

COMMSDAY SPEECH 13 OCTOBER 2015

Now is a very good time to take stock of the Australian communications industry and how it is governed. That's going to be my theme this morning and I hope it will be the main topic of conversation for the duration of this Congress.

The reasons for it being a good time for reflection are easy to see.

They start with recent changes to the leadership of the Federal Government, including the elevation of a former Communications Minister to the Prime-Ministership, the appointment of a new Communications Minister, an enlargement of the Department of Communications, and several reviews of significant areas of communications policy either underway or completed.

If you are concerned to ensure a greater focus on the long-term competitive structure of our sector, these changes represent opportunities to shift agendas, to elevate discussion to the highest levels of government and think beyond debates around NBN rollout methodologies.

While the last objective has been talked about for a while it has not happened. We like to put things off.

Recently, the Chairman of the Productivity Commission, Peter Harris, delivered a keynote speech at the Australia Competition Policy Summit, lamenting the lack of progress in responding to the Harper Review.

Harris began by reminding us what Bruce Billson, then Minister responsible for competition matters, had said when launching the Harper Review.

"...this Review is long overdue and will help identify microeconomic reforms and long-term improvements to build strong foundations for a more productive and competitive 21st century Australian economy".

Harris' starting point was that most of the response to Harper was dominated by disproportionate focus on what to do with Section 46 of the Competition and Consumer Act, which he argues is *"...probably more a totem for how far we have fallen off the pace in national economic reform"*.

Harris' argument applies to the communications sector as much as any other, although he did not focus directly on communications policy or regulation in his speech.

A sector that has been covered by more reviews than just Harper should be near the top of the areas in need of a reinvigorated reform agenda. If you are in any doubt, consider the vital role this sector plays managing infrastructure and distributing information needed for a modern economy.

Telecommunications is one of the most significant areas of the economy to attract specific purpose economic regulation.

This is something purist economists often resist because sectoral economic regulation risks entrenching intervention in markets, risks stakeholder capture and can lead to rent-seeking.

These are all valid concerns. Sectoral regulation is often determined with an eye to accommodating commercial interests and the state of technology at a given point in time rather than rigorously reviewed outcome-based objectives or very broad concepts of consumer interest.

If one accepts that proposition, the general application of economy-wide competition policy should be the ideal. Any accompanying sectoral regulation should be seen as something that needs to be designed to wither away eventually once its founding purpose has been achieved.

In essence; in regulating we accept the Augustine notion: *“Oh Lord make me pure, but not just yet”*. (But definitely one day soon!)

Likewise, it should be seen as best practice to separate policy-making from regulation, and both from government run or financed commercial activities.

This is something all governments struggle with; particularly in the Australian telecommunications sector. Nor do they make it easy for themselves.

It's very hard to manage clean outcomes when you have placed execution of a major public policy initiative in the hands of a GBE, such as NBNCo, which also has a mandate to deliver that initiative against a sustainable business plan.

That's not just a challenge for the GBE, it's a challenge for a GBE's shareholders within government.

There was long a question mark over the policy role of the predecessor departments of the present Department of Communications and the Arts in a competitive market while they remained principal shareholders for Telstra and its predecessors.

This was compounded by the protracted process of corporatisation, then three-stage privatisation. Yet, having rid the Department's predecessors of this, we managed to reapply the shackles by making the present Department a shareholder of NBNCo.

In saying this, however, I am not foreshadowing a revisionist argument against the idea of having an NBN. But we do need to begin thinking about its longer term governance arrangements.

This includes providing for how it might be sold once the purpose of having a government funded and operated NBN is fulfilled.

Vertigan touched on the latter task by advocating greater separation of functional business lines within NBNCo.

It is pleasing to see this has been heeded, albeit with the implicit assumption that overlapping network infrastructure technologies will be a foundation for competitive enterprises.

Similarly, careful thought needs to be given to how NBNCo might be structured and priced for sale if the day eventually comes; as it should, that the organisation achieves its primary purpose of rolling out effective national broadband network infrastructure.

Too often in Australia there has been a temptation to structure and price bottleneck public infrastructure for sale to maximise short-term capital return at the expense of wider economic priorities.

Privatisations should also be designed to deliver other outcomes; such as enabling competition, delivering better quality services to consumers at lower prices and creating sustainable commercial enterprises.

It has been argued that not all of these failings came to pass with the eventual privatisation of Telstra, but some did. There is also a strong case that political apprehension about being accused of diminishing rates of return for Telstra's large retail shareholder base has led to less than optimal public policy outcomes.

We need to pay more attention to these things in the Australian telecommunications environment.

Unfortunately, NBNCo seems willing to initiate, and possibly confuse, wider commercial and public policy initiatives beyond its intended mandate.

We should be concerned about this. Recently, NBNCo has begun to push the bounds of its remit in challenging or less than considered ways:

- seeking ACCC support to develop a POI backhaul service;
- considering new satellite services, and;
- discussions with airlines about alternative developing in-flight communications services.

The POI initiative, for example, is both commercially interventionist and ill-considered.

It comes several years after a major debate on the topic was settled in favour of architecture that carriers have since relied to make significant capital investments. Carriers have configured their own infrastructure in ways that may now be undermined at taxpayer expense.

True, there may be a case about lowering the capital cost of market entry for new players, but that debate was settled some time ago. So what is the justification for reopening it at taxpayer expense when a viable commercial wholesale market exists?

The Government recently introduced *Access Regime and NBN Companies* amendments.

Legislation to clarify how NBNCo can deal with non-commercial assets makes sense, but it should not be used to allow a GBE to wander into existing markets that are competitive and well served by private operators.

If not managed closely, a straying NBNCo has the potential complicate policy frameworks and functioning commercial markets in ways that may be very difficult to remedy.

We should adopt an adaptive policy approach governed by an unbending principle that interventions such as NBNCo should be designed to disappear or be wound back once the need for them recedes or their or core task is fulfilled.

This is often difficult because it requires the simultaneous application of historical knowledge without sentimentality, policy and political discipline and vision. All are rare commodities, exceptionally rare to be found together.

ACMA Regulatory Reform

Against the backdrop of other recent competition and regulatory reviews (Harper; Vertigan), the ACMA Review provides an opportunity to consider whether Australia has a regulatory regime that is appropriate to nurture and unlock the future potential of the communications sector.

The current structure of the Australian communications sector regulatory environment has led to a situation where regulatory decision making as a whole can appear to be inconsistent; certainly lacking in a strategic or unified approach.

There is also significant duplication between the two major telco regulators and a lack of agility to respond to rapidly changing market developments.

Curiously, instead of regulation slowly falling away as competition has increased (as was the original intent when current arrangements were developed in late 1990s), the requirement for an industry specific regulation has remained constant.

Furthermore, the market dominance exercised by the incumbent, former government owned monopoly supplier has only grown despite its stunting effects on its competitors and the market generally.

According to John Durie of The Australian, *“Telstra’s share of the telecommunications industry profits has risen from 84 per cent to 88 per cent over the past four years after factoring in losses clocked up by Vodafone Australia”*.

But does our regulatory framework need to be so complicated?

The current regulatory structure is multi-layered with responsibilities dispersed amongst a number of different bodies. Policy and regulation falls under the remit of the following:

- The Minister for Communications;

- Department of Communications;
- Australian Communications and Competition Commission;
- Australian Communications and Media Authority, and;
- the Attorney-General's Department.

In addition to formal statutory regulation, the industry administers self-regulation through bodies such as the Communications Alliance and NBN Co's Product Development Forum.

As an approach, the Australian structure is somewhat idiosyncratic. It combines elements of an industry specific regulator (ACMA) with elements of an economy-wide competition regulator (ACCC).

Whilst it could be argued that this approach draws from the best of both worlds, the opposite could equally apply. There appear to be a number of potential deficiencies with this structure:

- Objectives and priorities between the regulatory agencies may not always be aligned which can result in contradictory policy outcomes;
- There is a clear risk of duplication of activities;
- This structure may lack appropriate flexibility to adapt to increasing technological change and the market disruption this may cause.

The present structure does not promote regulatory consistency.

Whilst all agencies administer acts that have the promotion of the long term interest of end-users as the main objective, their methods differ.

For example, Optus is not aware of ACMA assessing its decision using the same long term interest of end-users method that the ACCC uses. Such differences can have an important impact on the sector.

Each agency will set its own priorities and interpretations. The priorities of one agency may not align with those of another; indeed, on occasion the priorities have seemed to come into conflict.

Let's look at the process to set price terms and competition caps on spectrum allocations.

The ACMA's stated objective is to ensure the efficient allocation of spectrum from a technical perspective. The ACCC provides advice on competition elements of any allocation. By contrast, a government's objective is often to maximise revenue achieved at the auction.

Quite often the three different priorities will give rise to different auctions rules that may be internally inconsistent. It is not clear to industry beforehand which one of the three approaches (technical, promotion of competition or revenue raising) will ultimately drive the terms of an auction.

This conflict was evident in the Digital Dividend auction of 700Mhz and 2.5Ghz spectrum. A complex auction process designed to illicit true market value for the spectrum was undermined by a parallel decision to set high reserve prices.

Then there is the pricing of fixed line access services.

The ACCC has decided to reduce prices for access to Telstra's copper network on the basis of detailed modelling of costs and application of its established pricing principles and objectives to promote the long-term interests of end-users.

Despite this, the ACCC's access price reductions appear to conflict with the Department of Communication's role in supporting one of the NBN's two shareholder Ministers. This has seen the unusual step of the Department arguing against the proposed access price reductions.

Ofcom Proposal

Optus believes such examples support a strong case to reform the current regulatory structures along the lines of a single industry specific regulator.

Importantly however, this should not provide a platform for a more intrusive regulator – but rather for more effective and targeted regulator. There should be a presumption against regulation unless it can be justified to deliver a net public benefit.

Ofcom in the UK could be considered a “best-practice” model to replicate: it operates as the combined competition, pricing and technical regulator for the communications sector.

What's more the UK has successfully managed to avoid the potential pitfalls of a specific-purpose industry regulator sharing overlapping jurisdiction with an economy-wide competition regulator, although this achievement may have been assisted by the overlay of European competition jurisdiction.

A similar model deployed in Australia could lead to more consistent, effective and focused decision making that reduces costs and provides transparent strategic priorities as well as a more holistic and common-sense approach to regulation of the sector in Australia.

Others argue that that the US FCC also represents best practice telecommunications regulation, but I am not so sure. The FCC is a more political beast, that has taken some twists and turns in its life. Its recent record may be more serendipitous than Ofcom's performance.

Issues of Competition

Effective competition policy is critical to the future economic well-being of the nation and yet the existing institutional structures put in place over two decades ago are failing to keep pace with the complexities and change in technologies that embody the modern digital age.

Institutional structures should provide the appropriate tools, expertise and strategic focus to deal with the breath of competition issues which are like to arise in the years and decades to come.

Optus has supported the recommendation made from the Competition Policy Review regarding the establishment of an independent body – the Australian Council for Competition Policy. Such a council could ensure the policy settings keep pace with digital and technologic changes and they could undertake market studies.

More broadly, Optus submits that market power exists across several communications markets and is caused by factors other than vertical ownership of bottleneck infrastructure. This trend is likely to continue as competition moves away from infrastructure layers towards content and services layer.

We do not, however, support the establishment of a new single national independent regulator for access and pricing functions: rather we suggest that a single-specific regulator for the communications sector (as noted

above) would ensure a holistic and consistent approach to regulation of the sector.

An alternate approach exists, one that allows for an Ofcom style telco-specific regulator. Such a regulator could co-exist with the ACCC -possibly sharing Commissioners, fundamental guiding principles or even a supervisory board.

As I said at the beginning, the political time may be right. A Federal Government that was embarked on a fresh start, with a renewed sense of common purpose, could simultaneously pick up where Harper left off, draw on several telco-sector reviews, recognise that the ACCC is stretched for the foreseeable future and begin to look to a world where NBNSCo's job is done.

This might be a big agenda, but is one a new Communications Minister could grasp with the backing of a well-informed Prime Minister.