

Frequent Flying Furphies

by

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“Of course it's the same old story. Truth usually is the same old story.”
– Margaret Thatcher

A. Introduction

Thank you for the invitation to address the Melbourne Press Club.

I had prepared some fresh comments about the benefits of broadband to people, communities and enterprises in Australia. But that will have to wait for another day.

After yesterday's outpouring by the ACCC Chairman² on the subject of Telstra and broadband – and media reaction to it – I think it is important to **take a more sober look** at some of the high-flying furphies and set the record straight.

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² Graeme Samuel, AO

B. Review the Broadband Bidding

It is often useful to review the bidding. How did we get to this point in the **public dialogue and debate about broadband in Australia?**

1. The broadband deficit in Australia

- A **new management** was installed in Telstra on 1 July 2005. Our new CEO, Sol Trujillo, made a clear **commitment to transform Telstra into an integrated media-communications company**. This included: (1) rebuilding the core – the core network, core business support systems (such as billing) and core operating support systems (such as data bases)
- Our **experience in the bush** and a visit to an Isolated School on a cattle station in Blackall in July 2005. [Lismore Story]
- **Australia's position at rank #17** among the those at the bottom of OECD list – such as Spain, Portugal, and the Czech Republic.
- The **lack of attention to telecommunications infrastructure** issues by the nation's political and civic leadership.
- The **lurking economic threat** – to high-paying jobs, productivity growth and economic and community development – to Australia's future and its ability to compete in the global economy

2. National Broadband Plan –

- **Proposed by Telstra** in August 2005
- **Result:** Rejected by the Government in September 2005
- **Reason:** Not given
- **Benefits:** broadband to 100 percent of Australia – with 6.5 mbps to 98.5 percent and 1.5 mbps to the remaining 1.5 percent.

3. Fibre-to-the-Node (FTTN) –

- **Proposed by Telstra** on 15 November 2005
- talks with ACCC started in March 2006
- **Result:** Impasse between Telstra and ACCC announced on 7 August 2005, when Telstra pulled the plug on the talks
- **Reason:** Unable to reach agreement on costs³
- **Benefits:** high speed broadband to more than 50 percent of the premises and 60 percent of the people in five capital cities within 40 months – with expansion to Canberra, Newcastle and other urbanized areas as soon as commercially possible

4. The National 3G Wireless Broadband Network called Next G™

- **Proposed by Telstra** on 15 November 2005 – plans to build new, nation-wide 3G network
- **Result:** Completed the build after 10 months and flicked the switch on 6 October 2006, 3 months ahead of schedule.
- **Reason:** The wireless space is largely a regulation-free zone so the Telstra Board and management thought the risks to shareholder investments were minimal.
- **Benefits:** a nation-wide high speed broadband wireless network that reaches 98 percent of the people (soon to be 99 percent) with network speeds of 3.6 mbps – to be turned up to 14.4 mbps in March 2007 and 40 mbps in the first quarter of 2009. The Next G™ network is a “next generation” internet protocol (IP) network and serves handsets as well as turbo cards that can turn a laptop or desktop computer into a high speed broadband device.

³ Though agreement was reached on many important and difficult issues, we did not get into a serious discussion of provisions to safeguard the investment of \$4.1 billion of Telstra shareholder money from being confiscated by regulatory actions.

Now, those are the facts. Let's look at some of the furphies.

C. Some Furphies

1. Telstra should focus on its business and leave regulation to the government.

The fact is 50 percent of our revenues are regulated. So as we pay attention to business we must, by definition, pay attention to regulation. Those who think otherwise are, as I have said, living on another planet.

Note that in each of the above examples that you will find **“Telstra proposes”** or **“Telstra completes”**. Telstra's leadership has been sticking to its knitting, doing the job that needs to be done – building towers, digging trenches, laying fibre-optic cable, bringing high speed broadband to all Australians, no matter where they live.

Telstra's management is investing billions – that is with a “B” – rebuilding the core network, streamlining business support systems and upgrading operating support systems.

2. Telstra should just “play by the rules” and quit trying to change the rules.

From the CEO to the field tech, Telstra plays by the rules every day. The job of the leadership is to figure out how to:

- meet consumer needs,
- transform consumers into customers,
- advance shareholder interests, and
- serve the national interest – all within the existing commercial, regulatory and technological environment.

That's what 99.99 percent of Telstra employees do.

A few of us try to change the rules – primarily those in my shop, called Public Policy & Communications. That's our job –

and in a democratic society in a shareholder-own company it is an important and honourable job.

Reason: **The rules are antiquated**, The existing rules:

- discourage investment
- hurt consumers and
- undermine business competitiveness.

The rules were developed more than 10 years ago – and these are the rules under which one of the most rapidly changing and evolving industries in the world ⁴ is being governed. During the past ten years:

- **technology** has changed – especially revolutionary advances in IP network switches and speeds, broadband over wireless, and even broadband over copper.
- **consumer preferences** have changed – especially as the needs of consumers and businesses become more highly segmented as people move to more specialized applications that permit them to live their life their way
- the **competitive environment** has changed – with more than a hundred companies now competing in the telecoms space
- the **structure of the industry** has changed with global giants moving in to compete against Telstra, owned by more than 1.7 million Australian mums and dads
- the **role of government** as changed – as 82 percent of Telstra is now privately owned.

But regulations have not changed. In fact they have become more onerous and more intrusive.

So, yes, like many before us and like many in other industries, **we are trying to change the rules in order to better serve:**

- the **interests of the nation**
- the **needs of consumers**
- the **requirements of business and government**

⁴ Perhaps surpassed only by the biotechnology industry.

- the **rights of shareholders** to reap the rewards of their investments and not be forced to ship them to the foreign owners of those who compete against them
- in short, **we are spending other people's money**. And when you spend other people's money attention to risk-taking and security demand a high threshold.

3. **Hard-hitting debate in the marketplace of ideas is a bad thing and should be avoided in a democratic society.**

I noted today's headlines and lead paras describing yesterday's comments by Chairman Samuel and Minister Coonan with a combination of amusement and sadness.

- "The truce is broken"
- "Samuel delivers broadside"
- "Samuel delivers blistering attack"
- "Telstra relations with government sank to new lows"

Let me give you my take on things. My grand-daddy told me that whenever you have a choice between a **simple explanation** and **complex explanation**, take the simple one; it is more likely to be the right one.

What is the simple explanation. Let me try:

- a. **Every stakeholder and nearly every individual in this country has a strong interest in seeing the rapid build-out of high speed broadband** to every home, business and enterprise in Australia, no matter where it is located.
- b. Especially **Telstra** – for commercial reasons.
- c. Especially the **government and the ACCC** – for sound public policy reasons
- d. Especially **user sectors** – such as the media or small and mid-sized enterprises – for commercial reasons
- e. **BUT, the ACCC cannot or will not give Telstra bullet-proof assurance** that it will not declare a Telstra broadband build and force Telstra to sell it to foreign-owned competitors at below-cost prices.

- f. **AND, the Telstra Board and management will not risk spending \$4.1 billion of shareholder money** to invest in FTTN, which would bring high speed broadband to more than 50 percent of the premises and 60 percent of the population in 40 months.

It's that simple. It's an impasse. A disagreement about what is prudent.

- **There is no gaming**, despite fairy tales to the contrary.
- **There is no bluffing**; journos, policy makers, regulators and the public should know by now that the New Telstra does not bluff.
- **There is just a plain old disagreement.** There is also some lack of trust (but we are working on that) and a lack of agreement on data about what things really cost (and we are working on that, too).

There is also a need for institutional reform. Reason. There is a dangerous concentration of unfettered power in the ACCC – which, in our view, has the ability to take money out of the back pockets of Telstra shareholders and give it to competitors and/or to set prices in a way that uses shareholder money to fund public purposes that should be funded by the entire industry or the government or all consumers – and not just Telstra shareholders (and we are working on that as well).

4. Telstra demands exclusive use of its proposed FTTN or fibre network and does not want to give access to competitors.

The facts: Telstra's March 2005 proposal to the ACCC to build FTTN is called the "HAS". HAS stands for "High-Speed Access Network." Note the work ACCESS.

- We proposed a high speed access network.
- Every competitor would have access to FTTN on the same terms and conditions as Telstra business units.

- Another furphy.

5. Telstra wants government money to subsidize FTTN.

The facts: The FTTN fibre project would have cost \$4.1 billion. Investments by Telstra shareholders would be used to cover 100 percent of the costs.

- We did not ask for government money
- We did not expect government money
- We did not want government money.
- Another furphy.

6. Telstra is gaming the regulator.

The facts: Telstra and the regulator disagree. The regulator believes he is protecting the public interest by reserving his right to regulate (i.e., declare) a fibre build-out. Telstra believes it is serving the public interest by building out broadband services where shareholder investments can be protected from confiscation by the regulator.⁵

- That's why Telstra built the Next G™ national high-speed broadband network to 98 percent of Australians – the world's largest, fastest wireless network.
- That's why Telstra proposed to build and pay for the FTTN fibre network

7. Telstra can get all the assurances it needs to safeguard shareholders if it will apply for an exemption as provided in the law.

The facts: Exemptions don't work. There are all kinds of reasons:

⁵ The fact is no nation's economy can grow and prosper if its government gets a reputation for not respecting property rights, which includes taking private property (e.g., shareholder value) for public use without just compensation.

- **It takes a long time** – measured in years – to get through the exemption process...and you don't have much if you get to the other end.
- **All exemptions are appealable** – so once, again, there is no certainty, or you wait until the appeals are finished before investing.
- Finally, and most important, **the ACCC hand that giveth can taketh away**...or it can be taken away by others in government.⁶ So there is no certainty and when you are spending \$4.1 billion your shareholders want to have a modicum of certainty.

8. The public owns the Telstra network; they built it.

The fact is the British colonialists built the network; it was taken over by the old PMG. It went through several transformations – including privatization.

- Individual and institutional investors now own the network.
- Since 1997 when privatization began, the government has received more than \$75 billion as it sold off the network and other assets.

Let me close with this observation:

The world has changed enormously in the decade since privatization and since Australia began designing a new regulatory regime for telecommunications. Given all the changes over the past decade, I don't think it is unreasonable to consider that perhaps the regime needs to be re-examined. The current regulatory settings are riddled with unintended consequences that:

- discourage investment,
- stunt innovation,
- slow growth and
- impede the international competitiveness of Australia's businesses and communities.

⁶ And it happened in the Foxtel case.

It was my privilege last year to address the annual meeting of CEDA. My dinner address elicited some fair but sharp questions from a few of those in attendance. At the close, ASX chairman Maurice Newman delivered the “thank-you” comments, reminding me and the audience that **there have been many examples throughout Australia’s history where a small group started to advocate for change and reform** and everyone dismissed them – and then slowly, over the years, a majority came around to adopt the reform positions they were advocating.

The only one I knew about at that early date – where someone prevailed against the odds – was Darryl Kerrigan’s success in the delightful Aussie movie *The Castle*. You’ll recall Kerrigan never gave up. He rallied his friends. He rallied his neighbours. He never lost faith. In the end, he prevented the authorities from confiscating his home and his property for public use, so they could expand the airport.⁷

But Chairman Newman had more compelling and historic issues in mind, citing the **dollar float** and **trade liberalization** as examples.

I was intrigued by his comments, so I looked into these issues. Here’s what I found, for example, on the trade protection issue.

For many years, as I understand it – from the mid 1960’s to the early 1990’s – the Australian economic debate was dominated by the trade and tariff protection issue. Up to that time, according to Keith Hancock,

Protection had been more than a policy: It as been a faith and a dogma. Its critics...dwindled into a despised and detested sect, suspected of nurturing an anti-national heresy. For protection is interwoven with almost every strand of Australia’s democratic nationalism. It is a policy of power; it professes to be a policy of plenty...With such unity of spirit subsisting between private interests, public opinion, and the Commonwealth Treasury, it is not surprising that the tariff has grown rapidly both outwards and upwards.⁸

⁷ In the beginning, I should also have said that I like Aussie movies...like *The Oyster Farmer* and *Look Both Ways*. But my all-time favourite, so far, is *The Castle* with Michael Caton and Anne Tenney.

⁸ From Keith Hancock’s classis essay on the cult of trade protectionism in Australia, from his book, *Australia*, published in 1930 and available on the Internet.

Still, support to reform tariff laws and regulations grew over the years. Labor Prime Minister Gough Whitlam broke the ice with a 25 percent across-the-board tariff cut in 1973. Eventually, the manufacturing sector faced massive tariff reductions from the late 1980's through the 1990's. Vested interests in manufacturing, I'm told, argued that such tariff cuts would cause the manufacturing sector to decline.⁹

But as the tariff cuts took hold, the nay-sayers were proven wrong¹⁰ – even in what you called the “rust bucket” or “rust belt” states such as Victoria and South Australia.¹¹

Still the facts are beyond dispute: Tariff cuts and competitive pressures worked to:

- **make industries more competitive,**
- **resulting in much lower prices for consumers,**
- **leading to a significant boost in innovation and investment.**

Amazingly to those who believed the doomsayers and those who want to “just leave things like they are” – Australia is now exporting automobiles.¹²

⁹ In addition to reading Keith Hancock and several other authorities on the resolution of the tariff issue in Australia, my education on this issue has been greatly enhanced by discussions with Henry Ergas and his staff at CRA.

¹⁰ In fact, the reforms made the manufacturing sector more innovative and more competitive – though a few manufacturing industries did continue to decline, as would be expected in any economic restructuring. Prior to the tariff cuts, manufacturing was characterised by ageing capital and a largely unskilled workforce. Back then, I'm told, the auto industry resembled its Eastern European counterparts rather than Japanese or Korean car factories.

¹¹ In the US, we called our manufacturing region the “rust belt” and it included the Midwestern states around the Great Lakes. Few of them “recovered.” Instead the **successful states transformed their economic base into new industries or used new technologies to retool and transform traditional industries** such as steel making, auto manufacturing, mining, farming, and the like.

¹² Auto exports were unthinkable before the tariff cuts – when the only exports of cars took place under dubious export facilitation programs which traded off tariffs on inputs for export performance. According to the Productivity Commission, **Australian car industry's exports nearly trebled in the 6 years following tariff reforms**, with exports of components approaching \$2 billion a year. The Australian car industry is now responsible for more exports by value than some of our traditional agricultural industries.

So, you've been through this before. I've been through this before. Changing things is never easy – whatever it is:

- your own personal habits,
- the culture of a company, or
- the policy of a nation.

But, still, we all need to try. And the best way to succeed is to:

- **practice transparency** and trust the good judgment of most people most of the time to be able to separate fact from fiction,
- **believe in the marketplace of ideas** and the ability for the good ideas to beat the bad,
- **give people the knowledge and tools** to become change agents themselves.

That's the way most democracies work. That's the way it seems to have worked in Australia historically on other issues.

People see a need for change and they try to persuade others. Those who seek change are not anti-government or anti-competition or anti-regulator or anti-anything.

They just have a different view of what is best for citizens, shareholders or others where they have a responsibility. So they engage. They have a conversation. They argue. They may even quarrel from time to time.

But that's how public policy is made and then refined in most democracies. And from what I have seen and learned, it's not that much different here, except that the role of citizen-based civic leadership groups seems to have waned over recent years.¹³

It is our hope at Telstra that someday opinion leaders – the government, regulators, opinion leaders, business and civic leaders – and the public will come to understand that **fundamental reforms are needed in the way that**

¹³ On this point, see Philip M. Burgess, "So, What's New? A Journey Across Political Cultures," Paper prepared as background for remarks delivered to the annual dinner meeting of CRA International, meeting in Canberra, Australia on 8 December 2005.

business is regulated, including the telecommunications business, if we are to achieve a

- pro-investment,
- pro-innovation,
- pro-competition,
- pro-regional parity, and
- pro-growth future for all Australians, and not just those who live in its largest cities – and for future generations, and not just those enjoying the benefits of today's technologies.

Thank you for your kind invitation to be here today, and thank you for your attention.

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