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Wednesday, February 12, 2003

Mr Ken Walliss
Director – Convergence
Telecommunications
Australian Competition and Consumer Commission
GPO Box 520J
Melbourne VIC 3001

Dear Ken,

**Bundling in Telecommunications Markets
Draft Information Paper**

ATUG is pleased to provide comments to the Commission to assist in the development of its approach to monitoring bundling conduct and to investigate and evaluate potential ant-competitive behaviour.

The issues canvassed in the Draft Information Paper stem from the Commission's decision in the Foxtel/Optus matter. A summary of the concerns that ATUG has about that content sharing agreement, which are relevant to the Draft Information Paper, are at Attachment 3.

ATUG's submission covers a number of issues and a general statement of our concerns regarding the strength of competition. Our position on competition comes from survey work conducted in the Corporate and SME business user markets. The picture is one of substantial market power that will be further leveraged by bundling into the residential market. Details are at Attachment 1.

ATUG's continuing concerns about the effectiveness of the current regulatory regime implementation in promoting competition are summarised at Attachment 2 which is an extract of our submission to the ongoing Senate Inquiry into the Australian Telecommunications Network.

For ATUG the questions raised by the Information Paper are:

- 1) Reduction in the “addressable market” – delay has been identified as an unhelpful a feature of the regulatory process in the telecommunications industry, to the point where amendments to the Trade practices Act in both 2001 and 2002 were designed to address this problem. The Commission’s suggested approach to assessing reductions in addressable markets post–facto, when combined with recent ACA survey data (summarised at Attachment 5) indicating users are suffering “choice fatigue”, may mean too little, too late in terms of promoting competition. The timing of such inquiries is a key issue.
- 2) ATUG suggests the Commission consider making the assessment of “substantial market power” ahead of any specific case arising as one way of speeding up the process
- 3) The Commission notes that “addressable market effects may be more pronounced in the event that competing carriers and CSPs are not able to supply some services within the bundled package.” It may be that consideration should be given to ensuring that any bundled product is available to ensure competitors can offer competitive bundles. Recent amendments to the Trade Practices Act should enable speedier resolution of price and non-price terms and conditions of supply for such services.
- 4) Pricing and bundling – ATUG is concerned that the current set of powers the Commission has in respect of pricing will not lead to timely outcomes in assessing predatory pricing and vertical prices squeezes.

The tariff filing powers as ATUG understands them oblige reporting but do not give the Commission any powers of approval in regards to the tariffs filed. ATUG notes that ACA powers on performance reporting which have now been amended with the introduction of the National Reliability Framework to provide the ACA with more pro-active powers to ensure outcomes are achieved. It may be that the tariff filing powers need to be strengthened to enable pro-active monitoring of pricing of bundles.

- 5) Tests for predatory pricing and vertical price squeezes – The discussion in this section assumes “product” based markets are being assessed. ATUG suggests the Commission should give consideration to using “customer” based market definitions – such as Government and Business Customer, SME customer, residential customer, regional customer.
- 6) ATUG suggests early consideration be given to the pricing issues surrounding bundling of fixed line services given the fact that there is an “access deficit” associated with this service. The issue of predatory pricing in regard to bundles that contain this product ought to be advanced, particularly given the low level of competition in this area.

ATUG therefore supports the Commission's suggestion that use of the Record-keeping rules power to require information from Telstra in regards to residential bundling conduct. It is important that this information is sought and provided in a timely fashion otherwise delay may result in reduced competition and increased customer acquisition costs down the track. Attachment 4 summarises ATUG input to the discussion paper on Disclosure of Record Keeping Rule, March 2002.

Yours sincerely,



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Attachments

- 1) ATUG assessment of competition – survey reports
- 2) ATUG submission to Senate Inquiry on The Australian Telecommunications Network
- 3) Foxtel/Optus submission extracts
- 4) Record keeping rule submission extracts
- 5) ATUG Review of ACA research
- 6) ATUG Profile
- 7) ATUG Policies

Attachment 1

ATUG Assessment of Competition

ATUG's views on the competitiveness of the Australian telecommunications market, are based on its surveys of business users.

Top 100 Survey

ATUG's Top 100 survey conducted in April/May 2002 revealed the following conclusions of relevance to this Inquiry:

- 1) Telstra's dominance among Top 100 companies is comprehensive. 30% of those interviewed use Telstra exclusively, even though most of these companies have previously used other carriers. Moreover, most companies using multiple carriers limit their usage to two and in the vast majority of cases Telstra is the main supplier, typically capturing around 80% of the company's annual telecommunications budget.
- 2) Reasons for Telstra's continuing dominance relate largely to its network reach, and the economies of both scale and scope. Put simply, there are many products and services demanded by Top 100 companies that only Telstra provides.
- 3) Significantly, there is very little use of resellers among Top 100 companies. There is a clear and consistent preference for dealing directly with carriers that own and operate their own networks. For this reason, after Telstra, Optus emerges as the next most widely used provider and remains the only other carrier to have had a significant impact in the large corporate segment.
- 4) Among locally based carriers AAPT/Telecom New Zealand, PowerTel, UeComm, RSL Communications and Macquarie Corporate Telecommunications have made some inroads into the Top 100 – but to a very limited extent. Among global service providers, only BT, Equant, MCI Worldcom and Infonet rated a mention.
- 5) Some Top 100 companies have been willing to consider using Vodafone and Hutchison for mobile service, but these two companies have been largely unsuccessful in winning business from large corporations. This is despite substantial direct investment by both companies in their own networks. There is also a perception among the Top 100 that mobile services are one of the main areas where competition hasn't worked. The basis of this assessment is that the non-Telstra networks don't have adequate rural and regional coverage; and that there is insufficient price and product differentiation in mobile services.
- 6) While Telstra continues to attract criticism for its "complacency", "arrogance" and "public service mentality", corporate users frequently concede that these problems are less acute now than 5 years ago. Importantly, these criticisms were less frequent than the praise given to Telstra for its improved marketing, reduced prices,

greater flexibility and responsiveness, diversified service offerings and efforts to improve service generally.

- 7) Assessments of the performance of new entrants were also mixed. The main criticisms related to lack of depth in product offerings, reliance on Telstra for network coverage and support, failure to deliver on promises, “hopeless” service and various forms of added cost and inconvenience in having to manage an independent carrier while also dealing with Telstra. Offsetting these negative assessments were views that entrants were easier to deal with than Telstra, provided services at lower cost, mitigated operating risk through network diversity, in some cases have superior capabilities based on specialisation, and, in some cases, there was a willingness to package services more attractively than Telstra (eg by selling dark fibre).
- 8) While it is fair to say that many companies see competition as being beneficial and having delivered some positive outcomes, there are four key areas of concern:
 - Telstra’s continuing dominance is linked to its network reach and coverage, particularly in regional areas;
 - There is an expectation that prices should fall further;
 - Mobile and data services are two areas where competition is seen to have delivered little or no benefit, while broadband has been slow to develop due to cost and supply constraints; and
 - Competition is not seen in terms of how many suppliers exist but how effective they are – and for some respondents, at least, there is a view that fewer competitors, each operating on a larger scale, is preferable to a market comprised of Telstra plus a large number of niche and small companies.

Users face a conundrum – to get the coverage and product range they want, often Telstra is the only provider capable of meeting the full needs.

The user’s experience is not one of buying in a strongly competitive market. Users point to examples such as high prices for leased lines, high prices for mobile and fixed to mobile calls, use of the Standard Form of Agreement in contracts with corporate customers and complexity as evidence of a market that is still not robustly competitive.

SME research

ATUG is currently conducting research into competitiveness in the SME sector. Preliminary findings from this market reveal:

- 1) Communications and IT are regarded as critical to business by 90% of the businesses surveyed (sample size 313, national and regional companies).
- 2) Fixed phone is considered to be the best value service ahead of Internet
- 3) Mobile phones, although a high usage service, are clearly considered to offer the least value
- 4) 55% of SMEs use an intermediary for access to some part of their communications and IT services.

- 5) The most important communications and IT services are fixed phone and fax, computer equipment and mobile phones and the Internet.
- 6) Expenditure on communications services has increased over the last twelve months.
- 7) 61% of businesses ranked expenditure on Total Communications and IT services in the top 5 expenses for their business
- 8) In the key product lines (fixed phone and fax, mobiles, 1800/13 numbers, broadband, and other data services) Telstra is earning over 80% of the total revenue. Only in Internet services do we see strong competition with Telstra only earning 44% of the sample revenue.
- 9) The SME sample indicated the best communications companies were – Telstra (65%), Optus (19%), Vodafone (5%)
- 10) The following reasons were given: Telstra – familiar and satisfied, biggest/oldest company; Optus – competitive rates; Vodafone – service/products are good.

The use of intermediaries in this segment means there is less concern about providers owning their own networks. The importance of the “core” services – phone and fax – reinforces the significance of competition in delivering price and other benefits to end users.

Attachment 2

Extract from ATUG's submission to the Senate Inquiry into The Australian Telecommunications Network, August 2002.

The objective of open competition in telecommunications was (and must remain) to promote the long-term interests of end users and the efficiency and international competitiveness of the Australian telecommunications industry.

However, there are a number of tensions between these policy objectives and what has been achieved in practice.

It is increasingly clear that users cannot rely on the market and self-regulation to deliver outcomes.

After a number of years of open competition in telecommunications, it seems:

- 1) A privatised incumbent operating in a competitive industry will always focus on maximising shareholder returns
- 2) The "light touch/industry self-regulation" approach has not been effective in protecting end users
- 3) The focus on process rather than outcomes has led to delay rather than decisions – we need time limits and transparency for all decisions about access
- 4) The "one size fits all focus" on infrastructure (facilities) competition rather than services competition has resulted in wasted capital and a negative reaction from the capital markets to further innovation
- 5) The size and spread of the market have created difficulty in diffusing competition beyond the CBDs. Progress has only been achieved by direct Government funding
- 6) Users need much clearer, cost-oriented supervision of pricing.

A combination of regulatory focus and Government funding has been essential to securing outcomes for end users. The market alone has not delivered the results. The Customer Service Guarantee, The Universal Service Obligation, the new ACA National Reliability Framework for Monitoring and Reporting on Quality of Service, ACA mandated Mobile Number Portability are all important regulatory tools. In addition Government funding and industry funding for USO obligations has provided in the order of \$1 billion direct funding for development of services in regional, rural and remote Australia.

The role of the ACCC has been important in achieving the basis for competitive wholesale offerings on call services, access services, mobile services and lately broadband services."

Since that submission, further amendments (November 2002) have been made to the Trade Practices Act but these have not yet been fully implemented and ATUG's concerns about the effectiveness of current regulation remain.

Attachment 3

Extract from ATUG Submission to Proposed Foxtel/Optus content sharing agreement, April 2002.

ATUG first raised its concerns about bundling in its submission to the Commission on the proposed Foxtel/Optus deal in April 2002. ATUG's concerns at the time were:

- 1) The long-term interests of end users will not be well served if Telstra winds up owning both the national copper network and both the HFC cable networks and controlling the STB access to the house. This would be a significant reversal of the facilities competition that has been a cornerstone of policy to date.
- 2) The long-term interests of end users will not be served if service based competition is further weakened by the power of Telstra to bundle all communications services including Pay TV if others (except Optus) are not able to offer equivalent bundles.
- 3) Any outcome which would lead to the possibility of higher prices for users because of further concentration of market power in telecommunications should be reviewed very carefully and regulatory responses put in place as a pre-condition to approving the agreements, if that is the ACCC decision."

ATUG's specific concerns about the Foxtel/Optus proposal were:

- 1) Content Exclusivity – access for content providers such as C7, TARBS, ABC
- 2) Access to content for carriers and carriage service providers – such as TransAct and Neighbourhood Cable. From ATUG's perspective the key issue raised by the agreements centres on the implications for competition in the delivery of telecommunications services.
- 3) Access to content services for other retail telephony providers – such as AAPT and Hutchison. At the services level, there is clear evidence from recent ACA surveys that residential users only want to deal with one service provider. This makes access to Pay TV content services for retail bundling with telephony and internet services key to competitive survival for companies such as AAPT, MCT, PowerTel, Hutchison and Primus.
- 4) Technology neutral policy should remain a feature of the telecommunications industry, unlike the media sector where policy has been technology specific eg free to air TV, pay TV, datacasting, narrowcasting, analogue/digital TV.

Attachment 4

Extracts from ATUG's submission to the ACCC discussion paper on Regulatory Principles for Public Disclosure of Record-Keeping Rule Information, March 2002.

The policy objective of competition in telecommunications services is to increase choice for users and thus to deliver price and service benefits and innovation.

The promotion of competition can be achieved by a mix of structural means, regulatory means, information and market pressure. The tools to be applied, in ATUG's view, depend on the level of competition in a particular market, measured not only by customer share but also by costs, revenues and margins.

Information is clearly as an important tool for the ACCC in administering competition regulation in the telecommunications industry. The two main areas of focus, assessing anti-competitive behaviour and guaranteeing access to network services on terms and conditions that are reasonable, both rely on access by the ACCC to proper information.

ATUG supports the Commission's view that disclosure of record-keeping information can promote competition by:

- 1) Reducing the **information asymmetry** between access providers and access seekers
- 2) Increasing the **transparency** of decisions with regard to part XIB and part XIC matters and
- 3) **Informing** consumers, policy makers, other firms and investors to enable them to participate more effectively in the telecommunications market.

INFORMATION ASYMMETRY

Disclosure is an important answer to the information asymmetry problem identified. As an alternative to mandatory disclosure, the ACCC might consider using industry wide ADR processes for certain decisions eg access deficit and interconnect rates.

Given the increasing movement of the industry, with the help of the ACCC, towards dispute resolution rather than arbitration (a move ATUG applauds) it is important that information disclosure is not confined to that collected in arbitral processes but applies also to information gathered under the record-keeping rules.

ATUG suggests that the developing communications skills of the industry in alternative dispute resolution processes should be applied to an industry based determination of the access deficit and the interconnect rate going forward. The ACCC and industry participants should develop an industry-agreed position on these important questions.

Such an approach could help to achieve the open, speedy and transparent access as discussed in recent amendments to the Trade Practices Act.

The concern expressed in the Act that disclosure be constrained by regard for the legitimate commercial interests of firms rests on an assumption that the legislation has been effective in promoting competition. ATUG does not believe this has been achieved yet given the revenues, margins and profitability of Telstra compared to any, indeed all, of the competing firms. The focus should be on promoting competition until success has been achieved against this paramount objective. The relevant tests are whether disclosure is in the long-term interests of end users and whether disclosure would promote competition.

TRANSPARENCY

ATUG supports the disclosure of information as a means of ensuring transparency of regulatory decision-making, a concern traversed at length by the Productivity Commission Report. Concerns by participants as to the basis for ACCC decisions should be eased by the disclosure of the information on which these decisions are based.

INFORMING OTHER PARTICIPANTS

For purposes of reassuring users that progress is being made in the competitiveness of the industry, information should be publicly available on an aggregated basis. This assurance is more important given the direction of price movements upwards over the last 6 months. The ACA Annual Report 2000-01 (page 48) indicates that the vast majority of benefits to consumers from the telecommunications regime have been **non-price** benefits (89% of upper limit benefits of \$12 billion). Given the small % that price benefits comprise after 5 years it is important that the ACCC adopt a positive position on information disclosure to the public to ensure that price changes are cost related.

ATUG has a preference for public disclosure wherever possible in keeping with our specific policy of Informed Choice. For competition to be effective in the telecommunications industry not only the competitors but also users need to have a secure information base on which to make decisions about prices. Where markets are clearly competitive the need for this information support is not required. Where a product or service is essentially monopoly provided then information about costs should be readily available to competitors and users.

ATUG is of the view that information should be made publicly available by ACCC at the time of any price increases in services that are not yet competitive, to provide assurance to the public that increases are cost related.

Attachment 5

ATUG review of ACA research

The ACA's Annual Report on Telecommunications Industry Performance 2001-02 shows stronger industry performance over 2001-02 and clear gains in consumer benefits "although consumer satisfaction had declined in many areas." The report also "found that Australian households were between \$595 and \$878 better off in 2001-02 than they would have been without these reforms."

The Allen Consulting Group Report for the ACA "Benefits Resulting from Changes in Telecommunication Services" finds that Australia economy is \$10 billion better off in 2001-02 because of reforms in telecommunications. This report goes on to make the point that "winning industries include the telecommunications industry and those industries that supply goods to the telecommunications industry." Not surprisingly "States and Territories with a greater proportion of telecommunications activity have benefited the most from the telecommunications reforms."

These positive findings have to be balanced by user reality as reflected in other reports. For example, the ACA findings reported in its Customer Satisfaction Survey 2002 Special Report No.12. For example, at page 7, 67% of residential users and 64% of business users think line rentals are too high or at page 9 "dissatisfaction levels with overall fault repair were very high and the highest reported since the survey began in 1998."

The percentage of customers who were satisfied with customer service when contacting phone company with a request or question has dropped from 71% of small business users being satisfied in 2001 to only 50% being satisfied in 2002.

Satisfaction in small business with the overall technical quality of mobile phones has dropped from 75% satisfied in 2001 to 60% in 2002, with lower satisfaction for non-urban small business users at 48% - less than half of those surveyed.

Users find it difficult to compare information supplied by service providers, with around 49% of small businesses saying its difficult to compare offers (fixed and mobile) from the same company and 52% to 56% saying it's difficult to compare offers between companies.

Overall, satisfaction levels with the increase in competition and price competition declined in 2002 for both fixed line and mobile phone services. Responses were similar across both household and small business respondents. Both groups were less satisfied with price competition than with the general increase in competition.

The ACA's conclusion, "The 2002 consumer satisfaction survey results indicate a general decline in satisfaction across most aspects of telecommunications services measured. The survey results suggest that the respondents did not perceive an overall improvement in many aspects of the telecommunications market. Growing

dissatisfaction was also evident in the 2002 survey, particularly for customer service (fixed phones), fault repair (of fixed phones), quality of information provided to consumers by fixed phone services providers (among small business respondents) and the level of price competition in the fixed phone market, (among household respondents).”

All of which agrees with work ATUG did in early 2002 to assess the view of big users of telecommunications services on how competitive the industry is. The finding reflected continued dominance of the market by Telstra because of their network reach and the depth of their product range.

An important conclusion comes from this assessment of the various reports on the industry. It is important that users be asked regularly and directly for their views on progress in telecommunications reform. It is too easy to look at macro-level indicators such as CSG performance and draw the conclusion that service is fine, or to look at time to answer statistics for service centres and conclude that customers requests for information are being satisfied and so on.

Important developments in telecommunications competition and performance reporting and management in 2002 have centred around the collection, assessment and use of finer grained information by both the ACA and the ACCC, to achieve what we all set out to achieve with telecommunications reform “the long-term interests of end users and the international competitiveness of the Australian industry.”

Attachment 6

ATUG Profile

ATUG was established in 1980 by a number of corporate users of telecommunications with the purpose of achieving a de-regulated telecommunications market. ATUG's mission is to achieve world class telecommunications services at world class prices for Australian businesses.

ATUG seeks to influence government, regulatory bodies and suppliers to ensure they contribute positively to the ongoing development of the communications industry.

ATUG actively promotes the use of telecommunications as a strategic resource that business can use to improve both efficiency and market position.

ATUG endeavours to ensure its members have the necessary knowledge to make the best use of modern communications services through regular branch meetings, workshops, focus groups and peer-to-peer activities conducted in all Australian states.

ATUG is a member the Government's Broadband Advisory Group.

ATUG is a member of the ITT Industry Training Advisory Board.

ATUG has been appointed Vice Chair Asia Pacific Region, International Telecommunications Users Group.

ATUG is a member of the ACA's Consumer Consultative Forum.

ATUG is represented on the Board of the Australian Communications Industry Forum.

ATUG is represented on the QLD Government Communications Information Advisory Board

Attachment 7

ATUG Focus Policies

ATUG's Objective

To achieve high quality telecommunications services at OECD benchmark prices for Australian businesses.

Competition

ATUG supports sustainable competition as the best way to deliver choice, reduced prices and innovation. In some areas, ATUG believes competition has stalled. Proactive involvement by government and regulatory bodies is needed to achieve more timely outcomes for the long term benefit of end users. Prices for telecommunications services should be cost related.

Open Access

ATUG believes practical equality of access to the Local Loop and PSTN, on fair and reasonable terms and conditions, is essential to effective competition. This has not yet been achieved. The ACCC should determine and make publicly available indicative prices, terms and conditions for supply of critical network services.

Broadband Connectivity

The benchmark for communications connectivity is affordable always-on broadband access at minimum 256Kbps. Strong competition in service delivery, government initiatives and policies to support content development will accelerate take-up.

Mobiles

ATUG will work for significant reductions in international roaming and fixed-to-mobile charges.

Users should have access to the most extensive network coverage possible. ATUG will work to achieve national roaming between carriers on fair and reasonable terms and conditions.

Informed Choice

Telecommunications contracts are too complex. They should be in plain English format, readily understood by the users of the services to enable "fit for purpose" choice of service quality and fairer negotiation of prices.

Regional Telecommunications Services

Fairly priced up-to-date communications services are essential for economic and social development in regional, rural and remote Australia. Policies must be put in place to support the development of such services in cases of market failure.