

**VODAFONE SUBMISSION TO THE  
AUSTRALIAN CONSUMER AND  
COMPETITION COMMISSION**



**ACCC Discussion Paper: Proposed Variation to make  
the GSM Service Declarations Technology-Neutral**

**12 October 2001**

# 1. Introduction

- 1.1 Vodafone welcomes the opportunity to present its views to the Commission on the proposed variation of the GSM service declaration in order to include CDMA services.
- 1.2 Vodafone does not support a broadening of the scope of the service definition for this declared service. A broadening of the scope of the current regulation has the potential to have far reaching implications for the future regulation of mobile services in Australia. Our reasons for this include:
  - Our continuing view that the regulation of GSM termination is not warranted. Given its similar market characteristics, we have no reason to believe that our arguments against the regulation of the GSM service would not also apply for CDMA;
  - The fact that the regulation of GSM services was not required to pass the Long Term Interests of End Users (LTIE) test. We consider that it would not pass such a test if it was applied today. We consider that a LTIE test should be applied if the ACCC seeks to extend the current regulation to include CDMA services.
- 1.3 We provide further details on our views below.

## 2. The history of GSM termination regulation

- 2.1 It is worth examining the history of the GSM Access regulation. The regulation of the GSM termination service was deemed as part of the introduction of the new telecommunications legislation in 1997. Because of the nature of deemed services, the ACCC was not required to conduct a public inquiry and assess the service against the Long Term Interests of End Users (LTIE) Test.
- 2.2 The LTIE is a key hurdle that all services are required to pass before declaration can be applied. For example, the recently announced inquiry on the linesharing service requires the ACCC to conduct a complete LTIE test before the service can be declared.
- 2.3 While there has been a large amount of analysis conducted on the GSM termination service including considerable public consultation on proposed regulatory interventions to apply, all this work has been done in an environment where the service is already declared. It has not been done as a result of a objective study of whether such regulation is warranted because of proven market failure and evidence that such regulation would result in net long term benefits to end users.

### **3. The test for regulatory intervention**

- 3.1 The essential test for a regulator in deciding whether or not to intervene in a market is to assess whether a durable market failure exists and that there will be benefits to end-users of direct intervention. In essence, it is critical that a problem exists before deciding whether or not to apply regulation. Even where market failures exist, the regulator must be sure that intervention is likely to lead to net benefits to end-users.
- 3.2 These key tests are necessary to protect against unnecessary regulatory intervention. There are well acknowledged costs of regulatory intervention that need to be balanced against the potential benefits of such intervention. As highlighted by the Productivity Commission, the costs of regulatory intervention are potentially large and difficult to measure:

Apart from their obvious compliance costs, they can also produce their own set of inefficiencies because they involve the use of imperfect instruments devised under circumstances of asymmetric information and uncertainty by regulators. They impose rules on markets that can have chilling effects on entrepreneurship and innovation.

Further, regulators may be captured by various interests and have objectives of their own. .... And unlike the businesses being regulated, a regulator or competition body has more complex governance arrangements, and objective measurement of its success is difficult.<sup>1</sup>

- 3.3 If these costs were to be ignored, regulation could be easily justified across a broad range of competitive telecommunications services, even where such regulation was not warranted. Such action could be justified on the basis that if problems occurred in the future they could be more easily addressed if such regulation was in place. However, given the reality that regulatory intervention imposes significant costs, it is critical that intervention is tightly focused on areas where long-term problems exist and where intervention, properly applied, is likely to lead to more efficient outcomes in the long term.
- 3.4 Vodafone considers that if these tests were to be applied, it is not apparent that the regulation of CDMA services would be warranted. We discuss this in more detail below.

### **4. There is no evidence of a problem in the CDMA market that justifies intervention by the ACCC?**

- 4.1 The ACCC has produced no evidence to suggest that a durable market failure exists for the CDMA access service. A similar lack of evidence surrounds the regulatory approach for the GSM access service. Such evidence is a critical

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<sup>1</sup> Productivity Commission (2001) *Telecommunications Competition Regulation*, Draft Report, p. 2.42

element of the process that should be followed before regulatory intervention is introduced. Without such evidence, Vodafone considers that the ACCC risks imposing unwarranted and unnecessary regulation on CDMA services.

- 4.2 It also appears that there is little if any appetite within the industry for such regulation. We are not aware of any party that has argued in favour of the regulation of CDMA services on the basis of a market failure in that market. Vodafone and others noted during the ACCC's inquiry into the regulation of the GSM access service that applying such regulation potentially created competitive advantages for CDMA carriers due to the fact that these carriers will not be subject to direct regulatory oversight from the ACCC. However, at least in Vodafone's case, this argument was made to point out the need to conduct a 'first principles' assessment of the need for such regulation – not to argue that such regulation should be extended to CDMA services.
- 4.3 Given this, we would question the rationale for imposing regulation on CDMA services. Before regulation is considered there must be some evidence to suggest that there is a problem in the market that needs addressing. Without such evidence, it is difficult to justify the imposition of regulation. For instance, the absence of regulation (or the threat of regulation) does not appear to have resulted in different and higher termination rates for CDMA services compared to GSM rates. This would appear to be an important general test for whether regulation is warranted.
- 4.4 Vodafone considers that there is a better way to approach the issue. Rather than broadening the scope of regulation to capture 'close substitutes', there should be an analysis conducted on whether a market failure exists for these CDMA services. If such a market failure can be identified, then an analysis should be conducted to ascertain whether there would be net benefits to end users of applying regulation to this service.
- 4.5 If it is found that there is no justification for such regulation, Vodafone contends that this would call into question the need for the regulation of the GSM access service.

## **5. Competitive neutrality is not a sufficient reason to regulate CDMA services**

- 5.1 The CDMA service is a close substitute for the GSM service. For this reason, it is easy to understand the logic of including CDMA within the service definition of the current regulation in order to prevent competitive distortions in the marketplace. However, using such logic ignores the fact that the regulation of the original service (GSM) was not subject to a 'first principles' review to assess the need for regulation. Applying the principle of competitive neutrality to argue for a broadening of the scope of regulation may in fact lead to an unnecessary

expansion of regulation to areas where it was not justified in the first place, thus compounding the initial regulatory error.

- 5.2 Simply applying regulation to CDMA services on the basis that similar regulation applies to its close competitor – GSM – is insufficient and inappropriate. In Vodafone's view the ACCC should conduct a robust and objective LTIE analysis of the CDMA access service on its own merits. If the outcome of the LTIE analysis shows that regulation is not warranted – then Vodafone considers that it would be appropriate to apply a similar logic to GSM.
- 5.3 Our key point – and one we are keen to test in the future – is that the GSM termination service would not pass the LTIE test. Vodafone has outlined our reasons and a considerable amount of evidence to back up our claims on this in numerous submissions to the ACCC.
- 5.4 There are a number of reasons why the GSM service should not be subject to regulatory intervention. These include:
  - The difficulty and inappropriateness of trying to separate the termination service from the rest of the revenue sources that make up the mobile service;
  - The well acknowledged fiercely competitive nature of the mobile market and the lack of evidence that super-normal profits are being earned by mobile carriers;
  - A large and growing range of substitutes for the GSM termination service (for instance on-net mobile to mobile traffic, SMS and email) ; and
  - Evidence of significant and ongoing reductions on GSM termination rates that appear to have had no impact on fixed-to-mobile retail rates.

## **6. Other issues: originating access**

- 6.1 The originating access service was declared as part of the general declaration of GSM access service. However, as Vodafone has outlined in previous submissions to the ACCC, we do not consider that such a service exists.
- 6.2 We note that the concept of 'originating access' has been included in the proposed service definition for the new declaration of mobile access services (see page 40 of the discussion paper). Vodafone disagrees with the Commission's analysis of the mobile origination service (as outlined on page 11 of the discussion paper).
- 6.3 In relation to the GSM service, Vodafone does not consider that a fixed line carrier providing 1800 or 13/1300 inbound services purchases GSM originating

access services to supply these services to mobile subscribers. The end to end call service from the mobile to the inbound service is supplied to the mobile subscriber by the mobile carrier. It is the mobile carrier who sets the tariff for the call, and bills the subscriber for the call.

- 6.4 It is true to say that without the origination service the service cannot be supplied. It is equally true to say that without the inbound segment of the call, the end to end service cannot be supplied. There is an equal dependency between the mobile provider and the inbound service provider to come to an arrangement which makes supply of the service viable and attractive.
- 6.5 This particular call case is much more akin to the mobile to mobile call case. Both parties have commercial imperatives to reach agreement. Regulatory intervention is definitely not required.
- 6.6 For this reason, Vodafone considers that this service should be undeclared.
- 6.7 We also note that since the service has been declared there have been no originating access services offered in the market place. Technical arguments aside, we consider that this market test should be reason enough for the originating access service to be undeclared.
- 6.8 In the event that the ACCC decides to continue with the current service definition, we note an error in the draft service declaration. It appears that this has been carried over from the GSM service declaration, where there is a similar error.
- 6.9 In particular, the proposed service declaration of GSM and CDMA originating access service on page 40 of the discussion paper has the following as one of the elements of the service description:

a) Access via a AS number ranges required to achieve the objective of any-to-any connectivity unless the AP has not sought or is not seeking terminating access to the end- customers in question

- 6.10 The 'nots' in this section confuse the definition, making it unworkable in practice. It is nonsensical because if the access seeker has requested terminating access, then there would be no need to apply regulation on the originating access service, as none would exist by definition. The section should be redrafted as follows:

a) Access via a AS number ranges required to achieve the objective of any-to-any connectivity unless the AP has sought or is seeking terminating access to the end-customers in question

## 7. Summary

- 7.1 Direct regulatory intervention in a market is a serious step for a regulator to take especially when such intervention is intended to influence prices that have been struck through commercial negotiation. This is because regulatory intervention can have a number of significant costs, many of which are indirect in nature. It is imperative that such action is underpinned by evidence that current market outcomes are inefficient and will continue to be so without regulation. Without such tests, there are risks that competitive markets become unnecessarily regulated and incentives to invest and innovate are adversely impacted.
- 7.2 The risks of regulatory overreach are evidenced by the current ACCC inquiry into whether to broaden the scope of GSM access regulation to the close substitute service of CDMA. There is no evidence that a market failure exists in the CDMA market. Regulation should not be extended.
- 7.3 An alternative would be to conduct a review of whether such a market failure exists for the CDMA access service. Vodafone considers that the CDMA access service would not pass the LTIE test. This view is based on our long-standing view that if a similar review was conducted regarding the GSM access service that it would result in a similar outcome.