

Aligning Regulations with National Needs The State of Play

by
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A. Introduction

G'day everyone.

Welcome to Melbourne Cup Day!

I'm told that the Melbourne Cup is known as "the race that stopped the nation."

Is that correct?

Well, I was looking at today's agenda. Did you notice at 2:45 this arvo we are taking a break for the Melbourne Cup?

We now have a new moniker for the Melbourne Cup:

"It's the race that stopped Sol." [or] "Nothing will stop Sol except the race that stops the nation."

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Just think about it: **Andrea Grant somehow negotiated a one-hour break later today to watch the Melbourne Cup.** This is astounding. It's the first time I've seen Sol give in to something like this.

Imagine the scene in Sol's office:

- **Andrea says**, "Sol, I have a great idea for the leadership retreat. Let's take a break for an hour on Tuesday so our leaders can watch a horse race."
- **Sol says**, "Great idea, Andrea. This is why I pay you big bucks. I see no worries at all in substituting an hour at the track for an hour at work. Why don't you also arrange for an office sweep. That will add to the excitement."
- **Andrea responds**, "'Done dot Now.' 'We can do it dot Together.' 'Anything dot Possible.'"

Andrea is a genius. She has him figured out.

This is such a surprise because everyone knows Sol works hard – and works us hard.

And everyone knows it – even outside of Telstra.

Two Fridays ago, I was coming down the elevator at 400 George. A young woman got on at Level 26, the home of APRA – the Australian Prudential Regulation Authority.

Prudential Regulation...now there's an oxymoron if there ever was one.

The woman looked at me and said, "You're a Telstra guy, aren't you?"

"Yes," I said. She said, "Well, thank God it's Friday."

"Yeah," I said, "only two more days of work."

On this special day of horse racing, **I have to make a confession.**

It's a major confession.

You know I go by the name of Phil – which stands for Philip.

If you didn't know it, **Philip means “lover of horses.”** Google “Philip, definition” and you will see.

Here is the punch line: Philip is not my real name.

My real name is Phar Lap.

Phar Lap Burgess.

I changed my name by deed poll when I was 18. That's when I found out why my dad had named me Phar Lap.

My dad's brother – my uncle – was a pharmacist. In California. He liked to bet on horses. He was also an expert in poisons....and he was a friend of Tommy Woodcase.

Well, you can figure out the rest. **Phar Lap went to the great equine heaven during a visit to California.** That was 75 years ago this year – in 1932.

Let me just ask everyone here a question – I am going to ask, **“What nation is responsible for poisoning Phar Lap?”** Put your hands together when you hear the right one:

- Was it Germany?
- Was it Japan?
- Was it the UK?
- Was it East Timor?
- Was it the United States?

Now that is really important for Sol to hear...and Greg Winn, and Dan Burns, and Bill Obermeier, and Carol Johnston, and JoLynne Whiting and Tom Lamming, and Linda Christian and other Yanks who are here in Australia.

They need to know that the anti-American stuff they all experience from time to time is not about Vietnam or Iraq or even George Bush. It's about the Americans who poisoned Phar Lap.

Australians don't go after Tarek Robbiati or Joe Schultes and or Andy Ellis or even Andrea Grant. Why? Because people from Italy and Germany and the UK and New Zealand (where Phar Lap was born) didn't kill Phar Lap.

Sol, we did it. Actually, my uncle did it...and that is why I changed my name.

B. Set the scene – and setting the record straight

Since coming to Australia in July of 2005, I've **tried to get my teeth into Australian history and culture**...including things like Phar Lap and horse racing.

One way is by **travelling around the country**.

I have been to 51 communities in Australia since January of this year – to spread the broadband message and to listen to the people outside of Sydney and Melbourne – acting on advice I got a long time ago from Geoff Booth. Geoff told me, “You know, **people out in regional and rural Australia have a different view of the world** and you need to know and what they are thinking about and what's on their mind.”²

Another is by **using public transportation**.

I use public transportation in the city and the surrounding region. That leads to interesting conversations and a unique view on people in an urban setting.

I have also spent time **reading**.

Reading is usually a good way to understand a society and a culture not of your own, where you are privileged to work or visit. My excursion into reading includes:

- **History books** by Robert Mann, Keith Windschuttle, and Thomas Kenneally.

² That was good advice...and I took it. It's the same in the US and in other places I've lived and worked: People outside the capital cities have a different – and usually more communal – view of needs, priorities and possibilities compared to the urban crowd. They also have a more realistic view of their own vulnerabilities – living every day with the threat of drought, floods, wind storms and infestations.

- **Social commentaries** like *The Lucky Country* by Donald Horne, *Silencing Dissent* by Clive Hamilton and Sarah Maddison, *Acting on Conscience*, by Frank Brennan, and, of course, the writings of Hugh MacKay – most recently, *Advance Australia Where...?* And journals such as *Quadrant* on the right and *The Monthly* on the left.
- **Playrights** like David Williamson – in fact I just saw *Don's Party* this past weekend at the Opera House.
- **Children's books** such as Norman Lindsay's *The Magic Pudding* (first introduced to me by our colleague, Kate McKenzie), and perhaps most importantly – for me at least,
- **Aussie movies** – like *The Castle* and *Kenny* and *The Dish*, and, of course, *Breaker Morant*, *Lantana*, and *The Oyster Farmer*.

But there's another source of knowledge about a culture. I'm thinking here of **museums**. There are the big ones – like the **PowerHouse Museum** and **The Australian Museum** for natural history and culture here in Sydney or the **Jewish Museum** in Melbourne or the **Maritime Museum** in Fremantle, where I first touched Australia II, the fabled winged-keel winner of the 1983 America's Cup.

But **my favourite are small museums are run by volunteers**. My “most favourite” are called **Telstra Museums** – and they've been **established by retired Telstra employees**. Even though they are not the biggest, they are among the most interesting and educational museums I've experienced.

I'd like to **welcome to the stage a good friend and a very special man**. His name is **Brian Mullins**.

Come on up here, Brian.

Brian works tirelessly as a volunteer – along with many other volunteers – at the Telstra Museum in Bankstown, and travels around the country demonstrating the Morse Code to anyone who will listen.

Brian worked at Telstra from 1956 to 1978. He was a telegraphist. In fact, Brian tells me that we had telegraphists on the payroll until 1987 – and (don't let Greg Winn know this) we still provide telegraphy services in some areas.

Brian is **special person to me for many reasons – but let me name two right now:**

- The first is that he was a **member of the PMG's 1957 Morse Code graduating class, the last class to teach Morse Code**. The MorseCodians, as they call themselves, just celebrated their 50th anniversary at a luncheon here in Sydney a few weeks ago. It was my privilege to attend. I was the youngest guy there. I have learned a lot from Brian and his friends about Telstra and the heritage we all enjoy.
- The second is that **Brian received an AO in June** – an Order of Australia Medal. He received it for his commitment to the community and to preserving Australia's telecommunications history.

Brian has a message for us today...

<Good morning everyone.

If the people of the Victorian Age were to come back today, they would be amazed and surprised – especially by airplanes, movies, and mobile phones.

But they would not be surprised by the Internet.

I am an expert in the Victorian Age Internet. We called it the telegraph. It had an operating system called the Morse Code.

As Telstra installs new, wireless technologies and services that can reach around the world – such as Next G™ – I know that Anything is Possible. I have seen it in my lifetime.

Welcome and have a good day.>

Thanks for coming today, Brian. We appreciate all that you do – and all that you have done.

It's a great privilege to know Brian – and it's inspiring to feel his commitment to preserving the telecommunications history of Australia.

I am immensely **proud of the work he does** – along with his dedicated team of **volunteers** – and they do it **each and every day** to keep the nation's telecommunications history alive...a history created by Telstra and its ancestors.

I asked Brian, “**How do you keep re-supplying your pool of volunteers?**”

He said to me, “**That all depends on you and your mates in the leadership.** If Telstra staff retire happy and proud of Telstra’s achievements during their time of service, we get lots of volunteers. So we at the Museums want you to **keep up the good work.** Do more Next GTMs; do more BigPonds; do more IP builds. That makes us all proud; and that brings retirees to the Telstra Museums where they can **keep the flame alive.**”

When you have a free weekend, think about **a family visit** to one of our Telecommunications Museums – in either Bankstown (NSW), Hawthorn (Vic), or Clayfield (Qld). Your whole family will enjoy it. Tell them you work at Telstra. You will get some good stories – and a good education.

Or **organize a visit for your team** – to learn about our heritage and to meet the **men and women who paved the way for us** – by the work they did at an earlier time.

Thanks again, Brian – and also to all the men and women you work with everyday.

C. The “good old days”

There has been a **lot of change since the Morse Code. Indeed there has been a lot of change since the privatization of Telstra back in 1996:**

- **Technologies** have changed – and the diffusion of wireless technologies is only the most dramatic.
- **Consumer preferences** have changed as people seek choices, convenience, control, simplicity, and mobility in everything they do and in every appliance or device that they use.
- The **competitive environment** has changed – with more than 450 ISPs, 160 competitors in the wireline space and 4 major wireless carriers.
- The **ownership structure** has changed – with the full privatization of Telstra, completed last year. Telstra’s network and its other assets were purchased by private shareholders. **Telstra assets were bought**

and paid for by 1.6 million shareholders. They now belong to the shareholders – not to the government and not to the community.

Still, despite these changes, regulations have not changed – and there is a lingering worldview that somehow Telstra is:

- A **government agency** subject to direction by elected officials – so if an MP wants to force Telstra to spend shareholder savings or to keep Telstra from cutting costs, they pass a law or issue a new license condition. If you are a consumer and you have a problem, you call your local MP and he or she will call Telstra...though thankfully consumers are beginning to understand that it is Telstra, not the government, that is bringing advanced telecommunications services to Australia.
- A **community property** to be used to serve community goals – so, for example, some people think that Telstra should not shut down uneconomic pay phones that don't pay their way unless the community agrees – even though they are paid for by Telstra shareholders and not by the USO. This is another way of saying, that Telstra shareholders should use their money to subsidize the social policies of a government or a community.
- A “**magic pudding**” that just keeps on giving. The only trouble is, the needs of the nation – for broadband and for services to the bush – must be provided in a commercially sensible way. Private companies like Telstra can participate in helping to solve community problems and to serve the national interest. But we must be able to earn a commercial return or its equivalent on the investments we make to provide the infrastructure and services that are needed.

In recent months, there has been a **new theme**. The media call it “**pay-back**” – i.e., **retribution in retaliation for Telstra’s stoush with the Government**.³

During the past two years, we have taken initiatives – considered by some to be aggressive, by others not aggressive enough, and by still others to be just what the doctor ordered – to **educate elected leaders, the public and even our shareholders about the new realities**, including the fact that the Board and management have fiduciary responsibilities under the law to treat every shareholder the same and to **protect and advance shareholder interests**.

One result of this education process has been political and social controversy. Under the leadership of **Will Irving and the Telstra legal team**, we have taken the regulator to the Federal High Court and won. We have challenged decisions by the Minister of Communications – for example, her decision to give \$1.0 billion of taxpayer money to the government of Singapore to invest in WiMax, an inappropriate technology for regional, rural, and remote Australia.⁴

All this has come to be known in the media as “**Telstra’s stoush with the Government**”. More recently, media commentators have said that anti-Telstra decisions – like to the Government’s billion dollar gift to Singapore to subsidize SingTel Optus/Opel to compete with investments by Telstra shareholders – are **pay-back or retaliation for our challenging the wisdom of government** policies and regulations.

In fact, what is going on is pretty straight forward in most democratic societies: **We are simply challenging decades of entrenched thinking about the way Telstra ‘should’ behave and act.**

³ It is an interesting commentary on the political culture in Australia that pay-back and retribution are apparently OK, that payback is an expected and accepted way of doing business with the government. Now, every political system has payback – even political systems that go by the name of “marriage” or “office politics”. But it is not accepted or OK in most political systems to engage in payback in a public sort of way. In the US – to use a recent example – the federal Attorney General and a close friend of the President just lost his job because he engaged in sub-rosa payback. He denied it, but was still forced out of office. In Australia, apparently, payback is OK. In fact, the media even feel free to turn the spotlight on payback to a private company for not toeing the government line – and not on the government for doing it.

⁴ The great German historian and military theorist Carl von Clausewitz once said that “War is diplomacy by other means.” The same goes for litigation: “Litigation is politics by other means.” And, like war, litigation should be used sparingly and when all other avenues for shaping public policy have been exhausted or when litigation can open up other avenues for politics. See Carl von Clausewitz, *On War*, Oxford: Oxford University Press, 2007 edition (1832).

In the “good old days” that meant to serve politicians rather than customers and shareholders. The controversy is based on our decision to reverse years and years of appeasement. These changes mean:

- no more waking up in the morning and **bowing to Canberra** before listening to the customer.
- no more **appeasement**.
- no more **“bubble wrapped” public policy** where there is no controversy and no bruises – where no one is held accountable for decisions that waste taxpayers’ money and mortgage the nation’s future prosperity to the political decisions of foreign governments.

Laced through all this media commentary is a **nostalgia for the “good old days”** – back when Telstra had what the media commentators call a **“constructive” relationship** with the Government.

Although much was achieved in the “good old days”, as many of the people in this room will remember clearly, **the good old days were not as good as they used to be.**

Just as Neville **Chamberlain came back from Munich** where he traded appeasement for a piece of paper that would bring what he called “peace in our time”, we discovered that deals based on appeasement **mean nothing** in the light of day.

Things are not always as they seem.

The “good old days” may have been good for **the Government and its deficit reduction program. After all, the Government garnered more than \$75 billion in equity sales, dividends and other benefits from the Telstra privatization.**

But the “good old days” were also a time when the Government and the regulator **picked the pockets of Telstra shareholders**, reduced choices to consumers, and stunted innovation.

In the winter of 2005, the Telstra Board and the new management team made a decision to **challenge policies of the Government** and the **practices of the regulator** that:

- depress **investment** in telecommunications,
- destroy **shareholder value**,
- reduce **consumer choice**,
- stunt **innovation**, and
- leave Australia in the **bottom half of the OECD** in terms of **broadband penetration**.

In the “good old days”, **the Government sold Telstra shares to punters for more than \$7.00 a share.**

At one point, **the Telstra share price reached a peak of \$9.16** and then fell to \$5.00 – all *before* Telstra’s new management team arrived in July 2005.

Since the arrival of the new management team 28 months ago, the Telstra share price has fluctuated between \$3.45 and \$5.14. Shareholders who bought into T3 instalment receipts one year ago have, at this point in time, enjoyed **capital gains in the order of 60 per cent**, and the investment receipts have outperformed the ASX 200 during this time.

As long suffering T2 shareholders know, **the real reduction in shareholder value occurred between 1999 and 2003**, when the shares fell almost 60 per cent from a peak the \$9.16.

In the “good old days” from T1 – eight years before the arrival of Sol Trujillo – Telstra was assailed by a **barrage of adverse regulatory decisions. These regulatory decisions:**

- significantly **raised the costs of doing business**; or
- **reduced revenues**; or
- **reduced choices** for consumer; or
- **subsidized competitors**, or
- **subsidized the social policies** of government.⁵

No matter how you look at it, **regulations destroyed shareholder value.**

⁵ These decisions – every one since privatization – have been identified, rated, and catalogued by Tony Warren, Jane van Beelen and others in the Telstra Regulatory Affairs group.

Let me give you a **few examples** to jog your memory:

- **Regulated wholesale prices were slashed below cost** – by as much as 80 percent in some cases. For example, since the year 2000, the regulated price of an unbundled copper line in metro areas has been **reduced by over 70 per cent.**⁶ The regulated price of spectrum used for broadband collapsed by an astounding **80 per cent since 2003.**⁷
- During the period of appeasement, **compensation paid to Telstra for serving uneconomic areas in remote Australia** – the Universal Service Obligation or USO – **declined precipitously.** In 1998, the Government regulator⁸ calculated the **cost of the USO at \$550 million** per year.⁹ Yet, **compensation this year will slip to \$145 million** – not \$550 million – **despite skyrocketing costs** of copper, labour, vehicles and fuel since 1998. That is one-fourth of the last official estimate of the actual cost, with the difference paid by the Telstra shareholder. **That does not sound like a ‘fair go’ for Telstra shareholders.**
- Telstra’s ‘play nice’ approach resulted in **10 so-called competition notices** prior to the arrival of the new management in 2005. These exposed Telstra to **tens of millions in contingent liabilities.** They also **hurt shareholders and consumers** because they:
 - **Delayed the roll out** of broadband services;
 - **Stopped residential broadband bundling;**
 - **Protected higher prices charged by competitors** from competition; and
 - **Stifled market growth.**

⁶ Unbundled copper line was \$63.25 in August 2000, reducing to \$17.70 in August 2006

⁷ Regulated price of spectrum used for broadband was \$15 in September 2003, reduced to \$2.50 in August 07

⁸ The regulator (then the ACA, now called ACMA) estimated the USO cost in 1997-98 at \$548 million. We have rounded up to \$550 million just to make it easier to recall and compare. Source: Yolanda Chorazyczewski’s USO white paper (2007).

⁹ It should be noted that if you reverse engineer ACCC numbers, the costs for serving the bush exceed \$1.4 billion per year. Telstra estimates the annual cost at \$1.8 billion. But, even if we use the government’s own number – \$548 million – **Telstra shareholders are left holding the bag...** a bag costing them more than \$400 million this year.

- In 2004, Telstra was prevented from using the **“Zero dollar” (or “\$0”) claim in its advertising** – even though Telstra’s competitors use (and continue to use) the same claim with impunity
- In 2005, the Government imposed a **“rural presence plan” requirement on Telstra, but not on any other carrier**. This gave the Government unprecedented powers to micro-manage Telstra, even to the point of over-riding Board decisions. These are amazing powers to give to government, especially when they apply to only one enterprise in an industry.

For example, if Telstra has to do a rural presence plan each year, **why shouldn’t all the carriers?**

It would be easy for **SingTel Optus to provide a “rural presence plan”**.

- The **title page** would say “Optus Rural Presence Plan”
- The second page would say **‘We did nothing last year’**
- The third page would say **‘We don’t plan to do anything next year’**, and
- The final page would say **‘The End.’**

It would not be a great burden on Optus to file such a plan...or any other carrier for that matter.

Ziggy and Frank Blunt used to say, “If you see an Optus truck in the bush it is either lost or stolen.” Next year, Optus may be out in the bush looking for taxpayer-supported subsidies that the government has spread around for them, free of charge. Like a government-sponsored Easter egg hunt.

D. The reality of the New Telstra – educate, advocate, engage, persist

Throughout this 10-year “play nice” period, **Telstra management negotiated behind the scenes to mitigate the impact of each and every decision**. And, it is true, some really crazy ideas were averted.

But where did it really get us? No where. It is not surprising that our chairman, Donald McGauchie, said in a recent speech to the Australian-Israel Chamber of Commerce (AICC) in Melbourne, **“We tried appeasement, and it did not work”**.

So where are we now? That is a question many people are asking – and it’s a good question and a timely question.

I was asked this question about 10 days ago by a reporter. I was in New York to spark media interest in our transformation progress. I was riding in a New York taxi – dodging in and out of traffic. I got a call on my Next G™ phone from a reporter at the Sydney Morning Herald.

He said, “What are you up to on the regulatory stuff? Haven’t you really stuffed it? – with the Government and the journos?” You gotta love ‘em, these journos. They have such a way with words...

Still, I talked to him at length about appeasement not working. I reminded him that there is a New Telstra – that our purpose in life is now to deliver results to shareholders and customers and not to win a popularity contest with the Government or journos.

I told him we have **moved from appeasement to a principle-driven approach** – to seek regulatory reform that will allow us to serve customers and shareholders. This means **a new approach** that requires us to:

- **educate,**
- **advocate,**
- **engage,** and
- **persist.**

And not just accommodate – not just roll over and salute.

I told my journo friend, “Take the **Broadband Australia Campaign** (called BACK) for example. The campaign is **less than a year old**, and I am **very pleased with the results.**”

“How can you be, **you have nothing to show for it?**” the reporter shot back.

“**Really??**” I said. “You must be smoking something. Just try these for examples:

1. **Public awareness and interest** in high-speed broadband before we started our campaign was measured in single digits. **Now it is over 60 per cent in most polls.**

2. In response to growing public in the broadband issue, **the ALP made broadband a campaign issue** and moved it to the front pages.
3. In response to the ALP, **the Coalition moved broadband into its menu of campaign issues.**
4. Reflecting the growing public focus on broadband– especially outside Melbourne and Sydney, **the Coalition increased the Broadband Connect payout to regional Australia by 40 per cent – from \$600 million to nearly \$1.0 billion.**
5. The Government **reversed its view on the timing of regulatory reforms.** Helen Coonan said as late as March that **no regulatory reforms would be considered until 2009**, which means reforms couldn't be enacted until 2010. **In June – five months after the start of the Telstra broadband campaign, the Minister:**
 - **trashed the previous over-the-horizon deadlines,**
 - **appointed an “expert panel”,**
 - **sidelined the ACCC,**
 - **asked the panel to consider regulatory reforms that will permit a broadband build out, and**
 - **directed the panel to make recommendations by mid-2008.**

This **journo kept on pushing back** – he said, “Yes, but there are no results for Telstra.”

I said, “Look, problems we face weren't created in a day. They developed over decades. They also won't be solved in a day. In the meantime, **all these developments work to our advantage and move us in the direction of positive regulatory reform.**”

You will recall that in September 2005, our Board and CEO decided to **sideline the policy of appeasement that Telstra had followed for years.**

At that point in time, we initiated a **policy of stakeholder engagement**, headed by our communications team. Andrew Maiden reviewed the major elements (and innovations) that are at the core of this initiative – including:

- **public education,**
- **shareholder engagement,**

- **truth-telling**, and
- **employee activism**.

Then, in February 2007, **we turned up the heat** by establishing the *Broadband Australia Campaign* – we call it the **BACK Campaign**. **BACK** included action-oriented initiatives that reinforced aims rooted in our September 2005 reorientation – namely to turn:

- **shareholders into activists**,
- **employees into advocates**,
- **consumers into customers**, and the
- **public from complacency to concern** about the nation’s future if the broadband drought went unattended.

What I made clear to the journalist was that **anytime you seek to change policy through “constituency lobbying”,¹⁰ there are four stages:**

- First – **increasing awareness**
- Second – **increasing interest**
- Third – **mobilizing supporters**. This means sparking actions to achieve reform and building the coalitions to do it
- And finally – **enacting reform** of policies and regulations.

We have **won the first three stages** – and we will **win the fourth**.

The image of the iceberg shows you what is happening. The process of increasing awareness, interest and mobilizing for reform are the **stabilising formation – the hidden strength – under the iceberg**. Just ask the captain of the *Titanic* about the power of the iceberg below the waterline. These three elements are the foundations that support **enacting the reform** – which is the **tip of the iceberg**... the part that is seen by everyone.

To his credit, my journo friend then asked me **“OK, what is winning?”**

I told him, we have two markers – a general and a specific:

- The specific: To achieve reforms that can **safeguard shareholder investment as we build out (or turn on existing) high-speed broadband networks** – such as Fibre-to-the-Node, and

¹⁰ Constituency lobbying is the approach used when direct lobbying and negotiation fail.

- The general: To achieve a **pro-investment, pro-consumer and pro-innovation media-comms environment**.

And that is what we are working towards.

I then said to the journo, “I have spent a large part of my professional life trying to improve governance and strengthen public administration – and the process and outcomes of regulation in Australia are not up to world ‘best practices’ and are doing damage to the economy every day.”

For example, **in every market economy, the function of regulation** is to:

1. **protect the consumer** – to expand consumer choices and to ensure public health and safety;
2. **promote investment** – in part to encourage innovation so the consumer will have more choices; and
3. **foster a healthy and competitive industry** – again, to give the consumer more choices.

Now, if we apply these widely accepted criteria to Australia, we find that **the ACCC fails on every count** in the telecommunications space.¹¹

Perhaps the most vivid proof point is investment – where **telecommunications ranks #12 in investment growth** over the past three years among the 14 sectors of the economy.

If you subtract the substantial investments by Telstra, then the result is even more damning: Without Telstra, telecommunications has a negative -7.5 per cent investment growth over the past three years – in a sector that should rank at least #2 or #3, given Australia’s distance from major world markets and population centers. We call this indictment of the ACCC’s record, “the ACCC hockey stick”.

E. Question to Kate McKenzie

¹¹ It is not only in the telecommunications space. It is others as well – such as transportation. The ACCC is stunting investment, dampening entrepreneurship, and meddling in the management of enterprises.

It is very important to change the regulatory settings. They depress investment and hurt everyone – including consumers, shareholders, enterprises and communities.

They also have a direct impact on our business units. To help me in this, I'd like to ask **Kate McKenzie, our Telstra Wholesale chief, to answer a question for us all.**

Kate, how is **regulation impacting the wholesale market?**

Hi Phil. Look, we've had a string of shockers from the ACCC.

Our costs keep going up and prices set by the ACCC keep going down.

Every punter knows what the theorists over at the ACCC don't seem to know: We live in an environment where the costs of fuel, labour, vehicles, copper and everything else we use to build and maintain networks has gone up. But despite rising costs – just think how the price of fuel and copper have gone up in the past year or so:

- *the ACCC have dropped the price of the “unbundled local loop” (called ULL) from \$22/month (which was too low to begin with) a year ago to \$14.40/month, and*
- *the ACCC have dropped the price of LSS (or “spectrum sharing” – used to deliver broadband) from \$9.00/month (again probably too low) to \$2.50/month.*

Stop and think about it: You can't buy a cup of coffee for \$2.50 most places.

What's worse – the new prices were backdated – that is, the ACCC is requiring Telstra to pretend that the new price was the old price and refund our customers the difference between the new price and the old price going back TWO years. That's what I mean by “pretend prices” and, I suppose, what you mean when you talk about the regulator “pillaging the wallets of our shareholders”.

It's not just money we are talking about here. Because of these new “pretend prices”, there is no incentive for other competitors to invest in competitive infrastructure. It is much cheaper to have an alliance with the ACCC to get a low-cost ride on Telstra's network. Why build, which is expensive, when you can buy so cheap.

In addition, Telstra Wholesale customers (like Optus, for example) are switching from resale services to ULL and LSS. But they are not winning new customers. They are just pocketing the extra \$7.60 (in the case of ULL; or \$6.50 in the case of LSS), a gift

to the bottom line, courtesy of the ACCC. All this, mind you, in the name of competition.

Just so you don't think I'm blowing smoke, let me give you some facts and data.

- *From October 2006 we have gone from 148,000 ULL services to 340,000 services this past month. That means the number of ULL lines has more than doubled over the past 12 months.*
- *From October 2006, we have gone from 208,000 LSS services to 360,000 now.*

In fact, as Sol and the retail people mentioned yesterday, most of Telstra's competitors are still losing customers even with these low access prices...at least for now. At some point, when our competitors start dropping prices and giving back some of that \$7.60 to their own customers, I imagine our retail units will match them so as not to lose Telstra market share. At that point in time, we will have a regulator-induced price war – courtesy of the Government for not enforcing its policy of national uniform prices (called “averaging” at wholesale) and the ACCC for regulatory settings that depress investment and will ultimately undermine true competition.

In the end, it seems pretty clear that if this keeps going there will be no infrastructure investment from anyone and we could end up in a price war. In either case the country, the industry and consumers all lose. You called telecommunications policy a “mess” in one of your commentaries in The Age. I think you nailed it.

Thanks Kate.

I love your point about **“All this in the name of competition.”**

Here is another case of ACCC “pretend”. They have “pretend costs”; “pretend prices”; and “pretend competition” because none of this activity is about new investment, new products, new services or any of the other benefits of real competition. What you have here is subsidized competition, thanks to the backward-looking policies of the ACCC and the unwillingness of the government to enforce its policy views.

By the way, that's why I have called the ACCC a “rogue regulator”. Some mistakenly think it is name-calling. However, I use the term “rogue regulator” decidedly. The ACCC is not under the policy control of elected leaders. **The ACCC plays by its own rules.** That's not the way regulation should work in a democratic society.

F. Regulatory milestones – the reviews, the regime, and the regulations

The regulatory challenges that Telstra **face are real**. They are not imaginary. Regulations are not “light-handed”. Make no mistake about it, we are faced with **onerous and intrusive regulations** that pillage the savings of our shareholders:

- to subsidise the social policies of the government, and
- to prop up competitors, including the foreign-owned, that happen to be favoured by the Government or the regulator.

This is why the Board and the **new management drew a line in the sand** and said “No more! At least not without a fight.”

Since the new approach¹² was adopted in September 2005, **significant regulatory and policy outcomes have been achieved to the benefit of consumers and shareholders alike**. These include:

- **A public commitment by the ACCC Chairman to forebear on Next G™ – that is, not to regulate Telstra’s billion dollar Next G wireless, broadband network**, a decision worth hundreds of millions to Telstra shareholders.¹³
- A public commitment by **both major parties to bring forward a review of telco-specific regulations** – including USO funding for the bush – despite earlier assertions by the Minister that these policy settings were all locked down until after 2009.

In addition, while the media and even our internal comms have been focused on Broadband Connect and FTTN, **Tony Warren** (heading Regulatory Affairs) and **David Quilty** (heading Government Relations) – often working in tandem with General Counsel **Will Irving** and the Legal team – achieve positive results and significant wins that go largely unnoticed and unheralded – week after week and month after month.

¹² Driven by the pro-investment, pro-consumer, pro-shareholder and pro-innovation values and principles.

¹³ Nor should it be regulated. Any carrier that wants to build a nation-wide wireless broadband network is free to do it. They can put their money on the table. Buy from the same vendors that we do. Dig holes, build towers, lay fibre, arrange for handsets, and do all the other things done by Telstra with \$1.1 billion. If they aren’t willing to make the investment, they should not be able to have a free ride on the investments of (and risks taken by) Telstra shareholders.

Consider, for example, **important wins over the past six months:**

- Secured favourable rulings on **access prices** by:
 - Achieving a reduction in **regulated mobile termination rates**, down to 9 cents per minute – saving the company more than **\$50 million a year**.
 - Achieving a **1 cent per minute interconnect rate** rather than the original 7/10 of a cent per minute – **saving Telstra \$48 million** a year in wholesale revenue alone.
- Achieved favourable rulings in the area of **price caps** by:
 - Securing acceptance of our new methodology for price controls, allowing **subscription-based pricing innovation** – worth **\$250 million to Telstra**, and
 - Defeating the **proposed ACCC action on price control breaches** regarding school pricing and the 0198 process – **worth tens of millions of dollars to Telstra**.
- Reduced **red tape** by:
 - Removing most **accounting separation requirements**, and
 - Achieving revocation of the **general and special digital data service obligation**, facilitating shutdown of ISDN and removing the obligation to sell one-way satellite services.
- Mounted “**rear guard actions**” by Telstra to make bad things better. We call these the “**Hey Jude victories**”, in the name of The Beatles – *Take some bad songs and make them better*. These include mitigating punitive wholesale price reductions, costly operational separation plans and a discriminatory local presence plan.

In addition, during the past year we have, at Sol’s direction, involved nearly every business unit and corporate support unit, such as F&A, in a multi-million dollar project to totally **redesign, build and test a new Telstra Cost Model**...this time, based on actual costs, not theoretical costs. This will allow us to submit a **new ULL undertaking in 2008**.

G. The principles of principled decision-making

We have come a long way. We are driven by Sol to be **principled in all that we do**. Principled leadership happens when men and women of integrity take the helm of an enterprise, **and let principles drive their actions**.

In the public policy arena, this means, for example:

- Put the **customer first** – e.g., through policies that promote investment, innovation and facilities-based competition.
- Increase **shareholder value**, protect shareholder investments.
- **Protect intellectual property**, commercial advantage, and shareholder rights.
- **Say what you mean and do what you say**.
- **Persist; persevere; do not blink**.
- **Develop confidence-building** with allies and adversaries alike, based on no surprises, consistency, transparency and principled decision-making.
- **Take a post-partisan approach** to candidates issues, strategies and parties – with a focus issues and forbearance on the rest.

These principles are in the best tradition of business enterprise in the public square and many have roots in Australian history and culture.

But my journo friend said to me, “...**you have pissed off the Government** and that’s not the way you **get policy change in Australia**.”

I uttered another disbelieving “**Really?**” in response. I told my friend that he needed to **read Australian history**.¹⁴ Reason: Telstra’s current approach to public policy reform is very **consistent with the mainstream of business-in-the-public-square in Australian history** – maybe not today, but over the long sweep since Federation and especially since WW II.

I told him to:

¹⁴ I later found out my journo friend is from New Zealand, so perhaps we should cut him some slack for his blind spots around Australia history.

- Read about the **role of the banks in the Chifley-Menziess election of 1949**¹⁵.
- Tell me there was no conflict when **tariffs were removed**.
- Tell me that there was no conflict when the **dollar was floated**.
- Tell me there is no conflict today about so-called **AWA reforms**.

There is no question that **Australian business – including Telstra – has become compliant in recent years.**

But the bubble-wrapped, compliant approach to politics and policy making is not the mainstream of Australian history.

Policy making and policy reform are a rough and tumble business. And it should – because a lot is at stake.

- As an old philosopher once said, “Politics ain’t bean-bag.”¹⁶
- Another said, “Civilized people argue. Barbarians club each other.”¹⁷

Our purpose in life is not to satisfy the Government or win a popularity contest with journos.

Our purpose is to **delight customers and reward shareholders.**

Right now we are **winning the votes in the market place** – and those are the votes that count.

- Our market share is going up.
- Our ARPUs are going up.
- Our churn is going down.
- Everything that should be up is up, and

¹⁵ The election hinged on the policies of the Federal Labor Government, especially bank nationalisation. Prime Minister Chifley intended to bring all of the banks under Government control, a policy that labelled “socialist” by the Coalition. In addition, the Coalition promised to end widely-unpopular wartime rationing. The election took place against the background of the developing Cold War and growing fears of communism.

¹⁶ According to Frank Reuven, “In simpler times, before toys became...computerized, a mother would sew a little sack from a spare piece of cloth or an old sock, fill it with dried beans, and give it to her children to toss back and forth. Their game, called beanbag, conjures up a sweet, wholesome past...The humorist Finley Peter Dunne evoked this Arcadian era when his character Mr. Dooley observed that “politics ain’t beanbag.” The phrase became a favourite refrain of two alumni of Boston’s Democratic machine, President John F. Kennedy and House Speaker Tip O’Neill,

¹⁷ Michael Novak, theologian and social commentator.

- Everything that should be down is down.

We are winning where it counts. Each one of us – and the teams we lead – are playing a vital role in that process, every step of the way.

H. Policy reform, not politics or personalities

Remember that **our public policy purpose is to influence the policies – we are agnostic about the politics**. If our reform ideas help one party and hurt another, that's life – but the principle is that we are focused like a laser on the reforms and not the people or the politics.

My journo friend then asked me, “**Are you looking forward to a new Government.**”

“Of course we are,” I said. The reality is **there will be a new government on the morning of November 25th** – a new government if the ALP wins and a new government if the Coalition wins. So, yes, we look forward to a new government.”

In preparation for the new Government, **I issued a company-wide communication two weeks ago** confirming that we are neither bi-partisan nor non-partisan. **We are post-partisan.**

Post-partisan means that we will not get involved in partisanship at either the personal or party level. However, **we will be engaged in the issues.**

Elections, in my view, are about candidates, issues, parties and strategies. Candidates, parties and strategies are beyond our interest. However, we will continue to speak out on issues that affect our employees, shareholders and customers.

I. Post-election scenarios

Let me conclude by talking with you about our **post-election scenarios.**

Our **post-election planning includes** revisiting and reviewing the economics of a fibre roll-out in anticipation of the new Government.

The Federal Government has released **Guidelines for their Expert Taskforce on FTTN**. If the Coalition is re-elected and the new Government

adopts the FTTN timetable of the old, Telstra will be expected to lodge a competitive FTTN bid under this process by 14 February 2008.

We have met with the Government on these issues...and others, at the highest levels...and, just so you know, this is a process in which Sol is personally and continuously engaged.

We have also held **periodic meetings with the Opposition** – again, at the highest levels – on matters related to **a national broadband plan**, including Telstra’s role should the ALP win the election.

Our internal planning, however, is not predicated on a “Labor win” or a “Coalition win”. Listen closely to this.

Our internal planning is based on **two scenarios** – a “make love” or a “make war” approach by the new government:

- **The “make love” approach** assumes the new Government (of whichever political stripe) wants to **partner with Telstra** and others in the industry to **achieve the fastest possible broadbanding of Australia** – and to take Australia to the top in telecommunications among the OECD countries.
- **The “make war” approach** assumes the new Government wants to continue to **treat broadband as a political football** rather than a pressing national need – and to treat Telstra as a community property and **shareholders as people to be plundered** rather than a formidable partner with a lot of assets that can be used to advance the nation’s prosperity in rather short order.

I want you to know – and, again, please listen closely, that **we will approach the new Government, whoever it is, on November 25th as if they want to make peace** and get something done for the nation’s telecommunications future.

If they do, we are all ears and ready to roll – and we have some ideas of our own.

If they don’t, we will continue to educate and advocate – doing our best to persuade shareholders and the public that current telecommunications

policies and regulations are **harming consumers, shareholders and the nation.**

It is our view that, despite election rhetoric, both the ALP and the Coalition might see the **many advantages to a principled approach to telecommunications reform** – one that

- recognizes **shareholder rights**,
- expands **consumer choices**,
- **takes advantage of the assets** represented by Telstra,
- **promotes investment** by the entire telecommunications industry,
- **achieves the broadbanding of Australia**, and
- **advances the national interest.**

That's why we will work with whatever government wins the election,

I personally believe **the new government will want to see nation-wide broadband deployment** at the earliest possible date.

I also believe Telstra will end up building FTTN – **because it is in everyone's interest for FTTN to be built** and Telstra is the only company able to do it – and do it fast and economically.

And if I am wrong, then I know we have a Plan B and that it, too, will be good for consumers and shareholders.

That was the story I told my journo friend from the SMH. So, was any of this reported? Some, but not much. Pretty typical.

But it is **important for you all to know this, to understand where we are heading, and to know we will not be deterred from our principles that are:**

- **pro-consumer,**
- **pro-shareholder,**
- **pro-innovation, and**
- **pro-investment by the entire industry.**

J. What's next?

So what are **the next steps?**

Let's start with the basics. Telstra's transformation is the **most comprehensive change program advanced by any of the world's major telcos**. In two years, Telstra has achieved outcomes that are unrivalled among its peers. We are:

- **achieving a world-leading turn-around** in arresting the declining performance as an incumbent,
- **winning in key strategic battlegrounds**: Wireless, Broadband and PSTN retention,
- **winning new customers and expanding market share with new products and services** based on integration and convergence,
- **growing impressive new capabilities** in content,
- **achieving world-class status in the wireless space**, having passed Japan and South Korea with the Next G™, the world's largest, fastest and most advanced wireless, broadband network,
- **developing new high-growth assets** internationally,
- **building a scalable low-cost operational base**,
- **assembling a world-class management team with global experience**, and
- **building a pan-regional media-comms powerhouse** with global reach

We will **continue to strive to change the regulatory settings** that are aligned with national needs so that Telstra can invest in Australia's future.

- We will be **relentless** in our pursuit of principled reform.
- We will continue to **advocate** for consumer choice and shareholder rights.
- We will continue to **speak out** for regulatory settings that are aligned with national needs and our fiduciary responsibilities.

In short, we will **continue to forge ahead** to get the policy changes and regulatory settings that are required to allow our **industry**, our **employees**, our **shareholders**, our **customers**, and the **country** to prosper.

We will **not lose the faith**. It is important that we all stand together on these tough issues. But not only stand together, **but speak out together and individually** – **from the many social and community venues where we have a voice**.

I know from care study of the EES surveys that our employees:

- look up to you,
- listen to you,
- seek to understand you – if you talk straight to them.

I want to close today by asking that you **explain to them why we are taking this path** and **why we need each and every person in this company to support what we are doing, to stand up for Telstra ...actively – by:**

- **joining Telstra Active Supporters,**
- **learning facts and data** on Telstra's achievements
- **understanding the character and sources of attacks** on Telstra consumers, shareholders, and employees.
- **writing letters to the editors,**
- **calling talk-back radio,**
- **contacting MPs** and other elected officials
- **engaging friends and neighbours**
- **refuting attacks** on Telstra
- **showing pride in our many achievements** for consumers, shareholders, the industry, and the nation – including the world's first nation-wide high-speed broadband wireless network.

That way we will win this argument. Anything *is* Possible.

Thank you.

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