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## Drawing the line on equity and efficiency

*It's not too late to save the bush in regard to broadband, John de Rider writes.*

Both the Australian Competition Commission and the Australian Competition Tribunal have put economic efficiency ahead of equity in flat contradiction of government policy on telecommunications pricing. Unless the Minister enforces the government's chosen balance, country customers will be deprived of broadband services and Telstra will not proceed with the deployment of its proposed high speed network.

The tribunal's refusal of Telstra's appeal against de-averaged pricing of unconditioned local loop is not as clear-cut as the ACCC suggests. All seven findings against Telstra are about the level and not the structure of prices. Yet, the key issue is about cross-subsidies.

There is a conflict between economic and social policy. Competition drives prices towards costs – everywhere. But, social policy through price controls on Telstra dictates that consumers pay the same price everywhere. For some years the policy was parity in metro-country local call pricing. In March 2006 this was extended to line rentals; at least, some line rentals.

The policy applies only to “basic” line rental, currently defined as Home Line Part and Business Line Part. They are essentially resale products that allow wholesale customers to resell local service without the service being preselected to Telstra for long distance calls. But, as the tribunal agreed, this does not mean that Telstra is free to de-average its other rental products.

Telstra appealed to the tribunal to bring the “rogue regulator”, the ACCC, to heel. Specifically, it argued that the average retail pricing forced on it by its price control obligations should be mirrored in averaged ULL pricing. The tribunal's decision came close to agreeing, on my reading.

It seems very sympathetic to the arguments for averaged pricing. It accepted that price controls were a real constraint on Telstra. And, while it accepted that ULL prices in urban areas would increase with averaging, it argued that efficient access-seekers should still be able to compete with Telstra. So, why did it not endorse averaging and government policy?

Part of the answer lies in the interpretation of “promoting competition”. The tribunal has traditionally viewed competition as more important than competitors. I think it is peeved that the 2006 amendment to section 44H(4)(a) of the Trade Practices Act replaced “would promote competition” with “promote a material increase in competition”. Hence the comment: “Averaging may not inhibit the ability of efficient access seekers to

compete with Telstra in retail markets, but that does not mean it enhances their ability to compete”.

Telstra’s argument is actually that it would be the one to provide the increased competition if the cream-skimming between de-averaged ULL prices and averaged retail prices could be eliminated in urban areas.

Without averaged ULL prices, Telstra has only two options, in the tribunal’s view: lower urban retail prices towards de-averaged costs to match competitors, or refrain from competing in urban areas by holding prices. It says that “neither strategy would, in principle, enable Telstra to meet both its price caps and earn sufficient revenues to cover costs in a way that would be consistent with meeting its legitimate business interests”.

Telstra argued that there would be increased infrastructure and service based competition in urban and country areas respectively as a result of averaging. The tribunal notes that the former may result in by-pass of ULL but that this risk “did not totally undermine” Telstra’s case for averaging.

Everyone agrees that averaged prices are not economically efficient and result from retail price controls. And the tribunal argues that without averaged ULL prices, Telstra is caught between a rock and a hard place. However, while the tribunal decided that it can have regard to government equity objectives “if relevant”, it dismisses the equity objective because it does not support the efficiency objectives!

Optus argued that the Universal Service Fund is the appropriate social policy instrument for compensating Telstra for any losses it incurs in providing retail services at below-cost prices in rural areas. But, the tribunal suggests that Telstra has a case in arguing that the USF, set without reference to costs, does not provide such compensation and Telstra could then seek to “match its revenue to the efficient forward-looking costs of providing the ULL in both urban and rural areas by averaging”.

Now, only a Ministerial Direction to the ACCC on averaging ULL can settle this conflict between equity and efficiency differently and open the way to increased investment in new broadband networks.

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