Telstra Corporation

Submission to the

Senate Standing Committee on
Environment, Communications
and the Arts'

Inquiry

into the

Telecommunications Legislation
Amendment (Competition and
Consumer Safeguards) Bill 2009

Executive Summary

Telstra welcomes the opportunity to respond to the Government's Telecommunications Legislation Amendment (Competition and Consumer Safeguards) Bill 2009 (the "Bill").

Telstra reaffirms its support for a national high-speed broadband network, embodied in the Government's National Broadband Network ("NBN") vision. However, as Telstra has previously stated, the Bill is unnecessary and will make it harder to achieve the Government's core policy objectives in the telecommunications sector – namely, bringing high-speed broadband to Australian consumers and changing the structure of the Australian telecommunications market.

The NBN is the key to achieving both these objectives. However, the Bill will:

- impede the achievement of the NBN vision;
- reduce competition, especially in the mobile and media markets;
- harm consumers, particularly those in rural and remote Australia;
- not necessarily result in industry reform; and
- potentially destroy value for the approximately 1.4 million Australian shareholders who purchased Telstra shares from the Government over the past 12 years and have a significant detrimental impact on our employees.

Therefore, Telstra has no choice but to oppose the passage of the Bill in its current form.

If the Government decides to proceed with the Bill, we believe that it is only sensible that the Senate delay debate until after the conclusion of constructive discussions between Telstra and the Government over the NBN and the completion of the Government's NBN Implementation Study. We would also urge that significant amendments are made to the Bill.

At present, the Bill is premised on the erroneous assumption that competition has failed and that the primary cause of this failure is Telstra's vertical integration. On the contrary, competition has not failed and the casual use of the term 'dominance' to describe Telstra's market position is misleading.

In fact, Australia's telecommunications market continues to see:

- extensive competitive entry – the most recent data from ACMA indicates that there are currently 172 licensed carriers in Australia, with 17 new entrants in the last year and over 670 internet service providers;[1]
- price reductions – the most recent ACCC data identified for the 2007-08 year a 5.5% decline in the real prices for fixed line services, including an 11% decline in long distance charges, a 5.4% decline in the prices for mobile services and a 5.4% decline in prices for DSL broadband; [2]
- substantial product innovation – including faster mobile broadband offers and a vast array of business services such as cloud computing;
- significant customer turnover; and
- amongst the most advanced, highly automated wholesale processes and systems offered by an incumbent anywhere – including British Telecom after 4 years of separation.

If there is a failure in the telecommunications industry, it is in the critical area of investment. Many market participants are simply not making enough capital investments, especially in high-speed broadband infrastructure. In the five years to June 2009, Telstra made capital investments totalling

[1] Australian Communications and Media Authority, *ACMA Communications Report 2007-08*, November 2008, pp. 23-24.

[2] Australian Competition and Consumer Commission 2008, *Changes in the prices paid for telecommunications services in Australia, 2007-08* Melbourne, p.101.

more than $23 billion. That equates to 70% of all capital investment for the telecommunications sector.

To put that in proportion, Telstra has a 62% share of the market, but it is ploughing far more than its share back into capital to meet the future needs of the market. Telstra's revenues may be three times larger than its nearest competitor, but its investments are four times greater. In short, Telstra is the only telecommunications company in the nation pulling its weight on infrastructure investment. It is reasonable to conclude that Telstra's competitors have decided it is better, under the current regulatory regime, to ride on the back of Telstra's investments than risk their own capital.

The failure of the private sector to invest in fixed high-speed broadband infrastructure is in part a function of the cost of deploying optical fibre in a country like Australia, with such a large land mass and relatively small population. However, it is also a function of the significant investment uncertainty created by the current regulatory regime. Australia has the unique situation where the competing cable network operator prefers to use cheap regulated access to the Telstra copper network, rather than upgrade and utilise its own cable infrastructure.

The Government's NBN vision seeks to partially address the issue of cost through direct government investment. In contrast, this Bill does not address the regulatory uncertainties faced by private investors, including Telstra shareholders.

Functional separation

A central component of the Bill is the functional separation of Telstra. The Bill and associated Explanatory Memorandum fail to take into account what international experience has demonstrated – that a functional separation of this magnitude takes years to implement, disrupts network and product investment cycles, has a detrimental impact on consumers and wholesale customers, and, ultimately, fails to deliver greater transparency and equivalence to access seekers. That is why most OECD countries have refused to follow the example of the United Kingdom and New Zealand and go down the functional separation route set out in the Bill.

One outcome is certain, functional separation will, for many years, divert Telstra management and resources away from migration to the NBN. At a time when Australia needs more investment in next-generation technologies, the only telecommunications company with a track record of sustained investment will be taken offline.

Wholesale supply terms and processes have improved significantly since 1997, but perceptions have not caught up and have been coloured by the fierce debate over future fibre networks. Telstra remains committed to taking further steps to address the perceived need for greater equivalence and transparency during the transition to the NBN. What is required is a solution that is simple, cost-effective and quick to implement; does not detract from the industry's ability to help the Government implement its NBN plans; and, importantly, does not degrade customer service. Functional separation is not that solution.

A more effective way forward lies in embedding equivalence in Telstra's new network and IT systems, which are used to provision, operate and maintain all retail and wholesale services: to design equivalence into the 'network DNA', rather than inefficiently divide the Telstra organisation into separate virtual companies.

In brief, the Bill needs to be amended to ensure functional separation is not unreasonably burdensome on Telstra shareholders, does not put at risk customer service and does not impede the transition to the NBN.

Structural separation

The Bill seeks to create the incentive for Telstra to structurally separate before the NBN is completed. Structural separation of incumbent telecommunications carriers has been considered periodically in Australia and overseas. In the vast majority of cases, including Australia, it has been rejected as a policy where the costs overwhelmingly outweigh the benefits. The considered view has been that structural separation destroys value in the industry. In the U.S., where it was implemented, it has been subsequently unwound.

The new proposed Part 33 of the *Telecommunications Act 1997* should therefore be deleted.

Regardless of the legislation, Telstra's position on structural separation is clear. It would only be considered if the Board and Management of the company were convinced it were in the best interests of Telstra shareholders. Telstra will continue to talk with the Government, but we cannot agree to proposals that fail to give fair value to our shareholders. We will also continue to inform and consult shareholders as appropriate.

Access to spectrum

The Bill proposes to deny Telstra access to spectrum required for the future generation of wireless services unless we agree to vertical and horizontal structural separation. Given that the NBN delivers the Government's preferred industry structure and that wireless is not a regulated service there is simply no policy rationale for such exclusion. The Australian mobile industry is highly competitive, with three separate national networks. Taking Telstra out of the market for next generation spectrum will make the mobile market less competitive and punish the telecommunications company that has not only led innovation but invested in the world's fastest mobile wireless network covering 2.1 million square kilometres.

Denying Telstra access to spectrum will undoubtedly hurt consumers, particularly those in rural and remote Australia, by depriving them of an upgrade path with reduced competition and innovation. It will put at risk Australia's place as a global leader in the mobiles market. Telstra staff would face greater job uncertainty if Telstra is excluded from this growth market. Taxpayers would also lose as a result of lower payments for the spectrum; and by potentially exposing them to compensation claims if in substance, rather than form, Telstra is forced to divest assets to participate in future spectrum auctions.

Denying Telstra access to spectrum would also do nothing to achieve the NBN.

The relevant sections of proposed Part 33 of the *Telecommunications Act 1997* should be deleted accordingly.

Divestiture of FOXTEL/HFC

The Bill also seeks to force Telstra to divest HFC cable and its interest in FOXTEL (along with structural separation) in order to avoid being excluded from spectrum for future generation mobile services.

Telstra's shareholders have invested significant sums in these assets. To require them to divest their interests in these assets just as they are becoming profitable is unjust and raises questions of sovereign risk.

There is no consumer or competition benefit from requiring Telstra to sell these assets. Even the ACCC, which has previously advocated divestiture of the HFC cable, in its recent submission to the Government's regulatory reform consultation, recognised that, with the rollout of the NBN, there will be fewer pro-competitive benefits from requiring Telstra to divest its HFC network. Moreover, Australian consumers would likely be worse off from the forced divestiture of FOXTEL as a result of increased concentration in media markets, with News Corp and Consolidated Media Holdings being the most likely acquirers of Telstra's interest in FOXTEL should Telstra be forced to divest.

The relevant sections of proposed Part 33 of the *Telecommunications Act 1997* should be deleted accordingly.

Changes to the access regime

Telstra supports changes to Part XIC of the *Trade Practices Act 1974* that will more closely align it with the access pricing arrangements used in other industries. However, because the Bill contains none of the explicit and inherent safeguards for access providers present in other regulatory frameworks, it gives the regulator much greater discretionary power than in those other industries. Indeed, this Bill is highly unusual in that it gives the regulator significant powers without setting out very careful prescriptions on how those powers should be used.

By failing to give sufficient guidance to the regulator on how its significant new powers should be exercised, the Bill gives telecommunications infrastructure investors far less certainty on how their investments will be regulated than investors in all other regulated industries – even if their infrastructure is literally in the same trench. This oversight will inevitably reduce investment (or increase cost) to the detriment of Australian consumers and employment in the Australian telecommunications industry.

The changes to Part XIC need to be deferred until clear policy guidance to the regulator, along the lines of other industries, is included in the legislative package.

Changes to the Anti-Competitive Conduct Regime

The Bill exempts the ACCC from procedural fairness obligations. There is no policy justification for a Government agency not to adhere to normal administrative processes that support fair decisions and efficient use of public resources. Indeed, as a 'model litigant', the ACCC should at all times be required to meet an even higher standard of procedural fairness.

The relevant changes to Part XIB should be deleted accordingly.

Structure of this submission

This submission is divided into three sections:

Section 1 details the effect this Bill would have in practice. It is clear that, if implemented as currently drafted, the Bill would actively harm core policy objectives including:

- addressing the equivalence and transparency concerns associated with vertical integration;
- promoting competition, including competition in the vibrant mobiles and media sectors of the Australian economy;
- promoting investment in new and innovative technologies;
- promoting economic and social development in rural and remote Australia; and
- ensuring a smooth transition to the NBN.

Section 2 addresses the key misconceptions underpinning the legislative package. The data clearly shows that the Australian telecommunications market is far more competitive than the selective and misleading material provided in the Explanatory Memorandum would suggest. The facts also show that the problems with the current regulatory regime are far more complex than the prevailing and self-serving industry view that "it's all Telstra's fault".

Section 3 summarises the specific amendments Telstra believes are required to the regulatory package.

While we are disappointed the Government has felt it necessary to introduce the Bill, we remain committed to working constructively with the Government to fulfil its NBN vision in a way that is in the best interests of our shareholders, our staff, our customers and the nation.

To reiterate, Telstra submits that this Bill should not be passed in its current form. Rather, consideration of the Bill should be deferred until after the conclusion of constructive discussions between Telstra and the Government over the NBN and the completion of the Government's NBN Implementation Study. In any event, significant amendments to the Bill are required to address the very real problems the Bill, if enacted, would create.

1. Impacts of the legislation

The Explanatory Memorandum makes clear that this Bill is intended to promote a range of policy objectives, including:

- addressing the equivalence and transparency concerns associated with vertical integration;
- promoting competition, including competition in the vibrant mobiles and media sectors of the Australian economy;
- promoting investment in new and innovative technologies;
- promoting economic and social development in rural and remote Australia; and
- ensuring a smooth transition to the NBN.

Telstra submits that, if the Bill were implemented as currently drafted, these core policy objectives – objectives Telstra supports – would not be achieved. Instead, they would be significantly undermined.

Vertical integration – equivalence and transparency

The Explanatory Memorandum places great stress on fixing the so-called 'problem' of vertical integration.

Vertical Integration is not the unambiguous negative that the legislative package seems to assume. It reduces costs and facilitates innovation – creating benefits that can, in a properly structured access regime, be enjoyed by all consumers. In a major review of almost 200 studies of vertical integration, Lafontaine and Slade concluded by expressing surprise at the weight of evidence in favour of integration:

> *...under most circumstances, profit-maximising vertical integration decisions are efficient, not just from the firms' but also from the consumers' point of view. Although there are isolated studies that contradict this claim, the vast majority support it. Moreover, even in industries which are highly concentrated so that horizontal considerations assume substantial importance, the net effect of vertical integration appears to be positive in many instances. We therefore conclude that, faced with vertical arrangements, the burden of evidence should be placed on competition authorities to demonstrate that the arrangement is harmful before the practice is attacked.*[3]

Joskow draws a similar conclusion, suggesting that regulatory hostility to vertical integration is misplaced except in extreme conditions:

> *...there is substantial support in the empirical literature for various efficiency motivations for vertical integration. There is minimal empirical support for anticompetitive foreclosure motivations. This suggests that there is little empirical support for the anti-trust law's traditional suspicion of and hostility towards vertical integration and related non-standard vertical contractual arrangements, except under extreme conditions...*[4]

Given the weight of evidence in favour of integration, and given the major and irreversible interventions proposed, Lafontaine and Slade's 'burden of evidence' should apply to the Bill. It should be up to the proponents of separation to demonstrate that the current arrangement is so harmful that the very considerable costs involved in separation are justified.

Some proponents of separation have used structural reforms in other utility industries to support the case for the structural separation of Telstra. However, on closer inspection, the separation

[3] F. Lafontaine and M. Slade, (2007) 'Vertical integration and firm boundaries: the evidence', 43(3) *Journal of Economics Literature* pp.629-685.

[4] P. Joskow, 'Vertical Integration' (2006), available at econ-www.mit.edu/files/1191.

requirements in these other cases are less extensive than those that already apply to Telstra under operational separation and, in any event, have caused problems. For instance:

- separation between retail and local distribution networks (equivalent to Telstra's Customer Access Network) has not been required in electricity;[5]
- separation in rail has failed – with NSW returning to vertical integration[6] and the Victorian metro rail and tram franchisees financially failing;[7] and
- separation in gas and electricity has not resulted in a reduction in regulation, indeed over time more and more regulation has proven necessary to deal with the investment coordination issues that arise from vertical dis-integration.[8]

Equivalence and Transparency: In practice the key concern with vertical integration appears to be the issue of equivalence and transparency – how to give access seekers surety that the terms and conditions of access they obtain are equivalent to those that Telstra provides to its own retail division.

There is clearly a gap between perception and reality in this debate. Kip Meek, the former Ofcom Commissioner responsible for introducing functional separation in the United Kingdom, has said that, unlike the UK, there is simply no evidence of severe problems of discrimination – discrimination being the motivation for the functional separation of BT – in Australia.[9] The ACCC has never successfully prosecuted Telstra for the kind of extensive discrimination that would surely be required to justify functional separation.

Telstra acknowledges that, despite our ongoing efforts, the ACCC and many of our wholesale customers continue to express concerns that access seekers perceive they are not able to acquire declared services on an equivalent basis to the services that are provided to Telstra's own customer-facing units. While the structurally-separated wholesale only NBN is the medium term solution to these perceptions, Telstra understands that an interim solution is being sought.

There is a solution that is simple, cost-effective and quick to implement, does not detract from the industry's capacity to assist the Government to implement its NBN plans and, importantly, does not degrade customer service or benefit. This solution leverages Telstra's IT transformation to require that:

- the underlying operations support systems (OSS) are designed and operated in a customer agnostic fashion;
- the wholesale business unit "plugs into" these customer agnostic OSS at the same level and with the same functionality as the retail customer facing business units;

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[5] For example, in NSW, Integral, Country Energy and Energy Australia are vertically integrated in networks and retail supply. In South Australia and Victoria, energy retail and networks are separated, but this was a commercial choice not a Government mandate.

[6] Following inquiries into major rail accidents in NSW, the Rail Infrastructure Corporation, which owned the tracks, was combined with State Rail, which operated the passenger trains, to form RailCorp in 2004: see Railcorp 2003-2004 Annual Report http://www.railcorp.info/publications/annual_reports.

[7] Just three years after privatisation, the Victorian public transport system was in crisis: National Express walked away from its contracts and Yarra Trams and Connex were facing insolvency. The Victorian Government engineered a consolidation of metro systems and took country services back into public ownership. A non-profit body – MetLink – was established between private and public transport operators to run network-wide functions such as planning, ticketing and timetable publication and was partly funded by State: see report of Victorian Auditor General: http://archive.audit.vic.gov.au/reports_par/ptfranchising_report-1.pdf and http://www.metlinkmelbourne.com.au/news/.

[8] For example, creation of a central transmission planner within the Australian Energy Market Operator at the direction of the Ministerial Council on Energy, 13 April 2007: see http://www.ret.gov.au/Documents/mce/_documents/MCE_Direction_to_AEMC20070713112430.pdf; and report of the Australian Energy Market Commission: http://www.aemc.gov.au/Media/docs/National%20Transmission%20Planner%20Final%20Report%20to%20MCE-448faa16-c4c0-4f52-a922-114975692985-0.pdf

[9] Kip Meek, Operational Separation in Australia and the UK, Annex A, Telstra submission on vertical integration, 25 June 2008.

- the interfaces, processes and systems offered to wholesale customers provide a high level of automation, are designed to meet wholesale customer needs, and permit wholesale customers to compete on an equivalent basis with the retail customer facing business units;
- wholesale customer information be held in logically separated modules within Telstra's systems which cannot be accessed by employees in the retail customer facing business units;
- external review, including by the ACCC, of these interfaces and systems to allow verification that they are delivering equivalence and providing information security;
- the operational separation around the wholesale business unit be increased to reinforce its autonomy; and
- a Telecommunications Adjudicator, working with the ACCC, be established to help resolve systemic technical issues between Telstra and wholesale customers – and that decisions would be binding on Telstra.

The practical effect of this approach would be to embed equivalence in Telstra's network and support systems and processes – equivalence would be part of the "network DNA".

Functional separation: In contrast, the proposed solution in the Bill – functional separation – will not improve equivalence and transparency in a cost effective, timely manner during transition. Whatever benefits functional separation may bring in the longer term, in the short to medium term it will needlessly impose costs, needlessly consume resources, and needlessly disrupt customer service. Functional separation will be to the detriment of consumers and industry in the short term – the very period for which a solution is being sought.

Specifically, the international evidence and Telstra's own analysis demonstrates the following implications of functional separation:

- **Harms retail consumers:** The adverse impact on retail customer service, as a result of the need to implement systems changes required by functional separation at BT, was widely reported in the UK in 2007.[10] Retail service levels fell significantly in the period after separation because BT had to rebuild its systems and processes from the ground up. BT retail service levels have still not recovered - in 2008 BT was named the UK's worst landline provider in a customer satisfaction poll, with the poor service attributed to the change to new computer systems – changes mandated in part by separation.[11] There is no reason to believe similar retail customer impacts would be avoided in Australia. On the contrary, Telstra has almost completed the implementation of an IT transformation which has enabled Telstra's front-of-house customer service representatives to view, in a single system, all of a customer's services with Telstra. This systems transformation has been an enormous exercise and not without adverse customer impacts during its implementation that led to increased levels of customer complaints. Imposing a requirement that certain of Telstra's retail services should be supplied on a functionally separated basis would require these brand-new systems to be scrapped and rebuilt. Worryingly, this may undermine the customer-centric capability in which Telstra has invested heavily, lengthening customer handling times and necessitating additional hand-offs.
- **May reduce rather than enhance wholesale customer service:** In the UK, poor wholesale service levels – substantially below the levels currently provided to wholesale customers by Telstra - were a key rationale for functional separation. However, in the first two years of functional separation of BT:
  - Openreach's provisioning of unbundled local loops ('ULLS') and shared loops ('LSS') dropped by 20% in the immediate period after the equivalent systems requirement commenced, consistently failed to meet target provisioning times, and showed only modest improvements over the next two years;[12]
  - there was no improvement in the timelines for provisioning of business wholesale line rental ('WLR') lines, with only 86% of new lines being provided on time in

[10] See, for example, A. Tims, 'Why is BT failing to activate new telephone lines?', *The Guardian*, 5 October 2007; L. Bachelor, 'BT sends out busy signal as customers wait to get a line', *The Observer*, 26 August 2007.

[11] M. Hickman, 'It's not so good to talk – BT is named worst landline provider', *The Independent*, 8 April 2008.

[12] Ofcom, December Evaluation Report, para 6.48.

both July 2005, pre-functional separation, and in October 2007, two years after functional separation (for the majority of the intervening period the performance was actually lower than 86%);[13]

> for business and residential WLR, the average number of faults per 100 lines actually increased after functional separation;[14] and

> the time taken to fix faults has improved slightly since functional separation, but Ofcom concluded that "Openreach has been unable to maintain a reliable standard of service."[15]

To implement functional separation, Telstra's wholesale resources, IT systems and processes would require major modifications to support Telstra's retail business units and thus accommodate at least a four-fold increase in business volumes. This would require additional wholesale resources, a redistribution of numerous front-of-house and back-of-house functions across the retail and wholesale businesses, along with numerous IT systems and process changes. As with any system changes, customer disruption is inevitable as systems and processes are re-engineered, and wholesale resources are diverted to deal with a massive new 'customer' in Telstra's retail business. The evidence cited above from the UK is precisely to this effect.

- **Harms shareholder interests:** Despite a reassurance in the Explanatory Memorandum that "separation is good for the share price" (p. 31) Government-imposed functional separation, as foreshadowed by the Bill, will impose significant costs and distract resources for a significant period of time:

> BT commenced implementation of functional separation in January 2006 and implementation is still not complete. The official costs to date total £153 million (AUD 273 million).[16] Unofficial estimates put the costs much higher – possibly between £600-800 million.

> Telecom New Zealand commenced implementation of functional separation in April 2008 and, while the organisational changes have been implemented, the requirements that Telecom Retail acquire Telecom Wholesale services are to be implemented over many years – out to 2015. The reported cost to implement functional separation at Telecom New Zealand is NZ$200 million (more than AUD$160 million).[17]

> Telstra's best estimate of the cost of implementing functional separation, on the basis of Telstra's internal estimates and the experience of BT in the UK and Telecom New Zealand, noting the minimal guidance provided by the Bill on what the Government is likely to require, is in the range of $500 million to more than $1.2 billion.[18]

Promotion of competition

The Explanatory Memorandum states that "the Government's key objective is to promote an open, competitive telecommunications market to provide Australian consumers with access to innovative and affordable services" (p.5).

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[13] See Ofcom, *Service level guarantees: incentivising performance*, 10 December, 2007, paras 4.6 and 4.7.

[14] See Ofcom, *Service level guarantees: incentivising performance*, 10 December, 2007, para 4.7.

[15] See Ofcom, *Service level guarantees: incentivising performance,* 10 December 2007, para 4.8.

[16] See BT, *BT Group Plc Annual Report and Form 20-F 2009,* p. 37 *BT Group Plc Annual Report and Form 20-F 2007,* p. 40.

[17] See Telecom New Zealand, *Response to Determination on Operational Separation,* 26 September 2007.

[18] Telstra's CFO disclosed the NPV cost impact of Telecom New Zealand- and BT-style functional separation at Telstra's annual results on 13 August 2009 as 4 cents per share (cps) and 10cps respectively. Telstra has issued 12.443 billion shares.

However, key elements of the legislative package have the potential, if enacted, to significantly reduce competition in the Australian communications market – particularly in the rapidly evolving mobile and media market segments where, to date, a more benign regulatory setting has allowed Telstra and others to invest and innovate. Indeed, aspects of this Bill seem designed to penalise Telstra for its superior performance in competitive markets.

Limits on access to LTE spectrum: The Bill excludes Telstra acquiring or using spectrum for advanced wireless broadband services (LTE spectrum) in certain circumstances.[19] LTE spectrum is required for the roll-out of the next generation of high speed mobile broadband services to Australian consumers – sometimes referred to as 4G.

In its current state, the mobile market in Australia is recognised as extremely competitive.[20] Australia now has three national major mobile network owners providing national 3G wireless broadband services. There are also a number of smaller players entering the wireless broadband market using a range of technologies and spectrum bands. There has also been rapid growth over the past two years in wireless broadband.[21]

Denying Telstra access to LTE spectrum will mean that Telstra cannot continue to invest and innovate to provide customers with world-leading mobile services. That means there will be less competition, less investment, less innovation, less employment and, potentially, higher prices. This decision will penalise consumers and businesses, stymie innovation, and cruel competition. Currently, Australia is a leader in the provision of mobile broadband services. Unless a competitive market is maintained where providers are driven to invest in upgraded services and new technologies, improvements to mobile broadband services will not be as prompt and will no longer be national. The newly-created mobile duopoly will focus service enhancements on large markets such as Melbourne, Sydney and Brisbane.

The Explanatory Memorandum does not explore or seek to justify the negative competition, employment and consumer impacts of the exclusion of Telstra. Nor does it explain how a potential 4G duopoly between Singtel Optus and Vodafone Hutchison Australia – in those parts of mainly urban Australia that they choose to serve – is in the interests of Australian consumers. Such an outcome clearly contradicts the Bill's stated objective of promoting competition. Australian consumers, particularly those in rural and remote Australia, will bear the costs of reduced competition, to the benefit of these competing carriers – and their shareholders.

Divestiture of FOXTEL/HFC: The Bill also requires Telstra to divest its share of FOXTEL and its ownership of its HFC network should it want to acquire LTE spectrum. The argument in the Explanatory Memorandum is that divestiture of these assets would increase competition. In fact, there is no pro-competitive effect arising from the divestiture of either asset.

Requiring Telstra to divest its FOXTEL holding will have no effect in downstream markets – such as mobiles or broadband – because, since November 2002, FOXTEL has been bound by the provisions of a Section 87B Undertaking to the ACCC to make available to operators of cable, satellite or microwave networks the FOXTEL subscription television service and to do so on terms and conditions approved by the ACCC. These undertakings mean that Telstra's competitors have the opportunity to access and bundle FOXTEL content. In short, there is no enhancement to competition arising from Telstra divesting its share in FOXTEL.

Far from being pro-competitive, a requirement that Telstra sell down its FOXTEL interest is more likely to result in greater concentration in media markets as News Ltd and Consolidated Media Holdings are the most likely acquirers of Telstra's interest. In other words, rather than increasing competition, requiring Telstra to divest FOXTEL would be likely to result in the consolidation of media assets in Australia to the detriment of Australian consumers.

Similarly, the competition arguments for the divestiture of the HFC network have always foundered on the simple fact that there is an alternative network – the Optus HFC cable – in place. The imminent arrival of the NBN surely suggests that changing the ownership structure of the Telstra HFC will in no way affect the competitive dynamics on the ground. Even the ACCC, which has previously advocated

[19] Specifically, Telstra can only acquire or use LTE spectrum if it voluntarily structurally separates and divests its share in FOXTEL and its ownership of its HFC network, unless the latter requirements are waived in the Minister's discretion.

[20] ACCC (2008) *Telecommunications Competitive Safeguards* 2007-2008, p.32.

[21] ACMA (2008) *Communications Report 2007-2008,* p.46.

divestiture, in its recent submission to the Government's regulatory reform discussion paper, recognised this when it said "if the NBN Co is independent of Telstra, there may be fewer pro-competitive benefits in the longer term from requiring Telstra to divest its HFC network."[22]

Promotion of investment

According to the Explanatory Memorandum, "stakeholders' main areas of concern ... [include] that Part XIC in its current form does not provide sufficient regulatory certainty for investment" (p. 48). Telstra agrees and has joined with the ACCC and others in the industry in calling for changes to Part XIC of the *Trade Practices Act* to improve regulatory certainty to promote much needed investment in the Australian telecommunications industry.

Unfortunately, the changes proposed in the Bill to Parts XIC and XIB have the potential, if enacted, to significantly increase regulatory uncertainty and, hence, reduce investment in telecommunication markets. The Bill proposes to afford the regulator unconstrained powers of intervention that are unparalleled in any other industry in Australia.

Part XIC changes: Resolving the cost of the underlying copper network for access pricing purposes is the key to improving regulatory certainty. All access pricing exercises are complex; however, Part XIC has been particularly contentious because, unlike other industries, the cost of the underlying asset base is re-estimated every few years (whereas in gas and electricity the regulatory asset base was resolved at the outset, with subsequent disputes confined to a relatively small number of issues). It is this fact, plus the lack of agreement on the most appropriate method of assessing the asset base, that has unsurprisingly led to a high level of disputes.

Telstra, therefore, welcomes changes within the Bill that seek to align the regime more with that used in other industries – in particular moves towards the use of a Regulatory Asset Base ("RAB") approach to access pricing. However, the Bill goes only half-way to that solution: it introduces the concept of a RAB and grants extensive price-setting powers and discretions to the ACCC, but contains none of the safeguards that are present in other industries. As a result, infrastructure investors such as Telstra, mobile network owners and NBN Co. are given no regulatory certainty.

The key differences between the proposed telecommunications regime and the gas and electricity market regimes, which dramatically increase regulatory uncertainty, are set out below.

- **Binding rules of conduct:** The Bill gives the ACCC the power to make binding rules of conduct at any time. It can specify the contractual terms of access, force an access provider to spend capital, and require access seekers to purchase services. The binding rules can be general, or targeted at particular industry players. There is no requirement for procedural fairness, and no stated process that must be followed. This power is unprecedented in any Australian industry.
- **Regulatory framework:** Under the Bill, the ACCC will be largely responsible for developing the framework to regulate access to declared services and implementing that framework through the access determination power. In contrast, in gas and electricity, the regulatory framework has been specified by a separate rule maker, either the Australian Energy Markets Commission ('AEMC') or the Ministerial Council on Energy ('MCE'), and then implemented by the regulator. The proposal to grant unilateral powers to a regulator is unprecedented.
- **Price setting:** The Bill gives the ACCC the power to unilaterally determine what prices best reflect the framework it imposes. In contrast, under the relevant gas and electricity regulatory frameworks, the process commences with a proposal from the service provider. The regulator must then consider that proposal against a clear set of regulatory provisions and principles.
- **No merits review:** While significant new regulatory powers are embodied in the Bill's amendment to Part XIC, merits review is conspicuously absent. The principal objective of merits review, as stated by the Administrative Review Council ('ARC'),[23] is to ensure that administrative decisions are correct (in the sense that they are made according to law) and preferable (in the sense that it is the best decision that could have been made on the basis of the relevant facts). Typically, such rights are only removed where regulators have limited discretion. That is not the case here. Abolishing appeals on the merits of the ACCC's decisions

[22] ACCC submission to Government regulatory reform discussion paper, June 2009, p.9.
[23] See http://www.ag.gov.au/agd/WWW/arcHome.nsf/Page/FAQS#a6.

only increases regulatory uncertainty, especially in view of the dramatically expanded powers. Telecommunications will be the only national utility industry in which there is no merits-based review of the regulator's access pricing decisions.

Part XIB changes: The major change to Part XIB is the removal of the requirement of procedural fairness relating to the issue of a 'Part A' Competition Notice. This reform stems from the Federal Court's decision in April 2007 to overturn the most recent competition notice issued by the ACCC because the ACCC had failed to afford Telstra procedural fairness. The Court said:

> *Telstra was not given a reasonable opportunity to consult, or to comment and make submissions, or to change its conduct to avoid the issue of the Competition Notice. Telstra was denied the opportunity to be heard in respect of the new and different subject matter. The statutory scheme, which included the right to such opportunity in order to afford procedural fairness, was not complied with. It follows that Telstra was denied procedural fairness.*[24]

This judgment is not justification for removing rights of procedural fairness from potential recipients of Competition Notices. If anything, it is justification for increasing procedural fairness and accuracy in ACCC decision making. The Government's underlying concern with Part XIB is the lack of speed around the issue of Competition Notices. The simple fact is that a competition notice is an administrative instrument. If used incorrectly, it is potentially damaging, hence the need for proper administrative process and administrative law protections. If not, how can any investor have confidence that the power will not be misused?

In summary, the changes to Part XIC and Part XIB contained in the Bill will significantly increase regulatory uncertainty by allowing *unfettered* regulatory discretion. This will not provide the industry with the guidance and clarity it requires during a period of significant transition. Investors in any infrastructure project in Australian telecommunications will, under the provisions of this Bill, have far less certainty on how their investments will be regulated than investors in all other regulated industries. This will inevitably reduce investment (or increase its cost) to the detriment of Australian consumers, an outcome that directly contradicts one of the Bill's core objectives.

Social and economic development of rural and remote Australia

The Government's NBN announcement includes an ambitious agenda for those Australians that live in more isolated parts of the country. Unfortunately, key elements of the legislative package have the potential, if enacted, to significantly reduce investment in new and innovative services in rural and regional Australia.

Limits on LTE spectrum: As noted above, excluding Telstra from access to LTE spectrum would significantly harm customers, especially those in rural and remote Australia. The Telstra Next G™ Network is by far the largest mobile network in Australia, covering more than two million square kilometres – double the geographic size of its nearest competitor. Telstra is recognised globally as being a leader in innovation and service delivery. The Next G™ Network's superior coverage is now relied upon by a range of customers in different industries such as farmers, mining companies, aquaculture companies, research organisations and the Royal Flying Doctors – all of whom have come to rely on it for both its higher speeds and better coverage, all of whom would rightly expect Telstra to continue to invest to improve data speed and coverage.

Denying Telstra the opportunity to continue to invest in this network to provide all Australians – not just those in capital cities – continued access to world-leading technology has no sound policy justification and can only harm the thousands of consumers in rural and remote Australia who have come to rely on the Next G™ Network.

It is difficult to believe that other carriers, such as SingTel Optus or Vodafone Hutchison Australia, will fill the gap. These carriers have no plans for their existing networks to match Telstra's coverage. These carriers have never focused on serving rural and remote Australia, preferring instead to focus on areas of high population density in order to maximise their profits.

The surge in wireless broadband in Australia over recent years can be pinpointed back to Telstra's decision to build the Next G™ Network. That investment spurred Optus and Vodafone to make similar investments and, on seeing the growth and potential in the market, a host of smaller players chose to invest in their own infrastructure. The ACCC has expressly acknowledged that "more extensive

[24] Telstra Corporation Limited v Australian Competition and Consumer Commission (No 2) [2007] FCA 493 at 181.

competition was evident in mobile services, with Telstra's investment in 3G networks in recent years driving much of this development".[25]

In its approval of the merger to create Vodafone Hutchison Australia (VHA), the ACCC recognised the need for significant investment to enhance mobile network capacity as required by bandwidth-hungry mobile broadband services.[26] If Telstra is not in the market with LTE it is unlikely that Optus and VHA would continue to make investments in a truly national 4G network. What is more likely is that they will be under far less pressure to spend capital on their infrastructure in rural and remote Australia and more of their capital will be directed to their mobile network businesses in other countries. Locking Telstra out of LTE spectrum will harm broadband infrastructure competition in the areas where it is most difficult to achieve.

Ensuring a smooth transition to the NBN

The Explanatory Memorandum clearly views the Bill as part of the move to NBN. Unfortunately, a number of elements in the package have the potential to significantly hamper the transition to the NBN – particularly the diversion of resources inherent in functional separation; the high degree of uncertainty around any structural separation undertaking; and the lack of recognition that service performance is impacted by geographic factors and the absence of vertical integration.

Diversion of resources away from NBN migration: The time to implement functional separation will be more than six years if the BT functional separation model is imposed. BT itself will have taken nine years when its implementation is complete. BT's biggest problems have been in migrating retail legacy services to the new equivalence products. The same scenario in Australia would create a double migration for most customers – from current legacy Telstra retail services to new legacy retail services based on legacy wholesale products and then to the NBN. This double migration doubles the risk of customer service and billing problems, and, with millions of lines involved, doubles the potential for service chaos. It is for these reasons that Telecom New Zealand is allowed to bypass the requirement to migrate legacy retail products to legacy wholesale products.

In any event, Telstra could not commence implementation until its new IT systems were fully implemented in 12 to 18 months' time. The greatest source of expense and waste associated with the BT functional separation model was the requirement to re-engineer and/or duplicate IT systems.

If Telstra is required to functionally separate along the lines of the BT model its human, capital and systems resources would be fully engaged in a significant IT transformation to enable Telstra Retail to buy from Telstra Wholesale. Those same resources would not simultaneously be available to develop new systems to purchase fibre access from NBN Co. In practice, Telstra would be forced to focus on meeting its functional separation milestones and defer any transition to the NBN until after separation was implemented.

Uncertainty around any structural separation undertaking: The Bill, as currently drafted, contains a number of provisions that create significant uncertainty for the Telstra Board and management when considering whether to commit to structural separation. For example, the Minister's power to waive the requirements for Telstra to divest either or both of the HFC or Telstra's interest in FOXTEL does not flow automatically from the acceptance of a structural separation undertaking by the ACCC. This means Telstra has no certainty that it will, in fact, receive the benefit of those waivers if it commits itself to a structural separation undertaking – an undertaking from which, under the Bill, Telstra may not withdraw. It is not clear that Telstra could lodge a 'conditional' structural separation undertaking.

Similarly, there is no certainty that – if Telstra submits a structural separation undertaking, the ACCC accepts that undertaking and Telstra then implements that undertaking– Telstra will be allowed to bid for LTE/4G spectrum. The Minister retains the power to exclude Telstra from LTE spectrum when it becomes available.

Telstra cannot be certain that any waiver will not, in the future, be revoked since, under the *Acts Interpretation Act*, a power to make an instrument carries with it a power to revoke the instrument unless the contrary intention appears. Unless that contrary intention is present (which is not at all clear) it does not matter whether the ACCC accepts a structural separation undertaking and the

[25] *ACCC Telecommunications Reports 2007-08*, p.iii.

[26] ACCC, *Public Competition Assessment on Vodafone Group plc and Hutchison 3 Australia Pty Limited – Proposed merger of mobile operations*, 24 June 2009, paras 41, 77, 78.

Minister initially grants the waivers for FOXTEL and HFC divestment, because the Minister could revoke those waivers before the LTE/4G spectrum becomes available. This point is not made to call into question the bona fides of any waivers entered into by the Minister, but is material because there is no guarantee that the current Minister will have oversight of this portfolio in 2013.

Other issues are that, with the removal of the ordinary access undertaking provisions, there is no obvious statutory machinery to allow for the resolution or "locking in" of access prices for existing declared services as part of a structural separation undertaking proposed by Telstra. Similarly, there is no obvious ability for the Government to extend the interest that Telstra may acquire in NBN Co. beyond the 15% cap imposed through the adoption of the definitions of 'control' from the *Broadcasting Services Act*.

Service performance: The changes in the Bill with respect to consumer safeguards in the main introduce new powers for the Minister to make standards, rules and benchmarks. While Telstra trusts that the Minister would consult on the making of standards, rules and benchmarks to ensure a proportionate, effective enforcement regime, there are no safeguards against burdensome regulations that do not recognise Telstra's unique challenge of providing quality services across Australia's vast and challenging terrain. Moreover, Telstra notes that the USO remains uncosted and underfunded. The Government's long term vision for the broader USO and the role of NBN Co. is not clear from the Bill, yet is a key issue to be addressed in the transition to the NBN.

The Bill gives the Minister a new power to make standards and to set minimum compliance benchmarks concerning the supply or proposed supply of wholesale carriage services to a wholesale customer where the supply is capable of affecting the capacity of the wholesale customer to comply with the Customer Service Guarantee ('CSG') (i.e. enabling supply of a standard telephone service). However, these changes do not recognise the current boundaries of wholesale and retail provision, nor the as yet undefined boundaries once the NBN is operational. For example, today, when providing a product such as ULLS to an access seeker, Telstra Wholesale is not aware or advised of the purpose for which the service is purchased. Even if it is used to supply voice, it could be subject to a waiver of the CSG. In the future, the reality of the vertically separated industry structure enabled by the NBN means that interaction and cooperation to determine responsibilities as between retail and wholesale customers will be vital. In Telstra's view, this important industry issue should be resolved through industry discussions between both retail and wholesale providers (including NBN Co.) and the appropriate regulator, rather than be prematurely addressed via this legislation.

2. Factual errors

The Explanatory Memorandum to the Bill contains a number of factual inaccuracies. Telstra considers it important to correct those errors so that the Senate can properly consider the purported rationale for the Bill and whether its provisions are necessary and sound policy.

These inaccuracies reflect and perpetuate a series of myths about the state of competition in the Australian telecommunications industry; the way the regulatory process currently operates and the problems that need to be addressed. These myths are propagated by those in the industry that benefit from continued and strengthened regulation. They should not be the basis for considered policy reform.

This section sets out the facts to address these factual inaccuracies:

- that Telstra's level of horizontal and vertical integration is unusual by global standards;
- that competition in telecommunications markets is insufficient and ineffective;
- that separation is a global trend;
- that broadband market concentration is increasing;
- that investment by competitors in their own facilities in Telstra exchanges is limited; and
- that Telstra is the cause and major beneficiary of disputation and delay in current regulatory processes.

Telstra's level of vertical and horizontal integration is not unusual

The Explanatory Memorandum repeats the oft-cited but misleading claim that "Telstra is one of the most integrated telecommunications companies in the world…" (p.3) and "compared to most other countries, Telstra's level of integration is unique" (p.35).

While Telstra is vertically and horizontally integrated, this is typical rather than unusual among Telstra's global peers.

Virtually every major incumbent telecommunications carrier in the world is vertically integrated, including the incumbents in the US, Germany, France, Italy, the Netherlands, Ireland, the United Kingdom, Spain, Sweden, Denmark, Switzerland, Belgium, New Zealand, Singapore, Malaysia, Taiwan, Japan, Hong Kong, China, Indonesia and South Korea. Vertical integration is also the preferred structure of entrant carriers, including SingTel Optus (Australia), VHA (Australia), Cable & Wireless (UK), Virgin Media (UK), Hutchison Telecom (Hong Kong), Starhub (Singapore), KDDI (Japan), FASTWEB (Italy), SFR (France) and Comcast Time Warner (US) (see Annexure 1).

Nor is Telstra's horizontal integration unique or unusual. SingTel, AT&T, Hong Kong Telecom / PCCW, Deutsche Telekom and Bell Canada all offer at least as broad a range of services as Telstra – including a full suite of fixed telephony services, mobiles/wireless, payphones, broadband, content, data networks, pay television and directories. The following carriers also offer a similarly broad range of services, except that they have sold off (or do not own) a directories business: Telecom Italia, Telecom New Zealand, Verizon, Qwest and SingTel Optus (see Annexure 2). While some of the carriers listed here do not own the networks over which they supply these services, as discussed above regarding the HFC divestiture proposal, there is no substantive reason why this would matter in the Australian context.

Competition in telecommunications is neither insufficient nor ineffective

The Explanatory Memorandum cites selective data to support "the Government's view that Telstra's high level of integration has hindered the development of effective competition in the sector" (p.3).

The full data clearly show that the Australian telecommunications market is far more competitive than the selective and misleading material provided in the Explanatory Memorandum would suggest.

The ACMA *Telecommunications Report 2007-08* (November 2008) reports that, as of June 2008, there were:

- one hundred and seventy two licensed carriers – of these, 17 licences had been issued in the preceding 12 months;[27]
- four mobile carriers (now three) operating six mobile networks covering between 96% and 98.8% of the Australian population;[28]
- four operators of HFC networks covering 2.6 million homes in metropolitan and regional centres;[29]
- an estimated 678 internet service providers (ISPs) in operation using a range of different access technologies;[30] and
- 372 fixed-voice service providers operating in Australia. Of these, 210 offer service over the conventional fixed-line network (the public switched telephone network or PSTN) including PSTN pre-selection providers and resellers. Another 268 service providers operate in the VoIP market including service providers, resellers and system integrators, and 106 provide both PSTN and VoIP services. ACMA research suggests that 12% of internet households have used a VoIP service.[31]

The ACCC report on *Communications Infrastructure and Services Availability in Australia 2008* also shows that:

- Telstra, Optus, AAPT, Amcom, Ergon, Nextgen, PIPE Networks, Primus, QLD Rail and Soul all operate backhaul networks in metropolitan and regional areas across Australia – in fact some backhaul routes are serviced by three or more operators; and
- approximately 23 ISPs have invested in their own DSLAM/MSAN equipment to enable DSL service provision to more than 65%of the population, with most investing in ADSL2+ equipment,[32] a fact that surely refutes the misleading comments in the Explanatory Memorandum that Telstra has managed to stall competitor access.

The Explanatory Memorandum is conspicuously silent on price movements, which are universally regarded as a more accurate indicator of the state of competition than simple market share or numbers of market participants. This is a surprising and misleading omission, given that the ACCC report on changes in the prices paid for telecommunications services in 2007-08[33] (issued simultaneously with the ACCC report that is cited in the Explanatory Memorandum on market share) reports price movements in that year consistent with an effectively competitive market:

- an overall 5.5% decline in the real prices for fixed line services (incorporating an 11% decline in prices for national long distance and a 10.1% decline in prices for local call services, 6.4% decline in fixed to mobile call prices and a 4% decline in international call prices);

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[27] ACMA, *ACMA Communications Report 2007-08*, November 2008, p.24.

[28] Ibid. p.23.

[29] Ibid. pp.16 and 23.

[30] The Australian Bureau of Statistics reports that 37 ISPs have more than 10,000 active subscribers.

[31] Ibid. pp25-26.

[32] ACCC 2008, *Communications Infrastructure and Services Availability in Australia 2008* Melbourne, p.14.

[33] ACCC 2008, *Changes in the prices paid for telecommunications services in Australia, 2007-08* Melbourne, p.101.

- a 5.4% decline in the real prices for mobile services; and
- a 6.2% reduction in the prices paid for dial-up and fixed line broadband Internet services (incorporating price reductions of 5.4% for DSL broadband and 5.9% for cable broadband).

An oft-cited counter to the data is the purported statistic that "Telstra generates 90% of the industry's profits". Besides being wrong, this claim misses the point. The proportion of industry profit should be highly correlated over time with the proportion of investment. Therefore, while Telstra generates around 57% of industry revenue and 76% of industry EBITDA (excluding Sensis and our international businesses) it accounts for 71% of industry capital employed in financial year 2008-2009.[34] Including all of our consolidated business, over the five years to June 2009, Telstra invested more than $23 billion of capital. That is 70% of the total industry investment, significantly higher than Telstra's 62% share of industry revenues over the period.

Over the last five years, Telstra has invested more than four times as much as our leading competitor, yet our revenues are only three times as large. It is evident that SingTel Optus has chosen not to invest in Australian fixed line residential networks. Its hybrid fibre-coax (HFC) network, once state-of-the-art, now lags well behind overseas cable networks such as Virgin,[35] Rogers[36] and Comcast,[37] that have upgraded to the DOCSIS 3.0 standard and offer broadband speeds of at least 50 Mbps (Comcast offers 160 Mbps[38] and Virgin is trialling 200 Mbps)[39] with carrier grade voice over broadband. SingTel Optus, by contrast, still uses 1990s cable telephony technology,[40] has not upgraded from DOCSIS 1.1[41] and lags Telstra on maximum cable broadband speeds.[42] At a customer level, it has declined to invest in lead-ins to more than one third of the homes passed by its cable,[43] preferring instead to rent Telstra's copper lines even where its HFC passes the front door.

Separation is not a global trend

The Explanatory Memorandum gives the clear impression that separation measures have been used successfully in a number of countries and are regarded around the world as the answer to concerns about equivalence and transparency:

> *"Functional separation is a regulatory tool that has been used successfully in other countries such as the UK and New Zealand and is being considered by the European Commission, to address the underlying incentives that fixed-line incumbents have to favour their own retail businesses."*[44]

The reality is that:

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[34] These statistics summarise data collated by Telstra from public reporting of twelve Australian telcos (Telstra, AAPT, Amcom, iiNet, M2, Macquarie Telecom, Pipe Networks, SP Telemedia, Vodafone Australia, Singtel Optus, Primus Australia and Hutchison Australia) for the 12 months to June 2009 (except for Vodafone Aust (to March 2009) and SP Telemedia (to July 2009).

[35] Virgin Media Second Quarter 2009 Results, press release dated 6 August 2009, p.1.

[36] Rogers Second Quarter 2009 Financial and Operating Results, 28 July 2009, p.2.

[37] http://www.cmcsk.com/high-speed-internet.cfm.

[38] http://www.cmcsk.com/high-speed-internet.cfm.

[39] Virgin Media Second Quarter 2009 Results, press release dated 6 August 2009, p.1.

[40] ACCC Final Decision, *Telstra's exemption application in respect of Optus HFC network*, November 2008, p.63.

[41] ACCC Final Decision, *Telstra's exemption application in respect of Optus HFC network*, November 2008 at p.79.

[42] See http://www.bigpond.com/internet/plans/cable/ showing Telstra's maximum cable speed of 30 Mbps, and http://personal.optus.com.au/web/ocaportal.portal?_nfpb=true&_pageLabel=Template_woRHS&FP=/personal/bundles/fusion&site=personal showing Optus' maximum cable speed of 20 Mbps.

[43] ACCC Final Decision, *Telstra's exemption application in respect of Optus HFC network*, November 2008, p.11.

[44] Explanatory Memorandum, p.4.

- The UK and New Zealand are among only a handful of OECD countries that have implemented functional separation. The other 23 OECD countries have not mandated any form of vertical separation. See Annexure 3.

- In the US, functional, structural and ownership separation have all been attempted and all have been reversed.[45] The Pennsylvania regulator abandoned structural separation after three years, describing it as an "intrusive remedy designed to fix a problem that has not been shown to exist."[46] The Regional Bell Operating Companies which were split out of AT&T were allowed to vertically reintegrate into long distance services if they met a competitive checklist of behavioural safeguards, including the kinds of non-discriminatory operations supports systems and wholesale interfaces which Telstra has in place.[47]

- A number of European regulators have explicitly rejected functional separation. The French regulator, ARCEP, has said "the apparent appeal of [separation] must not be allowed to mask the difficulties involved."[48] The Dutch regulator, OPTA, has described separation as a disproportionate regulatory response.[49] In response to concerns from the EU Competition Commissioner about the impact of separation in investment in competing infrastructure,[50] the European Commission watered down the Telecommunications Commissioner's separation proposal. Under European law separation may only to be imposed as a last resort measure where all other regulatory attempts to address discrimination have been tried and failed.[51] Telstra's wholesale interfaces and customer agnostic OSS provide a consistently higher level of service to wholesale customers than most EU incumbents, including BT after four years of separation.

Broadband market concentration is not increasing

The Explanatory Memorandum cites the ACCC report on *Telecommunications Competitive Safeguards 2007-08* to conclude that there has been an upward trend in concentration in the retail broadband market segment. Telstra's market shares for retail broadband subscribers have, according to the ACCC, risen from 47% in 2005-06 to 58% in 2007-08. The unprecedented powers proposed for the ACCC by this Bill are in part justified by this apparently alarming growth in market concentration (p.23).

Telstra cannot reconcile these figures with its own market share assessment. In our full year results for the relevant years we provided the market with the following subscriber (SIO) market share assessments:

2005/06	2006/07	2007/08	2008/09
44%	47%	48%	45%

[45] See Jamison and Sichter, US Experiences with Business Separation in Telecommunications, Annex C, Telstra Submission on Vertical Integration and Separation, 25 June 2008.

[46] See Jamison and Sichter, p.17.

[47] FCC, *In re* Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, Docket No. 96-98, *First Report and Order*, 11:28 F.C.C.R. 15499 (Aug. 8, 1996).

[48] See La Lettre de l'Autorité, No 55, March/April 2007 available at www.art-telecom.fr/uploads/tx_gspublication/lettre55.pdf (French version). It also noted that functional separation gives rise to a whole range of costs and does not remove the need for regulation; and that proper accounting separation appears to be an effective means of controlling price discrimination. As to non-price discrimination issues, it suggested that a proportionate remedy might seek separation of systems, together with a code of practice and case-by-case investigation powers.

[49] OPTA, 2 March 2007, Letter to market parties entitled *All-IP: Policy Rules and Separation of Functions*. Ref: OPTA/TN/2007/200309.

[50] 'Brussels Split over Telecoms', Financial Times, 25 September 2007 reports that "sharp divisions have emerged" in the EC, and that two Commissioners (Neelie Kroes, EU competition chief, and Günter Verheugen, the industry commissioner) have attacked Commissioner Reding's proposal.

[51] http://ec.europa.eu/information_society/policy/ecomm/doc/library/proposals/dir_better_regulation_en.pdf.

These figures, which include Fixed and Wireless Broadband subscribers, do not support the conclusion of increasing market concentration.

Competitor investment in Telstra exchanges

The Explanatory Memorandum cites ACCC figures for June 2008 to show that, out of 5,069 Telstra exchanges, only 521 (10%) have had competitors' facilities installed – concluding that regulatory uncertainty appears to have played a part in curbing more extensive investment by competitors (p.48).

This statement misleadingly ignores the distribution of population across Telstra exchanges. The 521 exchanges referred to may only be 10% of the total, but those exchanges serve more than 65% of the population.

Moreover, it is not regulatory uncertainty that has curbed more extensive rollout. Rather, because the ACCC required Telstra (against its wishes) to geographically de-average access prices, competitors have only installed facilities in a mere 71 out of 749 regional Band 3 exchanges and in only 12 out of more than 3,700 rural Band 4 exchanges because competitors face higher wholesale access prices there – for example, in excess of $100 per line per month in Band 4 exchanges. Competitors have only invested in those exchanges where the regulated wholesale access prices enable them to make a profit.

Beneficiaries from regulatory delay

The Explanatory Memorandum claims, without any supporting evidence, that "Telstra is the main beneficiary of this delay and disputation" and "the use of regulatory and legal processes appears to be one way in which Telstra maintains [its] dominance" (p.49).

In reality the problems with the current regulatory regime are far more complex than the simple view that it is "all Telstra's fault".

The current regulatory regime commenced in July 1997 and, perhaps naively, it encouraged companies to negotiate access to Telstra's network and, if they could not agree, to lodge disputes for arbitration by the ACCC.

It is not widely known, but access seekers do regularly agree terms with Telstra on a commercial basis. However, in a climate in which the ACCC has continued to reduce prices there is little incentive for access seekers to negotiate commercially and great incentive to lodge disputes with the ACCC. For example, the ACCC reduced ULLS prices from $35 per month in March 2002 to $12.30 per month in July 2006 – a 65% reduction; the ACCC recently announced a reduction in the LSS price from $2.50 per month in 2008/09 to $1 per month in 2009/10 – a 60% reduction in one year.

Further, the ACCC has readily asserted jurisdiction to arbitrate 'disputes' even when access-seekers have agreed and signed contracts with Telstra. Combined with the lack of clear price-setting directions in the Act or any agreed valuation of Telstra's network, this has been a recipe for dispute and litigation.

Access seekers and Telstra alike have sought to optimise their positions under the regime, including by exercising their legal rights, which is both their prerogative and duty to shareholders.

In early September, access seekers wrote a public letter to the ACCC Chairman complaining about one aspect of an ACCC draft pricing decision that they believe may increase their costs. In recent weeks, the Competition Tribunal ruled on regulation exemptions that were agreed by the ACCC and Telstra but litigated by access seekers. The one "competition notice" issued against Telstra in the last four years was annulled by the Federal Court which found the ACCC had not followed due process.

These examples demonstrate that industry participants have taken every opportunity to protect and advance their interests. Shareholders expect no less of any of us. The failings in the regime are more deep-seated than the behaviour of any particular party.

3. Proposed changes to the Bill

As stated above, Telstra firmly opposes the Bill. The current problems with the telecommunications market in Australia stems from a lack of investment in infrastructure caused by the current regulatory regime, not from a flaw in market structure. This Bill will exacerbate those problems, not fix them. It is unworkable, damaging to both Telstra shareholders and the interests of consumers, and will act to undermine the achievement of the Government's vision for the NBN, a vision which Telstra supports. The Bill should therefore not proceed.

To the extent that the Government decides to proceed with the Bill, then the following section describes the minimum amendments to the Bill required for that vision to be achieved.

Telstra's comments below follow the legislative structure of the Bill.

Part 1 – Amendments relating to Telstra

Voluntary Undertakings given by Telstra - Structural Separation and HFC & FOXTEL divestiture

- Delete the entirety of proposed Part 33 of the *Telecommunications Act 1997*- Voluntary undertakings given by Telstra [clause 21 of Part 1, Division 1].
- Delete related amendments to definitions in *Radiocommunications Act 1992* and *Telecommunications Act 1997* [clauses 1 to 20 of Part 1, Division 1], and to Parts XIB and XIC of the *Trade Practices Act 1974* dealing with the consideration of voluntary undertakings given by Telstra under those parts [clauses 23 to 28 (except 25) of Part 1, Division 1].

Functional Separation of Telstra

- Amend proposed section 74 of Division 2 of Part 9 of Schedule 1 of the *Telecommunications Act 1997* to add additional design principles to the ***functional separation principles***, including the following:
  - > the principle that functional separation must not be unduly burdensome on Telstra;
  - > the principle that functional separation must not degrade retail or wholesale service quality;
  - > the principle that functional separation must not impede Telstra's ability to compete on a fair and efficient basis;
  - > the principle that Telstra is not required to physically separate information systems or networks and that the retail business unit and network/wholesale business units may utilise common customer agnostic information and network operations systems directly through equivalent interfaces;
  - > the principle that Telstra may establish internal non-customer facing network units which can provide insourcing of services on an arms' length basis to the functionally separate retail business unit and the network/wholesale business unit; and
  - > the principle that Telstra may continue to use across the company, on an arms' length basis, support services such as human resources, legal, technology and network planning.
- Delete the Minister's broad discretion under proposed sections 70 and 71 of Division 2 of Part 9 of Schedule 1 of the *Telecommunications Act 1997* to specify the services which are subject to functional separation (**Declared Network Services and Regulated Services**) to limit the regime to bottleneck services which are regulated under Part XIC of the *Trade Practices Act 1974*.

- Delete the discretion of the Minister under proposed sections 77 and 80 of Division 2 of Part 9 of Schedule 1 of the *Telecommunications Act 1997* to vary a draft or final functional separation undertaking. If the Minister has concerns with what Telstra has proposed or seeks changes to a final functional separation undertaking, Telstra should be required to redraft its undertaking. This is likely to produce a practical outcome.

- Amend Part XIC of the *Trade Practices Act 1974* to provide that the ACCC cannot use any of its powers (including making an Access Determination or Binding Rules of Conduct) in a manner which is inconsistent with a final functional separation undertaking.

Control of Use by Telstra of certain spectrum licences

- Delete the entirety of the proposed Part 10 of Schedule 1 of the *Telecommunications Act 1997* [section 22 of Part 1, Division 1].

Part 2 – Telecommunications Access Regime

Part XIC amendments

- Access Determinations - Given that the access determinations will be the fundamental building block of the new access regime it is critical that:
  > clear and detailed legislative criteria or rules with respect to costing methodology are prescribed to guide the exercise of the ACCC's discretion to make access determinations and fixed principles. The matters set out in proposed section 152BCA are too broad and uncertain [clause 116 of Part 2, Division 4, subdivision A]; and

  > merits review of ACCC decisions is available.

- Delete proposed Binding Rules of Conduct power [clause 116 of Part 2, Division 4A].

- Delete proposed Interim Access Determinations power - proposed section 152BCG (and related sections). It is inappropriate for the ACCC to make interim access determinations without undertaking public consultation or affording affected parties procedural fairness [clause 116 of Part 2, Division 4, subdivision A].

- Delete the requirement for access providers to lodge copies of all access agreements with the ACCC. This requirement is unnecessary as the ACCC has adequate powers to obtain documents relating to "*designated communications matters*" under section 155 of the *Trade Practices Act 1974* and the lack of clarity around the preservation of confidentiality on such documents risks distorting commercial activity and outcomes in wholesale markets [clause 116 of Part 2, Division 4B].

- Clarify the relationship between access determinations and the standard access obligations (SAOs). Currently, there is inconsistency between the fundamental principle that access determinations must conform to the SAOs (new subsection 152BCB(3)) and the apparent intention that an access determination can add to the SAOs (paragraph 152BC(3)(e)) as well as grant exemptions from them (paragraphs 152BC(3)(h) and (i)). While the access determination may be a useful vehicle for exemptions, it should not be able to add to the SAOs which must remain paramount - for example, it should be made clear that an access determination cannot require a person to supply a service other than the declared service.

- Clarify the relationships between access agreements and access determinations (as well as with undertakings and arbitral determinations, under the transitional arrangements) by, for example, making it clear that an access agreement can deal exhaustively with a particular matter. Unless clarity is provided, the issue of 'inconsistency' is likely to give rise to frequent disputes as, under this new regime, it is the key to identifying access seekers' and access providers' rights and obligations. It should not be possible for parties to undermine the sanctity of access agreements that have been commercially agreed.

Part 3 – Anticompetitive Conduct

Part XIB amendments

- Delete proposed section 151AKA(9) which removes the requirement of procedural fairness for Part A competition notices [section 159 of Part 3, Division 1].

Part 4 – Universal Service regime

Obligations of Primary Universal Service Providers

- Reinstate the qualification on the Universal Service Obligation "To the extent necessary to achieve the obligation mentioned in subsection (1)(a)" in proposed subsection 9(2). Without this change, it may be argued that a Universal Service Provider is required to supply a standard telephone service upon request to an end user, even though that end user may have access to or may already be taking a standard telephone service from another person - and thus already meeting the "reasonable accessibility" requirements in subsection 1(a) without the USP having to supply service. This would in effect require the USP to either wastefully duplicate infrastructure or be forced to take services from the other network provider even where the terms of supply are unreasonable or uneconomic and unnecessarily adding to the USO costs to be met by the industry [section 166 of Part 4].
- Reinstate the qualification on the Universal Service Obligation to "take all reasonable steps to" fulfil the obligation. While the Minister has the power to determine circumstances in which the USO obligation does not apply, it is unworkable and unrealistic to have an absolute obligation in a country as geographically and climatically diverse as Australia. For the same reasons, the Minister could not possibly determine a comprehensive list of circumstances in which the obligation does not apply [section 174 of Part 4].
- The new Ministerial powers with respect to Standard Telephone Services and Payphones should be subject to a requirement of reasonableness. What is reasonable should be defined by reference to the objects of the part of the legislation dealing with the Universal Service Obligation, namely section 8A, and additional statutory criteria reflecting the practicalities of the supply of services in a country as geographically and climatically diverse as Australia. This should including such concepts as the scope for practical workable engineering solutions and the foreseeability of customer demand and requirements in particular locations [section 175 of Part 4].

Part 5 – Customer Service guarantee

Retail performance standards and benchmarks

- The new Ministerial power to set performance benchmarks with respect to the compliance with a Customer Service Guarantee standard set by ACMA should similarly be subject to a requirement of reasonableness. In this case reasonableness should be defined by reference to the section 3 objects of the *Telecommunications Act 1997* [section 182 of Part 5].

Wholesale performance standards and benchmarks

- Delete the provisions relating to Wholesale performance standards and benchmarks. As a practical matter, wholesale services are "inputs" into downstream retail services. These downstream retail services may involve multiple network platforms and service delivery systems of which a single wholesale provider may not have end to end visibility and/or control. As a result, the concept of wholesale performance standards and benchmarks as envisaged by the Bill is unworkable in its current form [section 178 of Part 5, first bullet point; sections 179, 183, 184, 187 and 189 of Part 5; section 182 of Part 5, Division 3; section 188 of Part 5, delete "or 117F" in proposed section 122A].

Part 6 – Priority assistance

- Telstra makes no comment on this part of the Bill as it expressly does not apply to Telstra.

Part 7 – Infringement notices etc

- Insert a new provision as section 572J(4) of the *Telecommunications Act 1997* that acknowledges that the payment of a penalty in accordance with an infringement notice is not, merely because of the payment, regarded as having contravened the relevant civil penalty provision or listed infringement notice provision or having been convicted of an offence constituted by the same conduct. This recognises that the payment of an infringement notice should not constitute an admission, given that the issue of an infringement notice is not equivalent to a court determination, and the evidentiary threshold required for the issue of an infringement notice is low [clause 195 of Part 7, Division 1]. The amendment would also be consistent with the proposed infringement notice regime contained in the *Trade Practices Amendment (Australian Consumer Law) Bill 2009* [section 87ZH(2) of that Bill].

- The party receiving an infringement notice should be afforded a right of appeal or the decision to issue a notice should be subject to merits review.

- Amend the provisions of Part 7 that use the wording "if a person's conduct constitutes a contravention of..." or similar wording to refer to "an alleged contravention" to reflect that the issue of an infringement notice is not a finding of breach [section 572E(3), (4), (5), (6)] and to ensure consistency with the other provisions of Part 7 [see for example sections 572E(2), 572F(1)(c) and (2), 572G(1), 572J(2) and (3) and 572K].

- Amend section 572E(4)(b) to include a new carve out for carrier licence conditions set out in Parts 5, 6 and 7 of Schedule 1 of the *Telecommunications Act 1997*. The Explanatory Memorandum indicates that the carve outs from the infringement notice regime contained in section 572E(4) are as a result of these provisions being more appropriate for the ACCC or another Agency to enforce [p.198]. However, the ACCC's role in Part 4 of Schedule 1 is similar to its role under Part 5 and Part 7 of Schedule 1 (that is, to act as arbitrator in the event of the parties failing to reach agreement). Accordingly, Parts 5 and 7 of Schedule 1 should also be excluded from the infringement notice regime. Further, given that the majority of Schedule 1 would then be carved out of the infringement notice regime, it would seem inconsistent to include Part 6 of Schedule 1 as part of the regime, and Part 6 should also be excluded.

- Amend the maximum number of penalty units able to be specified by the Minister by way of determination to 500 penalty units [section 572G(3)]. It is not appropriate for the maximum number of penalty units to be 18,000 (currently $1,980,000) or for this to be ascertained by reference to the maximum penalty otherwise applying for a contravention of a carrier licence condition or service provider rule under Part 31 of the *Telecommunications Act 1997* [Explanatory Memorandum p.200] given that the issue of an infringement notice is not subject to the same evidentiary thresholds as would be required prior to a court determining that a contravention has occurred.

- Amend the ability of the ACMA to declare specified provisions to be listed infringement notice provisions so it is subject to a requirement for the ACMA to consult with interested parties prior to such a declaration [section 572E(7)]. The Explanatory Memorandum notes that "it is expected that the ACMA will undertake consultations with the Attorney General's Department and the Department of Broadband, Communications and the Digital Economy". However, given the consequences of the ACMA declaring a provision under this section, it should be required to undertake broader consultation as to the appropriateness of declaration. The requirement to comply with the consultation requirements in Part 3 of the *Legislative Instruments Act 2003* should also be included as a note to section 572E(7), similar to section 572M(2).

Part 8 – Civil penalty provisions

- Remove sections 577K(1), 577K(3), 577L(1) and 577L(3) relating to the control of use of spectrum licences by Telstra as civil penalty provisions [sections 577K(4) and 577L(4). These penalty provisions should fall away consequent on the deletion of Part 33 as discussed above.

Facilitating an agreement on NBN

If, despite Telstra's submission, the separation regime in the Bill is retained, the Bill, as currently drafted, contains a number of provisions that create significant uncertainty for the Telstra Board and management when considering whether to commit to an agreement with the Government on the NBN. These include:

1. The Minister's power to waive the requirements for Telstra to divest either or both of the HFC or Telstra's interest in FOXTEL does not flow automatically from the acceptance of a structural separation undertaking by the ACCC. This means that, to the extent the provisions of the Bill were to be used to implement any agreement on NBN, Telstra has no certainty that it will, in fact, receive the benefit of those waivers if it commits itself to a structural separation undertaking, which under the Bill Telstra may not withdraw. It is not clear that Telstra could lodge a 'conditional' structural separation undertaking.
2. Telstra has no certainty that if it submits, the ACCC accepts and Telstra implements a structural separation undertaking the Minister will not nevertheless use his (or a future Minister's) powers under the *Radiocommunications Act 1992* to impose competition limits barring Telstra from bidding for LTE/4G spectrum when it becomes available in the future.
3. The *Acts Interpretation Act* (AIA) may allow the Minister to revoke a waiver. Generally speaking, section 33(3) of the AIA provides that a power to make an instrument carries with it a power to revoke the instrument unless the contrary intention appears. So, unless that contrary intention is present (which is not at all clear), even if the ACCC accepts a structural separation undertaking and the Minister initially grants the waivers for FOXTEL and HFC divestment, he (or a future Minister) could then revoke these before the LTE/4G spectrum becomes available in 2013.
4. With the removal of the ordinary access undertaking provisions under Part XIC, there is no obvious statutory machinery to allow for the resolution of access prices for existing declared services with the ACCC as part of any agreement on NBN.
5. Both Parts XIB and XIC will be amended to provide that if Telstra has engaged in conduct to comply with a voluntary undertaking then in performing a function or power under XIB/XIC the ACCC must have regard to the conduct to the extent that the conduct is relevant (proposed sections 151CQ and 152ER). Notwithstanding this, there is no prohibition on the ACCC exercising its powers in a manner inconsistent with a voluntary undertaking. By contrast, a special access undertaking given for a non-declared service does have primacy over the Part XIC powers and it is unclear why the same should not apply to a structural separation undertaking (which the ACCC will have approved in the first place).
6. There is no obvious ability for the Government to extend the interest that Telstra may acquire in NBN Co beyond the 15% cap imposed through the adoption of the definitions of 'control' from the *Broadcasting Services Act*.

Annexure 1

Examples of vertically integrated telcos

	Asia Pacific	Europe	North America
Incumbents	Telstra (Australia)	Deutsche Telekom	AT&T
	Telecom New Zealand [a]	France Telecom	Verizon
	SingTel (Singapore)	Telecom Italia	Qwest[c]
	Telekom Malaysia	KPN (Netherlands)	Bell Canada
	Chunghwa (Taiwan)	eircom (Ireland)[a]	
	NTT (Japan)	BT (Britain)[c]	
	PCCW-HKT (Hong Kong)	Telifonica (Spain)	
	China Telecom (PRC)	TeliaSonera (Nordic countries)	
	PT Telkomunikasi (Indonesia)	TDC (Denmark)	
	KT (South Korea)	Swisscom (Switzerland)	
		Belgacom (Belgium)	
Entrants	SingTel Optus (Australia)	Cable & Wireless (UK)	Comcast Time Warner[c]
	Vodafone (Australia)[b]	Virgin Media (UK)	Cable Charter Communications[c]
	Unwired (Australia)[d]	SFR (France)	Cox Communications[c]
	TelstraClear (New Zealand)	FASTWEB (Italy)[c]	
	Hutchison Telecom (HK)	Casema (Netherlands)	
	Starhub (Singapore)	UPC (Ireland)[c]	
	KDDI (Japan)		
	Maxis Communication Berhad (Malaysia)		

Notes: ‘a’ denotes vertical separation has been considered but not implemented. ‘b’ denotes vertically integrated across mobile business only. ‘c’ denotes vertically integrated across fixed line business only. 'd' denotes vertically integrated across wireless broadband business only.

Annexure 2

Range of services provided by Telstra, SingTel Optus and a selection of overseas telcos

Service	Telstra	SingTel Optus	SingTel	BT	PCCW-HKT	AT&T	Bell Canada	Deutsche Telekom	Qwest	Verizon	Telecom NZ	France Telecom	Telecom Italia	Eircom
Access and interconnection	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Local	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Domestic long distance	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
International long distance	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Mobiles	✓	✓	✓	✓(2)	✓	✓	✓	✓	✓	✓	✓	✓(11)	✓	✓
Payphones	✓	✓	✓	✓	✓	✓	✓	✓	✓(6)	✓	✓	✓	✓	✓
Internet access (ISP)	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓(12)	✓	✓
Internet content	✓	✓(1)	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Data networks (LAN, WAN, VPN)	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Pay television	✓	✓	✓	✓(3)	✓	✓	✓(4)	✓	✓	✓	✓(9)	✓(13)	✓(15)	×
Directories	✓	×	✓	✓	✓	✓	✓(5)	✓	×(7)	×(8)	×(10)	×(14)	×	✓

Notes: 1. myZOO (in partnership with ninemsn). 2. MVNO on Vodafone Network. 3. BT Vision. 4. ExpressVu. 5. BellZinc. 6. Sold large portion in 2004 but still maintains some payphone assets as shown in 8 Feb 2007 SEC Filing Form 10-K. 7. Sold in 2003. 8. Sold in 2006. 9. TCNZ resells Sky's basic package (Digital Start-up). Other channels are billed to the customer directly by Sky. 10. TCNZ sold its Yellow Pages Directory Group subsidiary in 2007. 11. Orange. 12. Orange 13. Orange TV. 14. Sold Pages Jaunes Groupe SA in 2006. 15. Alice offers IPTV services. Telecom Italia Group owns La7 which offers some Pay TV services such as soccer games.

Annexure 3

Instances of vertical separation around the world

Country (OECD countries marked with *)	Is separation mandated?	Comment
Australia*	✓	Operational separation.
Austria*	✗	
Belgium*	✗	
Canada*	✗	Some early requirements to operate a separate wholesale division but not the extensive functional separation measures required in the UK. More focus on ensuring equivalent OSS, as in US.
Czech Republic*	✗	
Denmark*	✗	Recent report by regulator found that competition was limited and said that consideration should be given to functional separation.
Finland*	✗	Historically separated local and long distance companies have been allowed to integrate.
France*	✗	Specifically rejected by the regulator.
Germany*	✗	
Greece*	✗	
Hong Kong	✗	
Hungary*	✗	
Iceland	✗	
Ireland*	✗	Voluntary separation offered by eircom but has encountered difficulties and fallen by wayside with Babcock & Brown difficulties. Comreg did however consider that eircom underestimated the systems difficulties and costs of separation.
Italy*	✓	Structural separation proposed by the regulator but Government is backing away from, preferring voluntary form of operational separation which is a mix of UK functional separation and Australian operational separation.
Japan*	✓	US RBOC approach of regionally vertically integrated entities. However, in next generation network environment, Ministry has recognised value of vertical integration
Korea*	✗	
Luxembourg*	✗	

Country (OECD countries marked with *)	Is separation mandated?	Comment
Mexico*	✘	
Netherlands*	✘	Voluntary form of operational separation which is less extensive than Australian model. Regulator doubted value of UK model.
New Zealand*	✓	Incremental implementation over period to 2015 and limited application of equivalence to legacy retail services.
Norway*	✘	
Poland*	✘	Regulator reported in Q3 2008 that pending the amendment to the EU Access Directive there was no legal basis to require functional separation. The regulator also thought that "extraordinary circumstances" would need to be established before separation could be required.
Portugal*	✘	The Portuguese regulator has recently commissioned an external research report on separation which, while not recommending an option, concluded that structural separation would carry very high costs, identified the investment and planning co-ordination problems of any separation model and acknowledged that it was difficult to attribute the improvements in the UK market to separation or to the regulatory decisions on ULLS. The report appeared to favour a limited functional separation of next generation and layer 2 broadband access.
Singapore	✘for existing network ✓for FTTP	Separation of Netco and Opco for new FTTP. Regulator considering functional separation for legacy network, although this is unlikely.
Slovak Republic*	✘	
Spain*	✘	
Sweden*	✓	The Swedish Parliament has passed a law empowering the regulator to recommend separation. Incumbent has voluntarily separated and regulator reviewing.
Switzerland*	✘	
Turkey*	✘	
United Kingdom*	✓	
United States*	✘	Ownership, structural, functional and operational separation all tried and abandoned. More focus on equivalent OSS.