

4 October 2009

Committee Secretary
Senate Standing Committee on Communications
PO Box 6100
Parliament House
CANBERRA ACT 2600

**TELECOMMUNICATIONS LEGISLATION AMENDMENT (COMPETITION AND
CONSUMER SAFEGUARDS) BILL 2009**

SUBMISSION

Introduction

1. This submission is made by me as an interested individual, a concerned taxpayer, and Trustee of a Self Managed Superannuation Fund which is a shareholder in Telstra. It is not Confidential.
2. Prior to my retirement in 2000, I was Deputy Chief Executive of the Australian Postal Corporation. During that time I represented the Corporation before the National Competition Council and this Standing Committee on matters concerning the regulation of Australia Post's monopoly domestic letter service. I believe that experience is relevant to this Inquiry.

Outline of Submission

3. Only two of the three primary parts of the Inquiry are addressed :
 - 3.1 Telstra's vertical and horizontal integration and the proposed separation of its retail and wholesale businesses; and
 - 3.2 streamlining the access and anti-competitive access regimes.
4. The third part concerning consumer safeguards (the USO, CSG and Priority Assistance) is of little consequence compared with the above. In fact as the name of the Bill implies, it is subterfuge to suggest the legislation is about consumer safeguards when its primary objectives appear to be an attempt by the Government to implement a quasi-nationalization of Telstra, and to safeguard NBN Co.
5. This submission assumes that the Government, through its NBN Co will construct the super-fast fibre NBN network, either with or without Telstra, over the next eight years, at an estimated cost of \$43 bn.

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6. Page numbers where given refer to the Explanatory Memorandum.
7. It is submitted that the proposed legislation:

- 7.1 reduces competition rather than enhancing it, and a better solution is available;
- 7.2 is based on unreliable, selective and biased information, so as to support the Government's argument;
- 7.3 is itself a flagrant misuse of market power by the Government;
- 7.4 deprives Telstra and its shareholders of natural justice;
- 7.5 fails to address the matter of acquisition of property on just terms; and
- 7.6 introduces into the Australian equities market a high degree of Sovereign risk for investors contemplating investment in infrastructure.

A Better Solution Than Separation

8. 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.3). It is fundamental that competition exists only where there is rivalry between two or more suppliers. This applies even if there are only two dominant suppliers, which is evident from the ACCC's recent inquiry into grocery prices. The ACCC Report released on 5 August 2008 confirmed that competition between Coles and Woolworths was "workably competitive" (ie at the retail level), and there was nothing "fundamentally wrong" with the supply chain (ie at the wholesale level).

9. The effect of this Bill is to create NBN Co as a monopoly supplier at the wholesale level, while at the same time emasculating the only serious other supplier: hardly an improvement in competition. It would have the undesirable effect of reducing all retailers to the same lowest common denominator, with retail price the only differentiator, rather than technical innovation, management expertise and customer service. A relevant analogy is the Electricity market in Victoria, where the structural separation of Distribution (wholesale) and Retail has failed to bring about real competition. Even worse, it has been inefficient by the establishment of a multitude of parallel infrastructure (call centres, billing systems, administration centres, retail outlets etc), each operated by the Retailers. These retailers make no value-adding contribution. For example, one major retailer, TRU Energy, does nothing to add value except for billing its customers. Even meter reading is contracted out, and customers are required to contact the Distributor (such as SPAusNet) in the event of supply failure. This is a likely scenario for the NBN, in the absence of proper competition.

10. A better solution is to enable two businesses to compete aggressively in the Australian telecommunications market. I submit that enabling NBN Co and Telstra

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to compete at the wholesale level would bring about more real competition, than what is proposed. Assuming Singtel (Optus), AAPT, iiNet, iPrimus et al will support NBN Co's wholesale network at the retail level, competitive rivalry could emerge as follows:

<u>Feature</u>	<u>NBN Co + Optus et al</u> (Wholesale/Retail)	<u>TELSTRA</u> (Fully integrated)
1. <u>Networks</u>	FTTHome - Cable Satellite (Optus owned) Wireless Broadband Hybrid Coax Cable (Optus)	FTTNode - Copper Not available Wireless Broadband Hybrid Coax Cable (Telstra)
2. <u>Broadband Speed</u>	Up to 100 mbps	Up to 20 mbps (ADSL2+)
3. <u>Retail Outlets</u>	Existing	Existing
4. <u>Coverage</u>	90% by FTTH	80% by FTTN
5. <u>Funding</u>	Taxpayers	Shareholders

11. One obvious advantage is that the cost to Taxpayers for the NBN remains unchanged. There is no inefficiency due to parallel assets (as occurred with the Hybrid Co-axial Fibre rollout), as the HCF, copper, satellite, wireless and retail networks already exist, and neither structural or functional separation would be necessary. There is therefore a potential major avoidance of costs to the Government if it attempts to acquire any of Telstra's assets without fair compensation which would be contrary to Section 51 (xxxi) of the Constitution. Given long-term regulatory certainty, and based on prior comments, Telsra may then proceed to roll-out its FTTN network.

12. There are sufficient differences in the retail offering to consumers, not just on price but also speed, coverage, product innovation and service. I submit that this solution would achieve the Government's stated intention of promoting a competitive market. It could be achieved by simply providing a degree of regulatory certainty in respect of the FTTN network during the period up to the construction of the NBN. If this is not acceptable to Government, a reasonable person might well ask what their true motive is.

13. While a FTTH network undoubtedly has many technological advantages, it is debatable if the NBN will be commercially viable only because of its promised speed and coverage, but that is what competition is all about. At this stage the Government has not released its estimates of prices or take-up so it is not possible to comment further on that aspect of the Bill. Even if pricing is subsidized by the Taxpayers, it

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becomes a matter of what do subscribers really need. The Table on page 31 of the EM must be of some concern to NBN Co when only 7.2% of subscribers in the United Kingdom have opted for services above 8 mbps, and Telstra's ADSL2+ can already provide up to 20 mbps at an average speed of 10 mbps.

14. A further advantage of two strong wholesale suppliers is the opportunity to streamline the access and anti-competitive access regimes. It is submitted that the need for access regulation would be minimal (if any) in such a robust competitive market. The only case for short-term access regulation should be in respect of the Telstra copper-network, it being the only legacy service from the pre-privatization period, up until the NBN enters the market. All other infrastructure (mobile, HCF, Foxtel) have been funded by Telstra's shareholders, in a free market which was available to competitors.

Quality of Information

15. Much of the supporting comments in the EM have come from Telstra's competitors, so the bias is understandable. They are hardly likely to present any of Telstra's positive attributes, such as the willingness to invest shareholders' funds into technological developments, construction of world-class infrastructure (NextG for example) and refinement of administrative and IT Systems. Singtel (Optus) has been content to sit on its hands, and to attempt to gain advantage through regulation, rather than risking its shareholders' funds. The comments are fuelled by extreme hypocrisy, such as Singtel's (Optus) contention that "Telstra's investment in Foxtel represents a significant threat to competition" (p.34), when Singtel itself is the largest Pay – TV operator in Singapore.

16. Apart from bias, the information is also highly selective so as to support the Government's own argument, without showing the full picture. For example, the Table on Page 1 of Appendix B includes a comparison of restrictions between ten OECD countries, plus Hong Kong. Countries not included are:

16.1 OECD. France, South Korea, Turkey, Mexico and New Zealand.

16.2 Non-OECD. China, India, Russia, Brazil, Indonesia and Sth Africa.

16.3 Singapore.

16.4 Other G20. Argentina and Saudi Arabia.

17. Some of these countries have no limitation on ownership of both Pay-TV and Telecommunications networks, and because of their leadership in Broadband services (eg South Korea) would have been at least as worthy contenders for comparison as Hungary, Belgium and Netherlands.

18. It is therefore submitted that the comments and information is not reliable or complete and should be considered in that light.

Misuse of Market Power

19. Section 46 of the Trade Practices Act 1974 (TPA) prohibits a person, business or corporation, with a substantial degree of market power, from abusing that power for the purpose of:

19.1 eliminating or substantially damaging a competitor; or

19.2 preventing the entry of a competitor into any market.

20. While the Government (as distinct from a Commonwealth Enterprise) is not subject to the TPA, it would be at least morally improper for it to act contrary to the Laws of the Commonwealth. Instead of simply flouting a law, a responsible Government would either amend the legislation, or act in accordance with it.

21. This Bill and the associated Government policy is a clear contradiction of S46 of the TPA, and any other person, business or corporation would be prosecuted by the ACCC if it acted in a similar manner. For example: "...Telstra will not be able to acquire spectrum for advanced wireless broadband while it remains vertically integrated, maintains its interest in Foxtel and owns a Hybrid Coaxial Fibre network" (p.37) is clearly a misuse of market power, intended to damage Telstra to the advantage of NBN Co. This misuse would breach both Subsections 46(1)(a), by damaging Telstra (forced sale of HCF and Foxtel) and Subsection 46(1)(b) by preventing entry into the advanced mobile broadband market by denying Telstra's access to spectrum.

Denial of Natural Justice

22. The Government proposes to allow the ACCC to set up-front prices and non-price terms for declared services (p.3). The Bill "also explicitly provides that the ACCC is not required to observe any requirements of procedural fairness in relation to the issue of a Part A Competition Notice" (p.4), which it can do without undertaking any consultation. This implies the ACCC is infallible, in which case the need for an Appeals Tribunal should also be questioned.

23. This is clearly a denial of natural justice, although it is noted that a judicial appeal process will still be available. Hopefully good use will be made of that process if the Bill passes and remains unamended.

Acquisition of Property and Other Damages

24. The Bill proposes that in the event Telstra fails to accept structural separation, it will be required to divest itself of its Hybrid Coaxial Fibre network and its 50% interest in Foxtel. I submit that the Board of Telstra is unlikely to agree to structural separation, given its fiduciary obligation to protect the value of shareholders' interests. A number of major institutional investors, together with many of Telstra's other 1.4 million shareholders, have already indicated (in the Press) that they would not support such a decision.

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25. That being the case, it would either be devaluing or require compulsory acquisition by the Commonwealth, bringing rise to a case for fair compensation as

prescribed by Section 51 (xxxi) of the Constitution. The EM fails to address this situation, other than a brief statement; “It has been widely observed that imposing mandatory structural separation on Telstra is likely to raise compensation issues” (p.23). Estimates on Page 28 of the EM are not conclusive, but it is clear that either structural or functional separation will take years and costs and other damages will amount to some billions. An analogous test case between the ASX and ASIC is likely to emerge in the near future which may provide some guide on the matter, in that case in respect of any forced transfer of Intellectual Property.

26. Telstra is a public company, purchased by its shareholders in good faith from the Commonwealth, which is now attempting to repossess much of its value by what should be considered as extortion. Shareholders are not being treated justly, and will no doubt pursue their rights through the High Court of Australia.

Sovereign Risk

27. This Bill is reminiscent of the attempt by the Chifley Labor Government’s attempt to nationalize the Australian banks in 1949. In the view of the Executive Director of the Institute of Public Affairs (BRW Oct 1, p.22): “ the Minister’s ultimatum of “break up yourself or else” amounts to a “semi-nationalization” and sets a dangerous precedent”.

28. It is likely to have a severe dampening effect on any major investor contemplating construction or expansion of infrastructure in Australia, as potential shareholders and debt financiers will now take into account the substantial sovereign risk involved, which is now a reality rather than a possibility. Potential investors into NBN Co itself will surely discount its total value because of this added risk, or alternatively seek a higher value for in-specie contributions (assets such as networks), and higher return on their investment.

29. While the Bill provides scope for the Minister to remove requirements around the HCF network and Foxtel (p.2), it provides no certainty to shareholders, who would be unlikely to trust their future livelihoods to a person who has already showed his hand at attempting to nationalize non-government assets.

Conclusions

30. The Bill smacks of retribution against Telstra and its 1.4 million shareholders because although it has never acted illegally, it has chosen to compete actively in the Telecommunications market, and has resisted over regulation by the ACCC and successive governments. Telstra’s competitors have, as a consequence held great sway with the composition of this Bill, rather than to acknowledge their own incompetence and lack of investment.

31. The Bill provides unprecedented power with the ACCC, an instrument of Government directed by its own Minister, in an effort to enhance the chances of commercial success of the NBN Co, itself wholly owned by the Commonwealth. In the Australian vernacular, this could be described as a very cozy arrangement. It is

also totally inconsistent with the Government's recent decision to use regulation to prevent the ASX from continuing as both regulator and operator.

32. The NBN is going to be built in any event because of the political consequences to the Government of not proceeding after already extensive delays. To achieve its objective of greater competition, Telstra provides the ideal competitor to NBN Co, without any further contribution above the Government's \$43 bn funding, and avoiding the value destroying actions to one of the leading Telecom companies in the World. Further saving to the Government will result from avoiding the need for High Court challenges and the resulting compensation payments.

Robert Ludlow