



Bringing the USO into the Twenty First Century

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Section 1. Executive summary

- 1.1 This submission is provided to the Senate Environment and Legislation Committee which is re-examining the Telecommunication Legislation Amendment (Deregulation) Bill 2014 and Telecommunications (Industry Levy) Amendment Bill 2014 in the context of the December 2014 revisions to the Telecommunications Universal Service Agreement between Telstra and the Commonwealth. Optus understands that the revised agreement between Telstra and the Commonwealth has simply re-confirmed the arrangements that were first agreed in 2011. However, Optus welcomes the opportunity provided by the Committee to re-examine these arrangements, particularly in the context of delivering a fit for purpose set of universal service arrangements in an NBN environment.
- 1.2 The Universal Service Obligation has been in place for over twenty years. Whilst the industry and technology has changed substantially over this period there has been little change to USO arrangements in terms of how it is delivered and funded.
- 1.3 The existing USO arrangements have been widely acknowledged to be deficient. As far back as 2008 the Regional Telecommunications Independent Review Committee (RTIRC) noted that:

“nearly all stakeholders dislike the current USO arrangements. Given this, the universal service regime as currently framed in the telecommunications legislation is not completely effective”.¹
- 1.4 The Committee recommended that the transition to a National Broadband Network provided a clear opportunity to deliver effective and much needed reform of the USO. However, successive Governments have failed to act on this opportunity. Instead we have a situation where the legacy arrangements will continue to prevail and at a higher overall cost to industry and taxpayers.
- 1.5 Agreements reached with Telstra in 2011 and revised in 2014 have effectively locked-in the legacy arrangements under a twenty year contract. These arrangements require Telstra to maintain its legacy copper network at an annual cost of some \$330 Million; or a potential total cost of around \$6.6 Billion over the contract period.
- 1.6 Optus shares the conclusions of the Glasson committee that the current USO arrangements are not fit for purpose and that the transition to the NBN provides an ideal opportunity for policy reform.
- 1.7 The objective of Optus’ submission is to encourage the Committee to recommend further consideration on how to achieve reform aimed at delivering a better outcome for consumers but at a lower cost for industry (including Telstra) and taxpayers. In particular, Optus supports the Committee recommending the Government conduct a wide ranging review into the USO as a key policy priority. The goal should be to recommend policy changes that ensure the USO delivers better outcomes and value for consumers, industry, competition and taxpayers

¹ Regional Telecommunications Independent Review Committee Report 2008, Page 194

Section 2. Background

Recap on the USO

- 2.1 The objective of the USO is to ensure that all Australians have reasonable access to a standard telephone service (STS) on request, and that payphones are reasonably accessible to all people on an equitable basis, wherever they live or carry on business. A “standard telephone service” is defined in Section 6 of the *Telecommunications (Consumer Protection and Service Standards) Act 1999* and must meet certain basic requirements, including:
- (a) local, national and international calls;
 - (b) 24 hour access to the emergency call service number;
 - (c) operator assisted services;
 - (d) directory assistance; and
 - (e) itemised billing, including itemised local calls on request.²
- 2.2 In addition to the above requirements, an STS that is supplied in fulfilment of the USO must also include the following additional features:
- (a) Provision of customer equipment (including a handset and/or equivalent equipment for people with a disability);
 - (b) The option of untimed local calls (including for mobile telephone services); and
 - (c) Provision of the Customer Service Guarantee including service connection and repair, and meeting specified time frames (including for mobile services).³
- 2.3 The USO also ensures access to the standard telephone service for people who cannot communicate using voice telephony because they are deaf or have a hearing or speech impairment. The obligation requires that an equivalent means of communication be provided, including appropriate customer equipment to enable equivalent access.
- 2.4 Telstra sets out how it intends to fulfil its USO in its Universal Service Obligation Policy Statement and its Universal Service Obligation Standard Marketing Plan. These documents cover matters such as Telstra's general approach to fulfilling the USO, as well as service availability, service description, service quality, connection and fault repair time frames, and complaint processes.
- 2.5 There is no regulatory requirement for Telstra to provide USO services using particular types of technology. Optus understands that whilst most USO services are provided over its copper network, Telstra does use other technologies, such as radio links (satellite and terrestrial), and wireless services.
- 2.6 In 2011, the Government introduced policy measures designed to ensure the continuity of basic universal service outcomes for customers in the transition to the NBN. In essence these policy changes sought to reform the administration of the USO (from a regulatory to a

² ACMA - Your rights to a telephone service – the universal service obligation

³ http://www.communications.gov.au/telephone_services/voice_telephone_services/connecting_the_telephone

contractual model) *without* fundamentally changing the nature of the USO. The Telecommunications Universal Service Management Agency (TUSMA) was established to administer the USO and enter into contracts with third parties to ensure its ongoing provision. Whilst the current Government has taken steps to abolish TUSMA the underlying administrative model will remain in place and TUSMA's responsibilities will be undertaken by the Department of Communications.

- 2.7 In practical terms Telstra will continue to assume responsibility for delivering the USO albeit under a contract. From 1 July 2012 Telstra has entered into a contractual obligation to deliver the STS for a term of twenty years. Once the NBN is rolled out, Telstra will operate as a retail provider of last resort to deliver the STS over NBN technology within the NBN fibre footprint. Outside the NBN fibre footprint Telstra has committed to maintain its copper network to provide the STS. As will be discussed below, changes were also made to the funding that Telstra will receive to fulfil these ongoing obligations.

Current funding arrangements

- 2.8 For the vast majority of services Telstra recovers the costs of fulfilling its USO through revenues received from customers. However, this may not be the case for services provided in high cost areas, typically the more remote or difficult to reach parts of Australia. In respect of these areas Telstra argues that it incurs higher costs to service these customers than it receives in revenue.
- 2.9 The prevailing policy view is that absent its regulatory or contractual obligations Telstra may not have an incentive to service these high cost areas. Therefore, industry as a whole has been required to contribute to the net cost of fulfilling the USO through an industry levy mechanism; the precise levy on each carrier is based on its share of total industry eligible revenue.
- 2.10 Prior to 2012 the annual level of USO funding was set by the Minister based on advice from the ACMA. More recently this was set at around \$145 Million per annum. An additional amount of around \$18 Million was set to recover the costs of providing the National Relay Service. Typically industry contributed around 40% of the costs through payments that ultimately flow through to Telstra, with the balance being borne by Telstra.
- 2.11 However, the Government (in the Definitive Agreements) agreed to substantially increase the annual USO levy amount to \$330-340 million to secure Telstra's support for structural reform and its participation in the NBN.
- 2.12 In recognition of the magnitude of the increase the Government committed to contribute to the annual funding by at least \$50 million for financial years 2012-13 and 2013-14, and \$100 million per annum after that. The residual costs will continue to be funded through an industry levy scheme, with amounts based on each carrier's share of eligible revenue. The table below provides a breakdown of the funding amounts before and after the policy change.

Change in USO Payments

Liabilities	Pre-2012	Post 2012
USO voice	\$ 131.3 m	\$ 230 m
USO payphones	\$ 13.8 m	\$ 40 m
Emergency call handling	..	\$ 20 m
USO Sub-Total	<i>\$145.1 m</i>	<i>\$ 290 m</i>
National Relay Service	\$ 17.9 m	\$ 20 m
Voice-only migration	..	\$ 15 m
Public Interest Services	..	\$ 0-10 m
TUSMA administration costs	..	\$ 5 m
TOTAL	<i>\$ 163 m</i>	<i>\$ 330-340 m</i>

Source: Explanatory Memorandum to the TUSMA Bill 2011

- 2.13 As a consequence of these changes, Telstra will receive a three-fold uplift in annual USO levy contributions; it will receive \$100 million per annum from Government and contributions from third parties will increase from around \$60 Million per annum to around \$90 Million per annum. However, as indicated in the section above there are no material changes in the basic obligations or scope of services Telstra will have to fulfil, notwithstanding this significant increase in annual funding.
- 2.14 The funding provided to Telstra under the USO arrangements is very significant, especially when looked at over a period of years:
- (a) Between 1997 and 2014 Optus and Vodafone have contributed some \$839 Million to Telstra under the USO levy scheme.
 - (b) Over the next 20 years industry and Government collectively is likely to contribute \$3.7 Billion to Telstra under the current funding arrangements.

Section 3. A failed policy

- 3.1 Whilst the concept of a universal service obligation to ensure customer needs are met has widespread industry support, the arrangements to deliver this have been subject to widespread criticism.
- 3.2 In 2008 the RTIRC noted that:
- ‘There is substantial controversy about the current USO arrangements and the Committee notes that nearly all stakeholders dislike the current arrangements. ACMA referred to the USO arrangements as a ‘broken concept’.*⁴
- 3.3 The committee outlined in some detail the failings of the USO arrangements. In summary it found:
- (a) Limited consumer understanding of the USO which was considered to be “vague” and subject to limited enforcement mechanisms. The committee indicated that in its consultations with the community it has found a poor awareness of the USO arrangements and an even poorer understanding of how they operate;
 - (b) That the current arrangements undermine competition since they fund a single supplier. In turn this provides limited incentives for Telstra, as the universal service provider, to improve its performance in high cost areas where it faces no competition;
 - (c) Funding arrangements that operate as an effective tax on consumers and as such are “inefficient and not well structured”; and
 - (d) A cost and funding structure which discourages or even precludes the use of alternative and more efficient technologies. There is no obligation on Telstra to use the least cost technology. Further, there is no requirement to ensure that contributions received from Government and industry is invested in the provision of universal services.
- 3.4 The arrangements in place today are little different from those in place when the RTIRC undertook its review. As indicated in the section above, the current delivery and funding arrangements have been locked-in under contract for the next two decades as a result of the NBN related policy changes. To some extent the problems identified by the RTIRC will be magnified by the NBN related policy changes since:
- (a) The annual level of industry and taxpayer funding for the USO has been increased substantially; and
 - (b) A separate obligation on NBN Co to price services at uniform levels nationally means that metropolitan consumers are effectively being required to pay two subsidies towards services provided to remote customers; the traditional USO subsidy for voice services; and a contribution towards the cost of supplying broadband services over NBN Co’s Fixed Wireless and Satellite networks.

⁴ Regional Telecommunications Independent Review Committee Report 2008, Page 182

Section 4. The NBN provides a platform for effective reform

- 4.1 In reaching its conclusion that the present USO arrangements are not fit for purpose the Glasson committee sounded a note of optimism about the future prospects under the NBN.

*“The Committee believes that the transition to the NBN presents the opportunity to fundamentally redesign the provisions that aim to deliver a universally available and affordable voice and other service of a desired quality and reliability”.*⁵

- 4.2 Optus shares this sentiment. The roll-out of the NBN provides a game-changing opportunity to reform how the USO is delivered and funded. Central to this are the requirements for NBN Co to:

- (a) To connect every premise in Australia; and
- (b) To offer entry-level products at a nationally uniform price⁶.

- 4.3 These obligations provide a clear platform for reform of the USO as they mean that; infrastructure will be available nationally, including in the most remote locations, to connect customers; and it will be made available at uniform wholesale prices which means it will be viable for multiple RSPs to be able to provide services to customers at affordable prices wherever they reside. Such uniform national wholesale prices would remove the need for a separate industry levy because a uniform national price is essentially a cross subsidy from lower cost/higher density consumers to higher cost/lower density consumers.

- 4.4 It is unclear why the opportunity to use the NBN infrastructure as a catalyst for reform of the USO was not taken in the 2011 reforms. This could have been driven by uncertainty at that time about the technical capability of the prospective new fixed wireless and satellite technologies to deliver adequate voice capability. To the extent that such concerns existed, Optus suggests that they were overstated.

- 4.5 Optus considers that the NBN broadband infrastructure is capable of delivering a high quality voice service.

Technical solutions

- 4.6 Both NBN Co’s fibre and fixed wireless technologies have been designed to provide voice capability. In respect of NBN Co’s fibre services, voice services can be provided through a VOIP solution (using NBN Co’s Uni-D port on the NTD) or through an analogue adaptor (using NBN Co’s Uni-V port). Similarly, voice services can be provided over NBN Co’s fixed wireless platform using VOIP technology. Optus understands that whether the voice is delivered by VOIP or analogue technology over these networks it will meet the requirements of the STS.

- 4.7 Since the fibre and fixed wireless platforms are designed to cover around 97% of the population, the delivery of the STS for the vast majority of households and businesses can be met through the NBN infrastructure. It remains unclear, therefore, why Telstra is required to keep its copper network in place within NBN Co’s fixed wireless footprint.

⁵ Regional Telecommunications Independent Review Committee Report 2008. page 194

⁶ The Coalition has indicated that this obligation will likely be amended to operate as a price cap rather than a strict requirement for uniform pricing, but this is unlikely to alter the principle that regional services will be affordable under NBN pricing.

- 4.8 This leaves the last 3% of the population; around 300,000 households. Under the current NBN plan these households will be covered by NBN Co's long-term satellite service, which is to be launched in 2016. As with NBN Co's fixed wireless service, it is likely that voice can be offered through a VOIP solution operating over the satellite broadband service. In fact a number of RSPs currently offer VOIP services over NBN Co's interim satellite service⁷.
- 4.9 However, Optus acknowledges that there may be circumstances where the technical quality of voice services over satellite may not be equivalent to that provided over technologies. This is due to latency associated with the up and down links. That said, it remains to be determined how significant such differences are and whether there may be compensating benefits from use of satellite (such as mobility). It would be useful to understand the proportion of current NBN satellite customers that use a VOIP service.
- 4.10 In addition to the NBN infrastructure, both Telstra and Optus have extensive mobile coverage including in the remote parts of Australia. In a submission to the 2007 USO review Telstra provided an analysis which suggested that only around 137,000 of its existing USO services were outside its mobile coverage. Telstra's mobile coverage has expanded since this date, which means a greater number of existing USO services might be capable of being delivered by mobile technology. Coverage is likely to be extended in the next three years by the Government's funding of its mobile coverage programme. Again, it would be useful to understand the proportion of "universal service end-users" that have a mobile service in addition to their fixed line service.

⁷ Refer websites of Skymesh (<https://www.skymesh.net.au/services/nbn/satellite/voip.php>) and ipstar (<http://www.ipstaraustralia.com/retail/ipstar-voip/>)

Section 5. Proposed way forward

- 5.1 Under the current arrangements industry and government is spending \$330 Million per annum on a scheme that is flawed;
- (a) It requires Telstra to maintain a legacy network that is likely to become increasingly non-strategic and subscale as customers migrate to the NBN;
 - (b) It requires industry to make substantial payments to Telstra for services that could otherwise be invested in more productive technology;
 - (c) Metropolitan consumers face a double cross subsidy to help fund regional services;
 - (d) It is a burden on taxpayers; and
 - (e) It is unclear whether it delivers meaningful outcomes for consumers.
- 5.2 Notwithstanding that the current USO policy arrangements appear to be locked in under contractual arrangements there is a compelling case to review the relevance and appropriateness of the current arrangements against alternative models. The key question is whether the USO can be delivered in a more effective way: that better meets consumers' expectations and at a lower overall cost to society.
- 5.3 Optus supports the Committee recommending the Government conduct a wide ranging review into the USO as a key policy priority. The goal should be to recommend policy changes that ensure the USO delivers better outcomes and value for consumers, industry, competition and taxpayers. Optus recognises that any reform must be beneficial to Telstra.
- 5.4 Issues that should be considered in such a review include:
- (a) An audit of USO designated premises to determine the precise number and the current technologies used at those premises;
 - (b) The relevance of the current scope of the STS and payphone obligations to consumers;
 - (c) The technical capabilities of alternate technologies to deliver the USO and the extent to which these may be delivering USO equivalent services today;
 - (d) The coverage of all alternate technologies and the costs of infilling any perceived coverage gaps;
 - (e) Alternate funding and investment models and their implications in terms of cost, impacts on competition and end-user prices;
 - (f) Structural options for the delivery of the USO (including whether NBN Co should assume ownership of the Telstra copper outside its fibre footprint).

Potential model for reform

- 5.5 To aid this discussion Optus has put forward the following arrangements that could be considered as a basis for reform:

- (a) NBN infrastructure should be the primary mechanism for ensuring customer connectivity. This should apply to each of the NBN platforms: fibre; fixed wireless and satellite;
- (b) To ensure that the STS is delivered over the NBN infrastructure an RSP could be designated as a retail provider of last resort (this could be Telstra or another RSP);
- (c) To the extent that NBN infrastructure cannot provide an adequate STS capability to a customer then the service could be provided over copper or mobile networks (if available);
- (d) NBN Co could take ownership of the Telstra copper outside the fibre footprint. This will ensure that copper is available to help meet the USO. More importantly NBN Co will likely have stronger incentives than Telstra to ensure that the USO can be delivered through more cost effective alternate technology, enabling it to decommission the copper more quickly and reduce its costs to serve;
- (e) Separate industry funding for the USO would not be required as the costs of supply will be included in access charges; and
- (f) Current Government funding for the USO (\$100M p/a) could be used to improve mobile coverage within the more remote areas of Australia, thereby providing additional options for delivering the STS to customers.