

Review of Telecommunications Specific Competition Regulation

Executive Summary

Macquarie Corporate Telecommunications (MCT) welcomes the opportunity to make this initial submission to the Productivity Commission's inquiry. It is Macquarie's intention to lodge a further submission in September to assist the Commission. The submission covers five main areas – regional services, the timing and nature of the review, the state of competition in telecommunications markets, the adequacy of the existing legislation and possible remedies.

Regional services

Regional telecommunication markets display significantly different characteristics to metropolitan markets and arguably require different regimes to engender competition. Non-metropolitan markets face high infrastructure costs and thin markets and therefore present considerable barriers to entry for potential entrants. In the medium term, technology of itself is highly unlikely to hold the entire answer. MCT suggests that a number of regional specific actions could address these issues. These include:

- Setting a specific regional legislative objective,
- Fast tracking declaration of regional services,
- Establishing specific powers in relation to regional facilities access,
- Setting minimum wholesale service levels in regional areas,
- Appointing a dedicated Regional Communications Commissioner at the ACCC and
- Reviewing the USO payment and delivery system and replacing it with a voucher system.

Timing & Nature of the Review

The Telecommunications market in Australia has evolved from a Government controlled monopoly less than ten years ago into its current state. The current legislative framework has been in place for around 3 years following a 5 year period of managed competition. That 5 year period granted key rights and privileges to the two full licence carriers and a further Mobile operator.

Since July 1997 the explicit restraints on competition have been removed and replaced with a regime that has specific features to deal with the issues in telecommunications markets. These needs arise from more than a century of monopoly or near monopoly control over markets and the essential interconnectedness of telecommunications. Whilst the existing regime has as its underlying tenet being pro-competitive, it has been slow to fully deliver. As the attached case studies show the ability of the legislation to deliver on its original promise have been mixed and more frequently not timely.

While MCT understands the need for the Commission in its issues paper to revisit the underlying questions regarding telecommunications regulation, it should take into account the exhaustive review that led up to the 1997 legislation and how early into its

effective life the regime actually is. In particular in many markets little has changed in that time. The factors underlying the need for a pro competition regime are just as compelling now and given the developments in overseas markets and Internet applications, the need for an open and competitive regime is more imperative now than ever before.

The State of Competition

There are many factors which impact on judging the state of competition and these are further complicated by the existence of different sub markets sometimes showing different characteristics. Some key identifiers would be the barriers to entry, market shares, price performance, the level of technical and marketing innovation, and the levels of investment, efficiency of investment and operational efficiency. The weight of evidence points to the conclusion that on most if not all of these key performance indicators the Australian telecommunications industry still has some way to go before it achieves best practice and in many cases it is not exhibiting the characteristics of a market which is driven by competition.

It is true that there are many new entrants in the industry since 1997, but in many fields of competitive endeavor, there has been little effective improvement since the duopoly days. Examples of improved competition might include STD by-pass and international calls, but these areas depend on continuing regulatory pressure for their development. Without arbitration rights, pre-selection and scrutiny of commercial churn processes it is unlikely that continuing competitive pressure will continue to be applied.

The underlying market power of Telstra in many areas remains significantly unchallenged and even with these pro-active regulatory interventions Telstra's market shares and pricing do not appear to have been significantly impacted.

The reason for this may be that the incumbent has such effective rights to vertical integration, price discrimination, non-transparent pricing and closed access to customer and cost information. This level of incumbent rights is exceptional by world standards for a truly competitive regime.

The end result is that in the key areas where competition is needed - like data services and underlying local call services - effective competition has been slow to develop and the overriding performance drivers are statutory price controls and mandatory minimum performance standards rather than competition.

Adequacy of the Existing Legislation

The existing legislation provides a solid and robust framework for access and great flexibility for the ACCC to focus in on important access issues and to make determinations that seek to resolve those access issues for the long-term interests of end users. Indeed there are many instances of other industries like transport and energy where comparable powers would lead to improved national outcomes.

Sometimes this flexibility has been at the expense of the time and cost to effect changes. For example the obvious local loop bottleneck, singled out for specific legislative attention in the US as early as 1996, has still not been completely addressed with some resolution for larger industry players perhaps to come later this year.

However it would be a significant mistake to think that the main tasks have already been addressed by the ACCC and there could be some relaxation of access rules. It is becoming apparent that as technology develops new bottlenecks will emerge and not necessarily restricted to that technology. For example the whole range of issues related to the convergence of broadcasting, datacasting and telecommunications remains open, as does the use of, and access to, customer information.

While the access features of the legislation have been quite effective, the legislation does not fully address of transparency of decision making and the management of industry information. These restrictions on information flows can have significant impacts on the ability of new entrants to compete effectively and fairly. For example, the legislation envisages a wide range of negotiated outcomes in instances where there is a clear imbalance of negotiating power and appears to rely on market mechanisms where there is no effective market place and wide information asymmetry.

Remedies

MCT believes that there are a number of key areas of the operation of the legislation that should be examined in order that it better achieves its original objectives.

The key proposals are:

- **Improve arbitration and complaint processes.** Increase the resources of the ACCC (and possibly also the ACA) outsource arbitration to professional arbitrators, the appointment of external experts by the Commission to assist in the arbitration process and impose strict timeframes limiting the length or number of submissions and replies that will be accepted.
- **Develop an incentive based regulatory approach,** that clarifies the ACCC's powers so that it can restrict specified activity (for example bundling of ADSL and long-distance retail services) until certain key access milestones are delivered.
- **Enhanced end user power.** Resolution of the network boundary issue has the scope to improve end user outcomes by increasing the scope of competition.
- Give the ACCC unambiguous powers to **deliver transparent, non-discriminatory and fair access pricing**, so that Australia is consistent with its WTO commitments and the practice in the EU and US. This approach would dramatically reduce arbitration and reduce delays.
- **Modify part XIB** so that it is more effective in dealing with access issues by removing ambiguities thus giving the ACCC a focussed tool to deal quickly and effectively with anti-competitive access activity.
- **Reduce the ambiguity of SAOs** so the ACCC can set absolute levels of performance, this would also improve transparency and regional outcomes.

- **Abolish the TAF**, so that fast track declarations can be effectively handled directly by the Minister.
- **Enable effective Record Keeping Rules** to unblock the existing delays.
- **Provide for effective access to information** so that informed open debate about key regulatory issues can take place and regulators held to account.

Review of Telecommunications Specific Competition Regulation

Macquarie Corporate Telecommunications Initial Submission

Macquarie Corporate Telecommunications (MCT) welcomes the opportunity to make this initial submission to the Productivity Commission's inquiry. It is Macquarie's intention to lodge a further submission in September to assist the Commission. The submission covers four main areas – regional services, the timing and nature of the review, the state of competition in telecommunications markets, the adequacy of the existing legislation and possible remedies.

Macquarie Corporate Telecommunications (MCT) is an Australian-owned and ASX-listed telecommunications company that focuses on the provision of telecommunications services and solutions to small, medium and large businesses. Formed in 1992, MCT offers a total communications package to its corporate customers, including voice service (purchased from third party major carriers), data services (increasingly through MCT's own recently installed carrier grade ATM based infrastructure), facilities and project management, and telecommunications consultancy.

Regional Services

Regional telecommunication markets display significantly different characteristics to metropolitan markets and arguably require different regimes to engender competition. Non-metropolitan markets face high infrastructure costs and thin markets and therefore present considerable barriers to entry for potential entrants. In the medium term, technology of itself is highly unlikely to hold the entire answer. These factors are partially offset by subsidy payments (USO), however distribution of the subsidy is flawed with a very large component of the subsidy available exclusively to Telstra thereby entrenching the incumbents position and further deterring new entrants and potential competitors.

As a consequence of these factors, there is limited competition in regional areas resulting in higher prices and a limited range of services. All of the proposed remedies would assist in the development of competition in regional markets. However, there are several regional specific reforms, which would assist in reducing the barriers to entry faced by potential entrants to regional markets.

Regional Objective

An over arching amendment to promote regional competition would an additional objective in Part XI of the TPA requiring the facilitation of competition within the non-metropolitan telecommunications market. The objective would require the ACCC to apply Part XI B and C in a manner favorable to engendering competition in those markets.

Fast Track Declaration

Implementation of a fast track declaration process for regional facilities and infrastructure would assist in opening up access and reducing the inherent delays and costs currently encountered by parties seeking access. Declarations would be made by the ACCC either in response to submissions from aggrieved access seekers or end users and/or in response to the Commission's own observations of market participants' behaviour.

Facilities Access

Regional facilities need to be opened up to multiple parties to allow service based competition to develop and avoid inefficient duplication of infrastructure. However, it is apparent that the facilities access regime is not effective as evidenced by the limited sharing of GSM transmission towers. To remedy this situation, the ACCC could be given overarching powers to prescribe terms and conditions for access to regional facilities and also to determine priority of access to those facilities.

Minimum Wholesale Service Levels

Part XIC requires that the technical and operational quality of declared services are provided on a non discriminatory basis however the regime does not prescribe any clear service standards. An aggrieved party must therefore overcome the difficult evidentiary burden of establishing that it is receiving services on an inferior basis to other operators. To remove this burden the ACCC could be given power to impose absolute service standards for wholesale products in regional areas thereby giving the Commission power to set minimum service standards for bottlenecks on a non discriminatory basis.

Regional Commissioner

To administer the regulatory regime in respect of regional markets and ensure a pro-active and expedient response to Part XI B and C actions, a Commissioner for Regional Communications could be appointed within the ACCC. The Commissioner would have jurisdiction over regional telecommunications, electronic information and broadcast issues and additional issues of relevance to regional services as assigned to him from time to time. It may be appropriate for the Commissioner to be co appointed to the ACA. The functions of the Regional Commissioner would include:

- Declaration of regional telecommunication infrastructure
- Overseeing XIC processes in respect of regional facilities
- Pursuing XIB actions in regional markets
- In the event the ACCC had power to impose pricing and conditions of access, formulating and enforcing pricing and conditions
- Participation in the subsidy (USO) quantification and allocation processes
- Monitoring and reporting on the performance of regional telecommunication markets
- Recommendations to Cabinet on issues pertinent to regional telecommunications

USO Delivery Mechanisms

MCT believes that the current USO arrangements are inadequate and are indirectly anti competitive. The USO regime was devised before the advent of competition within the sector and has only had very minor adjustments since then. The structure of the funding represents the entrenchment of a dominant provider, which MCT believes is not

adequately addressed by the tendering system currently proposed by the Government. This is of particular concern to MCT and other carriage service providers obliged to contribute to the funding of the USO and therefore entitled to an accountable and accurate process.

The process gives the assigned USO carrier access to USO funding to provide a subsidised service irrespective of the potential alternative offerings available. Therefore, while competitors are forced to compete with Telstra using “cost” based regional interconnect charges, which may not always reflect true costs, Telstra is able to apply the USO in order to subsidise its retail prices. Tendering would only partly resolve this issue, as the process would preserve a single provider of a service. Most critically neither process actually increases choice for the USO service customer.

It is on these bases that MCT and other industry players are reluctant to participate in funding a USO which lacks visibility in its costs and benefits and which excludes competitors from segments of the market. MCT believes that a reform of the USO beyond limited tendering trials is required if USO services are going to be improved and industry funding is to become widely accepted.

Adopting alternative delivery mechanisms, which efficiently fund and promote competitive outcomes for the various subsidy targets should ultimately reduce the level of subsidy required and improves service levels. This requires mechanisms which introduce competition, either for the market or within the market, and thereby provide an incentive to improve service levels and drive efficiency savings. At the same time, mechanisms should introduce competition in a manner that does not incur unnecessary costs and avoids duplication of infrastructure and investment.

One of the most effective means of driving competition within a subsidised market whilst leaving discretion with the end user is a voucher system. Essentially payments are made or rebates given to targeted customers to offset the cost of telecommunication services. The benefit of the system is that it leaves the choice of service and provider in the hands of customers allowing the forces of the competitive market to ensure service delivery. There are also important equity advantages from this type of approach that allow it to be targeted at areas most in need of services such as remote schooling, health services and commerce. Services would remain subject to current legislative price caps to reduce the risk of collusion. The system currently operates effectively in Scandinavia and in the Victorian power and gas markets.

Timing and Nature of the Review

In 1997, when the Government implemented the policy of deregulating the Australian telecommunications market, it recognised the dominant (and in some cases, exclusive) market position occupied by Telstra in the provision of the various categories of telecommunications services. Moreover, the impact of this market position on competitors and consumers was compounded by the fundamentally ‘inter-connected’ nature of the telecommunications industry (i.e. it is not possible to provide a basic range

of services without utilising Telstra's network infrastructure). For these reasons, the parliament enacted the industry-specific telecommunications competition framework in contrast to relying on the non specific framework contained in Part IV of the TPA. This framework was further strengthened in mid-1999 by the parliament on the basis of industry concerns of an overwhelming pattern of behaviour by Telstra characterised by non-cooperation and delay (including through expensive litigation).

The decisions relating to the structure and substance of the current legislation (1997) were developed by an extensive and lengthy consultation and investigation process conducted through the offices of the then Department of Communications and the Arts. The existing legislation was the result of that review and based of the experience of managed competition, which had been in place for five years, which had in turn evolved from a Government controlled monopoly. At the time it was passed the legislation had bi-partisan support. That current legislative framework has been in place for 3 years.

It is probably instructive to look at the actual record of hard achievements of the existing legislation and the extent to which they have facilitated open competition in a variety of telecommunication markets. They include:

- The deeming provision,
- A small number of new declarations,
- No access undertakings,
- No final access arbitrations and a small number of interim decisions, and
- A large number of unresolved arbitrations.

As the attached case studies for Data Service, Local Loop Unbundling, Number Portability, Commercial Churn and PSTN Undertaking demonstrate, the actual impact of the legislation on the operation of the market in the timeframe between the enactment of the legislation and this review has been somewhat limited. (See Attachment A)

The key factors that motivated the adoption of an industry specific framework have not diminished and are likely to remain material for the medium term. Telstra remains the dominant provider in all telecommunications markets with minimal reduction in market share since 1997.

The other key factor, the interconnected nature of the sector, has not diminished as the sector is inherently network based, being reliant on the interconnection between operators networks and, in particular, the ubiquitous Telstra network. The ability of telecommunication networks to interconnect fairly and efficiently with other networks is critical to the development of competition. Reliance on network interconnect is of particular relevance to the growing Internet sector where network peering underwrites the scope and currency of the sector.

The factors underlying the need for a pro competition regime are just as compelling now as they were 3 years ago and, given the developments in overseas markets and Internet applications, the need for an open competitive regime is more imperative now than ever before.

MCT submits that, given the delays in actually driving market-place outcomes from this legislation, the emphasis of this review should be on seeking ways to develop a legislative framework that enhances and protects competition and that the burden of proof must rest with those parties seeking any relaxation of the current regime.

The State of Competition in the Telecommunications Sector

MCT strongly believes that the level of competition in the provision of certain key telecommunication services remains inadequate in 2000 for commercial discipline to restrict market manipulation by dominant provider(s). This is particularly apparent at the wholesale level in the local call market and data and voice access in non-metropolitan markets.

Some key identifiers of competition would be the barriers to entry, market shares, price performance, the level of technical and marketing innovation, the levels of investment, efficiency of investment and operational efficiency. The evidence points to the conclusion that on most, if not all, of these key performance indicators the Australian telecommunications industry is lagging behind best practice and is certainly not exhibiting the characteristics of a market driven by competition and delivering benefits to consumers.

The underlying market power of Telstra remains significantly unchallenged and even with these pro-active regulatory interventions Telstra's market shares and pricing appear not to have not been significantly impacted. As a vertically integrated access and service provider, Telstra continues to be motivated to restrict access where access may result in competition in down stream markets. Telstra still holds significant market dominance and as of July 2000 Telstra retained 95% of the local call market, 77% of the long distance market, 85% of data and text and 95% of the telecommunication infrastructure access market. (source: *Telstra Private Client Investor Presentation, July 2000*) This dominance gives Telstra considerable market power which is reflected in market share, access to resources, substantial expertise, relationships with suppliers, and control of critical information and knowledge. The ability of Telstra to use its position poses a considerable risk to competitors and potential entrants and warrants specific regulation that firmly safeguards against anti competitive conduct.

Evidence of a lack of effective competition exists in Government's implementation of the Customer Service Guarantee that reinforces evidence of a lack of competition for users with less than five lines (all residential and most small businesses). In the presence of effective competition, service levels would be maintained at a level that met customer demand by the need to retain or obtain customers and would not require service level regulation.

Evidence of a lack of pricing efficiency can be found in the Productivity Commission's own research into Australian prices compared with Scandinavia and in particular how Australia's geographic dispersion does not explain the price differences between retail

prices in Finland and Australia. Further evidence in relation to wholesale pricing inefficiency can be found in the ACCC's comparison of unbundled local loop prices which shows Australia has the most expensive prices (up to 3 times the price for Germany).

Similarly, capital efficiency drivers and infrastructure duplication are not indicative of a competitive market. For example, intercapital transmission between Melbourne and Sydney has been subject to the lightest of all regulation and yet seems to be delivering the least efficient investment outcomes.

Wave Division Multiplexing (WDM) has the capability to enhance the capacity of a single fibre so that it would be capable of efficiently carrying the entire forecast load between Melbourne and Sydney for the next 5 years. The main cost of a fibre system is laying the fibre and whilst the deployment and upgrade of fibres is not zero cost, it is relatively low cost compared to the initial deployment cost.

However what has happened is that because the entrenched operators are restricting access to underlying fibres new entrants are forced to commit to uneconomic duplication of infrastructure and reproduce the most expensive transmission element. It is indicative that even in a market where the ACCC is most comfortable withdrawing from regulation, the underlying market dynamics are not producing outcomes consistent with competitive outcomes.

The Adequacy of the Existing Regulation.

Macquarie believes that whilst the regulatory structure is sound in principle, there are areas where the legislation, regime structure and administration have resulted in less than fully effective operation of the regime. MCT considers that it would be dangerous to envisage any relaxation in the existing framework and that indeed there are powerful arguments for a stronger and more streamlined approach.

One of the best features of the current legislation is that it is flexible and therefore forward-looking. The Australian framework envisages that Telecommunications should be a highly innovative and dynamic industry and legislators cannot easily determine future needs today. This is particularly relevant to the developing convergent markets where the interaction and overlap of telecommunications and broadcast services will require a regime that can adapt to the inherent complexities of regulating such a market. Indeed the flexibility of the access regime could provide a sound model for many other industries with bottleneck issues such as transport and energy.

As a general rule however the 1997 Competition Regime relies on "ex-post" regulation. That is, it operates to resolve disputes or moderate behaviour after the matter has arisen and for this reason should be seen as inherently light-handed regulation. This is evident in the access regime in Part XIC of the TPA which empowers the ACCC to intervene in the event that an access seeker and an access provider are not able to reach agreement and

in the provisions of Part XIB of the TPA which entitles the ACCC to intervene by issuing a competition notice where anti-competitive conduct has taken place.

Regulation of this type has clear benefits for an incumbent operator such as Telstra. It allows Telstra to continue to engage in anti-competitive conduct and attempt to stifle competition and provides no effective incentive for Telstra to avoid this behaviour.

Telstra's interests are served by continuing to engage in anti-competitive conduct, such as refusing to provide access on reasonable terms because, in most cases, even if the matter is taken to arbitration and Telstra is ultimately unsuccessful, this process is likely to be protracted and Telstra will continue to benefit until such time as the dispute is determined. Similarly, in relation to anti-competitive conduct which is proscribed under Part XIB, Telstra is again likely to benefit from prolonging such conduct notwithstanding the threat of a competition notice from the ACCC - as the longer it is able to sustain such conduct, the greater will be its ultimate benefit.

MCT does not seek to unfairly criticise the ACCC as the main administrator of the regulatory framework (or, indeed, the ACA, which also has some significant responsibilities related to issues such as number portability). MCT believes that given the basic nature of the regulatory framework that there needs to be a full review of the resources available to these agencies and potential alternative strategies related to dispute resolution, investigation of complaints and other associated regulatory functions.

The consequences of undue delay (for the industry and consumers) are accentuated in an industry as rapidly moving as telecommunications, where new technologies and products are literally becoming available on a month-to-month basis.

An important omission from the existing legislative framework is its failure to address the important issue of information asymmetry. This is particularly relevant in an ex-post environment that has heavy reliance on negotiated outcomes. In its position on Basic Telecommunications to the WTO on 14 February 1997 Australia commitment to interconnection provided:

“(a) under non-discriminatory terms, conditions (including technical standards and specifications) and rates and of a quality no less favourable than that provided for its own like services of non-affiliated service suppliers or for its subsidiaries or other affiliates;

(b) in a timely fashion on terms, conditions (including technical standards and specifications) and cost-oriented rates that are transparent, reasonable, having regard to economic feasibility and sufficiently unbundled so that a supplier need not pay for network components or facilities that it does not require to be provided; and....”

The current legislation fails to deliver transparency, non-discrimination, a publicly available offer or a reference offer. This failure is a significant cause of industry conflict, time delays and failed negotiations.

In summary, whilst the regulatory structure is sound in principle, there are areas where the details of the legislation, regime structure and administration have resulted in less than optimum operation of the regime. Part XIB has not been directly effective, even after the 1999 amendments, and to date there have been no successful XIB actions. Part XIC arbitrations have, and continue to experience undue delay and the declaration process remains convoluted. The record keeping provisions have not provided the transparency necessary in wholesale markets dominated by a vertically integrated operator. Finally, industry self-regulation has been an effective and equitable means of developing operational codes however, it is not effective in areas where industry members have competing commercial interests. As a result the operation of the TAF has been frustrating and demanding on resources.

Remedies

MCT believes that there are a number of key areas that should be examined in the existing legislation with a view to improving the outcomes and developing a regulatory structure that will facilitate the development of ongoing competition.

The proposals are:

- Improved arbitration & complaint process,
- Develop an incentive based regulatory approach,
- Enhanced end user power,
- Transparent, non-discriminatory and fair access pricing,
- Modify part XIB to target it more effectively,
- Reduce the ambiguity of SAOs so the ACCC can set absolute levels of performance,
- Replace the TAF,
- Enable effective Record Keeping Rules,
- Provide for effective access to information,

Improved Arbitration & Complaint Process

MCT believes that several steps can be taken to provide a more expedient and effective administration of Part XI B and C:

- a) An obvious step is to increase the resourcing of the ACCC (and possibly also the ACA) which should facilitate quicker handling of XI C (i.e. access) issues and would also allow the Commission to become more pro active in the administration and execution of Part XI B (i.e. anti-competitive conduct). This would not only serve to allow anti competitive conduct to be identified and addressed but should act to more effectively deter such conduct.

- b) The conduct of arbitrations is arguably not a key function of the Commission, which in turn is not resourced with the expertise to expediently handle arbitration (or dispute resolution at a more general level). The process could be outsourced to professional arbitrators thereby tapping expertise and also freeing up and allowing the more efficient utilisation of the Commission's resources for the investigations, inquiries etc. that may provide assistance and input to arbitration between parties.
- c) The appointment of external experts by the Commission to assist in the arbitration process and generally augment the Commission's resources would greatly benefit the operation of the Part XI B and C processes. This would be of particular assistance in technical areas.
- d) To date ACCC arbitrations have suffered through parties adopting an unduly legal approach to a process that should, by its very nature, be commercially and pragmatically orientated. The consequence has been delay and prevarication by the Commission due to having to respond to overly complex and lengthy submissions. This may, in part, be remedied by imposing strict timeframes and limiting the length or number of submissions and replies that will be accepted. Timeframes and procedures could be discretionary to be agreed between the parties and the Commission with the Commission holding a veto.

Incentive based regulation

MCT believes that to most effectively develop full and open competition in the Australian telecommunications industry, the regulatory regime needs to have the ability to effectively set up the correct dynamics. This would lead to a position where the interests of the incumbents, particularly Telstra, are best served by engaging in competitive, rather than anti-competitive, behaviour.

This can be achieved by giving the ACCC unambiguous powers to the lay down of ex-ante guidelines and regulations that promote this result. As has been observed above, the threat of ex post intervention by the ACCC fails to provide a strong incentive for commercially negotiated outcomes. The process of arbitration and the prospects of appeals can be exploited by dominant operators such as Telstra to slow market entry, which is to their advantage even if they ultimately lose.

An example of this type of regulation can be seen in the conditions imposed on the regional Bell Operating Companies in the US by the FCC. The Bell Operating Companies are only allowed to participate in the long distance service market where they have met with a 14 point competitive checklist. That is, the ability of the incumbent to engage in the provision of contestable services is restrained until it shows that it has met a certain benchmark for competitive behaviour.

As the FCC has observed about the need for such a competitive checklist,

*"We ... identify a minimum list of unbundled network elements that incumbent LECs must make available to new entrants upon request. We believe ... pro competitive goals ... will best be achieved through the adoption of such a list... we believe that negotiations and arbitrations will best promote efficient, rapid, and widespread new entry if we establish certain minimum national unbundling requirements. As the Department of Justice argues, there is "no basis in economic theory or in experience to expect incumbent monopolists to quickly negotiate arrangements to facilitate disciplining entry by would-be competitors, absent clear legal requirements to do so."... Historically, the incumbent LECs have had strong incentives to resist, and have actively resisted, efforts to open their networks to users, competitors, or new technology-driven applications of network technology."*¹

An example of the way in which regulation of this type might be applied in Australia would be for the ACCC publicly provide that Telstra is not able to provide DSL services, either on a wholesale or retail basis, until it is able to demonstrate that potential competitors are in a position to compete on a level playing field through sufficient and equitable access to the unbundled local loop service together with ancillary facilities access services. Regulation of this type would clearly change the dynamic for Telstra. It would be in Telstra's interest to provide access on reasonable terms to meet with the guidelines set by the ACCC in order that it may itself begin operating in the market for this new service.

Enhanced End User Power

The 1997 legislation, like the 1991 legislation before it envisaged a review of the Network Boundary Point (NBP). As far as Macquarie is aware neither of these reviews have been completed or reported on their findings. Macquarie believes that there are considerable potential benefits in unlocking the power of the final loop and placing that power in the hands of the end user.

For example the current NBP is sometimes defined at the building MDF or even the first socket, in principle the greater the distance that is under direct customer control (like internal wiring) the greater the level of competition will be. Macquarie suggests that the NBP should be urgently and fully reviewed as previously proposed. Appropriate amendment would give the customer the ability to choose the infrastructure provider, rather than allowing that decision to remain the preserve of carriers, giving the customer full control over the longest possible leg of the access.

¹ FCC, *First Report and Order: Implementation of the Local Competition Provisions in the Telecommunications Act 1996* (8 August 1996) para 241
<http://www.fcc.gov/ccb/local_competition/sec5.html>

Transparent non-discriminatory pricing

Open non-discriminatory pricing for retail services by the dominant carrier was a feature of the 1991 legislative regime. This blanket approach to pricing was abolished in 1997 and the safeguard of part XIB was introduced in order to curb anti-competitive activity by market participants with significant market power.

What was not fully allowed for in the 1997 regime was the pricing of “bottleneck” services, for which there were no specific non-discriminatory provisions except for a voluntary undertaking provision. Australia is virtually alone in not having some provisions, which require a supplier with significant market power to reveal its pricing of bottlenecks, and to price in a non-discriminatory fashion.

As discussed earlier Australia’s own Schedule on Basic Telecommunications to the WTO (S/GBT/W/1/Add.10/Rev.2) undertakes that interconnection arrangements are transparent and that agreements with a major supplier will be made publicly available (2.4) and that interconnection with a major supplier will be provided under non-discriminatory terms, conditions and rates (2.2(a)).

MCT suggests that this inconsistency could be remedied by adding a provision to Part XIC so that the ACCC has the power to impose an access undertaking on a major supplier of declared services and to enforce pricing under that undertaking in order to ensure that its application is non-discriminatory.

This provision would ensure non-discriminatory and transparent terms and conditions to declared bottleneck services and reduce the role of closed arbitration outcomes. It would also increase the accountability of the Commission by operating in an environment of open information and public decision making.

Much has been said and written of the national benefits that arise in retaining Telstra as an integrated telecommunications operation and not breaking it down into its component parts. Without entering into the debate about the benefits, there are certainly costs associated with a vertical integrated Telstra and the conflicts between its “retail” and “wholesale” ambitions. These costs are not borne by Telstra but by competitors and potential competitors who are denied the same transparent and unencumbered access to Telstra’s underlying bottleneck services. This is not only inequitable it is also inefficient because it enables Telstra to retain much of the benefit through reduced competitive pressure. This ultimately means that there is no mechanism (other than the recently weakened price control provisions) to ensure that these benefits are passed on to end-users.

The ACCC is limited in its ability to equitably and efficiently distribute these benefits between industry players when arbitrating prices for access. MCT proposes that the ACCC should have an obligation to apply a specific vertical integration dividend to TSLRIC costing in order to ensure that the wider benefits of vertical integration do not

unduly impede competition and that the benefits are passed on to end users. This provision could easily be added to the existing access pricing criteria.

Amendment to Part XIB

It is essential that the Commission possess unambiguous jurisdiction over matters it regulates. Part XIB has been of limited direct use in curbing excesses of market power because of the absence of this jurisdictional authority. This has occurred in part because of the requirements to define “telecommunication markets” and “substantial market power” on an individual case basis. Defining markets and market power is a complex, time consuming and often inherently imprecise task that in effect limits the Commission’s jurisdiction due to delay and uncertainty.

MCT suggests that a simplification for invoking a competition notice is that it applies when a carrier or carriage service provider has a dominant position or is in control of an element essential to a party seeking interconnection. This would give the ACCC more targeted and unambiguous powers to intervene in disputes.

For example under the existing rules if Telstra was placing unreasonable constraints on the availability of ULL services, and if the ACCC wanted to take action against Telstra, the ACCC would need to establish that a substantial degree of market power existed. In order to do that it would need to define the markets and then establish power in that market. Telstra may argue that because the ULL market barely exists that it does not have substantial power effectively removing the ACCC’s jurisdiction. Simplification along these lines would give the ACCC greater scope to act effectively against anti-competitive supply issues and eliminate delays and litigation.

Standard Access Obligations

The existing provisions of Part XIC provide for the application of Standard Access Obligations. The provisions require, amongst other things, that the technical and operational quality of declared services are provided on a non-discriminatory basis. The problem with this approach is that it does not provide for an unambiguous service standard to apply which has implications both for the quality of services provided overall and competition issues.

The competition issues arise because the onus of proof is effectively on the access seeker to show that it is receiving services on a discriminatory basis when it has very little, if any, visibility of how the access provider supplies services to itself.

This issue could be simply resolved by giving the ACCC power to determine absolute quality standards where required. For example, a critical issue regarding the supply of the ULLS is the availability and timing of information regarding network modernisation plans. In that case Telstra has asserted that it provides itself with no more than 3 months notice. There is no way to independently verify or enforce this assertion and, even if

there were, it would not resolve the competition issues associated with the need for notice.

This amendment would overcome that issue and lead to application of more enforceable minimum standards where applicable.

Replace the TAF

Industry self-regulation has been, and continues to be a useful model for development of technical compatibility and interconnect regulation. It has not been effective in areas where there are divergent commercial interests. Whilst the sector is dominated by a vertically integrated provider, issues related to access will invariably give rise to divergent commercial interests and therefore the TAF has become ineffective.

The TAF has essentially been required to act on a consensus basis. The result has been deadlocked positions, delays and tying up resources of smaller operators. The role of the TAF could be readily replaced by giving the Minister for Communications its powers to make recommendations acting in response to industry and end user submissions.

Record Keeping Rules

A further remedy to the issue of delivery of bottleneck services is to consider a model that ensures arms length dealing for the provision of wholesale access within vertically integrated operators. This would provide transparency of pricing and ensure equal treatment for competitors, enabling a more focussed measurement of service delivery of bottleneck services.

There are a continuum of responses which can quarantine wholesale services and provide arms length dealing. The most extreme is the creation of a separate entity however this may be unduly onerous, result in organisational inefficiencies and ultimately increase costs. Other responses are to separate the wholesale function through ring fencing of operations and accounts. An even more light handed and possibly effective measure is to rely on record keeping rules to provide transparency and the existing Part XI regulations to address or deter any anti competitive conduct that may be disclosed. To date these record keeping rules have not been enforced due to apparent legal impediments.

Open Information

It is desirable that the Commission's decisions be based on the broadest possible view of the issue at hand. Without substantial input from market participants, the Commission is ill equipped to ascertain the validity of specific factual arguments raised by any particular party. Requiring that information submitted to the Commission be made publicly available ensures that all parties are given the opportunity to provide their views on the validity of the legal and factual arguments raised by other parties. Without the views of various parties regarding the issues and facts raised by other parties, the Commission risks deciding the issues based on a one-sided view of the facts. The parties are usually in

a better position than the Commission to obtain and evaluate information relevant to the issues being considered.

Furthermore, exceptions should not be made to this principle for parties claiming that information essential to the decision making process is competitively sensitive, and that opposing parties should therefore be denied access to it. While it may be necessary for the Commission to keep some information confidential, measures may be undertaken to ensure that such information remains confidential, while at the same time affording interested parties the ability to view and assess the validity of such information. For example, in the United States the FCC and other U.S. agencies make use of a legal device known as a protective order for this purpose. A party may confidentially file sensitive business information upon which it relies. To view the information, other parties must enter into a binding agreement not to share the confidential information with any other part of its organisation, or to use it for any purpose other than providing its views to the regulator regarding the specific issue at hand. Violations of such protective orders are met with severe penalties.

Attachment A

Case Studies

Data Service

The Digital Data Service, which basically consists of terminating tails for data services, was declared for access purposes as part of the transitional arrangements in July 1997. However it became apparent very early that the declared service was inadequate to the purpose of achieving true access, so in late 1997 most members of the industry urged the Telecommunications Access Forum (TAF – the industry self-regulatory body established under Part XI C and comprising most participants in the industry) to amend the service description.

Telstra (a member of TAF) vetoed the proposed amendments and the ACCC subsequently decided to conduct a public inquiry into the changes. The inquiry and other ACCC investigations took place during 1998 and the revised services were finally declared in late 1998. MCT sought delivery of those services at terms consistent with the ACCC's pricing guidelines and Telstra offered unacceptable terms, forcing MCT to seek arbitration.

In mid 2000 MCT abandoned awaiting an ACCC interim determination and sought negotiation of commercial terms of access from Telstra. However there are still a number of open issues, particularly with regard to the delivery of services outside metropolitan areas.

During this three year process (still not concluded) consumers have been deprived of the full benefits of fully competitive provision of services (i.e. lowest cost and maximum range of services).

Local Loop Unbundling

Local loop unbundling is at the heart of service providers being able to access their own customers without the need to duplicate cable, however, it was overlooked in transitional declaration arrangements (in **mid-1997**) and so there are currently no access rights.

There was a lengthy TAF process where Telstra used its veto to block an expedited approach to the unbundling of the local loop and finally, under threat of ministerial intervention, the ACCC held a Declaration Inquiry during 1998. A decision to declare in-principle was made during 1999; however as technical arrangements have not yet been finalised there is no commercially viable access available as at **today**.

Number Portability

Portability is the ability for end users to retain the same telephone numbers when transferring between different service providers. Portability was identified as early as 1995 as being fundamental for the existence of effective competition. Significant delays and obstruction has resulted in the estimated introduction dates for number portability for free call numbers being 16 November 2000 and September 2001 for mobile numbers.

Commercial Churn

Commercial churn has been the only major test for the Part XIB anti competitive behavior provisions. The actions against Telstra were commenced in 1997 and due to the slow response of the ACCC and the unworkable evidentiary requirements of the provisions, were somewhat unsatisfactorily settled in February 2000.

PSTN Undertaking

A key element of the 1997 deregulation regime was to be the availability of standard terms and conditions for access to bottleneck infrastructure. The terms and conditions were to be established by carriers providing undertakings reflecting reasonable and fair terms of access to the ACCC. To date there have been no acceptable undertakings offered by the dominant carriers. Telstra's original undertaking for PSTN services proposed a charge of 4.73 cents per minute in contrast to the ACCC's proposed 1.5 cents per minute.