

Telecoms conference report

*A report of proceedings of the **Telecommunications - Deregulation... Privatisation... Reform Conference**, held by AIC Conferences in Sydney, 18 and 19 July*

Competition US style

Nicholas Johnson, Professor of Communications at the University of Iowa, was appointed as a Commissioner of the Federal Communications Commission in 1965 to regulate the AT & T private monopoly, occupying the position for seven years.

In response to his given topic, 'What Australia can learn from the USA', Professor Johnson felt the most he could offer was analogies and warnings: there were no direct parallels, since the US has never had a state monopoly to privatise. It did, however, face the introduction of competition with the forced divestiture in 1982 of AT&T's local telephone monopolies, following Justice Greene's judgment in an anti-trust suit brought by the Justice Department. The following developments have occurred since the divestiture:

- regarding employment matters, AT&T has reduced its staff from 950,000 to about 300,000, but the industry overall has as many employees today as AT&T did in 1981. This represents an overall reduction in the workforce, but not as drastic as the redundancies made it appear.
- investors have consistently doubled their money every five years.
- executive salaries have risen so markedly that the US now has the greatest disparity between the salaries of telcos' CEOs and employees of any of the 17 industrialised nations.
- regarding price, business customers are better off, with average call charges having decreased by 50% (largely because they are heavy users of long distance); residential charges have risen by 56%. It is

difficult to ascertain the extent to which price reductions are attributable to competition rather than technological change, since long distance costs have been consistently declining at the rate of 4% per year for the past 80 years.

- universal service penetration has increased from the low 90% range to the high 90% range, although penetration for the poorest Americans falls within a 70-80% range.
- quality of service has improved in the areas of sound quality and call completion rates; however, there has been an increase in massive system 'outages' which has seen networks servicing airports, stock exchanges, the eastern US corridor and the city of Chicago crash.

Professor Johnson's warning lay in the area of civil rights. He asserted that the convergence of content and carriage ownership looms as the 'greatest threat to American democracy this century'. In the US, the First Amendment (the right to freedom of expression) has been interpreted as including the right of media corporations to censor (refuse to carry) content over their networks. With their recent foray into information services, telcos may fall within this umbrella, regardless of access regimes. The only uncensored communications media available to all may soon be the postal service - although this is only a point to point service.

On balance, it was not clear whether the US is better or worse off as a result of divestiture and competition. It depends who you are: the poor and working class have borne the brunt of change badly, while large corporations and the rich are better off. Professor Johnson advised the

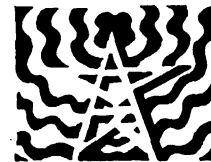
audience to listen to independent experts and, to ensure that his point was not missed, quoted approvingly from telecommunications journalist Stewart Fist: 'The [public] network is too central to the welfare of the society to risk allowing a commercial enterprise to have power to restrict its availability or use'.

The Democrats' position

Senator Cheryl Kerot commenced her address by asserting the ideological, rather than economic, motivation for the proposed Telstra sale. In her opinion, the Government could not devise better ways of increasing its revenue base and refused to recognise the economic contribution made by the public sector.

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She then outlined the primary economic notions underpinning the Democrats' opposition to the proposed sale of Telstra. First, privatisation was not economically justifiable: although \$7 billion of the expected \$8 billion received from the partial sale would be used to retire debt, the value of interest savings on the debt may not exceed revenue foregone. Further, the total value has been estimated by some academics to be in excess of \$50 billion - more than double the Government's valuation. To compound this, Telstra's value



was being further underpriced in an effort to ensure adequate investor demand for the float and quick revenue for the Government. This was consistent with the recent history of the undervaluation of privatised utilities in Australia - Qantas, CBA and the Commonwealth Serum Laboratories being cases in point. As a result, incumbent shareholders stand to gain at the expense of citizens.

Second, improvements in efficiency are not dependent on privatisation. The state-owned telcos of Iceland and Switzerland had the world's lowest prices and costs respectively. Senator Kernot acknowledged the need for some further staff cuts, but rejected an 'open-ended' approach to the task.

The Asian perspective

Diana Sharpe, a partner with law firm Gillet Sharpe, departed from her prepared speech to address a topic discussed by an earlier speaker, Leigh Baker of Oracle Corporation, on the experience of privatisation in Asia. While Mr Baker did not wish to draw conclusions for the Australian context, Ms Sharpe wished to address the differing cultural and developmental imperatives prevailing in Asian countries that made comparisons with the Australian situation inappropriate. For a variety of ideological, cultural and developmental reasons, Asian nations had a more opaque distinction between 'public' and 'private' sectors than Western industrialised nations. In Asian countries, privatisation was less an act of transfer of ownership of an existing infrastructure, but a re-definition of the role of the state and commercial enterprises in the development of the nation-state.

ACCC's new role

ACCC Commissioner David Lieberman's address was one of the

conference's more eagerly awaited. However, it disappointed those attendees hoping that the ACCC, which is soon to assume AUSTEL's regulatory functions, would adopt a more robust and interventionist approach to regulation than its predecessor.

In outlining the provisions of the Trade Practices Amendment (Telecommunications) Bill 1996, Mr Lieberman indicated his personal expectation that the new Competition Directions and Interim Competition Directions, which may be made where the ACCC is satisfied that a carrier or carriage service provider has engaged in anti-competitive conduct, would be rarely used. He also expected that the Tariff Filing Directions would only be used 'sparingly', stating that pricing was fundamental to competition and that tariff filings could have an anti-competitive effect by creating price ceilings.

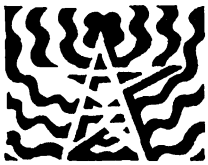
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Several conference participants, including ATUG's Barney Blundell, expressed dismay at this approach. They had considered AUSTEL's stance inadequate and were expecting the ACCC to be more aggressive in regulatory enforcement. Instead, the ACCC now appeared to be backing even further away from intervention. In reply, Mr Lieberman noted that he was speaking in a personal capacity only (not having yet discussed the issue with other ACCC members), but maintained that his duty was to apply the new law: lighter touch regulation being its intention.

Industry specific regulation

Professor Brent Fisse, a partner of law firm Gilbert & Tobin, declared his interest as legal counsel for Optus before arguing the necessity of industry specific regulation of the telecommunications industry. Stating that the Hilmer Report recognised the necessity of separate regulation in some industries, Professor Fisse argued that general competition laws would be inadequate to deliver workable competition in an environment dominated by an entrenched monopolistic structure. The particular issues of access and interconnection and, to a lesser extent, the extent and significance of vertical integration in the industry, also presented problems unique to the telecommunications industry that demanded specific regulatory solutions.

Professor Fisse challenged Professor Henry Ergas' comparative analysis of the regulatory approaches taken in New Zealand and Australia. First, Ergas estimated the costs of regulation in New Zealand to be approximately 20% of those in Australia. Fisse contested that no adjustment was made for population sizes, nor was an attempt made to quantify the costs of the New Zealand government's 'informal, but very active' role in regulating the industry. Second, Ergas argued that 'total factor productivity' in the New Zealand industry exceeded that in Australia. However, Fisse noted that, unlike Australia, New Zealand had privatised its carrier prior to the introduction of competition, and that Ergas' analysis did not differentiate between the respective efficiency gains of competition and privatisation. While Ergas criticised the 'heavy handed approach' of Australian regulation, Fisse questioned the hidden costs to the industry and consumers of not opting for the transparency of proper



administrative and judicial review processes.

Selling Telstra

An investment panel, comprising Macquarie Underwriting Limited's Belinda Hutchinson, ANZ Bank's Bob Peters and Hambros Australia's Chris Beare, was in broad agreement regarding financial matters relevant to the partial sale of Telstra.

There was no doubt that telcos were an attractive investment, offering substantially better yield and growth than other industries. The real issue was whether Telstra was a more attractive investment than other telcos in Italy, Germany and France that may also be seeking similar injections of equity around the time Telstra is hoped to be floated. Foreign investment would come primarily from financial investors, rather than international telcos, who would not invest in a company they could not control (individual foreign shareholdings in the one-third sale being restricted to 1.6% of overall equity).

Overall, Telstra is a very attractive investment, offering high profits, an extremely strong balance sheet and capacity to improve through efficiency gains. Although present inefficiencies lowered Telstra's value, the utility's capacity for significant productivity improvements may actually attract investors seeking windfall profits from an undervalued company. Investors would be seeking 'certainty', in the form of knowledge of the post 1997 regulatory regime (including the nature and extent of universal service obligations).

Although it would have been better for Telstra to have been floated a year ago, it remains eminently floatable - and the sooner the better.

Commenting from the floor, 'independent media analyst' Peter Cox played devil's advocate, raising some less attractive issues related to Telstra's profitability. Its international expansion has been 'a miserable failure', it is presently in the midst of an extremely expensive broadband rollout of questionable profitability, its FMO (future mode of operation) upgrade is behind schedule and, in the GSM mobile market, it will face a greater number of competitors when the network changes from analogue to digital. The panel declined to engage with Mr Cox on these matters.

USO

ATUG's Barney Blundell supported the Government's policy, outlined in *Better Communications*, to tender out the USO for particular geographical areas. The best approach, he argued, was to have Telstra nominate whether an area is a USO area, using criteria suggested in the BTCE *Communications Futures Project*. If so nominated, the area would be put up for tender, with the winning tenderer taking over the area, including equipment, for a period of 10 years. It would have to hand the area back after this time if it did not perform adequately. He expected that Telstra would win any such tender 90% of the time. He outlined a range of funding options, but expressed personal preference for a tax levied on all users at the retail billing level.

Telstra's Dennis Hambleton complained that the terms of reference for the Standard Telephone Service Review Group, announced recently by Senator Alston, appeared symptomatic of the usual policy approaches to USO in its 'blind commitment' to a higher data speed. 99% of the time, he said, it was impossible to discern

the difference between 64 kbps and 9.6 kbps because of limits on the service provider component. What was required was a qualitative assessment of the needs of specific consumer groups. For example, Telstra's polling amongst rural groups indicated that the main reason for their desire for higher speed data services was to reduce the time spent - and therefore the cost of - sending facsimiles. This goal could be achieved more simply and cheaply by the introduction of a special rural tariff. A better approach to resolving issues of consumer access was, therefore, the development of needs based selection criteria for specific user groups.

Helen Campbell, of the Consumers Telecommunication Network (CTN), stated that CTN was not, in principle, opposed to USO tendering, but asserted that tenderers must be subject to prior 'quality of service' checks, and successful tenderers must be subject to continual monitoring over the course of the tender contract. The main point of her paper, however, was to argue that debates on universal access focus too much on geographic, rather than other principles such as economic or equitable access. Presently, a number of marginalised groups, including the homeless, the elderly and the disabled, were prevented from enjoying the full benefits of societal participation that is, or should be, a right of citizenship.

Commenting on the USO issue from another panel, freelance journalist Stewart Fist quoted 'Metcalf's law' in arguing that the value of a network to society as a whole increases geometrically with its size. It was therefore myopic to regard USO purely as a cross-subsidisation process, the benefits of which only the immediately subsidised will enjoy. □

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