Universal service: still thinking

The federal government held a two-day event in Canberra in November to discuss key issues in rural and regional communications, including one of its biggest on-going telecommunications policy quandaries: what to do about universal service arrangements. Jock Given reports.

The waves from Telstra's $1.8 billion universal service net cost claim last year are still crashing ashore.

At a seminar in December 1998, the federal government set out an agenda for rethinking universal service. A year later, Telstra is still the sole universal service provider and the annual cost of universal service shared amongst the carriers hasn't changed.

The Government has indicated that a decision on new universal service arrangements is expected "in early 2000" and that "[a]ny new arrangements will commence on 1 July 2000 and apply for the financial years 2000/01 on".

In Canberra on 24-25 November, the Department of Communications, Information Technology and the Arts ran a conference which addressed possible new arrangements for universal service and reviewed the various funding programs established with monies from the sale of Telstra: "Networking the Nation" and the various initiatives being supported through the "social bonus" funds .

With universal service, the Government has got two parallel processes underway. It's trying to work out what the net universal service cost should be for the assessment periods already passed or underway (1998/99 and 1999/2000) and then it's trying to work out whether there's a better way of organising the whole universal service scheme.

Today's USO Scheme

Legislation passed earlier this year fixed the net universal cost for 1997/98 (the year for which Telstra submitted its monster $1.8 billion claim) at $253.32 million. It also fixed the cost for the next two years at that figure plus inflation. But it gave the Minister the power to determine an alternate amount. Telstra has asked the Minister to do so, using the ACA's estimate of the 1997/98 amount as the starting point.

The ACA assessed the net universal service cost for 1997/98 at $548 million: less than a third of Telstra's estimate but more than double the figure for the previous year. However, the Parliament had already passed legislation capping the figure at $253.32 million.

The Government has asked for four more reports from the ACA to help it in its consideration of the 1998/99 and 1999/2000 amounts.

The new reports, to be submitted by mid-January 2000, will provide an estimate of Telstra's net universal service cost (including estimates of the "forward-looking technology mix and the cost of the technology" which Telstra has needed and will need to use to fulfil its universal service obligations in 1998/99 and 1999/2000 and an estimate of Telstra's Weighted Average Cost of Capital). They'll also provide an estimate of the benefits Telstra gains from being the universal service provider.

The benefits of universal service

This is a significant feature which has not been examined in any detail in Australia before. The ACA has commissioned international telecommunications consultancy, Ovum, to undertake this work. Former Telecom regulatory executive, Jim Holmes, who runs Ovum's Australian operations, is doing it.

It's significant because it potentially provides another "big figure" to offset the net cost determined by the ACA, and thus reduce the amounts contributed by non-Telstra carriers. To date, the debate about Telstra's cost claim and the ACA's assessment of it have focused on how to accurately measure the costs of the uneconomic services Telstra is obliged to provide. What hasn't been explored is whether this figure is an accurate measure of the real cost to Telstra.

Most businesses provide some uneconomic services. They spend money tendering for jobs they don't get. They provide cheap rates or special deals ("loss leaders") for important customers or high profile activities. The question for Ovum, the ACA, the Government and the industry is whether Telstra would continue to provide any of these "uneconomic" services for its own commercial reasons if it were not required to do so by legislation. It's hard to see why it should be subsidised by other players in the industry to provide services which it would choose to provide anyway.

A discussion paper has been published, describing the areas where intangible benefits might accrue to Telstra or any other universal service provider. These include life cycle effects, ubiquity, brand enhancement and corporate reputation, payphone advertising, volume discounts and non-USO services.

Life cycle effects may accrue from serving unprofitable areas which become profitable over time. An area which loses money now may make money in the future, and being in there first as the universal service provider may give a company a head start in hanging on to, and winning, customers.

Ubiquity is the benefit of having an overall presence through being the universal service provider, which will encourage loyalty when customers move to other areas.

Brand enhancement and corporate reputation is the benefit which may accrue from being positively regarded as a result of being the universal service provider. Some of Telstra's "Making Life Easier" advertisements work on this theme. The company wants to be seen as the one that's always there for you, wherever you are and however challenging your needs are to satisfy. It's unlikely to achieve that reputation if it only serves immediately profitable customers. The difficult conceptual question is whether these kinds of benefits accrue as a result of the regulatory intervention of anointing Telstra as the universal service provider(in which case they might appropriately be offset against the cost of providing the services) or as a result of Telstra's own commercial activities.

Payphone advertising is the benefit which accrues from having payphones for corporate identification and advertising in uneconomic locations.

Volume discounts are the additional increment of discount on purchases for Telstra's total operations that might be attributed to the volumes purchased for universal service operations. Being the universal service provider makes Telstra bigger, and being bigger allows it to buy more cheaply from its suppliers.

Non-USO services - benefits might accrue from being able to supply additional services like customer premises equipment, wake-up and reminder calls and Messagebank, along with more sophisticated services like ISDN, frame relay and ATM services, using the infrastructure put in place as a result of the universal service operations.

This is complicated and difficult analytical territory, and theACA and their consultant has got very limited time to think it all through.

Post-2000 universal service arrangements

Then there's the really big one - have we got the whole universal service model wrong? Some participants at the government's Canberra event thought so.

The government has summarised the available options into three broad areas: industry funding, budget funding and consumer funding.

Industry funding is the way it works now. The costs of the universal service obligation are met by all licensed carriers in proportion to their share of total industry revenue. A number of modifications might be made to this scheme. Carriage service providers could be levied as well as carriers: this model was rejected when the current scheme was established because it was felt carriage service providers effectively paid anyway through the interconnection charges they pay to the carriers. Some carriers, most likely those earning revenues below a certain level, could be excluded from the liability. Or all carriers other than the one providing the services could be excluded from the liability: this was the model which effectively existed before 1991, where cross-subsidies within Telecom paid for all the uneconomic services.

Budget funding is the way many "community service obligations" are funded. The government makes a decision each year to pay a certain amount of money to make certain things happen. Beneficiaries of universal service arrangements worry that this would make the arrangements more vulnerable. And no-one seriously expects the government to welcome the prospect of even the current $253 million net cost being added to government expenditure and thus deducted from the treasured surplus.

Consumer funding would see an additional item added to individual phone bills, making transparent to consumers the cost of making the services they receive "reasonably accessible to all Australians on an equitable basis, wherever they reside or carry on business". A Medicare Levy, a Timor Tax, a GST, a USO levy. And perhaps an Olympics "Share the Spirit" leveller.

While industry funding seems most likely to stay, with some form of tendering introduced at least on a pilot basis to bring contestability to some of the markets currently treated as net cost areas, it is significant that the government has spent so much money in recent years on specific initiatives in rural and regional communications. The idea of a fund collected through a simple tax on telecommunications revenue, equal to around the current ACA estimate of the net universal service cost (say $550 million), and then allocated each year through a structured program of funding decisions, is not too far away from what has happened in practice, with the establishment of Networking the Nation and the "Social Bonus" initiatives.

While there are significant problems with all the available options, the government is under heavy pressure to do something to straighten out this on-going saga.

Telstra has got its hand out, demanding that its major share-holder produce a regulatory decision which delivers to the company some much larger cheques from Cable and Wireless Optus, AAPT and others. Those competitors are battling hard to keep the current universal service cost right where it is.