

# **SUBMISSION TO THE AUSTRALIAN COMPETITION & CONSUMER COMMISSION**

**In response to the discussion paper of August 2000 on the**

## **FUTURE SCOPE OF THE LOCAL CARRIAGE SERVICE DECLARATION**

RSL COM Australia Pty Limited (“**RSL COM**”) makes this submission in response to the Discussion Paper considering Telstra’s individual exemption application and the possibility of a class exemption for the local carriage service (“**LCS**”).

In this submission, RSL COM addresses the questions raised by the ACCC in the Discussion Paper:

- The individual exemption application.
- The class exemption.
- Future variations to the declaration of the local carriage service.

RSL COM has addressed the last issue first. RSL COM submits that the timing issues involved in any reconsideration of the declaration of the LCS, or any exemption from the Standard Access Obligations (“**SAO**”), are of primary importance.

### **1 EXECUTIVE SUMMARY**

- 1.1 It is premature to vary declaration of the LCS or exempt any carriers from the SAOs.
- 1.2 The effects of the declaration of the LCS cannot be determined until the LCS is unbundled, all access disputes regarding pricing methodology are resolved and the relevant market has had an opportunity to become self-sustaining in its operation.
- 1.3 Individual exemption for Telstra from the SAO would not promote the long-term interests of end-users (“**LTIE**”) of the LCS.
- 1.4 Each of the key considerations referred to by Telstra in its application is without foundation. In particular, there are no reasonably close substitutes currently available for the provision of the LCS, particularly for resale to a small to medium sized enterprise (“**SME**”).
- 1.5 A class exemption would not promote the LTIE. RSL COM submits that the issues it raises against Telstra’s application also apply in relation to the exemption of other carriers.

### **2 APPROPRIATE TIMING**

What are the views of industry participants, and the general public, as to the appropriate timing for consideration of possible variations to the local carriage service declaration, if any?
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- 2.1 RSL COM submits that the issue of timing is of primary importance in the treatment of any application for exemption from the SAOs and any variations to the declaration of the LCS.
- 2.2 RSL COM submits that it is premature, if not impossible, to assess the LTIE in light of the declaration until the declaration of the LCS has been put into effect in the manner intended by the Commission in two respects.
- 2.3 First, Telstra will only provide LCS as a bundled service with other product packages, notwithstanding the rationale of the declaration of the LCS as expressed in the Commission’s Report on the Declaration of Local Telecommunications Services of July 1999 (“**Declaration Report**”). Telstra offers local calls on a rebiller model with its other product packages, as described in the following table.

<b><u>Group</u></b>	<b><u>Description of Content</u></b>
<b>Local Calls</b>	All timed (eg NDD) and continued local calls that are subject to geographic numbers within the numbering plan and fall within the definition of “local calls” within PSTS and PSIS sections of the Standard Forms of Agreement (“ <b>SFOA</b> ”).
<b>Long Distance Calls</b>	STD and IDD calls that are preselectable and carried on the Telstra Network.
<b>Other Usage Calls</b>	All other usage calls that are not local or long distance call types being redirected via the Local Calls Product Package or Long Distance Calls Product Package (eg fixed to mobile calls, operator services, 1800/1300 calls, calls to data service codes, paging services will be redirected via this group).
<b>Access</b>	All PSTS and PSIS non-usage charges are to be redirected under this package. This package includes the rental charge for live access.
<b>Data</b>	Non-usage services within the Public Switched Data Services section of the SFOA (such as DDS backbone, routes and wholesale transmission services) but does not include, among other things, data services currently billed by BLISS.

- 2.4 RSL COM adopts the arguments of the Commission in paragraph 3.2 of the Declaration Report. The Commission referred to the risk of loss of efficiencies through access providers needing to separate internal processes so that each element could be provided as a separate service. However, RSL COM argues that Telstra’s recently developed Wholesale Billing Platform enables full unbundling without those associated efficiency losses.

- 2.5 The Commission also noted in the Declaration Report that full unbundling would not be warranted in the absence of demand for individual elements. RSL COM submits that end-users have demonstrated a sufficient willingness to use separate service providers for different call types.
- 2.6 RSL COM agrees with the Commission's comments in the Declaration Report that at least partial unbundling is warranted in promoting the interests of end-users and that LCS comprises a particular bundle of elements commonly sought by access seekers.
- 2.7 Second, carriers must be required to unbundle the LCS before any application for exemption should be entertained and before any variation occurs to the declaration. In its Draft Report on access pricing for the LCS of April 2000, the Commission proposed a retail-minus pricing methodology, as opposed to the TSLRIC methodology. Telstra maintains that TSLRIC is the appropriate methodology and has been charging wholesale rates for local calls accordingly.
- 2.8 Until these issues are resolved and a self-sustaining wholesale market for the LCS is able to develop, the effects of declaration on the LTIE cannot be determined.
- 2.9 With virtually all major service providers in an access dispute with Telstra over the price of the LCS and with other major carriers effectively refusing to supply the LCS at all, there has been no opportunity to accurately analyse the commercial case for resale of the LCS in the manner anticipated by the Commission when it declared the service.
- 2.10 The existence of these outstanding issues with regard to the supply of the LCS as declared gives rise to uncertainty as to the likely effectiveness of the declaration of transmission capacity. In light of such uncertainty, it is difficult to determine whether there is a strong commercial case for service provision based on the leasing of declared transmission capacity.

Over what geographic areas should the inquiry, or inquiries, be focused?

- 2.11 This issue needs to be considered in light of the difficulties associated with the likelihood of discrepancies in rates for declared and non-declared local calls and the complexities involved in distinguishing between these types of calls when they traverse exempt and non-exempt areas.
- 2.12 RSL COM submits that variation of the declaration of the LCS will lessen competition not only in CBD areas, where Telstra's dominance has not diminished regardless of declaration and will prevail if it is made exempt, but also elsewhere in Australia as service providers, particularly SMEs, find it increasingly difficult to compete in a range of services.

- 2.13 RSL COM anticipates that variation of the declaration could result in RSL COM being unable to obtain the LCS at a sustainable margin. Without a core base of local call customers, service providers, SMEs in particular, will be unable to keep a sufficient customer base for the supply of other associated services such as long distance calls. This will affect areas outside the CBD areas, particularly if many service providers are driven out of business.

### **3 INDIVIDUAL EXEMPTION FOR TELSTRA**

#### *Promotion of Competition*

- 3.1 RSL COM submits that until declaration of the LCS has effect on the conduct of carriage providers in the manner the Commission intended in the Declaration Report, it is premature to assess the effects of declaration (and therefore exemption) on competition.

#### *Market definition*

Is there a market that involves the wholesale supply of the local carriage service by carriers to themselves and other carriers?

- 3.2 RSL COM submits that until the LCS is unbundled, analysis of competition in light of a market for wholesale supply of the LCS is irrelevant.
- 3.3 There exists demand from end-users for a local call offering as part of a range of services that a service provider may offer. However, the extent of any specific market or sub-market for wholesale supply of the LCS is virtually impossible to assess because Telstra has not offered a service that meets the description of the LCS as declared
- 3.4 There is a potential market for the wholesale supply of the LCS. RSL COM meets some end-user demand for local calls by resupply of local calls provided by Telstra on the terms and conditions applicable prior to declaration. RSL COM also offers local calls to end-users via override on its leased lines. If Telstra (and any other carrier) offered the LCS, unbundled and priced on a retail-minus model, RSL COM believes that there would be significant demand from service providers for wholesale supply of the LCS.

How should CBD areas be described?

- 3.5 Telstra's definition of CBD areas as the Exchange Service Areas it classifies for its own internal purposes, is, as the Commission suggests in the Discussion Paper, a definition that can be varied by Telstra. RSL COM submits that a subjective definition is unacceptable.
- 3.6 Telstra's provision of local calls is subject to the classification of areas in Telstra's SFOA. There is no direct relationship between the Exchange Service Areas and the local charge zones.

- 3.7 Local call charge zones are established areas that appear to be stable and not subject to any variations that Telstra may make. In this respect, consideration of a CBD area may not be appropriate, unless that area fits exactly into a local charge zone.
- 3.8 To define a CBD area without reference to a local charge zone would introduce complexity that would be detrimental to the LTIE. It would be complex to determine which calls are covered by the declaration and which calls are covered by the exemption due to the likelihood that the rates for each will differ.
- 3.9 Consideration is also required as to the appropriate treatment of supply of a service while subject to the SAOs with a service supplied under exemption in circumstances where end-users make calls across adjoining local charge zones. Are such local calls treated under the terms and conditions relevant to the LCS as declared or under the terms and conditions relevant to an exempt service?
- 3.10 These issues of complexity associated with separate treatment of calls between particular areas may threaten the achievement of any-to-any connectivity to the extent that exemption effectively favours calls to some destinations over others.

What substitute technologies (which constrain the price and output decisions of carriers supplying the local carriage service) are currently used to provide the local carriage service, or are substitutes for the local carriage service, in the CBD areas? What technologies are likely to be used to supply the local carriage service or local calls in CBD areas in the foreseeable future?

- 3.11 The Discussion Paper identifies a number of potential substitutable services and technologies, including unconditioned local loop services (“ULL”), PSTN originating and terminating services, fibre optic loop services, LMDS technology or other wireless local loop networks, satellite and services supplied using transmission capacity.
- 3.12 RSL COM is of the opinion that none of these actual or potential broadband alternatives is a commercially viable substitute from the perspective of a non-carrier service provider resupplying voice bandwidth services. None of the proposed alternatives is likely to replace the current collection and delivery technologies to any great extent in the near future.
- 3.13 These options might be attractive to a larger customer where the opportunity exists to carry local (and other) voice calls on the same broadband technology as that on which data is being carried. However, for an SME, this is not commercially viable. Such small operations simply do not generate sufficient volumes of traffic to justify the expenditure.
- 3.14 Specifically with regard to ULL, those service providers who have indicated interest in using that service intend to offer broadband services. RSL COM suggests that Telstra itself considers high-bit-rate digital subscriber lines (HDSL) and asymmetric digital subscriber lines (ADSL) products as its competition to ULL services. This runs contrary to the argument that ULL is a substitute for the LCS.

- 3.15 Telstra's rates for ULL are significantly higher than the rates it currently charges for local calls, even on a TSLRIC methodology. To treat ULL as a substitutable service for the LCS is to require end-users to pay for broadband services when the current scope of apparent demand for local calls merely requires voice-grade service.
- 3.16 RSL COM operates predominantly in the SME segment of the market. In that segment, due to scale, the only available substitute for the LCS is the addition of local calls into the pre-selectable basket. The result would be that the four main call types (international, long distance, fixed-to-mobile and local) are all contained in the same basket. This would enable the customer to substitute one supplier for another in respect of all traffic or, alternatively, to use an override code to substitute on a call-by-call or call-type-by-call-type basis.

*Market share, new entrants and likely competing infrastructure*

Are there likely to be further new carriers supplying the local carriage service at a wholesale level in the foreseeable future? What type of technologies would new carriers be expected to use, and would entry be expected in the CBD areas (if so, in which areas)?

- 3.17 It is difficult to see how a competitive market can be facilitated for the supply of local calls simply by relying on the advent of new technologies. The infrastructure required to implement new technology will possibly be commercially viable for a small number of large suppliers.

What level of local call resale competition is occurring in CBD areas and is it expected to increase in the foreseeable future?

- 3.18 Local calls have always been available to end-users under the commercial churn/rebiller model, but only as part of the integrated service.
- 3.19 Various service providers have commenced to sell local calls at a lower rate. RSL COM commenced offering local calls via its leased lines. These calls are distinct from the LCS, which are rebiller-based. One of the primary reasons for RSL COM using leased lines for local calls was that RSL COM was unable to obtain realistic terms and conditions from Telstra with regard to the LCS, particularly with regard to price. Furthermore, it was clear that Telstra had no intention of providing the LCS as an unbundled service.
- 3.20 Other service providers commenced to offer local calls derived from a rebiller model. However, they were unable to do so without entering into a "whole of business" arrangement with the customer. This meant that they had to commercially churn the customer and provide all the integrated services, including help desk and fault management. RSL COM submits that this result was not the intention of the Commission as stated in the Declaration Report. The Commission states that a purpose behind declaration was to remove this integration and free the industry for competition in the LCS as a more narrowly defined service.

- 3.21 RSL COM is of the opinion that very little competition actually occurs in CBD areas. The best retail price available at present is \$0.15. This is the rate Telstra charges for its Neighbourhood call. Service providers must match the \$0.15 rate if they are to compete. Service providers operating on a rebiller model can only compete with this price if they retail the call for less than cost. RSL COM submits that this pricing tactic has raised a significant barrier to entry. RSL COM suggests that Telstra's share of local call sales remains at approximately the same level as it was since declaration of the LCS.

Would providing an individual and/or class exemption change the incentives for carriers supplying the local carriage service at a wholesale level or new re-sellers supplying local calls at a retail level? If so, how?

- 3.22 RSL COM anticipates that if Telstra were successful in its application for exemption they would refuse to supply wholesale local calls (via the rebiller model or any other non-network related mechanism). Alternatively, Telstra might insist on a price that would be prohibitively high so as to prevent RSL COM from obtaining a margin from a competitive retail price.
- 3.23 At present, Telstra argues that it is incapable of separating local calls from the integrated product packages. Assuming that is the case, Telstra could not supply any of the integrated services if it were to avoid supply of local calls to RSL COM. This would mean that an end-user who wanted to have a single bill for its fixed-wire services would be required to use Telstra for all these services.
- 3.24 Exemption would therefore reduce the incentive to compete in the supply of local calls by diminishing the ability of service providers to compete in any market segment where the end-user wishes to have a single fixed-wire bill.
- 3.25 In the alternative, if Telstra is capable of unbundling local calls, the effect of declaration should be examined subsequently to that occurring.

#### *Barriers to entry*

Are the sunk costs associated with rolling out new networks a significant barrier to entry for carriers supplying the local carriage service at a wholesale level in CBD areas? Do the sunk costs differ substantially between different technologies?

- 3.26 Sunk costs are virtually an absolute barrier to entry for an SME such as RSL COM. RSL COM can operate as an effective competitor only to the extent that it does not have to sink capital into building a retail level network. If it were to obtain a carrier licence and then embark upon a network-building program, significant amounts of capital would be required with uncertain return in light of the current dominance and deep pockets of the incumbents.

- 3.27 It is not in the interests of end-users that a potential competitor should have to be a licensed carrier. Such a situation limits the threat of competitive entry by requiring major capital investment. Exemption or variation of the declaration would stultify the “competitive fringe” of SMEs which currently has the potential to give rise to genuine competitive pressure in the resupply of local calls, once the pricing and unbundling issues are resolved.

Are there any other barriers to entry for new carriers supplying the local carriage service at the wholesale level in CBD areas, such as Telstra’s market share?

- 3.28 RSL COM submits that it is impossible to answer this question. Telstra’s market share is unknown (but probably unchanged from its dominant position prior to declaration). It is also impossible to assess the commercial case for investment in infrastructure in the CBD areas due to the absence of information about the effects of declaration, as outstanding issues regarding unbundling and pricing methodology are unresolved.
- 3.29 However, RSL COM submits that exemption would have the ultimate result of requiring Telstra’s competitors in the sale of local calls in the CBD areas to be vertically integrated carriers. Competition would therefore be further inhibited by the structure of the market and the inherent continuing monopoly that Telstra maintains over basic access, local calls and national long distance calls.
- 3.30 RSL COM also submits that the level of complexity that would arise if certain areas were treated as exempt from the SAOs would lead to overwhelming transaction costs for end-users to inform themselves of the comparisons between (and within) services and then to switch. This could only favour Telstra.

Are there any barriers to entry for new re-sellers supplying local calls at a retail level?

- 3.31 Despite declaration of the LCS, there is no margin to be made by a service provider in this type of call. Furthermore, local calls remain bundled with other services. The position has not changed significantly from the situation prior to declaration. If anything, margins have been squeezed further.
- 3.32 Going beyond the LCS and examining the alternative of leasing lines, PSTN originating and terminating services can presently be used to supply local calls. This can only be done by the use of override code and not by preselection. Using override codes is a disincentive to the end-user.
- 3.33 This disadvantage can be overcome by adding local calls to the preselection basket. The preselection basket would then hold all the major call types. End-users would have the ability to make an overall preselection of one service provider (and one bill) and then use the override codes from time to time as they wished.



- 3.34 The existing declaration of the LCS should remain at least until local calls are added to the preselection basket.

*Market dynamics*

Has there been growth in the demand for local calls in CBD areas since the local carriage service was declared (if so, in which CBD areas)? If so, has the growth been captured by incumbent carriers or new market entrants?

- 3.35 It is doubtful whether there has been any real growth in either the number of local calls or the minutes of local call traffic. Some minor redistribution via the rebiller model has occurred and RSL COM has been able to secure some business by offering local calls on its own network, but requiring end-users to use override codes. RSL COM derives most of its network-based local calls from the metropolitan areas and not the CBD area. RSL COM believes that Telstra dominates in the CBD area.

Is it expected that there will be growth in the demand for local calls in CBD areas over the foreseeable future (if so, in which CBD areas)?

- 3.36 RSL COM does not perceive any underlying drivers for an increase in demand for local calls in the CBD areas. To the extent that end-users prefer alternative technologies for internet and data transfer in the long term, RSL COM anticipates a drop in demand for local calls, where these calls are currently used for internet and other data purposes (bearing in mind that the declared service is for a voice-grade service).

***Efficient Use of, and Investment in, Infrastructure***

*Technical feasibility of supplying and charging for particular services*

- 3.37 RSL COM submits that the technical ability to unbundle the LCS is a crucial question but one that only Telstra can answer. As has been discussed already, Telstra maintains that it is unable to unbundle the LCS. RSL COM agrees with the Commission's suggestion in the Discussion Paper that Telstra bears the onus to demonstrate that supply of unbundled LCS is not technically feasible.
- 3.38 This issue has ramifications for the ability of a separate wholesale LCS market to come into being. It also determines the extent of the detrimental effect of exemption on service providers to whom Telstra refuses to supply the LCS and, necessarily (allegedly), other bundled services.

*The legitimate commercial interests of the supplier, including the ability of the supplier to exploit economies of scale and scope*

Since the Commission's report on the *Local Telecommunications Services*, what has been the impact of declaration on the legitimate commercial interests of the carriers supplying the local carriage services at a wholesale level (Telstra and other carriers)?

- 3.39 RSL COM has seen no evidence that Telstra has been affected at all by the declaration of the LCS. Indeed, Telstra has taken the view that wholesale arrangements in place prior to declaration are just as applicable to the LCS as declared.
- 3.40 The reason for this is clear. Telstra has not responded to the declaration and the Declaration Report by refusing to alter its pricing methodologies and failing to unbundle the LCS from other product packages. Until these significant issues are resolved, the declaration of the LCS cannot be said to have had effect in the marketplace.

*Incentives for investment in existing and new infrastructure*

- 3.41 RSL COM submits that exemption will have the effect of forcing service providers to invest in infrastructure because no other means will be likely to be available to gain access to local calls. RSL COM is of the view that such investment would be uneconomical in light of the economies of scale and sunk costs involved. This is also the case in light of the probability that demand for voice-grade local calls will not increase, as opposed to demand for broadband data transmission.

#### **4 CLASS EXEMPTION**

- 4.1 RSL COM submits that class exemption would not promote the LTIE.
- 4.2 Class exemption would send the wrong message to potential entrants. In light of the refusal by some carriers to discuss the supply of local calls, and Telstra's constructive refusal to supply the LCS due to its failure to unbundle and its adherence to a TSLRIC pricing model, class exemption would suggest that ignoring a declaration and its principles is a successful strategy for incumbent and future carriers to the detriment of SMEs.

#### **5 LIKELY MARKETPLACE IF EXEMPTION IS GRANTED**

- 5.1 RSL COM anticipates that the result of exemption for Telstra or any other carrier from the SAOs in the supply of the LCS, as declared, will be the carrier's refusal to supply the LCS on commercially viable terms and conditions.

- 5.2 The likely effect of Telstra gaining an individual exemption in CBD areas is that it would be unlikely that any service provider would be able to offer local calls in those areas. Without the ability to resupply the LCS it is unlikely that a service provider will be able to attract a sufficiently large customer base in order to compete in a range of services over broader geographic areas.
- 5.3 RSL COM anticipates that service providers would also lose access to all other rebill services. The loss of the other rebiller services results from Telstra's alleged inability to separate local calls from the remainder of rebiller services.
- 5.4 Exemption will therefore significantly reduce the end-user's choice of service provider and will alleviate downward pressure on prices and other terms and conditions.
- 5.5 RSL COM is of the view that it is premature to consider exemption from the SAOs or variation of the declaration of the LCS. It is irrelevant to analyse the current state of the market as an indication of the effects of declaration of the LCS. Until the LCS is unbundled and pricing issues are resolved, there is no relevant post-declaration market to analyse.

RSL COM Australia Pty Ltd  
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