The Vision thing

*To mark its absorption into the Optus group, **CU** undertakes a two-part overview of significant events in the life of Optus Vision. The first part details its birth into a startled and unwilling regulatory firmament...*

It is impossible for anyone not privy to dealings within the Optus Vision boardroom and amongst its management, shareholders and financiers to confidently analyse the history of the company.

With a business plan involving massive capital investment and putatively reliant on revenues from pay television, telephony and 'interactive' operations – of which only one constituted an established industry in Australia – it was evident from the outset that investors would need to be committed to (and often reminded of) the long term view: that in an age of business and technological convergence, ownership of a national broadband telecommunications network would assure Optus' success. The alternative was to be forever a tenant – protected or otherwise – on Telstra's proprietary network.

However, the apparent clarity of this strategic path must have appeared somewhat more opaque for investors. For pay television services, forecasted demand was highly speculative, programming costs were unknown and the competitive landscape was uncertain. The telephony business was dependant on the successful deployment of a cutting-edge network that would be required to interface with Telstra's and support a billing system that could adequately exploit the information it hoped to hive from Telstra. As investors would have known, any other services proposed to be delivered over the network were more the subject of a mission statement than a business plan. Added to this was the rapidly evolving nature of telecommunications itself: no-one was sure whether technological change might erode the advantages traditionally enjoyed by fixed network owners, and if so, to what extent. However, with success in the telecommunications industry – even for former monopolists – now requiring boldness, adaptability and large slabs of risk capital, Optus acted to remove the ceiling that would otherwise have limited its potential in the Australian market.

Optus' motives

Optus' commercial motives were reasonably straightforward. It regarded itself as at a perennial competitive disadvantage for as long as it was required to use Telstra's infrastructure to access the 'customer access network' (CAN), the web of telephone lines between customers' premises and the first local telephone exchange. While it was a relatively inexpensive matter to install its own links on high capacity trunk routes, the installation of a rival CAN was extremely expensive and, it was generally thought, commercially unviable. On the other hand, continued reliance on interconnection to Telstra's network constituted a galling prospect. Several factors loomed large. First, around half of Optus' costs would continue to be paid to its major rival in interconnection fees, and Optus would continue to be beholden to Telstra's priorities for infrastructure development. By building its own network, Optus could avoid these charges, set its own priorities and, if it wished, attract revenue by providing access to others.

Second, Optus would never be able to offer its customers a single telephone bill while it was unable to offer local telephony. This comprised an impediment to success, particularly in the residential market, whose importance only became apparent to Optus after it had entered the market. It soon realised, however, that the 'single bill' issue formed a triumvirate of consumer-sensitive network issues, alongside those of preselection and number portability.

Third, despite the erosion of its monopoly, Telstra would continue to receive all customer information so long as calls were carried through its exchanges. However, if Optus were able to build its own CAN and attract customers away from Telstra, Telstra would lose its control of information about these customers forever and Optus could make inroads into the former monopolist's 'information asymmetry'. Such information is extremely valuable and, arguable, critical to a service provider's success. Amongst other things, it enabled Telstra to track the consumption patterns of its customers, along with everyone else's. It enabled it to strategically market products and services, monitor the progress of marketing campaigns, more accurately cost services and thereby make informed predictions about profit, and calculate the market shares of all carriers and service providers using its network to carry calls. Optus had frequently complained to regulators that Telstra and the federal government knew its market share but Optus itself could only predict it. Moreover, such information is also valuable for those wishing to 'data mine'. While privacy laws could purport to restrict a carrier's such use of this information, it would always remain available to those its major investors entitled to board seats. Given that a number of board seats of Australian telecommunications are, or will be, occupied by foreign telecommunications companies, whose own domestic strategies would be greatly assisted by such information, the accumulation of sizeable information banks contribute significantly to a carrier's value.

The open access dilemma

Although the consortium that ultimately invested in Optus' pay television/local telephony venture was to be distinguished from the other operations of the Optus group, the Optus Vision corporate entity was conceived as a vehicle whereby the Optus group sought to roll out a public broadband network without having to grant interconnection and access to other carriers and service providers, pursuant to the obligations incumbent on general carrier networks under the *Telecommunications Act 1991* (1991 Act).

Under the 1991 Act, the government intended that the 'reserved rights' of general carriers be balanced by attendant obligations, amongst these the obligation to provide interconnection to other carriers in order to achieve the goal of 'any-to -any connectivity' and to stimulate competition in telecommunications services and facilities. Section 131 of the 1991 Act obliged a carrier to permit any other carrier to interconnect to its network if reasonably requested to do so. This provision was primarily directed at Telstra, the former monopolist with the only public network at the time of the 1991 Act's inception. Section 234 granted more limited access rights to providers of 'eligible services' (that is, the 'service providers' category within the meaning of the 1991 Act).

These obligations would generally have required Optus to grant open access at near cost to any other carrier wishing to access this network, and raised problems for Optus, which was unwilling to build a broadband network only to have its competitive advantage eroded by being having its rivals access the resource on a near-cost basis and being itself unable to fully exploit its economies of scope and scale by exclusively providing its own services over its infrastructure.

The loophole

Optus resolved this problem by exploiting a loophole in the 1991 Act. The loophole was created by the confluence of two legal implications: first, while non-carriers were prevented from building a network, they were not prevented from owning one; second, while carriers were subject to the access and interconnection obligations contained in the 1991 Act, non-carriers apparently were not. Optus therefore devised a strategy whereby a non-carrier would engage a carrier to build a public network on its behalf. The carrier would have no power to grant access to a network it did not own, while the owner, a non-carrier, would be free of the 1991 Act's carrier obligations. Optus therefore created a new corporate entity, Optus Vision , which would own a new broadband network. Optus Vision then engaged Optus Networks Pty Limited, the holder of the Optus group's general carrier licence, to exploit its statutory power to 'install and maintain' a public network on its behalf. Optus Networks would then lease from Optus Vision only the capacity it required for its own telephony operations. Capacity for pay television operations was leased by Optus Vision to Multicom Pty Limited, another Optus entity.

Carrier Associates Direction

However, Optus Vision was not completely off the hook, because it still constituted a 'service provider' under the 1991 Act and could therefore be subject to regulatory control. In particular, the Minister was reserved the right to instruct the regulator AUSTEL (the ACA's predecessor) to issue binding determinations for any relevant class of service provider.

The government reacted angrily to Optus' announcement, as its planned closed network ran contrary to the government's regulatory policy of open access – a policy that had enabled Optus to enter the Australian market. The Minister, Michael Lee, announced that he would direct AUSTEL to issue a service provider licence – the 'Carrier Associates Direction' – applying to companies in which one of the general carriers had an interest, and which obliged carrier associates (Optus Vision, and later, Telstra's equivalent vehicle, Telstra Multimedia) to provide access and interconnection to their networks as if it they were carrier networks.

Optus maintained the position that sustainable competition in telecommunications required facilities-based, not merely services-based, competition, which would not be economically viable to build if it were required to provide access to all-comers. It proposed instead the creation of 'regional monopolies', Australia would be broken up into geographical sectors, with Telstra and Optus being exclusive rights to install cable in discrete markets. The government rejected this proposal.

Finally, following a stand-off over the latter part of 1994, an acceptable compromise was reached which effectively granted Optus a closed network while saving face for the government. Optus was not required to grant access for pay television services until 1 July 1997, or possibly 1 July 1999. Moreover, Optus Vision was not required to grant access to a competitor unless sufficient capacity was available or if there were technological limits to carrying the service. More importantly, it was able to charge commercial rates for access rather than a set cost-based interconnect fee. This effectively enabled Optus Vision to exclude third party access to the network.

The next issue of CU outlines Optus' shareholding, programming and associated financial struggles...and competition from Telstra