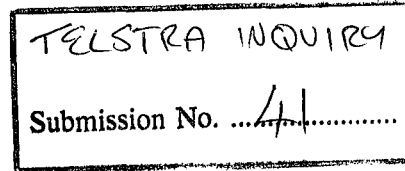




SERVICE PROVIDERS INDUSTRY ASSOCIATION

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31 January 2003



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

Dear Mr McMahon

Inquiry into the structure of Telstra

Thank you for your letter of 20 December and the invitation to make a submission to your Committee related to this inquiry. I include a brief submission addressing the terms of reference of the inquiry and drawing on SPAN's established views on relevant policy issues as well as comments contributed by some of our members.

As you will appreciate, our association represents a wide range of telecommunications service providers and associated organisations, including Telstra and its principal competitors as well as its major wholesale customers. Opinions on a range of policy issues display different attitudes across the membership, so that I cannot claim that the views included in our submission would have unanimous support. However, I believe that they reflect the core values of the association and that they are consistent with the views put forward by members when invited to contribute to this submission.

I hope that our submission assists the Committee in its very important task and offer further assistance or elaboration of the material at your convenience.

Sincerely

Phil Singleton
Chairman

*Submission to the House of Representatives Communications, Information Technology & the Arts
Committee*

*On it's Inquiry into the structure of Telstra
From the Service Providers Industry Association Inc. (SPAN)*

About SPAN:

SPAN is Australia's national association of telecommunications service providers, dedicated to building an open, competitive telecommunications industry. It was formed in 1993 when competition in provision of telecommunications services was beginning in Australia. It has grown to include around 80 members including major and newly established carriers, service providers and organisations providing equipment and services to the telecommunications industry. Further information about SPAN can be obtained from its website www.span.net.au and from its principal project website www.broadbandxchange.org.

SPAN's mission statement is:

- To foster open, effective and ethical competition in Australian telecommunications markets.
- To ensure all service providers obtain access to networks and facilities in a manner suitable for the provision of sustainable competition in services to end users.
- To ensure that members are committed to delivering the highest standards in customer service, innovative products and services and prices, which represent excellent value.

SPAN's objectives are:

- Provide an effective forum for all industry participants, including access providers and access seekers, to work co-operatively together to develop the overall market to their mutual benefit.
- Contribute constructively to the ongoing development of industry and regulatory policy; particularly through representation of members on self-regulatory industry bodies.
- Promote the highest standards of business ethics and behaviour.
- Provide information and other services valued by the membership.

SPAN's position on relevant policy issues:

The regulatory and policy environment governing the telecommunications industry has always been a priority for SPAN. A "Policy Portfolio" outlining SPAN's position on relevant policy matters has been a feature of our website during the past few years and for the past year, the following statement has been part of that policy portfolio:

"Legislative and Regulatory Structure

The Telecommunications Act 1997 provided a mixture of regulatory and self-regulatory arrangements that the government and the industry hoped would provide a satisfactory framework for the development of effective competition. Experience since 1997 proved disappointing due to excessive delays in resolving access disputes, declaration of bottleneck services and disputes over terms and conditions. The Telecommunications Access Forum (TAF) proved capable of writing an Access Code, but failed to progress access to essential bottleneck services.

SPAN welcomed the package of legislative amendments enacted in June 1999 and the further “fine tuning” amendments introduced by the Minister in October 2000 as well as the Productivity Commission reference to undertake a review of telecommunications-specific trade practices regulation. Despite these initiatives, concerns remain and debate continues about the adequacy of the current regulatory regime. With the government’s stated intention to complete the privatization of Telstra, the industry has emphasised the urgency that this imposes on the need to ensure that the regulatory regime protects against misuse of Telstra’s market power. This has focused debate once again on the need for some “structural separation” of Telstra’s customer access (fixed) network (CAN) from its value added and other services in order to ensure competitor access to the CAN on terms equal to Telstra’s own retail services divisions. Many believe that this proposal, while a possibility in the early 1990s, was lost in the wake of subsequent decisions involving partial privatization of Telstra, as well as market and technology developments. Nevertheless, discussion about structural separation continues. SPAN advocates a robust debate that will finally resolve this issue. That debate needs to consider a range of factors, including:

- The interests of residential and business consumers in metropolitan and regional Australia,
- The interests of Telstra shareholders,
- The practicality of various structural reforms that are proposed from a political, regulatory and governance perspective,
- The need for ongoing certainty for the validation of competitors’ business strategies,
- The role that greater information (e.g. cost and market) transparency can play in achieving desired outcomes,
- The need for ongoing arrangements for access to bottleneck services that transcend current technology and market considerations, and
- The need for incentives to invest in further development of the CAN to ensure that Australia’s position as a leader in telecommunications services is maintained and enhanced.”

Since the above position was established, the government has responded to the Productivity Commission Report with its Telecommunications Competition Bill 2002, which we support as a useful addition to the regulatory framework to achieve greater timeliness, transparency and certainty in the access regime. A later entry in the SPAN policy portfolio addresses the related issue of ownership of Telstra:

“Ownership of Telstra

The opportunity to structurally divide Telstra into a (publicly owned) national (natural monopoly) infrastructure provider and one or more competitive, privately owned value added service provider entities existed when government decided to establish a competitive telecommunications regime in 1991. Such a structural separation approach to competition may have avoided many of the difficulties experienced in establishing competition under the current regime. That approach still has its proponents.

However, current market developments in telecommunications would introduce difficulties in such an approach. Increasingly, the core Telstra network is being transformed through integration with broadband Pay TV delivery networks, Internet infrastructure and the dominance of data and packet delivery technologies. It would be very difficult today to differentiate between what should be a publicly owned natural monopoly and a privately owned entrepreneurial service delivery platform.

There are still elements of the “Structural separation” debate that need to be worked through (see Section 2., above).

SPAN concludes that the progression to full private ownership of Telstra is therefore inevitable and desirable, subject to strong regulatory monitoring and discipline to ensure competitors have the opportunity to enter the market and compete effectively, without unfair exercise of Telstra’s market power.”

Structural Separation Issues:

- The inquiry objective of examining “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” implies a scenario where the Commonwealth may own the core network and the other “businesses” would be owned by private and commercial investors. There are a number of issues that would flow from that scenario that the proponents of such an approach would need to deal with:
- There needs to be an incentive to invest in the core network to keep pace with technological developments, new applications, business models and market dynamics. This requires a balance of management skills covering long term investment as well as agility and sensitivity to current

market needs in one of the world's most rapidly developing industries. The track record of governments as owners and investors in such an environment is flawed and there is no indication that government's would make more effective investors than private owners. Indeed, trends across the globe have favoured privatisation and public/private partnerships to achieve efficient essential infrastructure development in many areas.

- Any decision to tackle the daunting task of delineating what should be included in the 'core' publicly owned infrastructure and what should be left out, let alone what regulatory structure should govern the interaction of the two organisations, would be a lengthy and difficult exercise. Because the industry is developing so quickly, the long period of uncertainty and preoccupation by industry management in dealing with these difficult questions would hold the industry back.
- It follows that proponents of structural separation accompanied by ownership changes need to establish in a practical way, rather than based on economic theory or ideology, what benefits that such action would produce. They also need to demonstrate how the difficulties outlined above would be dealt with quickly and decisively to avoid industry investment stagnation through uncertainty about the outcomes of the lengthy separation exercise.
- One of the most troublesome aspects of the current regime is the inevitable ambiguity and conflict that arises from the Commonwealth's dual roles of owner and regulator. The implied separation solution of Commonwealth ownership of the core network and private ownership of the other Telstra businesses would not resolve this issue thoroughly because ownership and regulation conflicts would still arise in the Commonwealth's management of the core network business. Disposing of the Commonwealth's shareholding in Telstra and acceptance of the role of regulator in the interests of the "long-term interests of end users" and development of an efficient, competitive industry seems the most obvious way of overcoming this problem.
- There may be other ways to capture the benefits of structural separation without the down-side outcomes mentioned above. One would be voluntary (or if necessary mandated) and effective structural separation within a Telstra private ownership model. The various businesses, including the core network, could be held and managed in Telstra subsidiary companies each accountable for profit and investment strategies and exhibiting an external transparency and accountability that would provide many of the benefits that public/private ownership separation of the core network and other businesses might aspire to. This model would be much easier to establish than the alternatives and would imply sell-down of the Commonwealth's shareholding and the acceptance of a straightforward regulatory agenda for the Commonwealth.
- One of the objectives that the Committee should consider in this inquiry is the aim to enhance the competitiveness and performance of Telstra. Corporations around the world are striving to identify core competencies and maximise returns and performance of their various organisational elements. Such a strategy would surely suggest to Telstra that each of its major elements (e.g. core network, wholesale, retail, mobiles, media/content, international) should be accountable for its individual performance and contribution to the overall company objectives and shareholder return. Transparency of operational and performance data among those entities could be associated with a drive to increased efficiency and shareholder return, as well as a more level playing field for customers of Telstra's wholesale company. It is more likely that Telstra will prosper and be successful internationally if its various components are positioned to compete fairly and openly with local competitors in an open and transparent framework. Harvard's Professor Michael Porter and others have established the strong link between success in meeting strong local competition and success in international markets.

The Committee's task:

For a variety of reasons, the Committee may find that a simple model of structural separation as implied in its objective statement is not feasible or advisable. If this were the case, it would be wrong to assume that the status quo should be accepted as a satisfactory basis for medium/long-term industry regulation. The industry is far too dynamic to render any long-term regulatory strategy immune from constant review and probably frequent adjustment. In any case, the Committee is urged to bear in mind the following regulatory imperatives:

- The need to maintain an effective competitive framework which will deliver benefits long-term to end users and investors, bearing in mind that the current imbalance in returns on investment between Telstra and its competitors is unsustainable,
- The need to ensure that the Commonwealth takes an active role in setting the national telecommunications agenda on infrastructure and technology issues after consultation across the industry,
- That the ACCC's capacity to administer the telecommunications access regime be strengthened and that it be provided with sufficient technical and other resources to arrive at independent and defensible assessments of services costs and prices,
- That services from the "core network" that are not readily available competitively should be available to service providers under terms conditions and prices that are transparent to the market.

We would be pleased to provide further information in support of this submission if the Committee requires and we wish the Committee success in reporting on this most important issue.