

The evolution of telecommunications regulation and competition in Australia

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1. Introduction

This paper describes the evolution of telecommunications regulation and competition in Australia since the commencement of a process of regulatory reform in the late 1980s. The focus is on changes in economic rather than technical regulatory arrangements. It considers the outcomes of reform to date by examination of key metrics such as the number of competitors, market shares and the prices of telecommunications services. It concludes by reviewing some issues of debate in regard to future reform.

2. Initial reforms

Up until the late 1980s telecommunications services in Australia were provided exclusively by three government-owned entities. These were Telecom Australia which provided fixed line services within Australia and a number of associated regulatory functions, the Overseas Telecommunications Commission (OTC) which provided telecommunications services between Australia and other countries and AUSSAT which owned and operated a national satellite telecommunications system used by the former two entities.

The process of regulatory reform aimed at introducing competition into the Australian telecommunications market began in 1989. The *Telecommunications Act 1989* established an independent industry-specific telecommunications regulator AUSTEL. The satellite operator AUSSAT was permitted to compete on a limited basis with OTC in the provision of overseas telecommunications services. Competition by non-government entities was permitted in the supply of value-added services, customer equipment, cable installation and 'private networks'. At the same time as this, Telecom Australia and the OTC were formally corporatised, transforming them into government owned companies.²³ Retail price controls were introduced as a means of increasing the efficiency of these businesses and achieving equity objectives.

A second round of reforms commenced in 1991 under the *Telecommunications Act 1991* and other related legislation. Telecom Australia and the OTC were merged into a single company, the Australian and Overseas Telecommunications Corporation (AOTC), which later changed its name to Telstra. The AOTC was granted a general carrier licence enabling it to offer national and international services, and a public mobile licence. The AOTC/Telstra emerged as a fully integrated incumbent operator of a ubiquitous copper/fibre public switched telephone network.

At the same time, the Government issued a tender for a second general carrier licence and a second public mobile licence. These were awarded to Optus Communications, the major shareholders of which were UK-based Cable and Wireless and US-based BellSouth. AUSSAT was sold to Optus in early 1992. In December 1992 a third public mobile licence was awarded to the UK-based Vodafone.

23. AUSSAT already operated under such a structure.

The *Telecommunications Act 1991* provided for interconnection and access rights for carriers to each other's networks and some more limited rights for service providers. Carriers were free to negotiate access terms and conditions, but failing agreement could obtain a determination from the regulator AUSTEL.

The 1991 reforms created an environment of regulated or managed competition, with an emphasis on facilities based entry. As a reflection of this, Optus commenced roll out of a Hybrid Fibre Coaxial (HFC) local loop network in the metropolitan areas of major capital cities in early 1995. Its business case for this was predicated on a joint voice telephony, internet and pay-TV offering.

In response to Optus's plans to develop a HFC network, Telstra commenced the roll out of its own HFC network at around the same time and in the same areas. Its network plans were centred on the supply of a competing pay-TV service through its half-owned affiliate Foxtel. Although this is understood to have been justified in part as a 'technology hedge' strategy, it has also been widely viewed as a 'telephony defence' initiative, to discourage its copper fixed line telephony customers from switching to the Optus network.

The *Telecommunications Act 1991* also saw the introduction of revised universal service arrangements whereby the industry as a whole was required to contribute to the net cost of unprofitable services supplied by Telstra. These were funded by a levy on all carriers in proportion to their share of timed traffic. Other consumer related protections included the continuation of a retail price control regime and the creation of an industry funded ombudsman to deal with billing related complaints.²⁴

3. *The current regulatory environment*

The current regulatory environment emerged in 1997 with the *Telecommunications Act 1997*. The Act provided for open entry of carriers and carriage service providers. The technical regulatory functions of AUSTEL were merged with the separate Spectrum Management Agency to form the Australian Communications Authority (ACA). The ACA was also given responsibility for overseeing a number of specific consumer protection requirements, which includes administration of the universal service arrangements.²⁵

In addition, under changes to the *Trade Practices Act 1974*, responsibility for competition regulation in telecommunications was transferred to the general competition regulator, the Australian Competition and Consumer Commission (ACCC). This involved insertion of telecommunications-specific access provisions (Part XIC) and anti-competitive conduct provisions (Part XIB) into the *Trade Practices Act 1974*.²⁶ Retail price controls on Telstra were also continued under the new regime. Telstra's compliance with these is overseen by the ACCC.

24. Sources of overviews of early telecommunications reforms include: H. Raiche and J. Given, 'The Policy Context' in A. Grant and J. Given (eds) *Australian Telecommunications Regulation*, Communications Law Centre, Sydney, 2001; and J. Foster, 'Australia' in J. Foster (ed) *Telecommunications in the Pacific Rim*, Prospect Media, St Leonards, 1999.

25. Legislative consumer protection measures include *inter alia*: the Universal Service Obligation that provides access to a standard telephone service to all people in Australia regardless of where they live or carry out a business; the Digital Data Service Obligation that makes provision for equitable access to high speed data services; and the Customer Service Guarantee which sets standards in relation to the timeliness of connections and fault repairs.

26. Content regulation is the responsibility of a separate media regulator, the Australian Broadcasting Authority.

The access provisions of Part XIC do not provide for a general right of access to telecommunications services. Access rights are granted following ACCC declaration of a service, although certain services were 'deemed' to be declared for the commencement of the new regime. In essence these were services covered by commercial access agreements under the 1991 access regime.

Table 1. **Services declared for third-party access**

- Domestic public switched telephone network (PSTN) originating and terminating services;	- Local PSTN originating and terminating services;
- Domestic GSM and CDMA originating and terminating services;	- Local carriage service;
- Transmission;	- Integrated services digital network (ISDN) originating and terminating services;
- Digital data access service;	- Domestic transmission capacity service;
- Conditioned local loop service;	- Analogue subscription television broadcast carriage service;
- Analogue broadcasting access service;	- Line sharing service.
- Unconditioned local loop service;	

In order for a service to be declared, the ACCC must undertake a public inquiry and be satisfied that declaration will promote the long-term interest of end-users. Alternatively it can declare a service on the recommendation of a specified industry self-regulatory body known as the Telecommunications Access Forum (TAF). The services declared to date (including the deemed declared services) are listed in Table 1 above.

Once a service is declared the ACCC can arbitrate terms and condition of access if parties cannot agree on the terms and conditions of supply. Access providers can also submit undertakings in which they can nominate terms and conditions of access. If the ACCC accepts such an undertaking, it cannot issue arbitrations at variance with the terms and conditions specified in the undertaking.

The Part XIB anti-competitive conduct provisions mirror reasonably closely general anti-competitive conduct provisions in the Act (Part IV) applying to other industries. A crucial difference, is that conduct which has the *effect, or likely effect*, of substantially lessening competition is prohibited under Part XIB, whereas under the misuse of market power provisions of Part IV, a breach occurs only if that is the *purpose* of particular conduct. This lower threshold reflects in part, the potential of incumbency control of upstream telecommunications markets to serve as a means of keeping competitors out of downstream markets. Part XIB of the Act also provides the ACCC with information gathering powers through the ability to issue record keeping rules and tariff filing directions.

Provision was also made in the 1997 arrangements for two industry self-regulatory bodies. These are the Australian Communications Industry Forum (ACIF) and the TAF mentioned above. The ACIF specialises in developing common technical and consumer standards for the industry. The TAF's focus is on self-regulation for matters in relation to the economics of access. As mentioned above, the TAF can nominate access service declarations to the ACCC and has the power to develop voluntary access codes. It has developed a code covering certain non-price terms and conditions, but has not proved effective in

reaching agreement among industry on price related terms and conditions of access. Recently the current body constituting the TAF agreed to disband.²⁷

The year 1997 also saw the sale of one-third of Telstra to private investors. A further partial sell down in 1999 reduced the Government's stake to the current level of 50.1%.

Amendments to the telecommunications specific parts of the Trade Practices Act in 1999 introduced additional flexibility to Part XIC arbitral processes in relation to access and a strengthening of the operation of the Part XIB competition notice regime.

In mid 2000, the Government initiated a review of telecommunications specific competition regulation by the Productivity Commission.²⁸ As a partial response to the Productivity Commission review, another set of amendments to the access provisions was introduced by the Government in September 2001. These included initiatives to improve information dissemination, extend provisions for backdating of arbitration determinations and to speed up arbitral processes. Key objectives were to reduce the incentive for early notification of arbitrations and to encourage greater commercial negotiation. The Government also proposes to introduce further amendments. These are outlined below.

To help encourage direct negotiations between parties the ACCC has moved recently to publish indicative access prices for a range of declared access services.

In summary, the current regulatory environment governing third-party access arrangements for telecommunications networks is best described as a co-regulatory framework, with reliance on various government regulators and self-regulation. Following a trend established under the previous regime, the emphasis is on the primacy of commercially negotiated access and interconnection arrangements. Arbitration is provided for where such negotiations fail to produce mutually agreeable outcomes.

Outcomes under the current regime

Since open entry in 1997, numerous carriers and carriage service providers have entered the telecommunications market. There are presently around 75 carriers – including four carriers operating mobile networks – and an even higher number of carriage service providers. Nevertheless, the market remains dominated by a couple of large carriers. There are around 900 internet service providers (ISPs) but again the main carriers tend to dominate this market.²⁹ In the CBD areas of major capital cities there are, in addition to Telstra's infrastructure, between 7 and 10 alternative optical fibre or microwave networks. New entrants have carved out major market shares in the mobile, data services, and inter-capital transmission markets. The price of an average basket of telecommunications services purchased by Australian consumers fell by 21.4% in real terms over the period 1997-98 to 2000-01.³⁰ There has been a substantial rise in the number and diversity of telecommunications services available in the market.

27. Legislative changes proposed to Part XIC of the Act include abolition of the TAF.

28. Productivity Commission, *Telecommunications Competition Regulation*, Inquiry Report, AusInfo, Canberra, 21 September 2001. The Productivity Commission is the Commonwealth Government's main review and advisory body on matters relating to microeconomic policy and regulation.

29. Australian Communications Authority (ACA), *Telecommunications Performance Report 2000-01*, ACA, Melbourne, 2001, p. 4.

30. Australian Competition and Consumer Commission (ACCC), 'Changes in the prices paid for telecommunications services in Australia' in *ACCC telecommunications reports 2000-01*, ACCC, Canberra, 2002, p. 80.

The growth of competition in particular market segments has seen the ACCC wind back some access regulation. Examples are the removal from the transmission declaration of major inter-capital routes and the imminent removal of Telstra's obligation to provide a wholesale local call service with respect to the CBD areas of major capital cities.

Notwithstanding the above developments, the incumbent Telstra remains the dominant telecommunications supplier by market share in almost every market in which it operates. It is highly vertically integrated and is reputedly one of the most horizontally integrated telecommunications companies in the world, with a presence in the fixed network telephony, mobile, ISP, data services, printed and on-line directories and pay-TV markets. This gives it significant economies of scope and access to bundling opportunities that, in addition to economies of scale, can make it very difficult for smaller players to compete against it. Its market shares in some key markets are shown in Table 2 below.

Table 2. Telstra's share of key markets

Market	Market share (%)
Retail basic access lines (June 2001)	83.2*
National long-distance revenue (June 2002)	75
International revenue (June 2000)	48
Mobile subscribers (March 2001)	45.5
ISP subscribers (July 2000)	23.7
Data services and enhanced voice retail revenues (2001)	38
Pay-TV subscribers (June 2001)	52.2

*. If resellers of Telstra lines are included the figure is 95.6%.

Source: Productivity Commission, 2001.

In relation to the quality of services, an independent inquiry into the adequacy of telecommunications services conducted in 2000 concluded that Australians:

generally had adequate access to a range of high quality, basic and advanced telecommunications services comparable to the leading information economies in the world.

However, the inquiry indicated that in rural and remote areas of Australia many people were provided with services that they regarded as inadequate. Particular concerns were expressed in relation to:

- The timely installation, repair and reliability of basic telephone services;
- Mobile phone coverage at affordable prices; and

- Reliable access to the internet and data speeds.³¹

Up until recently there had been a steady increase in annual consumer complaints in regard to service standards for service provision and fault rectification, particularly in rural areas.³² The reversal of the rise in recent years may be in part attributable to the imposition of higher Customer Service Guarantee standards by the Government in July 2000 and possibly other initiatives relating to service provision in rural areas.³³

Telstra's continuing dominance has reinforced the need for a strong access and enforcement regime to help nurture competition. It has also made the emphasis of the current regime in encouraging negotiated outcomes somewhat problematic at times. Indicative of this, the ACCC has been involved in a total of 40 arbitrations involving Telstra (out of 46 in total) since the commencement of the current regulatory regime. Many of these have taken years to resolve and involved considerable administrative cost.

In response to these and related difficulties, the Government introduced recently a bill into Parliament to amend further the Telecommunications specific parts of the *Trade Practices Act 1974* and the *Telecommunications Act 1997*.³⁴ Among other things, the bill provides for:

- An enhanced accounting separation model for Telstra, providing for greater transparency of its wholesale and retail operations;
- A requirement for the ACCC to publish model terms and conditions of access for core services;
- Removing merits review with respect to ACCC arbitration decisions other than on points of law;
- Increasing the incentives for the provision of access 'undertakings' that provide for industry-wide terms and conditions of access; and
- Abolition of the industry self-regulatory access body (the TAF).

The ongoing strengthening of the telecommunications specific parts of the Trade Practices Act is contrary to what was envisaged when the regime was conceived. There was some expectation that the ACCC's role would diminish over time and that the general competition laws could displace the need for

31. Independent Telecommunications Service Inquiry, T. Besley (Chairman), *Connecting Australia*, Commonwealth of Australia, Canberra, 2000, p. 5.

32. ACA, *Op. cit.* p. 39, and previous year's report pp. 24-5.

33. In 2001 the Government used a competitive tender process to allocate \$150 million in direct funding to upgrade infrastructure to provide untimed local calls, access to an ISP at a local call rate and other services to people living in the most remote parts of Australia. The Government has also funded a range of telecommunication services projects through a dedicated Regional Telecommunications Infrastructure Fund. These included a \$25 million tender to extend mobile coverage along major highways. In addition, competitive tendering for the provision of a standard telephone service (STS) has been introduced within two identified universal service areas under a pilot program. This entitles designated carriers and carriage service providers to compete to obtain the industry-funded subsidy previously only available to Telstra, for providing an STS in these areas.

34. The Bill constitutes the Government's main response to a review of the telecommunications competition regime by the Productivity Commission.

an industry specific regime. On the other hand, due to major pricing work carried out over the past several years and perhaps partly as a result of previous legislative amendments, the level of access disputation brought before the ACCC has diminished in the past year.

4. *Current debate about future reform*

Some issues featuring prominently in the current debate about future telecommunications industry reform include structural separation, privatisation and service standards in rural areas.

The ACCC is cognisant that Telstra's high level of vertical integration and its dominance in key markets places it in a unique position to leverage into related markets with the convergence of various telecommunications services. It has expressed the view that:

...access regulation alone may not be sufficient to curb market power in converging markets such that it may be necessary to consider whether structural separation of ownerships of inputs to these services is required.³⁵

The Government has not given any indication that it intends to pursue structural separation of Telstra. The opposition Labour Party has flagged it as a policy option with the possible objective among others, of maintaining the fixed network business under full government ownership.

Privatisation of the remaining 50.1% government shareholding in Telstra is a stated policy objective of the current Government. However this policy is contingent on demonstrated improvements in service standards in rural areas, and must also pass through the Senate where the Government lacks a majority.

The Government initiated an inquiry into telecommunication service standards in rural areas a couple of months ago. The inquiry is due to report its findings by the end of the year. This follows a previous inquiry in 2000, which indicated that services were deficient in many rural areas, and the introduction of recent initiatives by the Government to facilitate improvements.

5. *Conclusion*

Telecommunications regulation and competition in Australia has evolved substantially over the past ten years and is still evolving. There have been several positive market outcomes that have delivered benefits to consumers. Nonetheless the incumbent provider remains dominant by market share across a range of markets, which has served to test the access and enforcement regulatory regime. It has also meant that there has been a tendency towards regulatory tightening contrary to expectations when the current regime was put in place.

35. Australian Competition and Consumer Commission (ACCC), 'Telecommunications competitive safeguards' in *ACCC telecommunications reports 2000-01*, ACCC, Canberra, 2002, p. 18.