



DECLARATION OF THE DOMESTIC MOBILE TERMINATING ACCESS SERVICE

Response to the
Australian Competition
and Consumer Commission

5 July 2013



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1. Executive summary

Vodafone Hutchison Australia Pty Limited (**VHA**) welcomes the opportunity to participate in the Australian Competition and Consumer Commission's (**ACCC**) consultation process on whether to extend, vary or revoke the domestic mobile terminating access service (**MTAS**) declaration, or whether to make a new MTAS declaration.

VHA acknowledges that declaration of the MTAS has been in the long term interests of end-users (**LTIE**) and is a necessary part of a framework to promote of competition in the mobile and fixed services markets and any-to-any connectivity and that declaration could assist in to in the efficient use of, and investment in, infrastructure by mobile network operators (**MNOs**). However, in assessing how the declaration operates it is vital to recognise that MTAS is used for two important purposes. First, it is used by MNOs to carry mobile-to-mobile (**MTM**) calls between mobile networks. Second the MTAS is also used extensively in the provision of fixed-to-mobile (**FTM**) calls – these services are provided in a market that is structurally different to the mobile services market. The fundamental issue in regulating the MTAS is to ensure that, although necessary, declaration does not operate so as to simply enrich fixed network operators such as Telstra at the expense of pure MNOs and consumers. That in turn requires a careful consideration of the impacts of MTAS regulation on two distinct markets: the mobile services market and the fixed voice services market. Without such consideration consumer benefits that would otherwise accrue will not be realised and the LTIE will not be truly promoted.

If the ACCC proceeds to extend or vary the declaration, it must develop a coherent framework for assessing the dynamic implications of changes in the MTAS rate on the mobile and fixed voice services markets. In the absence of such a framework, regulation of MTAS rates risks compounding the structural problems in the fixed voice services market. MTAS is an essential input in the provision of FTM calls and lowering the MTAS rate reduces the cost of providing these calls. However, Telstra has not fully passed on previous mandated reductions in the MTAS rate to consumers. Between 2004 and the first quarter of 2013 VHA estimates the lack of FTM pass-through has led to \$1.4 billion in unrealised consumer benefits accruing to Telstra – this money should have stayed in the pockets of consumers rather than enriching one of Australia's most profitable companies. This lack of pass through of FTM prices has been a significant contributor to Australia's enduring flawed market structure, damaging competition in both the fixed and mobile markets. The ACCC must consider all options for addressing the market distortions caused by lack of FTM pass-through including: forbearance on further MTAS rate reductions; setting MTAS rates that are conditional on the level of FTM pass-through; or explicit retail price controls for FTM calls.

The role of the MTAS in the mobile services market (i.e., MTM) needs careful assessment. It is also important to recognise that the pricing of MTM MTAS does not have a significant impact in either MNO's business, or for its consumers. Generally traffic flows between MNO's are balanced; so the price of MTAS does not have an impact on the net costs to a MNO. With balanced calling patterns, the decline in revenue is offset by falls in the cost of terminating calls on other mobile networks. Therefore, the net impact on the recovery of efficient costs by the MNO is not directly impacted by the change in the MTAS. It is therefore inappropriate to attribute declines in the price of mobile calls to reductions in the MTAS. That said, we are of the view that MTM MTAS should continue to be part of the declaration as it establishes a worthwhile overarching framework for the regulation of MTAS.

Apart from variations to the MTAS declaration to address outdated references to legislation, VHA does not consider it should be varied in any other way. Specifically, VHA does not consider it necessary to extend the MTAS declaration to messaging services such as short messaging services (**SMS**) and multimedia messaging services (**MMS**). Nor does VHA consider it necessary to extend the MTAS declaration to expressly cover voice services which terminate on long term evolution (**LTE**) mobile networks



(**VoLTE**) or voice services over the national broadband network (**NBN**), as the current MTAS service description is technology-neutral and applies to voice services offered on any type of mobile network.

In short, the primary area of focus for the regulation of MTAS relates to Telstra's continuing market dominance in the fixed market. Until the MTAS price reductions of the past have actually flowed on to Telstra's retail prices for fixed-to-mobile calls (and therefore we see a demonstrable benefit to consumers) it is difficult to justify any action that increases their already inefficiently high margins. The \$1.4 billion of increased margin that Telstra has extracted over the last decade (to the detriment of other MNOs and consumers) has been a significant contributor to the inefficient market structure that continues to endure in Australia.

VHA's submissions on the various matters raised by the ACCC are set out below.



2. Relevance of the MTAS declaration

2.1 The MTAS declaration is still relevant

Despite the dramatic changes that have occurred in the mobile services market since the MTAS declaration was last considered by the ACCC, the fundamental economic rationale for declaration remains. That is, declaration promotes the LTIE through:

- promoting competition;
- promoting the achievement of any-to-any connectivity; and
- encouraging the efficient use of, and investment in, infrastructure.

Put simply, each MNO (including VHA) continues to have a monopoly over termination on its network. Without declaration, larger MNOs such as Telstra may refuse or constructively refuse to terminate calls on their networks from new entrants or existing, smaller MNOs. Horizontally-integrated operators who are both MNOs and fixed operators may also use their market power in the fixed-services market to raise the cost of fixed-to-mobile (**FTM**) calls to customers on their mobile competitors' networks.

This is problematic considering the lack of substitutes to the MTAS. While there has been an increase in the use of voice over internet protocol (**VoIP**) services in recent years, mobile VoIP usage remains small compared to conventional voice calls on a mobile network and cannot be considered a viable substitute at this stage. Furthermore, regardless of the technology that is utilised to initiate calls, MTAS is required for calls terminating on mobile voice networks. For these reasons, continuation of the MTAS declaration (when coupled with appropriate pricing principles) is likely to continue to promote competition in the mobile services market.

For similar reasons, the MTAS declaration has promoted and will continue to promote the achievement of any-to-any connectivity, including by ensuring that customers of each MNO will always be able to call customers of other MNOs. In so far as MNO-provided voice calls form a significant part of the traffic carried by mobile networks, declaration is likely to remain required for the promotion of any-to-any connectivity.

It follows from the competition analysis above that declaration is also more likely to promote efficient use of, and investment in, infrastructure by MNOs than the alternative (i.e., no declaration). By preventing MNOs from exploiting the monopoly characteristics of termination on their mobile networks, declaration is likely to promote allocative efficiency and ongoing investment in infrastructure, provided the correct regulatory settings are applied.

2.2 The MTAS declaration has promoted growth in the mobile services markets

Since 1997, when the MTAS was first declared, the mobile services market (comprising mobile-to-mobile (**MTM**) calls) has grown dramatically. As discussed in **section 2.1** above, declaration has promoted competition in the mobile services market, which is likely to have contributed to market expansion. That alone provides a compelling reason for retaining the declaration.

2.3 The increase in demand for data services

The ACCC has correctly identified that there has been a large increase in the consumption of mobile data in recent times. The growth in demand for data requires considerable investment in networks and infrastructure. However, efficient investments in infrastructure will not be achieved if MNOs are either over- or under-compensated for the use of that infrastructure for mobile



services. For that reason, the MTAS declaration continues to be relevant for ensuring the efficient use of, and investment in, infrastructure.

Furthermore, increased data usage does not make MTAS declaration redundant. As discussed in **section 2.1** above, mobile VoIP usage remains small compared to conventional voice calls on a mobile network and therefore cannot be considered a viable substitute. Furthermore, the MTAS remains relevant for VoIP calls which originate on fixed networks but terminate on a mobile voice network. This is in contrast to arrangements for voice calls carried entirely over IP (e.g., Skype-to-Skype calls), where the amount of data downloaded (data packets received) and data uploaded (data packets sent) is paid by each party (as part of a subscription for data services) regardless of who initiated the call – this is similar to the situation in some countries (e.g., USA or Hong Kong) where the receiving party pays to receive a mobile voice call.

2.4 The costs of regulation are low

When deciding whether or not to regulate the MTAS, the ACCC is required to weigh the cost of declaration against the benefits arising as a result of declaration. The benefits are discussed above and seem relatively uncontroversial. Generally speaking, the cost of MTAS declaration has also been relatively low. For example, there have been few disputes in relation to MTAS and (in comparison with fixed network declarations) a limited need for regulatory intervention, particularly in recent years. There is also no evidence to suggest a material increase in the costs associated with regulating the MTAS in recent times. Accordingly, VHA considers that the benefits of regulating the MTAS continue to outweigh the costs.

2.5 Should parts of the MTAS declaration be varied or extended?

As described in more detail in **section 3** below, VHA considers that the fundamental issue that the ACCC must address in relation to the MTAS declaration is assessing its impact on the markets in which the MTAS declaration operates. There are two distinct markets: the mobile services market and the fixed voice services market. There is no point in regulating the MTAS in a way that simply transfers revenue (however small) from a smaller non-integrated MNO to an integrated carrier such as Telstra, particularly in circumstances where it is already able to cross-subsidise its mobile operations with revenues obtained from its fixed line business. Furthermore, an assessment of whether MTAS declaration promotes the LTIE necessarily involves a consideration of its impact on both the mobile services market and the fixed voice services market.

VHA does not see a compelling case for the declaration of messaging services such as SMS and MMS as there is currently no evidence of a market failure in the retail market for these services. However the ACCC may wish to consider this further when it next considers declaration of the MTAS. This is discussed in more detail in **section 4** below.

As the current MTAS declaration service description is technology-neutral, VHA considers that the service description already covers VoLTE services. For this reason, VHA does not consider it necessary to extend the MTAS declaration in this respect. This is discussed in more detail in **section 5** below.

VHA also does not consider that the fundamental basis for MTAS declaration is significantly impacted by the rollout of the NBN. Although the NBN operates using IP protocols, much of the interconnection with MNOs occurs in a traditional switching environment, which is already provided for by the MTAS declaration. This is discussed in more detail in **section 6** below.

Finally, VHA agrees that the MTAS service description should be amended to update references from the “*Trade Practices Act 1975 (Cth)*” to the “*Competition and Consumer Act 2010 (Cth)*” as set out in **section 7** below.



3. Assessing the impact of MTAS declaration on the relevant markets

As outlined above, VHA considers that the fundamental issues that the ACCC must address in relation to the MTAS declaration are first, the identification of the relevant markets in which the MTAS declaration operates and has effect and second, an assessment of how to best promote the LTIE in each of these markets.

The ACCC must recognise that there are two distinct markets: the mobile services market and the fixed voice services market (in particular, the provision of FTM calls).

At this stage, VHA has not expressed a firm view as to whether the relevant market is the market for fixed voice services or a narrower market such as a market for FTM services. At various stages (and in differing contexts) the ACCC has considered both markets. For example, the Adam Internet Pty Ltd Statement of Issues¹ refers to a retail fixed voice services market, whereas the 2009 MTAS Declaration Inquiry Final Report² refers to a FTM services market. VHA considers that the market definition exercise should be approached with more discipline – for example, using the approach set out in the ACCC's merger guidelines – so that the market distortion, namely the failure of Telstra to pass through reductions in MTAS charges to consumers of FTM calls, can be properly analysed and appropriate remedies considered.³

The MTAS declaration has operated well in the mobile services market and has, as discussed in **section 2.1** above, promoted competition in that market. Each MNO is both an access seeker and an access provider of the MTAS for MTM calls. This means that each MNO has a level of countervailing market power and cash flows associated with the MTAS in the mobile market generally balance each other out. In circumstances where MTAS remains declared, small changes in the MTAS price would not have a significant impact on competition in the mobile services market.

However, there has been insufficient recognition of the consequences of requiring greater efficiency from mobile operators in the supply of the MTAS for an inherently inefficient fixed voice services market, specifically in relation to the supply of FTM calls. Mandated reductions in the MTAS rate over the past decade have led to excess and increasing margins on FTM calls which has benefited fixed network operators, particularly Telstra, and created a dynamic efficiency problem that has not been adequately recognised or addressed by the ACCC to date.

This submission is strengthened by the fact that there has been a lack of pass-through in the reductions of the MTAS price for customers of fixed voice services. Input costs for FTM service providers have decreased as the MTAS price has decreased. However, Telstra has, in real terms, failed to decrease the price of its FTM services. As a result, addressing monopoly power in one market through MTAS declaration and ongoing reductions in pricing has simply resulted in increased monopoly rents in another market, the fixed voice services market. In turn, this has meant that the main beneficiaries of reductions in MTAS pricing have not been consumers but rather the dominant fixed network operator.

¹ ACCC, *Statement of Issues, Telstra Corporation Limited - proposed acquisition of Adam Internet Pty Ltd*, 20 December 2012.

² ACCC, *Mobile Terminating Access Service – An ACCC Final Report of reviewing the declaration of the mobile terminating access service*, May 2009 (**2009 Declaration Inquiry Final Report**)

³ For instance, if the market definition is FTM calls then remedies such as pre-selection might be considered appropriate whereas this is less if the market definition is fixed voice services then such remedies are less likely.



- From an analysis of Telstra's publicly disclosed FTM data from the ACCC's *Imputation and non-price terms and conditions report*, VHA estimates that between 2004 and the first quarter of 2013 the unrealised consumer benefit from the lack of pass-through amounts to \$1.4 billion.
- Telstra's margin on residential FTM calls was 62% in the first quarter of 2013.⁴
- Telstra recently reported unit revenue from FTM calls of \$0.28 per minute compared to network unit costs of \$0.10 per minute – that is, its retail revenue is 280% of the cost of providing FTM calls.⁵
- Other fixed voice services have also been subject to price increases with Telstra recently increasing basic access charges by up to \$24 per year.⁶ Such price increases have occurred despite Telstra reporting EBITDA margins for PSTN services of 62% during the first half of its 2013 financial year.⁷

It is clear that Telstra has the ability to pass on more benefits to its customers, and that past reductions in MTAS prices have assisted the largest market participant far more than they have benefited consumers.

These issues must now be firmly and credibly addressed as part of the declaration process, especially considering there are mechanisms for the ACCC to do so. One option may be for the ACCC to address the problem at its source by imposing a requirement on MNOs, and particularly Telstra, to pass-through reductions in the MTAS price to customers of fixed-line services. There are other options including regulatory forbearance on further MTAS rate reductions or explicit retail price controls for FTM calls.

4. Declaration of SMS and MMS

VHA does not see a compelling case for extending the MTAS declaration to SMS and MMS. SMS termination is very different to call termination. In contrast to the role of fixed operators in the voice call market, the vast majority of interconnection in relation to SMS is between mobile operators. There is an inherent symmetry in SMS communications between their customers and less of the indirect network effects associated with voice calls. These features mean mobile operators have limited ability and very little incentive to exploit any market power associated with SMS termination.

VHA considers it to be unnecessary to declare SMS and MMS as:

- the markets in which SMS and MMS are supplied are a functioning effectively absent declaration of these services;

⁴ ACCC (2013), *Accounting separation of Telstra: Imputation testing and non-price terms and conditions report for the March quarter 2013*, July, <http://transition.accc.gov.au/content/item.phtml?itemId=1119980&nodeId=51b865093e30ec9a32346c9ced72202e&fn=Imputation%20and%20non-price%20terms%20and%20conditions%20report%20for%20March%202013%20Quarter%20-%204%20July%202013.pdf>, (Accessed 4 July 2013)

⁵ Telstra's TEM Public Report - FY13 H1 (available on the ACCC's website [A](#)).

⁶ ITWire (2013), 'Telstra hikes monthly access charges', 30 June, <http://www.itnews.com.au/News/348492,telstra-hikes-monthly-access-charges.aspx>, (Accessed 4 July 2013).

⁷ Telstra (2013), 'Telstra half-year results announcement 2013', 7 February, <http://www.telstra.com.au/abouttelstra/download/document/tls863-analyst-briefing-2013.pdf> (Accessed 4 July 2013).



- terminating access for SMS and MMS is supplied on a reciprocal basis. As a result, suppliers of SMS termination face countervailing buyer power when negotiating the terms of access;
- retail prices for SMS and MMS are low and decreasing; and
- there are effective substitutes in the form of over-the-top messaging applications (including email) that effectively constrain the SMS and MMS markets.

For those reasons it is difficult to see how declaration of SMS and MMS would materially promote the LTIE. The current treatment of SMS and MMS termination has not been an impediment to the efficient use of SMS and MMS retail services or investments in associated infrastructure. Moreover, the network demand from SMS and MMS is insignificant compared to voice and data services more generally and does not significantly affect the need for investments in new infrastructure and technology such as LTE.

Note that many of these points would also apply for MTM MTAS. But because it is hard to distinguish between MTAS that is used for FTM or MTM calling, for practical reason we believe that MTM MTAS should continue to be declared.

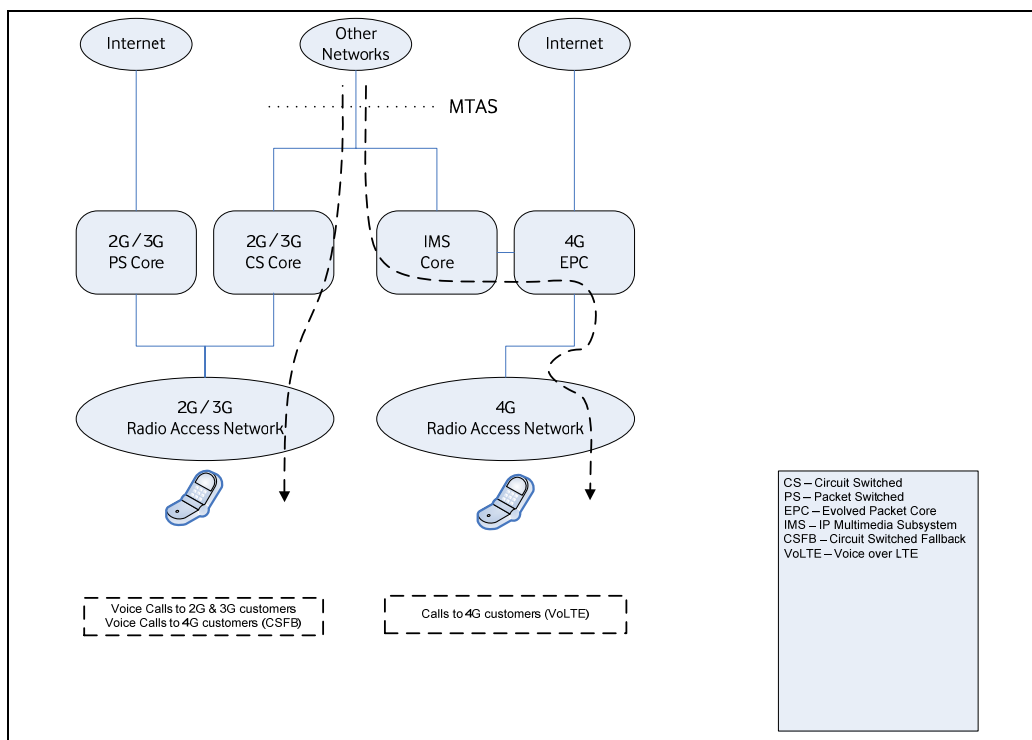
5. Declaration of voice services terminating on LTE networks

MNOs do not currently offer VoLTE services as the commercial ecosystem for this emerging technical standard is not yet sufficiently established. All voice services are currently carried over 2G and 3G networks using 2G and 3G circuit switched technology. This includes the provision of voice services to LTE customers.

However MNOs, including VHA, are currently investing in technology that could enable VoLTE to be provided to customers. VoLTE services may be launched during the term of the next declaration (assuming that the MTAS remains declared). Within a network, VoLTE calls are carried using Internet Protocol (IP) technology, and can be carried using either circuit switched technology or IP technology between networks. They will always be terminated using an IMS core (see **Figure 2**). For calls originating on other networks, MTAS will still be required regardless of which technology (including VoLTE) is used.



Figure 2: Technology schematic for the termination of voice calls on 2G, 3G & 4G networks



Source: VHA

In any event, given that the current service description for the MTAS is technology-neutral, it would likely apply to voice services provided over any type of mobile network, including VoLTE services. For that reason, as well as those set out above, VHA does not consider it necessary to vary the MTAS declaration to expressly apply to VoLTE services.

6. The effect of the NBN

VHA does not consider that the fundamental basis for MTAS declaration is significantly impacted by the rollout of the NBN. Voice calls originating on the NBN will have the same interconnect arrangements as other types of voice calls. That is, MTAS will still be required at the point of interconnect between the MNO and the NBN Retail Service Provider so that the mobile network can provide terminating access.

The current MTAS declaration service description is technology-neutral and applies to voice services offered on any type of mobile network, including voice calls originating on an IP-based network. VHA does not consider it necessary to vary the MTAS declaration to expressly apply to calls originating on the NBN.

7. Outdated references

As the ACCC identified in its discussion paper, VHA considers that the MTAS service description should be amended to update references throughout from the "*Trade Practices Act 1975 (Cth)*" to the "*Competition and Consumer Act 2010 (Cth)*".



8. Duration of the declaration

VHA considers that the duration of the declaration should align with the anticipated duration of the future MTAS final access determination (**FAD**) (assuming that the MTAS remains declared and an FAD is made). For this reason, the current MTAS declaration should be extended for a further three years, until June 2018, with a FAD implemented for an equivalent length of time. VHA considers a three year term appropriate as it provides MNOs and other access seekers with sufficient regulatory certainty to undertake investments, while at the same time recognising the rapid pace of change in the contemporary mobile environment (including moves towards VoLTE and VoIP) and the consequent need for the MTAS declaration to be reviewed more frequently.

9. Conclusion

VHA considers that there is clearly an ongoing role for MTAS declaration in its current form. The fundamental policy underpinnings for declaration remain: it has been in the LTIE and the benefits of declaration outweigh the costs. Furthermore, the service description is technology-neutral and, apart from minor amendments relating to outdated references to legislation, need not be varied at this stage.

However it is now imperative that, as part of this process, the ACCC recognise and address the extent to which the MTAS declaration has failed to sufficiently promote competition and efficiency in the fixed voice services market (and, in particular, the provision of FTM calls). That failure is not as a result of declaration itself, but rather as a result of the manner in which it has been applied. It is both necessary and open to the ACCC to impose requirements on MNOs, particularly Telstra, to pass-through reductions in the MTAS price to FTM calls so that *consumers* (and not the dominant Telco) are the beneficiaries of declaration.