Submission No 28

Australia's trade and investment relations under the Australia-New Zealand Closer Economic Relations Trade Agreement

Organisation: **AAPT Limited**

Contact Person: David Havyatt
Head of Regulatory Affairs

Address: **Level 21**
680 George Street
SYDNEY NSW 2000

Joint Standing Committee on Foreign Affairs, Defence and Trade
Trade Sub-Committee

Australia's trade and investment relations under the Australia-New Zealand Closer Economic Relations Trade Agreement

Submission by AAPT Ltd to the Joint Standing Committee on Foreign Affairs, Defence and Trade

July 2006

Outline

The Committee has been asked by the Minister for Foreign Affairs to review the ANZCERTA. The full terms of reference are;

> The Joint Standing Committee on Foreign Affairs, Defence and Trade shall examine and report on Australia's trade and investment relations under the Australia and New Zealand Closer Economic Relations (CER) Trade Agreement with particular reference to:
>
> - The nature of Australia's existing trade and investment relationships
> - Likely future trends in these relationships
> - The role of Government in identifying and assisting Australian companies to maximise opportunities under CER
> - Complementary policy approaches by the two governments

In its submission and appearance before the committee Telstra has repeated its request for the explicit inclusion of telecommunications in CER. This follows the decision by Ministers to not progress with this work.

In its submission Telstra made great play of its significant role in serving telecommunications customers with Trans Tasman needs. That is a role shared by Telecom New Zealand and its Australian subsidiary, AAPT. This submission is made by AAPT and is expressly drafted in terms of why the proposals in the Telstra submission are not in Australia's interest.

Overall, the Telstra submission is misleading, both in terms of the history of trade agreements and deregulation, and in terms of the benefits that might accrue to customers. These specific issues will be addressed further in this submission.

However, before progressing it is worth addressing the reason why telecommunications "harmonisation" has thus far been excluded. Governments say they have not taken up the suggestion according to Telstra because the regimes are still bedding in. Telstra in evidence to the Committee[1] suggested that it was because they are bedding in that this is a good time for harmonisation. It is AAPT's contention that the two Governments are right not to progress on harmonisation, because:

> (a) the regimes are indeed a lot more common than Telstra has represented. Indeed, AAPT interprets the recent announcements in New Zealand[2] not as a further step in harmonisation (as Telstra seems to see it), but as a demonstration why harmonisation would be premature.
>
> (b) the issue that most needs to be bedded in is the competitive market structures, not just the regulations designed to bring them about, and
>
> (c) it remains the expectation of Governments on both sides of the Tasman that eventually the telecommunications specific regime will be wound back and the industry will rely exclusively

[1] Dr Warren in the transcript of the committee's hearing of 12 May on page 9.
[2] Minister Cunliffe announced on 3 May 2006 the legislative unbundling of the local loop and other measures, see http://www.beehive.govt.nz/ViewDocument.aspx?DocumentID=25636.

(again in New Zealand's case) on generic competition law. In this context it would appear to make the most sense to prioritise work on the harmonisation of competition and consumer law as is currently being addressed by the Joint Australia/New Zealand Working Group on Trans-Tasman Competition & Consumer Issues being chaired by Paula Rebstock (Chair of the NZ Commerce Commission). The work of that committee is already making it clear that there is significant work to cover to simply harmonise these laws.

This submission is laid out in the following sections;

1. Description of AAPT and a brief review of the telecommunications market structures in Australia and New Zealand since the inception of CER.
2. A brief review of the purpose of Trade Agreements in general, and the specific inclusion of Telecommunications clauses.
3. A brief rebuttal of the claims that Telstra makes for end-user benefits from harmonisation.
4. A suggested way forward for the inclusion of telecommunications in CER on a sustainable basis.

1. Brief description of AAPT and market structures

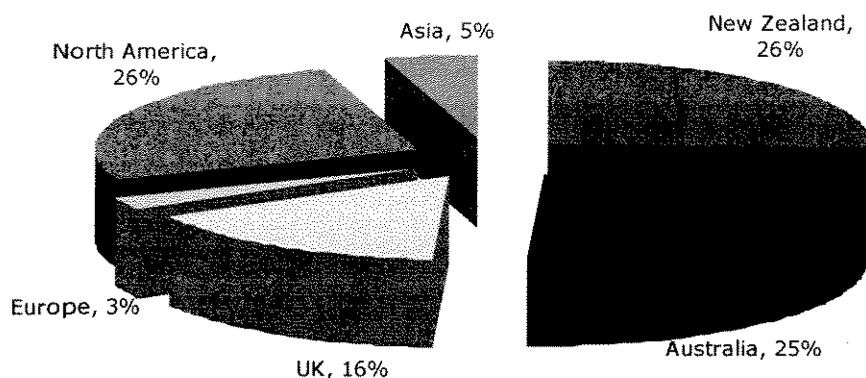
In the late 1970s and early 1980s a number of large corporations started to become frustrated in their corporate ambitions by the state of telecommunications. This was either because the lack of certain data services was inhibiting the utilisation of modern computing facilities, or because they were restricted from offering services to customers because of tight restrictions on interconnection.[3]

One of the firms in the latter group was Australian Associated Press (AAP), which was at that time commencing the provision of news services directly to the financial markets. As the Australian market commenced deregulation in 1991 AAP decided to take advantage of the new regime and exploit what by then was one of the largest private networks in Australia, and established a subsidiary, AAP Telecommunications. Over the next five years AAPT had a number of partners in this business, including Todd Corporation of New Zealand, MCI and SingTel. In 1996 the company was floated on the Australian Stock Exchange as AAPT. As a consequence of on market offers in 1999 and 2000 AAPT was subsequently fully acquired by Telecom New Zealand.

As will be noted below Telecom New Zealand was fully privatised over fifteen years ago, and the stock is widely held outside New Zealand. The graph below shows the geographic break-up of ownership at 31 March, 2006. As discussed in evidence before the committee only 26% of the company is held by New Zealanders, and 25% is held by Australians.

[3] See Ian Reinecke *The Phone Book* for a summary.

Geographic Analysis of Investors in Telecom New Zealand, 31 March, 2006.



Since its acquisition by Telecom AAPT has continued to build on its early success. The group's turnover in Australia is now $1.2B, which is only 3% of overall industry revenue, but is roughly the same as Vodafone. The Australian market continues to be dominated by Telstra and Optus. While there are, literally, hundreds of service providers competing in the Australian market, it is still a highly concentrated industry using any of the measures usually employed.[4]

It is worthwhile to note in summary that;

- AAPT was created from a consumer of telecommunications services
- AAPT offered services in competition to Telstra before Optus in 1991
- AAPT was the first telecommunications service provider to list on the ASX
- The Australian industry remains exceedingly concentrated.

The story in New Zealand is slightly different. Australia undertook a highly staged and gradual market opening from 1989 (deregulation of CPE), through 1991 (fixed duopoly, mobile entry, deregulated resale service provision) and finally the current regime in 1997. One could say the reform is not yet complete as the Australian Government is still the majority owner of the incumbent.

In New Zealand there was a far more dramatic move to deregulation in early 1989 and the sale of Telecom by tender was announced on 23 February, 1990; that is, the near simultaneous outright sale of Telecom New Zealand and the removal of all restrictions on market entry.[5] This was seen at times around the world as incredibly adventurous. In Australia the steady progression of duopoly and then full entry

[4] Competition regulators use either an HHI measure which is the sum of the squares of the market shares of competing firms, or they use a test of the combined market share of the largest 4 firms.

[5] It should be noted that this was an element of the "Rogernomics" referred to in the Committees roundtable. Mrs Howard rightly identified the greater facility for changing Government policy in New Zealand due to its single level of Government and unicameral parliament. However, this same facility had led the economy to be highly and over-regulated in the early 1980s. The ongoing New Zealand antagonism to regulation that is often ascribed as a cultural value had its source in the nation's real experience of detailed prescriptive regulation.

was a position promoted by Telstra (well, Telecom Australia then) and widely thought to be a move to protect Telstra. In fact the Australian change in 1991 was accompanied by the highly controversial decision to merge Telecom Australia and the Australian overseas carrier OTC.[6]

The successful bid for Telecom New Zealand for $NZ 4,250 million was announced on 12 June, 1990. The bid was for 100% in a consortium led by Ameritech and Bell Atlantic. The consortium partners would sell 5% to each of two New Zealand companies and otherwise sell down to 49.9% over three years.

The two biggest competitors in New Zealand are Vodafone, which operates the only other mobile network in New Zealand. Vodafone acquired this business in acquiring the assets of Bell South. The other is TelstraClear which came about from the acquisition by Telstra Saturn of Clear Communications. Clear Communications had been established as a consequence of the merger of consortia being developed by Bell Canada and MCI to enter the deregulated New Zealand market in 1989. Todd Corporation was initially a shareholder in both Clear and AAPT An interconnection agreement was negotiated with Telecom New Zealand in March 1991. As noted by McCabe; "The interconnection agreement was internationally unique in that it did not involve the government, any government agencies, or any intervention by the courts: It was negotiated by the two carriers alone." Unfortunately, this state did not endure as court actions subsequently commenced as Telecom was "adamant that Clear should pay an access levy as a contribution toward Telecom's service obligations". Ultimately the matter of interconnection would end in the Privy Council.

Telstra had established an office in New Zealand from its merger with OTC in 1992 to provide business services, primarily Trans Tasman links. In the mid 1990s Telstra made a further significant investment merging its New Zealand operations with Saturn, a subsidiary of UIH (and sister company to Austar) which was at that stage building an HFC (Pay TV) network in Wellington and Christchurch.

There are less competitors overall in New Zealand, but this is to be expected in what is a far smaller market with only one city (Auckland) of the size of the minor Australian mainland State Capitals. Consequently, the New Zealand market is also extremely concentrated.

In 2000 both Australia and New Zealand conducted reviews of their telecommunications regulatory regime. The Australian review was required under the 1997 Act which had foreshadowed that some aspects of the regime could be removed as competition developed. The New Zealand review was from a background of concluding that the "unique experiment" had not resulted in market opening keep pace with other economies.

Both reviews concluded there was a need for regulation. In the Australian case a raft of measures were introduced to try to reduce gaming of the regime, and the abandonment of the attempt at self-regulation of access – the Telecommunications Access Forum. In the New Zealand case a new Telecommunications Act was introduced that was largely based on the Australian 1997 Act including the creation of an access regime.

---

[6] See Patrick McCabe "New Zealand: The Unique Experiment in Deregulation" in Eli Noam et al (Eds) *Telecommunications in the Pacific Basin,* Oxford University Press. 1994. This article reveals that OTC was actively involved in considering bidding to acquire Telecom. The identities of the five short listed parties were not disclosed.

While there are numerous differences between the two regimes, the most notable feature is that both regimes have left the operation of the access regime to the generic competition regulator, which remains an unusual feature by world standards.

2. The purpose of Trade Agreements and the inclusion of telecommunications

Economists have long recognised a thing they call "the gains from trade". This is, in fact, nothing more than the flip side of the observation that Adam Smith made that there are efficiencies in specialisation. The general theory is that markets are good and their efficient operation is to be promoted.

In the more specific instance of international trade, the gains from trade occur by enabling individual economies to specialise. It is universally accepted by economists, but not policy makers, that "unilateral" free trade is a net benefit to an economy so long as the resources released by importing goods can be productively employed in other sectors. As a consequence, multi-lateral free trade is preferable to unilateral moves as it facilitates the process of readjustment in all economies and hence accelerates the realisation of the gains.

A bilateral free trade agreement is thus better than unilateral moves, but not as beneficial as multilateral agreements.

The history of CER is that it evolved from pre-existing Free Trade agreements. The earlier agreements were cumbersome and required the detailed negotiation for the inclusion of specific goods in the agreement. CER has always extended beyond goods to include services. The current description of the services component reads:

> *Free trade in services. New Zealand and Australian service providers can provide services in each others markets without any restrictions on the basis of a "negative listing" approach. New Zealand retains only two inscriptions (airway services and coastal shipping) and Australia only six (air services, broadcasting and television (x2), third party insurance, postal services and coastal shipping)*[7].

In its submission Telstra details the unfolding process whereby the inscriptions for telecommunications by Australia were withdrawn. It is worth noting that these were Australian, not New Zealand, inscriptions, and that these inscriptions reflected the unfolding state of telecommunications regulation in Australia.

Telstra also tried to draw contrasts between the way telecommunications has been included in the US and Singapore FTAs and its non-appearance in CER. While the actual substance of those sections will be discussed later, their non-appearance in an agreement dating from the early 1980s is hardly surprising.

In fact, the sequence of policy making in Australia worked in the direction of first goods and then services. Australia embarked on a number of marketing opening initiatives from the mid 1970s (the Whitlam 25% tariff cut) through to the 1980s (CER with New Zealand, an array of industry plans to reduce tariffs). Governments around Australia recognised that our agricultural and manufacturing industries were facing increasingly competitive markets, but that many of their inputs were not. The

[7] http://www.mfat.govt.nz/foreign/regions/australia/cer2003/cerbackgrounder.htm

Hilmer Committee reviewed the economy as a whole and thus the National Competition Policy was formed. Global trends and analytical work from the Bureau of Transport and Communications Economics were at the same time resulting in regulatory reform in these sectors.

It is not surprising that reform of competition in services followed reform of trade in goods, it was the reform in trade of goods that created the need for reform in services.

The specific inclusion of telecommunications provisions in each of the Singapore-Australia Free Trade Agreement and the Australia-United States Free Trade Agreement building on the GATS annex poses the question of why these provisions have been included. In conversation with DFAT and DCITA officials AAPT has previously advanced the view that there are potentially three separate reasons for these inclusions;

1. To create market opportunities. This would be the most obvious reason for the inclusion of telecommunications. Unlike other services like Finance the bulk of the delivery of telecommunications still relies on physical networks, though increasingly global competition is occurring at the service layer. Australia only has two domestic telecommunications companies that have really expressed interest in directly entering service provision in the wider Asian region.
2. To ensure adequate telecommunications services for other service based trade. This is akin to the original motivations for telecommunications reform in markets like Australia. It is only viable for banks, for example, to operate in markets with advanced telecommunications services. Market entry provisions ensure that these services can be provided.
3. To facilitate internal reallocation of resources. As described above the gains from trade occur as a consequence of the ability of each economy to reallocate productive resources inside the economy. All the micro-economic reforms within Australia fall in this category – including labour, energy and telecommunications markets.

To determine there is a need to specifically cover more aspects of telecommunications in the context of CER would require one or more of these characteristics to hold. None of them do as the New Zealand and Australian regulatory regimes both fully provide for all the elements typically required in Free Trade Agreements.

AAPT notes that the first meeting of the Australia New Zealand Business Leaders Forum included telecommunications in the list of the "seven key elements of a single market". However, AAPT is not aware of any Australian or New Zealand corporation that has identified the current state of telecommunications in either market as a current impediment to business activities. That is, other than Telstra whose interests are exclusively about investment.

3. A brief rebuttal of the claims that Telstra makes for end-user benefits from harmonisation.

AAPT remains totally unclear as to whether Telstra's argument is that telecommunications should be included in the CER agreement to reflect the current state of Australia's other major FTAs or whether Telstra's request is entirely due to a need to fundamentally "harmonise" regulation in the context of the Single Economic Market.

If it is the latter, then all Telstra's references to the other FTAs is merely atmospherics. However, on the assumption that Telstra genuinely believes that there are aspects of Australia's major FTAs on

telecommunications that are not provided for, the committee may like to ask the Department of Communications Information Technology and the Arts (DCITA) to provide a tabular summary of the requirements under the WTO, the two FTAs and how they would be currently met in each of Australia and New Zealand. A committee of APECTEL has recently compared evaluated all the APEC economies against the WTO criteria, an extract covering only Australia and New Zealand is attached as Attachment A.[8]. This demonstrates that both countries are at similar stages of WTO compliance.

AAPT notes that there has been no need for additional legislation in Australia to support the FTA provisions on telecommunications. We further note there would be no need for legislation in New Zealand were CRA to have the FTA clauses added.

Telstra claimed in their presentation to the Committee that they would have litigation rights under the Trade Agreement were the New Zealand decision not to unbundle made under the FTA provisions. AAPT notes that the Singapore FTA covers unbundling at Article 9.3in the following terms;

> Unbundled Network Elements
> (a) Each Party shall ensure that major suppliers in its territory provide to facilities-based suppliers of the other Party access to network elements for the provision of public telecommunications services at any technically feasible point, on an unbundled basis, in a timely fashion; and on terms, conditions, and cost-oriented rates that are reasonable, transparent, and non-discriminatory.
> (b) Each Party may determine, in accordance with its domestic laws and regulations, which network elements it requires major suppliers in its territory to provide access to in accordance with Article 9.3(a) on the basis of the technical feasibility of unbundling and the state of competition in the relevant market.

The US FTA covers unbundling in Article 12.10 in the following words;

> Unbundling Of Network Elements
> Each Party shall provide its telecommunications regulatory body with the authority to require that major suppliers in its territory provide suppliers of public telecommunications services of the other Party access to network elements for the provision of public telecommunications services on an unbundled basis, and on terms and conditions, and at cost-oriented rates that are reasonable, non-discriminatory, and transparent.

AAPT notes that both agreements make it clear that the decision on the scope of unbundling is determined by the law, and in the US case the only requirement is that the regulatory body has the authority to require unbundling. As evidenced by the 2003 Commerce Commission inquiry and decision, the New Zealand regime met that requirement. However, Telstra and others were unsuccessful in convincing the regulator to do so.

---

[8] Paper available at
http://www.apectelwg.org/document/download.jsp?fname=APEC_TEL33WTO_Reference_Paper_Implementation_2006_Update.doc&all_cd=010203&d_seq=3271 (last accessed 13 July 2006)

In fact, it was Telstra that continued to dispute the regulators call and actively lobbied for Ministerial intervention over the independent regulator, just as they have in Australia where they have sought the Government's direct involvement in establishing ULL prices.[9]

It appears to AAPT that the Minister in Australia agreeing to any request by Telstra to intervene on unbundling, given the Government's continued ownership of Telstra, would breach both the US and Singapore FTA.

A similar position applies to the provisions in both agreements in relation to number portability. While Telstra argues that number portability is not yet available in New Zealand, it has been available under the regime. Telstra may simply be unaware of the amount of effort it took providers like AAPT and Optus (for fixed) and AAPT and Hutchison (for mobile) to get the relevant regulatory bodies (both the ACA and ACCC) to exercise the relevant powers in Australia.

Telstra has made two specific claims about the benefits to end-users of harmonisation. The first relates to the high inbound mobile roaming rates in New Zealand. The second is the ease of single contracts.

The facts in relation to the mobile market is that there are currently only two mobile networks operators in New Zealand, Vodafone (operating a GSM network) and Telecom (operating a D-AMPS and a CDMA network). In Australia there are four network operators – Telstra, Optus and Vodafone operate GSM network and Telstra and Hutchison have been operating CDMA networks (though both are closing). All four operators are sharing in two 2.1GHz 3G networks.

Only the GSM operators have sought the ability to roam into New Zealand. While Telecom CDMA roams into Australia, Telstra has only recently commenced to roam their CDMA in New Zealand. However, when Telstra migrates to their 850 3G network it will be only able to roam on Vodafone again.

Consequently, Vodafone faces no competitive pressure on inbound roaming. Suddenly creating "one market" does not change this fact. Neither regime has ever declared domestic roaming – and Telstra has opposed it. The supposed saving of $31M a year in roaming charges is illusory and Telstra knows it.

The second major benefit is supposed to flow from the ability to have "one contract and one bill". There is nothing in the existing regime to stop a person who is a service provider writing one contract and offering one bill. AAPT is bemused by Telstra's inclusion of harmonisation of interception requirements under this customer heading.

Telstra has two other benefits – the making of technology decisions Trans-Tasman and the elimination of duplication of effort by regulators. AAPT notes that the Telecom group already does make Trans-Tasman technology decisions except in so far as we perform different roles as the primary access network provider in one market and a service provider in the other. In relation to duplication, AAPT believes more effort would be required to harmonise the regimes than is created by the existing "duplication".

---

[9] Note that events in New Zealand with the Ministerial announcement of May 2006 have overtaken the original decision making of the independent regulator.

4. A suggested way forward for the inclusion of telecommunications in CER on a sustainable basis.

AAPT notes that the continuing economic integration of Australia and New Zealand will continue the speed at which companies are operating on a Trans-Tasman basis. For this reason AAPT commissioned IDC to undertake research on corporations who have established a Trans-Tasman operational model.

That paper[10] concluded;

> While all of the executives interviewed had made progress towards the integration of their Trans-Tasman businesses and are beginning to enjoy the benefits of synergies between Australia and New Zealand, a number of goals had not yet been achieved. Future progress is expected and desired in the following areas:
>
> - Further leveraging the advantages and benefits from one location to another, such as best practice production techniques, customer management, supplier management and identifying and removing duplication
> - Conveying the reality that business units in both Australia and New Zealand are being treated equally by centralised service delivery functions
> - Better understanding of the differences between business units where competitive advantage can be identified and transferred
> - Breaking down barriers and more effectively managing attitudes of "us and them"
> - Improving the ease of transacting across different banking systems
> - Establishing a single Trans-Tasman currency
> - Establishing a GST treaty, to simplify and harmonise GST between the countries
> - Setting up single Trans-Tasman suppliers (ICT, Banking, Finance, and Energy). The advantages of a single Trans-Tasman suppler include:
>   - ➢ Decreased cost and effort to maintain multiple supplier relationships leading to an increased accountability of single suppliers
>   - ➢ Consistent Trans-Tasman standards that support common rollouts across both countries driving down costs and implementation time
>   - ➢ Ability to leverage Trans-Tasman size for buying power
>   - ➢ Simplifying communications of key transformational elements, such as business processes, reducing implementation time and payback time

As can be seen from this list, the primary requirements remain issues of banking and GST. The greatest interest from a user perspective is "Consistent Trans-Tasman standards that support common rollouts". Technical standards have not been a key feature of the discussion to date. Within APECTEL much work is occurring to develop common technical standards and mutual recognition programs. This is potentially a useful area, however it does not require regulatory harmonisation..

AAPT agrees that greater co-ordination between the ACCC and Commerce Commission would be desirable. In particular AAPT has previously noted and recommended the adoption of the New Zealand model where there is a dedicated telecommunications Commissioner. AAPT would support proposals that were both countries to have such Commissioners that they could be appointed as Associates to each other's Commission.

---

[10] Paper available at http://www.aaptbusiness.com.au/business/solutions/transtasman/whitePaper.cfm?o=420

AAPT would further support regular meetings that include both policy departments and regulators to undertake "stocktakes" of the current institutional settings in both markets. However, we would note that these meetings are more likely to be productive if conducted on the "economy to economy" model of APECTEL than the "government to government" model more traditionally associated with international relations.

Finally, AAPT notes that we have had numerous instances of "but they said in the other country" in relation to documents that were confidential to other country proceedings. The Telecom group has previously proposed to Telstra/TelstraClear that we agree that any information that one Commission has been privy to can be made available to the other covered by the same rules of confidentiality. Failing such agreement, the matter could be dealt with by legislation.