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Whither the Benefits of Privatising Telstra: the CEPU View

Ros Eason discusses the tension between the competing objectives of the privatisation of Telstra and the policy to be adopted when the duopoly ends and argues against the privatisation.

I gather from some of the media interest here this morning that the Communications, Electrical & Plumbing Union (CEPU) is expected to run up the red flag this session. Let me begin, then, by affirming the Union's implacable opposition to the sale of any portion of Telstra. We do not believe that such privatisation will deliver any of the benefits that are claimed for it by the Coalition. The overseas experience offers no evidence to suggest that privatisation, of itself, produces greater efficiencies in companies or delivers lower prices to consumers. Indeed, as we have pointed out several times, the Coalition's own policies give the lie to these essentially ideological claims: if privatisation is so good for the consumer, what need is there to introduce the Customer Service Guarantee?

However, what I want to discuss today is not the proposed sale of Telstra per se, but the relationship between privatisation and the range of very complex regulatory issues and choices we face as July 1997 approaches. For I think it is in this context that we can see most clearly why privatising Telstra is a lose-lose proposition for the Australian community.

Privatisation involves inevitable tensions between regulatory objectives - whether these be designed to protect consumers or the competitive process - and the goal of maximising Telstra's sale price. A light handed regulatory regime will suit investors, but will offer less comfort to Telstra's customers. If Telstra's sale price suffers, on the other hand, as a result of tight regulation, it is the taxpayers who will lose out. It is they who will ultimately have to make up the difference between Telstra's value under public ownership-measured by the discounted stream of its future profits and the final amount made available from a sale for the retirement of Government debt.

The equation will always end up in the negative. Privatisation inevitably involves undervaluation of assets, because of the premium private investors demand for carrying risk. But every pro-competitive safeguard and pro-consumer requirement exacerbates this problem. Nor can it be avoided by "learning" from the British experience because it is built into the privatisation process itself.

These are dilemmas that the Government now has to confront at the same time as it attempts to work its way through the thicket of issues arising from the duopoly review. We are indeed now less than 18 months away from the duopoly expiry date and are facing a policy black hole. Industry debate on the Exposure Draft of the 1997 legislation was curtailed by the Federal Election and the extent to which the Draft will be re-worked to reflect Coalition policy is unclear. There are tensions between several aspects of Government policy and the privatisation objective and there has yet to be any wide public discussion of the potential impacts of privatisation on access, investment, service availability and quality and on prices. All this adds up to a state of considerable uncertainty for the industry and for its customers.

It is a fact universally acknowledged that we still have a long way to go to get the 1997 legislation right. There are the problems of carrier definition; the need to balance the claims of carriers and service provides; the questions of both process and pricing that arise from the Exposure Draft's extensive unbundling provisions. There is the need to strike the right balance between discouraging uneconomic entry, with further wasteful replication of infrastructure, and the need to preserve appropriate incentives for investment, particularly in the newly emerging service areas.

Then there are the issues (on which the new legislative turf has yet to be turned) of defining, costing and funding the Universal Service Obligation. What, in future, will be the "standard service"? It is not too hard to see that the wider the

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definitional net is cast here, the more problematic the funding question becomes. For instance, I'm sure that Optus must have been aghast at John Howard's suggestion that ISDN could become the standard service under a Coalition Government, given the very large sums it would require to make this technology universally available. Would the industry as a whole be expected to pay for this qualitative leap forward, through the Universal Service Levy?

Above all these issues there sits the overarching question for the new legislation: What are the guiding policy principles for 1997? The Exposure Draft contains no general objects. When you combine this fact with the quite sweeping discretionary powers the draft gives to the Austalian Competition and Consumer Commission, you have a recipe for ongoing uncertainty of a quite high order.

The *Telecommunications Act* 1991, of course, specifies twelve general objects, including

- the efficient and economic supply of the standard telephone service
- maximising the efficiency of the carriers
- optimal rates of infrastructure expansion and modernisation
- accessibility of the standard service

In addition, the current Act sanctions the carriers' exploiting the economies of scope and scale open to them as infrastructure owners (Section 173). Similarly, the 1995 Ministerial Direction governing access to broadband networks acknowledges the efficiencies offered by vertical integration.

In short, the achievement of technical efficiency is put high on the Act's list of stated objectives and regulatory mechanisms (including the current conception of the BCS as an unbundled, end-to-end service) are enlisted in support of that outcome. At the same time, these protections offered to carriers provide incentives for investment, which in turn helps ensure the ongoing accessibility of both existing and new services.

The new framework does not, as yet, appear to have the same degree of coherence. For instance, the Exposure Draft contains no recognition of the existence of economies of scope and scale in the industry - a basic fact of economic life, one would have thought - or of the claims of technical efficiency. On the contrary, the unbundling provisions are a recipe for inefficiency, through loss of economies of scope. The final economic impact of such proposals will depend, of course, on the pricing of the unbundled network "components", but the point is that the draft offers no guidance in this area, through general objects, to the ACCC.

Indeed, it seems to the Union that there is a strong presumption throughout the draft in favour of what the economists like to call dynamic, as opposed to technical, efficiency - in favour of competition rather than the pursuit of scope and scale economies. In practical terms, this may produce a regime that favours service providers at the expense of carriers. This has always been a central danger of the review, given the Government's desire to see further competition in an industry where opportunities for large scale infrastructure investment are limited. The Union's concerns in this regard are heightened by the absence from the draft of the protections of intellectual property offered by Part IIIA of the *Trade Practices Act* (s.44B) and by the fact that the rights of facilities owners are accorded less systematic recognition than in the *Trade Practices Act*.

What, we need to ask, are the implications of this regime for investment and innovation, and hence for the development and accessibility of new services? (It must be remembered that the broadband networks of the current carrier associates will come under the new carrier definition after June 1997.)

The Coalition have indeed inherited a complex set of problems. Unfortunately,

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their own policies are likely to compound, rather than resolve, the difficulties the industry currently faces. The Coalition proposes, for instance, to have wholesale prices subject to a Ministerial pricing guideline in the post-1997 regime. How will this possibly work, given the variety of products and the multiplicity of "wholesale" prices that the unbundling provisions, together with rapidly changing technology, will create? Will the same set of pricing principles be applied to both narrowband and broadband networks? Is such regulation compatible with the Part IIIA approach to access upon which the Exposure Draft is generally based? What will be the effect of such pricing constraints on carrier margins and hence -to come back to the privatisation issue - on Telstra's sale value?

The Coalition position on wholesale price regulation is one of several instances of an interventionism which sits uneasily with the privatisation objective. Others are the requirement that Telstra accelerate its exchange digitalisation programme (FMO) to allow completion by mid-1997 and that it ensure availability of ISDN services within the same time frame. Simple supply constraints mean that the Coalition's FMO targets are unlikely to be met, though even a more modest speed-up will have cost impacts, particularly in the staffing area, when they will be least welcome. Figures quoted during the Federal Election suggest that these could be of the order of $1 -1.5 billion.

The costs of universal provision of ISDN are of an even higher order of magnitude. Coalition policy requires Telstra to "offer" ISDN where digitalised exchanges are available, but such offers can have little meaning unless lines are also conditioned for delivery of ISDN services. The costs of an Australia-wide programme could be more than $10 billion, without including the costs of ISDN customer equipment.

Other Coalition promises, such as the prohibition on carriers' charging for operator assisted calls, will also have their impacts on Telstra's bottom line. The Union has always opposed charging for Directory Assistance, so this is one area where we find ourselves quite comfortable with the Government's approach. Investors may be less impressed, however. Not only will Telstra be unable to raise revenues and contain staffing costs (by suppressing demand) through the introduction of DA charges; it would seem they will also have to drop charges currently in place for operator assisted ISD and IDD connections. Again the impacts on shareholder value are likely to run into the hundreds of millions.

No doubt the Coalition will soon be considering how some of these pre-election policies can be modified to smooth the path to privatisation. The point, however, is that there are bound to be trade-offs along the way. Who will pay for them? Regulatory interventions designed to silence the anti-privatisation forces in the Senate will be paid for by taxpayers in the form of a lower Telstra sale price. Consumers and competitors, on the other hand, will carry the costs of a light-handed regulatory approach.

Finally, we might ask what impact the privatisation of Telstra is likely to have on investment, especially in areas where the company is not guaranteed an economic rate of return. Here the Union would disagree with the view that corporatisation and deregulation already prevent Telstra from acting as a vehicle for Government policy. True, competition undermines the role of universal service provider that Telstra played comfortably in the monopoly era. But while the Government is Telstra's owner, it still may tolerate higher risks and agree to a lower rate of return than is likely to be acceptable in the private sector. Once Telstra is sold, however, the pressure will be on Government to bear the costs of uneconomic services directly, through subsidies either to consumers or to the universal service provider, who may in future be selected on the basis of competitive tendering. Given the constant pressures on Governments to cut budget deficits, the availability and quality of services in rural and remote areas could become uncertain indeed.

In the Union's view then, the privatisation of Telstra cannot be separated from these larger questions of telecommunications policy and, indeed, from economic and social policy more broadly. How will the industry be structured and regulated after June 1997? What role do we expect Telstra to play in the next phase of industry development, as we move towards a broadband future? Can we reasonably expect it to act as a vehicle for an egalitarian communications policy ? What role do we want it to play in the wider economy, in relation to local manufacturing and the export of advanced services to the Asia-Pacific region?

I return again to the question of the general objects of the new legislation. These need to be spelt out and, if necessary, challenged. We need some vision for the industry, for 1997 and beyond. We need greater clarity on the issues that have been raised this morning. Then perhaps the Senate may be in a reasonable position to debate whether or not Telstra should be privatised. When placed in this larger context, however, we believe the logical outcome of such a debate will be a resounding "No".

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