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Inquiry into Australia's relationship with India as an emerging world power

Organisation: **Telstra Corporation Ltd**

Address : **Federal Government Relations**
Canberra ACT

Inquiry into Australia's relationship with India as an emerging world power:

Telecommunications Services Market Access in India

Submission by Telstra Corporation Limited to
the Joint Standing Committee on Foreign Affairs, Defence and Trade

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1. Introduction

Telstra Corporation Limited ('Telstra') is Australia's largest communications carrier. Telstra's activities include supply of a wide range of converged information and communications technology ('ICT') services to Australian and offshore customers.

Given the international ascent over the past 15 years of Indian suppliers of information technology ('IT') and software services, an obvious consequence is that Telstra has significant interaction with world-class IT providers, including Indian-owned companies that are global suppliers. No company doing business in the ICT area can afford to ignore the high quality and price competitiveness that Indian IT and software suppliers provide.

Perhaps less well known, is that Telstra itself has an enviable reputation for the supply of ICT services across the Asia-Pacific region. A recent Gartner study found, based on several hundred multi-national corporate customer surveys, that Telstra is the best Internet Protocol — Virtual Private Network ('IP-VPN') supplier servicing the Asia-Pacific region.[1] Telstra's Global Business Services (www.telstraglobal.com) group provides these advanced networks and other ICT services to over 200 of the companies ranked in the Fortune 500, with sales offices in numerous Asia-Pacific locations including Mumbai, Delhi and Bangalore. Our customers cover a number of vertical industries including logistics, trading, manufacturing and government. In 2005, just the IT services that our Global Business unit supplies[2] experienced 35% growth in Hong Kong and 40% growth in Singapore. This growth is driven by both new contract wins and the expanding scope of services provided to existing customers.

One of the reasons why Telstra has been so successful in the Asia-Pacific market is that it enjoys the benefit of the extensive undersea cable and satellite data and voice connectivity provided by REACH Limited (www.reach.com), a company 50% owned by Telstra in a joint venture with PCCW Limited of Hong Kong SAR. REACH's undersea cable network is the largest and most diverse in Asia-Pacific. REACH holds operating licenses and landing rights in most major Asian markets, the US and UK, facilitating access to over 240 countries and territories

Therefore, Telstra is both a customer of Indian-owned global suppliers and a potential supplier to Indian customers, particularly corporate customers. Telstra believes that the current restrictions that India applies to foreign telecommunications services providers entering its market, and which Telstra and REACH have experienced first-hand, stand in stark contrast to the ease of entry that Indian suppliers enjoy to the Australian market. It is this lack of reciprocal market access that Telstra wishes to highlight to the Standing Committee on Foreign Affairs, Defence and Trade ('the Committee').

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1 Gartner, "Survey of Best International NSPs, Asia/Pacific", 1 November 2005.

2 Typical IT services supplied by Telstra Global Business include hosting services, infrastructure management, data centre services, security management, LAN/desktop support, disaster recovery services, solutions consulting and managed services.

2. Access to the Australian ICT market

As the Committee will be aware, Australia permits 100% foreign owned entities to enter the Australian ICT market, and supply services without restriction. The only restrictions on access to the Australian market by foreign ICT suppliers are those applied under the generic Foreign Investment Review Board criteria. (The exception is foreign ownership of Telstra, limited to 35% at present.[3]) There are additionally no behind-the-border restrictions on foreign telecommunications companies entering the Australian market, given that Carriers can obtain a licence under the *Telecommunications Act (C'th)* 1997 with very little administrative burden and at nominal cost, and Carriage Service Providers need not obtain any licence at all. Significant foreign investment has flowed into the telecommunications services sector in Australia over the past 15 years, and most of Telstra's leading competitors are majority or entirely foreign owned and controlled: SingTel Optus, Vodafone, Hutchison '3', AAPT, Primus, etc. Leading international competitors such as AT&T and BT are very active in the Australian corporate communications market. Similar ease of entry applies to the IT and software services market.

Telstra fully supports the openness of the Australian market and the competition that this openness generates. By competing with major international telecommunications suppliers in its home market, Telstra is able to develop and maintain the ability to be internationally competitive. Whatever restrictions the Indian government may apply to Australian suppliers entering its communications market, and however non-reciprocal market access between India and Australia may be, Telstra continues to support free access by Indian suppliers to the Australian market.

3. Indian-owned global suppliers to Telstra

Telstra has partnered with a number of world-class IT providers. These include Satyam and Infosys whose headquarters are based in India with offices around the world, including Australia. Also, Telstra has direct supply arrangements with Indian telecommunications carriers such as Videsh Sanchar Nigam Ltd ('VSNL') and Bharti, for telecommunications services in India which are acquired to enable Telstra to service its corporate customers' Indian offices. Additionally, many international suppliers use some Indian-based resources.

This global supplier profile is typical for a major telecommunications carrier.

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[3] Foreign ownership in Telstra is restricted by Part 2A Div 4 of the *Telstra Corporation Act (C'th)* 1991. The maximum foreign ownership limits are 35% in total by all foreigners and a limit of 5% applicable to each foreign person. Note that these limits apply to Telstra shares not held by the Commonwealth, i.e. the present effective limit is a little over 17% percent in total. Div. 8 and 9 prescribe additional rules: central management and control of Telstra must ordinarily be exercised within Australia; Telstra must ensure that it maintains a substantial business and operational presence in Australia, and must remain incorporated in Australia; Telstra's chairperson must be an Australian citizen, as must be a majority of its directors.

4. Telstra does not operate any call centres in India

Telstra does not operate any call centres in India. Telstra does not contract with any Indian call centre provider to provide any customer facing services.

To the contrary, last year Telstra initiated legal action against a competitor, Orion Telecommunications, over the activities of its overseas-based call centre staff who were engaging in misleading and deceptive conduct by falsely claiming to have an association with Telstra. This litigation was settled in March this year by Orion agreeing to provide undertakings to the Australian Federal Court regarding its future conduct.[4] The problem of unscrupulous telemarketing by certain competitors has escalated to such an extent that Telstra Country Wide has undertaken a consumer education campaign — called the 'Know it's Telstra Calling' campaign — to help customers handle telemarketers using high-pressure sales tactics and avoid having their service transferred to another carrier without their informed consent. The campaign supplies customers with tips on handling calls and a list of questions to help verify that the sales call is in fact from Telstra.

Telstra brings these matters to the attention of the Committee in order to address any misconceptions that may exist regarding Telstra's use of Indian-owned global suppliers, and to make the point that an open trading relationship has both benefits and disadvantages. Telstra believes that the benefits of an open trading relationship with India far outweigh the disadvantages, and Telstra is satisfied that it has sufficient means within Australian domestic law to deal with issues created by the use of offshore call centres by its competitors.

5. India's WTO commitments in respect of telecoms services

India's current multilateral World Trade Organisation ('WTO') commitments on access to its domestic telecommunications services markets date back to the General Agreement on Trade in Services ('GATS') concluded in the Uruguay Round, and the subsequent scheduling of specific basic telecommunications commitments in an additional protocol to the GATS which came into effect in 1998.[5] The commitments made by India at the time were extremely limited. India undertook to permit 25% foreign direct investment ('FDI') in domestic telecommunications services suppliers, and to review the opening of long-distance services in 1999 and international services in 2004. The FDI

[4] See, "Orion settlement a warning to unscrupulous tele-marketers", Telstra media release dated 2 March 2006, available at http://www.telstra.com.au/abouttelstra/media/mediareleases_article.cfm?ObjectID=37016

[5] The Fourth Protocol to the GATS acted to liberalize trade in basic telecommunications services and came in force on 4 February 1998. It consists of the Annex on Telecommunications, the country-by-country Schedules of Specific Commitments (including the commitments made by Australia and India), the country-by-country Lists of Exemptions from Article II of the GATS and the Reference Paper on Basic Telecommunications in which Members made specific commitments to reform their regulatory frameworks. It is this last document which India has redrafted in far more restrictive terms than most other signatories (including Australia, which has signed up to the standard form of the Reference Paper).

commitment for telecoms was listed at 25% in India's GATS Schedule even though under Indian domestic policy up to 49% FDI in telecoms had been permitted since 1994. India refused to commit to the standard text of the Regulatory Reference Paper, instead providing its own rewrite of that document and thereby excluding key behind-the-border regulatory protections for foreign suppliers.

6. Indian foreign ownership restrictions in respect of its domestic telecoms market

India maintained the 49% foreign FDI limit set out above in respect of all telecommunications services until November 2005. The only exception was Internet Service Provider ('ISP') licences, where 100% FDI was permitted. (Though a 74% FDI limit applies where the ISP licensee operates its own international gateway.)

In this submission Telstra wishes to focus specifically on restrictions on access to the Indian International Long Distance ('ILD') telecommunications services market. (An explanation of this Licence is provided in paragraph 7 below.) Previously, access to these licences was restricted by both direct FDI limits and by indirect behind-the-border hurdles in the form of high market entry licence fees, high annual licence fees, high capital investment requirements, and requirements for senior positions to be held by resident Indian citizens. Following extensive lobbying by overseas carriers, trade bodies, and government agencies, coupled with appeals by the Internet Service Providers Association of India in respect of licensing of IP-VPN services, in late 2005 the Indian Government and the Department of Telecommunications made some significant reforms to India's FDI regulation and the ILD and National Long Distance ('NLD') licensing regimes.[6]

Specifically, on 3 November 2005, the Indian Government increased the FDI ceiling on key telecommunications services from 49% to 74%. On 14 December 2005, the Indian Department of Telecommunications issued Guidelines relaxing the requirements for an ILD licence. The key changes are set out in Table 1 overleaf:

[6] Government of India, Press Note No. 5 (2005 Series) Issued 3 November 2005 concerning the Enhancement of the Foreign Direct Investment Ceiling from 49 Per Cent to 74 Per Cent in the Telecom Sector.

Table 1: Reforms to the ILD and NLD Licensing Regimes in India, Nov 2005

	Previously	Now
Foreign Direct Investment (“FD I”) limit	49%	74%
Minimum paid up share capital	US$5.7m (Rs 25 crores)	US$0.6m (Rs 2.5 crores)
Initial non-refundable licence fee	US$5.7m (Rs 25 crores)	US$0.6m (Rs 2.5 crores)
Annual licence fee	15% of Adjusted Gross Revenue	6% of Adjusted Gross Revenue
Network rollout guarantee	US$5.7m (Rs 25 crores)	US$0.6m (Rs 2.5 crores)
Financial bank guarantee	US$4.6m (Rs 20 crores)	US$4.6m (Rs 20 crores)
Network rollout obligations	Four gateway switches including voice interconnect	One gateway switch including interconnect (but voice not required)

The requirements for an NLD licence were amended to similar levels at the same time.

While these ILD licence requirements are still onerous compared to the requirements for similar licences in liberalised telecommunications jurisdictions, they do make it feasible for overseas operators to now contemplate acquiring ILD licences (currently, no ILD licences are held by overseas operators).

7. What is an International Long Distance (‘ILD’) licence and why is it of such interest to foreign telecoms carriers?

An Indian International Long Distance or ‘ILD’ licence permits the supply of network carriage services, providing international connectivity to network facilities operated by foreign carriers in other countries. Another name for these services is “bearer services”.

Bearer services facilitate the ultimate supply of end-to-end services such as voice, data, fax, video and multimedia, etc, to customers. ILD operators are not permitted to offer services directly on the Public Switched Telephone Network (“PSTN”) in India, but must do so through domestic licensees. But importantly, the ILD licence enables to supply of Virtual Private Network (‘VPN’) services (including IP-VPNs) direct to corporate customers in India. ILD service providers are also permitted to offer wholesale services to other operators.

8. The latest reforms announced by the Indian government to the ILD licence regime come with strings attached

Unfortunately, the latest reforms announced by the Indian government to the ILD licence regime come with strings attached. Some of the provisions described in the Press Note issued in November 2005 by the Indian government undermine the market liberalisation effects of the FDI and ILD licensing reforms, by making the ILD licence virtually unworkable for foreign operators.

Condition 1.7 of the ILD licence imposes a number of national security and law enforcement requirements, for example enabling call monitoring and tracing capabilities on licensees' networks, access to these capabilities by Indian government agencies, and restrictions on the locations at which facilities may be established. The following restrictions are the key ones causing difficulty:

> Clause 1.7 (iv) of the ILD licence:
> **Restrictions on the transfer of accounting, user and network information outside India.**
>
> Clause 1.7 (vii) of the ILD licence:
> **Restrictions on the international transit routing of domestic India traffic.**
>
> Clause 1.7 (vii) of the ILD licence:
> **Restrictions on remote access for maintenance/repairs from outside India.**

As they currently stand, these ILD licence conditions would be a serious impediment to providing international voice and data telecommunications services. Here are some reasons why:

- Telstra manages its international network from a facility located in Australia, the "Global Operations Centre' or 'GOC'. If Telstra is unable to measure traffic, bill users, or attend to software patches and the like from its GOC, it cannot feasibly provide services to its customers.

- The restrictions would also prevent customers from carrying out their own day-to-day business. For example, Australian multinational companies that make extensive use of Indian business process outsourcing ('BPO') services would be severely restricted in their ability to access and manage their back-office operations in India, and in managing their international networks that connect with India.

- Unless IP networks within India can always guarantee availability, restricting traffic routing to within India only will likely impede carriage of voice over IP ('VoIP') and IP-based videoconferencing services. These services require minimal packet loss and latency. Unlike traditional circuit-switched traffic, packet-based traffic will generally seek to route itself over least congested circuits, and these circuits may

in part be external to India. Saying that you cannot route your traffic over efficient and reliable routes that happen to traverse an offshore path, is like telling motorists in Sydney that they can't use the Harbour Bridge or the Harbour Tunnel.

Telstra is familiar with national security issues and fully appreciates the obligations that it must necessarily bear in ensuring that these matters are adequately addressed. However, the conditions imposed in the ILD licence go far beyond what security agencies elsewhere in the world require.

Following further extensive lobbying by overseas carriers, trade bodies, and government agencies, with the Indian Department of Telecommunications, the Telecommunications Regulatory Authority of India ('TRAI'), the Ministry of Communications, Office of the Prime Minister, Ministry of Commerce, Ministry of Finance, Ministry of IT, and with the Chairman of the Indo-US ICT Bilateral Dialogue, on 3 March 2006 the Indian Government granted a four month stay on these ILD licence conditions until 2 July 2006. Subsequent discussion with Indian government agencies indicates a willingness to amend the conditions to make them more workable for overseas operators. However, in the interim there remains much uncertainty around the ILD licence. Given the large amount of capital and voluminous documentation required to apply for the licence, this uncertainty has discouraged applications by foreign operators for the licence. The consequence is that the only entities licensed to provide international services in India, remain Indian suppliers.

9. The impact of a restricted international services market on upstream providers

The previous high regulatory barriers to ILD market entry in India meant that the principal Indian incumbent, VSNL, was largely unrestrained in the prices it charged for international private leased circuits ("IPLCs") and other international bandwidth services. Although the telecommunications regulator, the TRAI, sets IPLC ceiling rates for VSNL's IPLC charges, these ceilings are still significantly above open market rates for equivalent circuits elsewhere.

Until there is effective ILD competition, Indian operators have an overwhelming advantage on India routes as they can acquire distant end Australian half circuits at very competitive prices, but charge their overseas competitors high prices for the Indian end half circuits (a cost which they do not have to bear themselves as the actual cost of the circuit to them is a fraction of the prices they charge).

The Committee will be well aware of the extent to which India has led the business process outsourcing ('BPO') market worldwide. What is perhaps less well understood is that BPO demands high levels of international telecommunications capacity. However, because of the high prices which Indian operators charge other telecommunications operators for international halt circuits, it is difficult for these other operators to compete for the carriage of BPO services. Consequently, not only are non-Indian telecommunications

operators hamstrung in providing low cost capacity, but Australian end-customers for BPO services must pay higher connectivity charges to Indian operators than they would if there was equal opportunity for other operators to compete.

Particularly, Australian suppliers who specialise in high value services, such as architects and logistics providers, require high bandwidth network connectivity to successfully run offshore offices. The artificially raised costs of providing telecommunications network services into India mean that these Australian suppliers are disadvantaged in competing in the Indian market with their Indian competitors who do not face such costs.

Therefore, in order to bring down the price of Indian international capacity, it is essential that the restrictive conditions currently in the ILD licence are removed or suitably amended to allow overseas operators into the ILD market. Certain TRAI international resale initiatives proposed to be introduced in 2007 should also help in the competition process — provided that they are in fact implemented (see paragraph 11 below).

10. Restrictions in respect of landed submarine cable capacity

Despite the potential pro-competition effects of the changes in India's FDI and ILD licensing regimes, the continued exclusive control of submarine cable landing stations and associated facilities, such as backhaul, by the Indian incumbents constitute bottlenecks that may continue to stall market entry by foreign operators.

While an ILD licence permits a licensee to own and use submarine cable capacity landing in India, to be able to deploy that capacity commercially the licensee must be able to access the cable station where the cable system on which the licensee owns capacity, lands. That is, the ILD licensee must be able to connect its capacity landing in the cable station with domestic capacity that allows connectivity to the rest of India in order to provide services in the ILD marketplace. This cable landing station connection is known as "cross connection", and capacity from the cable landing station to the national trunk network is known as "backhaul".

Access problems in India have in the past been faced not only by the operators who land a submarine cable system at a cable station, but also by operators who have acquired elements of capacity on a cable system and wish to access their capacity at the cable landing station — to cross connect to another cable system in which they have capacity or to backhaul capacity which they have leased or built. All cable landing stations in India are currently owned by domestic Indian ILD licensees.

On 16 December 2005 the Indian telecommunications regulator, the TRAI, issued recommendations proposing cost-based equal access to submarine cable landing stations and associated facilities. However, these

recommendations have yet to come into effect. There is no obligation that TRAI recommendations be adopted by the Indian Department of Telecommunications or the Minister of Communications & Information Technology ("the Minister"). The powers of the TRAI are considerably more limited than the powers of its Australian counterparts. There are many examples of TRAI recommendations either being amended significantly or not being adopted at all.

Not only is there significant uncertainty about the final outcomes for TRAI recommendations, but the TRAI recommendation process seems, on occasions, to delay or take pressure off the final Department of Telecommunications or Ministerial decision making process. Taking TRAI's recommendations regarding cable station equal access as an example, TRAI's announcement in December 2005 that cost-based cable station equal access arrangements will be introduced did much to encourage overseas operators that, in conjunction with the new ILD licence terms, this would enable genuine international facilities competition. Accordingly, overseas operators commenced plans and arrangements to enter into the Indian ILD market in anticipation of this happening without the need to exert exceptional pressure on Indian government agencies to address cable station access issues. However, some five months later, there has been no further statement from any Indian government agency concerning cable station access, and there is no defined period in which final regulation must be issued.

As cable station access arrangements and costs are critical factors in establishing and rolling out international networks connecting to India, the continued uncertainty about these arrangements is a serious impediment to overseas operators' plans to apply for ILD licences, and their ability to commence negotiations with cable station owners for access to capacity on submarine cable systems landing at cable stations.

This example demonstrates the need for clarity in relation to the status of TRAI recommendations and the need for certainty about the adoption of those recommendations — or, at a minimum, the timeframe in which such recommendations must be either adopted or dismissed by the Department of Telecommunications and/or the Minister.

11. Prohibitions on the resale of telecoms services

With the exception of Internet services under an ISP licence, resale of telecommunications services is currently not permitted in India — i.e. only facilities-based licensees are allowed. Even resale of telecommunications services purchased at retail prices is prohibited. This contrasts sharply with the Australian regulatory regime where not only are resellers permitted, but they need not even obtain a licence, and in many cases they obtain the benefit of volume-based wholesale pricing.

Such a resale prohibition is out of step with the increasingly sophisticated market for international telecommunications services and constitutes a barrier to market entry:

- The international market is now characterised by layered chains of supply: cable builders sell large blocks of capacity to specialist wholesale carriers who in turn sub-divide the capacity to sell to smaller carriers which sell the capacity on both a wholesale and retail basis. Value-added features may be added at each layer of supply, but often capacity is simply resold from one layer to the next.

- The advantage of these chains of supply is that they allow aggregation of demand and, therefore, allow smaller operators to share in purchasing economies they would not enjoy if buying directly from the original capacity holder. Resale encourages the emergence of specialist wholesale providers.

- Prohibitions on resale have the effect of eliminating the intermediate wholesale markets. The effect is to reduce the overall level of competition and to reduce the scale economies which are passed to end users.

- Resale helps reduce the barriers to entry. While international capacity costs have fallen, the market is still characterised by the high fixed costs required to invest in capacity. Resale allows the wholesale purchaser of capacity to share some of the risk by reselling part of that capacity to another wholesale provider. A prohibition on resale, therefore, can raise barriers to entry and result in the market being characterised by a small number of large operators.

On 16 December 2005, the TRAI issued recommendations that the resale of IPLCs be allowed from February 2007. However, as noted above the Indian Department of Telecommunications and the Ministry are under no obligation to accept these recommendations. If such recommendations are not given effect, then Indian consumers and overseas operators will both be denied the major benefits and opportunities that resale offers.

12. Restrictions on foreign employees

As is the case with many of Australia's Asian trading partners, India prescribes restrictions on foreign employees in senior roles in telecommunications carriers. For example, in the new ILD licence, Condition 1.2 requires the majority of Directors on the Board including the Chairman, Managing Director and Chief Executive ("CEO") to be resident Indian citizens. Condition 1.7(iii) also requires the Chief Technical Officer ("CTO") and Chief Financial Officer ("CFO") to be resident Indian citizens. The Department of Telecommunications can notify further key positions to be held by resident Indian citizens.

Unsurprisingly, even the Indian incumbent telecommunications carriers have complained to the Indian government about these restrictions. The *Economic Times* reported in May under a headline, "Call Alert: allow foreign bosses at telcos, says DoT", that Tata Teleservices had made representations to the Indian government to amend the proposed ILD licence rules so that its current CEO, Darryl Green (a foreign national), could remain in his job.[7] The newspaper claimed that the Indian Department of Telecommunications had sent a memorandum to the Minister supporting such an amendment to the ILD licence conditions.

It is a matter for India to determine whether such restrictions are desirable, or whether they act counterproductively to restrict a company from hiring the most appropriate employees. Australia also maintains some rules of this nature, for example the *Telstra Corporation Act (C'th)* 1991 prescribes that Telstra's chairperson must be an Australian citizen, as must be a majority of its directors. However, the Indian restrictions are far more intrusive in forcing new entrants to its market to comply with these restrictions, and in applying the restrictions at both executive management and board level.

13. Conclusion

In this submission Telstra has explained some of the numerous hurdles facing foreign carriers wishing to enter the Indian telecommunications services market. While foreign investors do have significant investments in a range of Indian telecommunications assets, from mobile carriers to ISP licensees, the continuing controversy over the ILD licence restrictions illustrates the difficulty facing Telstra in participating in this key market. It is not only Telstra's shareholders that lose out, but also Indian corporate customers, when the Asia-Pacific region's best IP-VPN carrier is prevented from participating in the Indian market.

Telstra asks the Committee to recommend that Australian government and trade officials redouble their efforts to enable Australian suppliers to enjoy the same level of access to Indian markets, which Indian-owned suppliers currently enjoy in Australia.

[7] Manoj Gairola, "Call Alert: allow foreign bosses at telcos, says DoT", *Economic Times*, 24 May 2006