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**Inquiry into the performance of the Australian telecommunications regulatory regime**

**Senate Submission 8th April, 2005 – GSM Gateway Association Inc.**

This submission is in response to the invitation from the Reference Committee and sets out some of the issues that have arisen due to regulatory uncertainty in the Mobile Service marketplace in Australia. This market segment remains a high growth segment of the Telecommunications market. The segment has grown as the impact of the high priced calls from fixed services to mobile services has become a major part of the end user cost, now representing between 40 to 45% of a "typical" month telecommunications corporate voice bill. Our members compete directly in this market segment.

**Background**

In line with overseas technological developments, over the last few years a downstream widespread Mobile Services business has developed in Australia that is based upon equipment rental, arbitrage and the sale of Least Cost Routing (LCR) of mobile voice services. This emerging service delivers to end users, small and medium business a competitive Fixed to Mobile (F2M) GSM gateway service to that provided by the Mobile Network Operators (MNOs) and in turn places downward pressure on the price of provision of mobile call terminations. Simply put, our members offer competitive call termination services for corporate, domestic and international callers by either simple management, price based aggregation or LCR routing in the mobile services market segment of the telecommunications marketplace.

Whilst our members business has been ongoing for some years, in recent times the services have been able to be extended from the large enterprise market segment to the ME and SME market segments which are much larger. This extension has come about from new technology equipment and from the expansion of reach of broadband data services and the availability of affordable Voice over IP products. The business activity in which my members are involved was recognised as an element of the mobile services business in the recent ACCC MTAS review(1) regarding mobile services.

In mid 2004 we estimate that the annual Australian F2M termination market outside that of the MNOs was in excess of 500 million call minutes.

**Current Environment**

In more recent times in the Australian market, following the ACCC's further declaration of Mobile Services until 2009, our members have been subjected to a concerted, simultaneous and organised campaign to oppress, remove or deny access to the declared underlying services by upstream MNO providers or their Agents.

These same MNOs also offer the same services in the same marketplace as our members.

**Promotion of Competition**

GGA members generally utilise dedicated equipment, Fixed Cellular Terminals (FCTs) or Gateways to deliver a competitive service, converting F2M services to M2M and so avoid the monopoly rent arising out of effectively only one fixed termination service. The basic market principal is that in the F2M market place one MNO (Telstra) through another division exercises Significant Market Power (SMP, with over 80% of fixed terminations) and this control can be ameliorated by the direct delivery by the Gateway operator of the mobile call to the terminating MNO, avoiding the bottleneck.

By GGA members operating in a supposedly competitive marketplace (oligopoly of three MNOs) the resultant market pressure had delivered lower and sustainable end user cost related pricing and an alternate in the same marketplace, beyond the supposed scope of the SMP operator. This was how the marketplace operated until mid 2004 when the ACCC rebuffed the similar MNO submissions and re-declared mobile services whilst mandating lower F2M interconnect prices over a glide path of a few years. This is now under challenge by some MNOs who from our view also chose over the last period to re-interpret the regulatory regime boundaries.

GGA members also employ GSM Gateways as voice traffic aggregators so as to provide discounted mobile terminations and in doing so avoided the SMP of the traditional F2M services as described. Based upon volume aggregation across the MNO upstream products the Gateway operator can offer a range of other services that allow an end user to chose the most cost effective Least Cost Route service whilst not having to commit to a cross subsidised Whole of Business (WOB) relationship with any MNO and in particular Telstra. In turn, the end user is free to continue to seek the best commercial opportunities that are affected by a choice of services on offer from multiple suppliers in a competitive market.

The GGA services deliver F2M competitive services at between 20% and 45% discount to that offered today on a wholesale basis by the MNOs and until recently at levels below those mandated as the lowest access prices set in June 2004 by the ACCC. Wholesale prices now offered by the MNOs to GGA members are above the retail prices the same MNOs offer in the marketplace to non-aggregated end users.

Our recent experience in this marketplace underlines our belief that the current regulatory regime does not foster competition in the innovative and advanced use of mobile services. Instead it allows incumbent MNOs with SMP to construct their own internal regulations with little regard to the regulatory regime in order to eliminate downstream competitors. A similar gaming principal as was demonstrated in the ACCC to Telstra Competition Notice re Broadband services of February/March 2004, seems now employed by all MNOs as a regulatory gaming technique to deliver the two objectives of increased margin and less competition.

The whole competitive concept of post contract compensation as developed by the MNOs implies that the MNOs are cross-subsidising these declared services from other service income in a manner that a reasonable person could determine relies upon the distortion of the operation of an open and competitive marketplace. There is only one

product here, GSM mobile voice connection as it is declared and provided under monopoly conditions by upstream MNO providers. These same providers seem to wish to artificially tariff and bundle this single product/services and then add new content rules (unregulated) in order to restrict end users and other service providers from reselling this declared service. Also constructed since the MTAS are new "own SMP regulations" that allow the upstream supplier, based upon its own view alone, to seek to fine their competitors retrospectively for daring to compete or purchasing declared services. If allowed to stand, this "Ned Kelly" like activity alone exposes a major flaw in the current regulatory regime and legislation and paves the way for what our members would see will be the eventual failure of a number of currently competitive segments of the telecommunications market.

The overarching guide of light-handed regulation, a competition safety net and self regulation appears to have failed in this segment of the telecommunications market. This failure of the self regulation is illustrated starkly from a CSP perspective, by the operation of the invisible collusive body ACIF that has become a captured facilitator of less competition, a symptom of excessive market power that remained with the dominant operator post deregulation.

**Encouragement of Investment**

Historically the establishment of new and innovative applications and services in telecommunications comes from competition which, in turn, delivers cost related pricing the end user. It is our view that this was the aim that generally underpinned the telecommunications deregulation regime framework and the delivery of better and more timely services in the LTIE.

The investment in FCT and Gateway equipment mirrors what has been available in Customer Premises Equipment (CPE) for many years as a LCR feature to reduce the cost of F2M calls for large corporate users. Such applications have been purchased from the MNOs and associates for some years and the MNOs have been selling these products directly to these large users as part of Whole of Business (WOB) telecommunication bundles.

For non MNOs and CSPs to compete with these Mobile Virtual private network (VPN) services they need to purchase a mix of upstream mobile services and employ them in the same way as the MNO provides its services. Competition arise in the same market on price and performance and from the non MNOs and CSPs developing services with lower cost and/or introducing new and innovative applications of the products. Investment in equipment to deliver this type of product, either on an aggregated or standalone basis is of the level to that of investing in installing a complex digital PABX. Modern VoIP linking services have extended the customer reach and improved the economics of providing a viable service.

On the surface the regulatory environment encourages GGA members as either CSPs or switch-less resellers to invest in this CPE equipment in order to offer a service in the marketplace. Upstream contracts for service were entered into with initial simple terms and conditions reflecting a declared service. Subsequently, the MNO SFOA that is embodied in the these terms is modified by the MNOs with no reference to the downstream competitors has the terms varied and the services withdrawn even though they are declared services and acquired under different terms. The regulatory regime

thus appears to allow anti-competitive, retrospective and recursive changes to mobile contract terms and conditions if they do not suit the upstream MNO, and to do so, the MNOs are relying upon exploiting part 23 of the Act (1997) which may have never been intended for such an outcome.

Investment in this growth area is now no longer encouraged due to the anti-competitive actions of the upstream MNOs who stand to benefit from lessening competition and less pricing pressure that arises from an ordered competitive marketplace. As the competition safety net the ACCC is by design legalistic, slow and under resourced to prevent in a timely manner the commercial damage that this cartel-like action inflicts on the GGA investors. It should be noted that to lessen competition in this marketplace all the MNOs have to apply simultaneously the same terms and conditions to the downstream operators or the market distortion will fail from cross MNO service leakage, one to the other. This occurred in August 2004 whilst still supplying the same services to themselves and other corporate users.

The mitigation of revenue reduction trends arising from competitive pricing pressure from the GGA members in F2M market along with an increase in return from secondary markets that flow from related WOB business services where there is clearly SMP, from our view, may be one motive behind Telstra's conduct in this matter. The motive for the other MNOs is less clear as, on analysis, they both benefit from a conversion of F2M termination into M2M for their on net services whilst termination charges remain above mobile call charges. If there were any external market arrangement between the MNOs from some of the increased monopoly rent that is collected from generally reducing competitive pressure in the F2M market then this would be clear breach of the provisions of the TPA.

It is easy to see from the range of competition issues that the current environment has a number of open ended risks which, without better regulatory certainty and mitigation, will mean that less investment will be available going forward to introduce new and innovative services into this market segment.

**Protects Consumers**

Consumers are end users and are faced with a limited supplier marketplace. The current regulatory regime require that if one owns a so-called bottleneck facility such as the Mobile telecommunications network as do the MNOs then the owner of those facilities must provide 'access' to that network so that all the competitors can use them on an equitable basis.

GSM Gateways have provided competition in a segment of the market where prices are still high. The MNOs current conduct has damaged our members business, reputation and removed customer benefits from the marketplace. The competitive provision of F2M services provides the market with price pressure as it did originally in the fixed line areas to create the competitive conditions for the lowest sustainable and best quality services that come from a properly operating market. This is the best protection that consumers and end user can enjoy.

The GGA is of the view that the current action of the MNOs under the existing regulatory regime are potentially anti-competitive and may breach a number of sections of the TPA and the Telecommunications Act 1997. Within this regime there is little

timely action that our members can effect prior to suffering commercial harm from the upstream providers who are also the direct competitors.

Regardless of whether our members are proved correct or not the MNOs appear to be working on the basis that our members are small operators and, by denial and delay, they will prevail anyway. The UK experience of 2003 (2) is now in very stark replay in Australia even though ostensibly the underlying legislative principals are vastly different and based upon the premise of LTIE, Class Licences and access to declared services.

Set out below are the GGA responses to the questions posed by the References Committee.

**References**

(1)Mobile Services Review, MTAS June 2004 – ACCC
(2)Competition Appeal Tribunal – Case No. 1024/2/3/04 Floe vs Ofcom, 19 November 2004.

The Senate has referred the following matters to the Committee for inquiry and report by **23 June 2005**:

(1) Whether the current telecommunications regulatory regime promotes competition, encourages investment in the sector and protects consumers to the fullest extent practicable, with particular reference to:

(a) whether Part XIB of the *Trade Practices Act 1974* deals effectively with instances of the abuse of market power by participants in the Australian Telecommunications sector, and, if not, the implications of any inadequacy for participants, consumers and the competitive process;

**Response**
The Act defines anti-competitive conduct in the telecommunications industry, as occurring in two circumstances:

> where a carrier or carriage service provider has a substantial degree of power in a telecommunications market and takes advantage of that power with the effect or likely effect of substantially lessening competition in that or any other telecommunications market or
>
> where a carrier or carriage service provider engages in conduct which would contravene sections 45, 45B, 46, 47 or 48 of the Act where that conduct relates to a telecommunications market.

The provision of mobile services by the MNOs is covered under the Telecommunications Act and this forms part of the telecommunications industry and so is subject to the anti-competitive provisions of the TPA.

The GGA has observed the operation of Notices under Part XIB of the Act. Whilst an outcome was achieved in the Telstra Competition Notice matter it was over an extended period (over 12 months) and the Court imposed penalties and compensation with a result that at the end of the process it would appear that the outcome in no way to compensate for the loss of the competitors business and the market momentum.

To make such a suite of regulatory provisions work effectively they may need to be geared to the timing horizons that apply to the operation of a competitive SME business with only a single competitive telecommunications product to sell. The current legislation on Notices is thus alien to small to medium enterprise operators who generally cannot cross-subsidize the lost income sustained from competitor anti-competitive actions from other areas of their business as these simply do not exist.

Apart from this action the difficulties of the legislation and it legal constructs have meant Part XIB has been little used. The historical fact is that Telstra, Optus and Vodafone, the GSM MNOs have effectively enjoyed a regulatory holiday on the provision of Mobile services since deregulation in 1997 and there has been no proactive regulator to ensure compliance. This has resulted in the boundary between the LTIE and the good of the operator gradually creeping towards self interest with a result that by mid 2004 the MNO were writing there own legislation and rules on the content, how and where declared mobile voice services would be used by downstream competitors to suit their own business plans.

The backstop regulator, the ACCC has the right proactive charter :

> compliance with the competition rule (and other provisions of Part XIB) and, in particular, stopping anti-competitive conduct in the telecommunications market
>
> improvement in market conduct generally by carriers and carriage service providers

Unfortunately the framework imposed an industry self-regulation body between the operating market and the regulatory backstop, funded effectively by the major operators. Inaction here in self-regulation has meant that the backstop has become the only regulatory body but with reactive rather than proactive powers and resources. Some steps towards increasing the power of the ACCC have been made with the new Trade Practices Legislation Amendment Bill (No 1) 2005 through Parliament. There are plans to introduce further legislation which will provide more protection for small businesses (Trade Practices Legislation Amendment (Small Business Protection) Bill 2005) from unconscionable conduct and improve efficiency but, for the mobile services area, there may need to be more change.

Whilst the aims an objectives of this portion of the Act are laudable and necessary in a truly competitive market that has upstream competitors and dependencies (not an oligopoly for which is was originally conceived) to be actually effective in the real mobiles market it is recommended that a clear gating response timetable and obligation be now incorporated into the Part XIB to strengthen its effect. That timetable should have as a maximum, 28 days for response and a further 28 days for resolution with standard settlement fines and compensation if competition in this market segment is going to remain. Delay is the same as denial.

Whilst the use of the Courts to set damages is in concept correct, the marketplace reality for an SME operator is that the use of the legal system is a significant commercial tool that, in the main, greatly assists the large SMP holder and is a great disadvantage to the smaller competitor.

A Notice under part XIB enables third parties such as our members to bring an action for damages, but there is no such provision made under Part XIC and that needs to be also rectified. With regulatory improvements a simpler proactive competition notice regime may be the more appropriate way to minimise the financial impact of the alleged anti-competitive conduct on third parties.

(b) whether Part XIC of the *Trade Practices Act 1974* allows access providers to receive a sufficient return on investment and access seekers to obtain commercially viable access to declared services in practice, and whether there are any flaws in the operation of this regime;

**Response**

Part XIC sets out an access regime for certain declared services being either carriage services or services which facilitate the supply of carriage services. Under this regime, the ACCC as regulator may, after taking account of relevant criteria, declare a specific network service to make it available to access seekers

On 30 June 2004, the ACCC decided to allow the existing MNO GSM and CDMA terminating access service declaration to expire, and replaced it with a new declaration under s. 152AL of the Act. The new declaration provided an amended description of the mobile terminating access service that included voice services terminating on all digital mobile telephony networks.

Under Part XIC of the Act, the Commission may also declare carriage services and related services to be declared services. Carriers and carriage service providers who provide declared services are required to comply with standard access obligations ("SAOs") in relation to those services. The SAOs facilitate the supply of declared services by access providers to access seekers, in order that access seekers can provide carriage services and/or content services.

The SAOs are set out in s.152AR of the Act. Subject to class or individual exemptions made by the Commission, a carrier or carriage service provider must comply with the SAOs in regard to declared services it supplies either to itself or to other persons. In particular, s.152AR requires access providers to, among other things to:

"supply an active declared service if requested to do so by a service provider (subject to certain limitations) and to take all reasonable steps to ensure that the technical and operational quality of the active declared service supplied to the service provider is equivalent to that which the access provider provides to itself;"

The GGA members as SMEs may operate as CSPs and be subject to the above or as switch-less resellers aggregating on behalf of end users. In both cases when any of the MNO upstream suppliers became operationally interested in the ongoing provision of a competitive service from our members they potentially gained access to competitive information on customers, traffic loads, bill analysis, content monitoring (CDR tracking), call patterns or equipment recognition with disconnection action following shortly thereafter.

Contrary to the requirements of the Act in most cases once a competitive service to the MNO is located, regardless of ownership or contract arrangements the equipment is just turned off by blocking the equipment identity and the mobile SIM service is barred. Normally no MNO explanation is supplied or if supplied, it focuses on the "contravention of SFOA terms", "illegal termination of international traffic", "illegal equipment" or "operations as a CSP or Carrier". Potentially all of these "own regulations" reasons for member service denial are based upon internal regulations

generated by the MNOs in contravention to the intent of Part XIC as applicable to declared services and s.152AR of the Act.

In most cases the anti-competitive action has been generated internally by another part of the MNO and has been created by the MNO changing conditions of the service or the MNO imposing conditions on the use of declared services that it does not impose upon itself.

For example by invoking Part 23 of the Act the SFOA's are post execution modified, advertised and then the member's service denied or deleted or equipment that is in operation and approved is declared illegal and the spectrum access blocked. This latter action is of course potential use of technical regulation by a third party of Spectrum administered by the Crown. A registered list of MNO SFOA variations is held by the ACA and any inspection of the variation from June to August 2004 of all the MNOs would lead a reasonable person to conclude that these variations were not just coincidental as they all addressed the same issue in the same timeframe following the Draft ACCC MTAS report.

Under Part XIC there is no provision for damages and so these actions have grown unchecked, even if proved. In most circumstances, the onerous and slow competition notice regime may be the more appropriate way to minimise the financial impact of the alleged anti-competitive conduct on members as third parties but, on a historical basis, few such Notices have been executed in a meaningful timeframe and the GGA concerns with this series of instruments have already been set out.

Whilst Part XIC of the Act has all the good intentions it is ineffective in actually delivering any real world outcomes from an SME perspective or deterring upstream operators from utilising SMP positions to lessen competition from downstream SME providers and requires revision.

(c) whether there are any structural issues in the Australian telecommunications sector inhibiting the effectiveness of the current regulatory regime;

**Response**
The structural arrangements of the industry were debated extensively at the time of the deregulation in 1997 and followed on from the industry structure decisions that were taken in the early 1990's re the separation of wholesale and retail services of the then monopoly.

In the specific mobiles area of the telecommunications market the boundary between ownership, operation wholesale and retail appears blurred or non existent as the underlying premise of vertically integrated operators was perpetuated with the sale of Telstra as an integrated operator.

GGA members are faced with dealing with competitor MNOs that collect data from their operations to determine the level of business whilst at the same time having to purchase downstream underlying services from the same MNOs business and retail operations who report on the purchases. Fair and equitable competition as required under the Acts requires the MNO staff to, when faced with a choice of revenue enhancement or competitive loss for the MNO make "unpopular" choices if the choice involves supporting the competitors' business set against providing internal access to the competitive information by blind pooling. Anti-competitive behaviour is an impossible task to police and then to assure the SME competitor with little or no market power that the marketplace is fair and the MNO is abiding by the intent of the legislation when all around there is evidence to the contrary.

Given the constraints the GGA believes that the now very complex structures that are in place impose a requirement on the Government to have a mechanism to continue to readjust the levers to compensate for many distortions and the inevitable gaming that arises as new technologies and services are invented that did not form part of the original regime considerations.

(d) whether consumer protection safeguards in the current regime provide effective and comprehensive protection for users of services;

**Response**
The GGA has no input at this time on this matter.

(e) whether regulators of the Australian telecommunications sector are currently provided with the powers and resources required in order to perform their role in the regulatory regime;

**Response**
The GGA has provided comments on the effectiveness of the self regulation and regulatory safety net system. The role of ACIF to date has been ineffective and that has meant the all significant industry matters have to be dealt with by the ACCC.

It is our view that the ACCC should be given further proactive powers and resources in the telecommunications area. We also observe that the current self-regulation function represented by ACIF should be either substantially restructured so it becomes competition proactive and independent or abolished altogether and be replaced by a technical standards body that is not funded and/or controlled by the incumbents.

(f) the impact that the potential privatisation of Telstra would have on the effectiveness of the current regulatory regime;

**Response**
The GGA believes that further privatisation of Telstra with the current regulatory regime structure will perpetuate the inadequacies of the current system and in the Mobile services industry segment will mean that competition and service innovation, apart from that between the MNOs will be significantly lessened. This will ensure a resultant rise in service prices to the end users, as is already been argued by two of the MNOs in their recent responses to the MTAS undertakings to the ACCC.

The regulatory regime needs to be restructured to ensure the aims of the Act are able to be met prior to the further privatisation.

(g) whether the Universal Service Obligation (USO) is effectively ensuring that all Australians have access to reasonable telecommunications services and, in particular, whether the USO needs to be amended in order to ensure that all Australians receive access to adequate telecommunications services reflective of changes in technology requirements;

**Response**

The GGA members purchase services from licensed carriers and have no input on this question at this time.

(h) whether the current regulatory environment provides participants with adequate certainty to promote investment, most particularly in infrastructure such as optical fibre cable networks;

**Response**
The GGA has already set out it issues on certainty in investing in capital equipment in the Mobiles area and, in summary, believes that the regulatory regime needs to be amended so that purchasers of declared services may have certainty as to reasonable and equitable access to upstream service supply from underlying service owner MNOs who sell to themselves and operate competing services.

(i) whether the current regulatory regime promotes the emergence of innovative technologies;

**Response**
The GGA believes that current regime does not promote the emergence of innovative technologies such as those operated by its members if they impact the revenue base of the incumbent operators who have competing services and SMP and are prepared to exploit the inadequacies of Part XIC of the act. The GGA believes that this is the current situation in this section of the telecommunications industry.

(j) whether it is possible to achieve the objectives of the current regulatory regime in a way that does not require the scale and scope of regulation currently present in the sector;

**Response**
The current regulation arose from structural industry decisions following the Industry reviews of 1987-8 and the desire of the Government of the day to have a vertically integrated service provider of last resort which was, in part, premised on the older tyranny of distance arguments of a decade earlier. A two step legislative change program evolved and out of that then current regime was developed was supposed to deliver the benefits of deregulation to the end users via competition.

What has been delivered from this evolved regulatory structure is a series of record incumbent operator profits that prima facie indicate that the original goals may have been lost in the rapid technological changes that characterised the industry changes since deregulation and that the benefits unlocked may have not made their way to the end users as originally envisaged.

As has been presented the GGA members are in general SME organisations that are unable to normally deal with the current scope and scale of the legislative regime and would like to have clear an concise business rules that are generally in common with all other industry segments. Having chosen the current path it would seem now difficult to adopt a much preferred simpler approach. The GGA is keen to see the current system made work by upgrading the ACCC charter and resources to deal with a fully privately owned Telstra and its oligopoly brethren.

(k) whether there are any other changes that could be made to the current regulatory regime in order to better promote competition, encourage investment or protect consumers.

**Response**
The GGA has made a number of suggestions that are already set out in this response.

(2) That the committee make recommendations for legislative amendments to rectify any weaknesses in the current regulatory regime identified by the committee's inquiry.

**Response**
The GGA would encourage the committee to make recommendations that encourage fair and equitable competition in the telecommunications sector.