

THE STRUCTURE OF TELSTRA

*ACCI SUBMISSION
TO THE
THE HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON
COMMUNICATIONS, INFORMATION TECHNOLOGY AND THE ARTS*

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BACKGROUND

The Australian Chamber of Commerce and Industry (ACCI) is the peak council of Australian business associations. ACCI's members are employer organisations in all States and Territories and all major sectors of Australian industry.

Through our membership, ACCI represents over 350,000 businesses nation-wide, including the top 100 companies, over 55,000 enterprises employing between 20-100 people, and over 280,000 enterprises employing less than 20 people. This makes ACCI the largest and most representative business organisation in Australia.

Membership of ACCI comprises State and Territory Chambers of Commerce and national employer and industry associations. Each ACCI member is a representative body for small employers or sole traders, as well as medium and large businesses.

INTRODUCTION

On 11 December 2002 the Minister for Communications, Information Technology and the Arts, Senator the Hon Richard Alston, asked the House of Representatives Standing Committee on Communications, Information Technology and the Arts to inquire into the structural separation of Telstra's core network from its other businesses.

The Terms of Reference are:

That the Committee inquire into and report on the economic and social impact of structurally separating Telstra's core network from its other businesses and reducing the Commonwealth's current shareholding in Telstra's non-network businesses.

In conducting its inquiry, the Committee should consider the impacts of such a proposal on:

- The efficient provision of services to end-users, including businesses and residential customers in regional, rural and remote Australia;
- Telstras's ability to continue to provide a full array of telecommunications and advanced data services;
- Ongoing investment in new network infrastructure;
- The wider telecommunications industry;
- The telecommunications regulatory regime;
- Telstra's shareholder value and its shareholders; and
- The Commonwealth Budget.

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COMMENTARY

Telecommunications services have become a fundamental business tool. The importance of the telecommunications to business was shown in a pre-election survey of ACCI members in October 2001 which ranked telecommunications costs as the 5th most important issue facing business. It ranked just behind the cost of Government regulations and ahead of unfair dismissals as areas of most concern for business.

Further surveys on this issue showed that although there are many businesses which are experiencing major problems, it is still the case that the telecommunications system is performing well for the majority of Australian firms.

Central to these concerns of business has been the widening and deepening of telecommunications costs to businesses.

The growth in the number of telecommunications services available to business such as fax machines, mobile phones and the internet as well as increased use of all these services has resulted in business now using more telecommunications services more frequently.

Having an efficient telecommunications system in Australia is therefore vital to ensure that Australian businesses are able to compete with imported goods and services, as well as competing in international markets.

The important issues for business, are not just obtaining low cost and reliable telecommunications services but also about ensuring adequate investment in new infrastructure and investment in new technologies.

Given the reliance modern economies place on their telecommunications systems and the enormous changes occurring in telecommunications technologies and the international market structure, telecommunications has become one of the main public policy debates. The Organisation for Economic Cooperation and Development (OECD) is currently undertaking extensive research into this field, overseeing many different approaches to privatisation of formerly government owned telecommunications systems. Whilst the OECD's activities are ongoing, Australia should use the outcomes from the OECD studies to guide future decision making.

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Telecommunications Industry

Australia commenced privatisation of the telecommunications network in the early 1990s and the framework established then, and over the past decade, has resulted in the development of an industry which is dominated by one company. Such a market structure is not ideal for the development of a long-term competitive telecommunications market in Australia.

To help overcome this problem a complex system of regulations, programs and incentives have been put in place to allow access for many competing businesses to the same system. Australia currently has excellent telecommunications infrastructure. ACCI believes that a combination of these existing government activities combined with further coordinated investment in telecommunications infrastructure will result in Australia maintaining this infrastructure in a competitive market.

An area of particular concern has been the continued provision of services that are not commercially viable. Many services, particularly in regional areas are not commercially viable, yet are considered to be essential services. This problem will occur irrespective of the level of competition which exists in the Australian telecommunications industry. ACCI maintains that in this situation non-profitable services, which are deemed to be necessary services, should be explicitly funded by the government and tendered to all potential providers of that service, on a competitive basis. This, combined with the Universal Service Obligation on all carriers will ensure that minimum standard levels are achieved and all Australians have access to essential telecommunications services.

Investment in Infrastructure

Investment in existing and new infrastructure is a major issue for business. The rapid technological developments in telecommunications over the last decade have offered significant efficiency improvements for business and improved customer service. Failing to capitalise on future technological advancements would undermine the competitiveness of Australian business.

Alternatively, the duplication of infrastructure and the development of non-compatible technologies can create inefficiencies.

ACCI believes that irrespective of the structure of Telstra or the telecommunications market in Australia, the Government has an important strategic role to ensure that investment in the telecommunications industry continues to provide world class competitive services. The Government's role should be as a facilitator ensuring an efficient and effective infrastructure network.

*STRUCTURE OF TELSTRA***Structural Separation**

Structural separation is a concept relating to the separation of the incumbent telecommunications company's activities and can occur as a division between wholesale and retail operations or by geographical regions. Structural separation has been used successfully as the model to introduce competition to other government owned enterprises both in Australia and overseas. An example is the privatisation of the rail network in Australia where the Government retained ownership of the fixed rail system and sold the 'rolling stock'.

Whilst this model is considered to have been a success in a number of other industries, it has not been without problems. Issues such as access rights, price determination and sharing of resources are ongoing problems. These issues are also likely to exist if structural separation was introduced to the Australian telecommunications system. However, there are additional problems which may arise in the telecommunications environment, in particular, investment in new infrastructure.

The telecommunications industry is currently undergoing a period of rapid technological change with the introduction of a variety of mobile technologies, cable broadband, wireless broadband, satellite technologies and digital television services. This change distinguishes this industry from others where structural separation has been successfully implemented. With rapid technological change the increased demand for investment in infrastructure in multiple and competing technologies becomes increasingly complex.

One of the main problems with structural separation is that the government will retain/reclaim ownership of telecommunications infrastructure. This raises concerns regarding the efficiency at which this infrastructure can be provided. Furthermore, governments are notoriously poor at picking technology winners and this would create a range of new problems in managing future infrastructure investment. Decisions regarding investment in infrastructure are best determined by those who will seek a return on that investment.

It must also be recognised that the current industry structure does not necessarily result in the creation of a natural monopoly. A monopoly only exists where there is a single provider of a good and where there are no substitute products. Increasingly, new technologies such as mobile, broadband, wireless and satellite telecommunications are by-passing the local loop infrastructure. Whilst these technologies are not perfect substitutes and can still

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rely on Telstra provided infrastructure they do greatly diminish Australia's reliance on the 'last mile' of infrastructure which is owned by Telstra.

Increasingly, international opinion, and evidence, are weighing against the principle of structural separation. The OECD Directorate for Financial, Fiscal and Enterprise Affairs Competition Committee recently released a paper, for discussion by the Telecommunications and Information Services Policies Working Party.

This paper concludes:

"Seemingly simple in concept, structural separation is in practice complex with uncertain outcomes and many questions to be answered. The benefits of structural separation are uncertain with the costs potentially large. Certainly there is insufficient evidence that the benefits or structural separation are convincingly in excess of costs. In this context, it would seem more sensible to persevere with the current regulatory approach (with appropriate improvements and augmented by sanctions).

This is in contrast to earlier OECD Reports which had recommended that structural separation was a model which had been successful in the privatisation of other Government Business Enterprises and therefore should be considered appropriate for the telecommunications networks.

Whilst OECD discussions relating to structural separation are far from complete it is worth noting that there is not a precedent for structural separation in telecommunications having been successfully implemented in any OECD country.

ACCI recognises that the dominance of one player in the Australian market is inconsistent with creating a competitive market. However, Australia embarked on this course of privatisation in the early 1990s and is currently too far into the process to turn back. Indeed ACCI has resolved that Telstra should be fully privatised at the earliest appropriate time.

Had it been pursued from the early 1990s, structural separation may have resulted in a more competitive market. However, the cost of changing from the current structure of Telstra to an alternative model prohibits such a change at this stage. This current debate should have been concluded before privatisation of the industry commenced. We are 15 years too late.

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ACCI believes that the current system, whilst not without problems, will result in a competitive market with adequate investment in new infrastructure and an effective regulatory environment.

Problems with the Current Industry Structure

ACCI's position of opposing structural separation should not however, be interpreted as unequivocal support for the current structure.

Whilst the path for privatising Telstra was decided more than a decade ago, and ACCI supports the policy of seeking to gain the greatest return from the public asset, it is also essential that a competitive and efficient telecommunications market exist in Australia.

Increasing competition in the Australian telecommunications market should be a key objective of the Government. Achieving this will require both incentives for new entrants to invest in telecommunications infrastructure and an effective regulatory environment.

As already stated, investment in new infrastructure to either expand existing networks or to create new networks is an important issue for business. Investment in telecommunications however is hindered by large sunk costs, rapid technology progression and long return timeframes.

Attracting investment from either domestic or foreign businesses will require active intervention by the Government. The Government has already identified Information and Communication Technologies as a priority area for Invest Australia, but more targeted and active foreign investment attraction practices for telecommunications is warranted.

The ability to access existing telecommunications networks and services of competing carriers is also essential to the development of competition in telecommunications services in Australia. The telecommunications access regime, which is governed by the *Trade Practices Act*, provides for access by telecommunications companies to declared services supplied by other companies.

Carriers are generally required to provide other service providers with interconnection to declared services together with various other services (eg. billing data, billing services, conditional access equipment).

The ACCC, after consultation with carriers, determines the terms and conditions on which these services will be supplied. Negotiated

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contracts between parties are required to be submitted to the ACCC for acceptance.

Whilst the existing telecommunications regulatory environment is not within the terms of reference for this inquiry the adequacy of these arrangements in promoting competition in the long-term needs to be considered by government.

CONCLUSION

Structural separation as a concept for an alternative industry and regulatory structure for the telecommunications system in Australia, which if pursued before the early 1990s when privatisation of the industry commenced may have provided Australia with an efficient and competitive telecommunications market. However, a different competition model has been pursued in the Australian telecommunications system and we are now beyond the point at which we can reverse the current structure.

Whilst there are problems with the current industry structure, a combination of effective regulation, investment attraction and investment in new infrastructure can result in the creation of a competitive telecommunications industry. Finding the right balance between a competitive market and regulation is difficult in most industries and a number of other OECD countries are currently grappling with similar issues in their telecommunications industry.

ACCI believes that any discussion regarding the structure or role of Telstra should be in the context of a fully privatised telecommunications industry. This should remain a key priority for the Government.

Overall, ACCI believes that the Government's objective should be to maximise the value of its ownership of Telstra and move toward a fully privatised telecommunications industry in Australia.