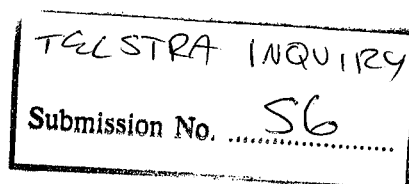


31 January 2003

The Secretary
House of Representatives Communications,
Information Technology & the Arts Committee
R1, Suite 116
Parliament House
CANBERRA ACT 2600



Dear Sir

Inquiry into the Structure of Telstra

Thank you for the opportunity to provide a submission to the Committee on the inquiry into the structure of Telstra.

Hutchison considers that the question of the economic and social impact of structurally separating Telstra's core network from its other businesses and reducing the Commonwealth's current shareholding in Telstra's non network businesses is a very significant issue for the telecommunications industry and for the benefits of real competition being provided to end users of telecommunications services in Australia over the long term.

For this reason, we wish to have recorded our concern at the extremely short time frame that the Committee has allowed itself to consider such an important issue and, as you will see from the enclosed paper, we consider that the optimal outcome from the Committee's inquiry is that the Committee recommend that a detailed review be undertaken of the questions before the Committee.

The key points which Hutchison wishes to make are detailed in the attached paper "Investigating the Benefits and Costs of the Structural Separation of Telstra" by Gans and King.

In addition, Hutchison's comments on some of the other issues raised are set out below.

The question of whether there should be separation of Telstra's core network from its other businesses cannot be considered as a new or isolated question. It forms part of the implementation of a long held policy to introduce competition to the Australian telecommunications industry.

During the last 15 or 20 years a number of models have been adopted by different countries to reduce the monopolist position of incumbent operators in the deregulation of their telecommunications industry. No one model has been dominant, and none has been without issues. In each country, including Australia, the model was chosen without any certainty that it would be successful.

It is becoming apparent that the policy choice in Australia to avoid structural separation and rely on regulation is failing to have any real impact on the monopolist position of Telstra. The fact that Telstra still receives over 90% of the industry's profits is one indication of this. The fact that the telecommunications specific provisions under the Trade Practices Act and other related telecommunication legislation continue to be tinkered with and amended in a piecemeal fashion is another indication that the approach taken will not work. Even the latest amendments (Telecommunications Competition Bill 2002) leave significant room for regulatory gaming at the expense of true deregulation. Whilst this latest regulation is welcomed, it is clearly limited and there is no certainty that it will resolve Hutchison's concerns about the impact of Telstra's monopolist position.,

The various forms of Telstra's anti-competitive conduct have been described in the numerous inquiries that have been conducted. This includes anti-competitive behaviour associated with bundling, control over innovation, access price manipulation, creating delays and inventing barriers to entry. Parts XIB and XIC of the Trade Practices Act are intended to deal with these issues but the lack of transparency in Telstra's operations make it nearly impossible to pursue suspected breaches. The primary problem of the current regulation is that it places the burden of proof in identifying anti-competitive conduct on those alleging it. One of the benefits of structural separation is that it would remove many of the difficulties in the current regulatory provisions intended to deal with Telstra's anti-competitive conduct.

Hutchison considers that the Government must acknowledge that the existing policy approach is reaching the limits of its effectiveness and that a new approach is needed if the objective of a truly competitive telecommunications industry in Australia is what the Government wants to achieve.

The structure of Telstra and its vertical and horizontal dominance of the telecommunications industry have driven most of the regulatory activity in the industry over the last 10 years. The increasing level of regulation in the telecommunication industry is proving to be costly and ineffective. These costs are borne by Telstra and all other participants in the industry, and are passed on to end users. It follows that the structural separation of Telstra would reduce the need for such regulation and thus the cost to Telstra and other participants in the industry. This cost savings should also flow on to end users, thus enhancing the efficient provision of services to those end users.

Hutchison acknowledges the complexity that would be involved in any structural separation, but this is a short term issue which should not be allowed to cloud the long term benefits. Structural separation would not be impossible, and has been undertaken by many equally complex organisations in Australia and overseas as part of deregulation.

As noted in the attached paper there is no evidence to suggest that structural separation of Telstra would have a negative economic impact and in particular would have no effect on the efficient provision of services to end users or on Telstra's ability to continue to provide a full array of telecommunications and advanced data services.

Fears that the separation of Telstra would have a negative impact on shareholder value and the Government's budget should be dismissed as irrelevant and short sighted. As noted above the reduction in regulatory costs alone would deliver benefit to consumers. Furthermore, the gains to all telecommunication users (and not just Telstra shareholders) from a more competitive telecommunications industry cannot be overlooked.

The claims of the negative impact on the Government's budget needs to be properly examined. A paper prepared by Access Economics (Further Reform of Australian Telecommunications Regulatory and the Budget Impact of the Privatisation of Telstra – June 2002) challenges the questionable assumptions about the value of Telstra and impact on the Government's budget. Some analysts (with apparent self interest) identify the impact on the value of Telstra and place

importance on the immediate proceeds from the sale of Telstra. They ignore that an efficient and competitive telecommunications industry will yield significant net benefits to the Australian economy over time. "Whether the Commonwealth Budget balance ultimately improves more by selling Telstra with or without its residual monopoly power is an empirical question that remains to be investigated"- Quote from the Access Economics paper.

In conclusion, Hutchison requests that the Committee does not let questions relating to the complexity of structural reform, the Telstra share price or the potential sale of the Commonwealths' shareholding in Telstra to deflect it from considering the importance of structural separation of Telstra to long term competition in the Australian telecommunications industry and the benefits this will bring to the Australian economy. Hutchison therefore asks the Committee to recommend a thorough review by an independent body such as the Productivity Commission.

Yours faithfully

Louise Sexton
General Counsel &
Company Secretary