raise, but before taking the most heavy handed regulatory approach available, the ACCC should have sought more detailed information, and undertaken a more thorough assessment of the market impacts of declaration. The recent late submission by Message 4U is a case in point. Declaration based on a particular service description is likely to have many unintended consequences that would be avoided by a lighter touch regulatory approach.

VHA's recommended way forward

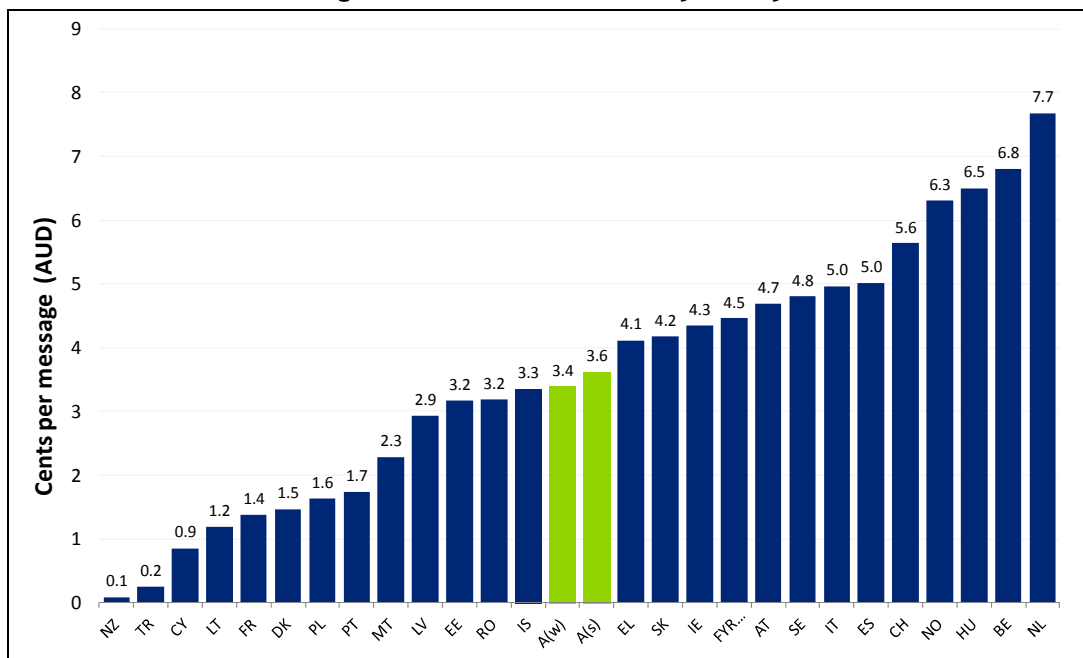
VHA would like to stress our view that there is a more effective way to resolve the ACCC's concerns. We recognise that the industry's current SMS terminations pricing is high compared to international benchmarks and I would like to reiterate that VHA is prepared to pursue commercial agreements that would reduce the SMS termination price that would avoid the need for declaration.

Instead of pursuing heavy-handed regulatory intervention, VHA recommends the ACCC provide a time limit (e.g. 30 September 2014) for industry to commercially negotiate alternative price terms for SMS termination and specify that parties be required to implement the new rates by a set date (e.g., 31 March 2015). This provides a timeframe that delivers outcomes consistent with the timing of any regulatory intervention on SMS termination rates that might be contemplated by the ACCC. This approach is consistent with the Government's overall policy objective of avoiding excessive regulatory burdens where less interventionist approaches deliver the same result. Of course we do recognise that the Declaration mechanism is an important part of the administration of the telecommunications industry, but not in the case of this service.

VHA notes that commercial agreements are likely to be reached quickly if the ACCC were also to informally indicate a SMS termination rate threshold below which, if met, would mean regulatory intervention was not warranted. In our view, commercial negotiations are likely can move Australia to the lower end of international benchmarks for SMS termination rates (see Figure 1) while avoiding arbitrage risks that arise from extremely low rates including potential unintended consequences (e.g., an increase in the amount of spam SMS).



Figure 1: SMS termination rates by country



Country list: AT: Austria, BE: Belgium, BG: Bulgaria, CH: Switzerland, CZ: Czech Republic, DK: Denmark, DE: Germany, EE: Estonia, EL: Greece, ES: Spain, FR: France, HR: Croatia, HU: Hungary, IE: Ireland, IS: Iceland, IT: Italy, LT: Lithuania, LV: Latvia, LU: Luxembourg, FYROM: Former Yugoslav Republic of Macedonia, NL: Netherlands, NO: Norway, NZ: New Zealand, PL: Poland, PT: Portugal, RO: Romania, RS: Serbia, SE: Sweden, SI: Slovenia, SK: Slovakia, TR: Turkey, UK: United Kingdom. Exchange rate: 1 AUD = 0.7293 EUR
Source: BEREC (2013), Termination rates benchmark snapshot, July.

Comments on the Message4U submissions

Message4U's related submission provides further confirmation of the problems with declaration of the SMS service. First, the issues Message4U raise relate to a specific, narrow market issue and do not demonstrate that declaration of SMS termination is warranted. Secondly, and more substantively, it highlights one of the main challenges with regulatory intervention on services, namely that it is difficult to design regulation that avoids unintended consequences. There is a trade-off between detailed technical specifications and generalised (i.e., technology neutral) service definitions. The former may introduce unexpected behavioural distortions because regulation covers too little, while the latter risks regulation covering too much. The level of demand and supply side substitutability, countervailing power and entry barriers critically inform how the ACCC should assess this trade-off. For instance, where demand-side substitutability is high, then technology neutral service descriptions should be preferred to avoid explicitly or implicitly tilting the competitive playing field in favour of certain technologies and businesses.

As outlined in our submission to the ACCC's Draft Decision, VHA is concerned the proposed definition for SMS is not technology neutral because it includes very specific terminology such as "spare capacity". By contrast, several parties have proposed the ACCC increase the technology specificity of the SMS definition by, for instance, proposing a reference to GSM Technical Specifications¹ or proposing that SMS should be defined as "an alphanumeric sequence of text"². The motivation for these

¹ Telstra 2014, *Response to the Commission's Domestic Mobile Terminating Access Service Declaration Inquiry – Report of the ACCC's Draft Decision*, Public version, 14 February, p32.



proposals is a desire for application-to-person (A2P) SMS to be excluded from declaration. It is argued that the assessment of whether SMS termination is deemed to be a 'bottleneck' service for access providers depends on the origination of the SMS from the access seeker. While we agree that services A2P services should not be declared, such a decision cannot be made in isolation, instead such a decision confirms that other forms of SMS termination should also not be declared. From a policy point of view, the assessment of whether a termination service is a 'bottleneck' cannot be conditional on the source of origination. SMS termination must either be a 'bottleneck' for all traffic regardless of origination or the ACCC must deem that SMS termination is not a 'bottleneck' for any traffic type. To do differently is counter to the ACCC's policy position that declarations should be technology neutral.

While differences in origination do not warrant limitations on the scope of declaration, origination-based price discrimination should be considered by the ACCC in its access determination. For instance, in the context of voice termination services, the lack of retail fixed-to-mobile pass through of past MTAS reductions may warrant the ACCC setting a different price for traffic originating on fixed networks than it does for traffic originating on mobile networks.

In summary, VHA's primary submission remains that declaration of SMS termination is not in the long-term interest of end-users. If the ACCC does not agree with VHA's primary submission then we recommend the ACCC take a technology and competitively neutral approach to the definition of SMS within the service description, which implies it should make no distinction in the definition regarding the origination of traffic and it should not adopt "technical" changes that have the effect of permitting discrimination based on origination.

Given the potential for significant and adverse unintended consequences, VHA requests the ACCC undertake a further consultation on the service description prior to finalising its decision on SMS termination declaration. In making this request, we recognise the ACCC may want to limit the scope of consultation to directly affected stakeholders and restrict the time available for further submissions. VHA notes that the DTCS service description definition benefited significantly from an industry forum facilitated by the ACCC. Given this is the first time the service is declared we believe that this would be a useful exercise for considering issues relating to SMS termination.

² Optus 2014, *Submission in response to the ACCC Draft Decision Report: Domestic Mobile Terminating Access Service (MTAS) Declaration Inquiry*, Public version, February 2014, p12.