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The Manager

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**ELECTRONIC LODGEMENT**

Dear Sir or Madam

**Transcript from Telstra Fibre to the Node Briefing – Q&As**

Attached is a copy of the transcript of the Q&As from today's Telstra Analyst Briefing on fibre to the node, for release to the market.

Yours sincerely

A handwritten signature in black ink, appearing to read "Douglas Gratton".

**Douglas Gratton**  
Company Secretary

## **TELSTRA TELECONFERENCE 7/8/06**

### **Q AND A**

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QUESTION: (.Jesse Hogan, The Age.) Good morning Phil. The issues you did get agreement with, like network access and the replacement of ULL, seemed to be a lot more contentious than price. Does this mean your decision to withdraw is purely a cost decision rather than a philosophical decision about access for competitors?

PHIL BURGESS: That's a very good question and an insightful question, too, because I think most people would have said five months ago we will never reach agreement on those kinds of issues of network access and so on. So, yes, I am very proud of, I think Graeme Samuel also is proud of the progress we made on some very tough issues. But, yes, the price was the reason, price was the reason, price and cost were the reason that we reached the impasse and that's reason enough because people invest in companies like Telstra or BHP or any other company because they want to get a return on their investment and we are going to do everything we can to make sure shareholders get a good return and when you start giving away your assets by below cost pricing, you are not serving your shareholders and we are not going to do that. We are going to do everything we can to protect their interests.

QUESTION: Just a second one. You said Telstra would not invest until the ACCC recognised the actual cost. Assuming G9 thought that the actual cost was fair, has this changed your position on co-operating with G9 either as an investor or someone that would buy wholesale access from a network if it went ahead?

PHIL BURGESS: I think if the G9 can do this at a lower cost, they ought to do

it, and if they succeed in doing it, then we will be first in line to be access seekers, so that is something that is their decision to make and if they decide to go ahead, that's fine.

QUESTION: So there is a possibility of being an access seeker but still not interested in being part of the actual project?

PHIL BURGESS: Sol Trujillo has made clear, and I agree with him, that if you look around the world it is hard to find very many examples of successful consortiums of this kind. I think it is better if one company takes a risk, makes the investment, builds it out, manages it, tries to serve their customers as best they can.

QUESTION: (Jennifer Hewett, the Financial Review.) Hi, Phil. You were talking about the idea of cross-subsidisation and the fact that Telstra accepted that was the government's view. But it seems that you will still be up for a lot of extra costs as far as you are concerned in cross-subsidisation, so I don't quite understand why the FTTN, stopping the FTTN stops the problem for you.

PHIL BURGESS: Well, it doesn't. The issue of being recompensed for the cross-subsidies that we are required by law to provide has been on the table for a long time and will continue to be on the table. The FTTN would have only hastened the decline in the cross-subsidy pools that would have been available, so we are not going to engage in a new investment costing \$4 billion that is just going to hopefully bring more revenues in on the IP side, but hasten the depletion of revenues that would otherwise be used to fund services to the bush, so that's an issue that is going to be with us, it is still with us, but if we stayed in the FTTN talks and accepted them, we would be in even deeper water than we are today.

QUESTION: This comes up of course just days, really a week before the

government has to make a decision on the further privatisation of Telstra. What impact do you think this will have?

PHIL BURGESS: I don't know. I haven't really considered that. I mean I have actually gone for a whole week without thinking about T3. T3 isn't our issue. Our issue is to serve customers and to advance the interests of shareholders and to hopefully build out wall-to-wall broadband services in this country through a combination of landline and wireless services and T3 is an issue for the government. They make all the decisions related to T3 and Sol and our leadership have pledged repeatedly, both in public and in private conversations, that we will do everything we are called upon to do to cooperate with the T3 process. We want to see T3 go forward, we want to see the sale, the retail sale happen, we want to see the entire block sold if possible, so we are in favour of T3, but it is not something we have any control over.

QUESTION: (David Crowe from the AFR.) Hi, Phil. Last December when the Federal cabinet was considering the ULL issue, out of the cabinet meeting came a statement by Helen Coonan on price parity with regard to ULL. Is that the fundamental government decision which made this fibre to the node project not possible? Do you trace it back to that decision?

PHIL BURGESS: Not at all. I mean the fibre to the node, the decision to do fibre to the node is because that is what we want to do to bring new integrated services to the country. That's what the country needs to move into the next phase of the digital revolution as these bandwidth-hungry applications begin to arrive in education, health care, all these other areas, and the decisions that were made last December by the government on ULL really didn't have a bearing on

this one way or the other. These plans were in the hopper last summer, last winter, last July and August and nothing that happened around the ULL at that time was related to these.

QUESTION: A follow-on question is earlier at the very start you talked about this round of talks with the ACCC. So in what circumstances could there be another round of talks with the ACCC? Would that for instance require government legislation to clarify this issue?

PHIL BURGESS: I think there is clearly a conflict between the policy-making branch of the government and the regulatory branch of the government. The policy-making branch of the government wants a national uniform price, the regulatory branch of the government is pushing for de-average prices which would have much lower prices in low cost areas like the central cities and much higher prices in the high cost areas like the bush.

If you are a theoretical economist, the point of view of the ACCC is unassailable, but in a country like Australia where you have 80 per cent of the people living in highly urbanised areas on a huge continental-size country, theoretical economics begins to break down because of the DDT factor, because of distance, density and terrain, and so that has to be fixed whether that gets fixed through legislation or whether that gets fixed through the principles sitting down and talking.

However it gets fixed, it is not going to get fixed by us, it is going to get fixed between the ACCC and the government and as far as we are concerned we will be dealing with the ACCC every day on all kinds of issues and as far as this issue is concerned, whether it is ULL or fibre to the node or any of these other big issues, as soon as we see there is an opportunity for making some progress, we will be

at the table if they will have us. I mean, look, the relationships that we developed I think with the ACCC and the senior staff and the working staff over there I think were very good. We, Graeme Samuel and I, talked at least once a week on the phone and met frequently until the end of June and talked after that on the phone and exchanged e-mails.

I think the important thing is that I think we built some trust, I think we built some credibility. We just couldn't reach decisions, a decision. We had a conflict in world view, we had a different view of how the world worked, we had a different view of cost and yet those differences of views were always carried out in the most professional and I have to say even sometimes with a lot of levity. I mean it was a good working relationship and when I talked to him this morning I told Graeme that I hope we can continue to find a way to address these issues in a professional way because we have to get it resolved, we have to get it resolved for Telstra, we have to get it resolved for the industry because this industry is not very healthy right now.

All you've got to do is read the stuff that's coming out from the other competitors and it is not good for Australia to be where we are among the OECD countries, ranked towards the bottom of the list. We are moving to an era, not in 10 years or five years, but over the next three to four years where there are going to be major new opportunities to improve productivity and for businesses and educational institutions and health care institutions and there is going to be huge new opportunities for household management and consumer convenience, but these are going to require a lot of bandwidth. You have places like Korea and Japan already moving to 100

megabits and here we are begging for the right to have our shareholders protected to build out a 24 megabit system.

So, we think that it is time for people to kind of get their head out of the sand, look around, see what's going on around the world and realise how this country can be very badly damaged if it doesn't play catch-up soon because, once you get far behind, business starts going other places and habits are not formed that would otherwise be formed. I think that we need to continue these discussions with the ACCC on a whole range of issues and with the government to make sure that we get the right policy and regulatory settings for the industry and the country.

QUESTION: (Lyndal Mcfarlane, Dow Jones.) Hi, Phil. Just wondering if this outcome represents the horrendous regulatory outcome John Stanhope was talking about with regards to the dividend policy.

PHIL BURGESS: I can't speak to that; that's above my pay grade. I think that's an issue for the board and for Sol Trujillo and John Stanhope and I have no idea what the impact on that kind of thing is.

QUESTION: Okay, and the contract with Alcatel, what will happen there? Will that be cancelled?

PHIL BURGESS: Once again that's above my pay grade. It's been on hold since December and what has happened to that will be a matter for Greg Winn and Sol and John Stanhope and others who are over this. What we do is try to - you know, those guys are in the business of running the business in the existing environment and we are in the business of trying to change the environment and how they do things in the environment they operate in is not something I know a lot about or spend a lot of time on. I know my job is to try to create a more favourable environment to grow the company, to protect

shareholders and to make it possible for our business units to serve their customers more effectively.

QUESTION: (Alan Kohler from Fairfax.) Just to be clear about it, are you saying that Telstra's refusal to invest in fibre is caused by the mismatch or the disagreement between the government and the ACCC over averaged or de-averaged prices between the bush and the city?

PHIL BURGESS: Yes.

QUESTION: That's it?

PHIL BURGESS: The fact is that until they decide whether they are going to have - they can have de-averaged it at wholesale like the ACCC wants to do and then de-average at retail. If they want to have it averaged at retail like the government wants to do, then you have to average it wholesale.

QUESTION: And you wanted to have a subsidy on the city, is that correct?

PHIL BURGESS: That's what the government policy is and we have no reason - we are agnostic on that. We just say no, they have to be together. We are agnostic on whether you have average retail at wholesale or de-average retail at wholesale, but you can't have average in one place and de-average in the other; it doesn't work. It's like fingers on a chalk board and drives everyone crazy, so what's happening now is that the policies of the government for national average price, the ability to implement that has been undermined very systematically and very rapidly by the policies, the regulatory policies of the ACCC which are de-averaging.

QUESTION: This doesn't just apply to fibre, this applies to everything, right?

PHIL BURGESS: Sure.

QUESTION: So are you saying Telstra will not invest in anything until this is

resolved?

PHIL BURGESS: No, because in other areas we don't face this issue. I mean in the non-regulated areas such as wireless it is not an issue, so what this means is that we will simply live by the rules as they exist and we will continue to do the other things that we are doing. We are building out a 3G network, we are doing a number of other things that we announced on 15 November and we will continue to do those.

QUESTION: (Gary Barker from The Age.) Hi, Phil. How far do you think, looking at it from the user's point of view and the need to have bandwidth, will the 850 megahertz network fill the gap anywhere in there? Is it an alternative, or not?

PHIL BURGESS: I think the 850 network will be a huge boon to the whole country. It is going to cover 98 per cent of the population and population centres and I think that it is going to make a huge difference, but there are limits to how much bandwidth you can get out of a wireless system. I mean physics establishes that, not Nokia or Telstra or anybody else, so there are laws of physics that we run up against pretty quickly. If we start thinking about the kind of bandwidth that the Europeans are dealing with, that is 50 and above, that the Japanese and the Koreans are working with, 100, or the kind that is now emerging in the United States where most of the DSL is 20, most of the cable is 30, we really need to have a landline build-out of fibre and there are all kinds of reasons for that, but bandwidth speed is one.

There are others that are also important related to security, reliability, those kinds of things, but I think what we need is a combination of technology. We have a situation now where the regulator is really favouring some technologies over others, favouring

some providers over others and this just has to get worked out before we can get a healthy industry in this country and may mean the kinds of investments that need to be made. We are not investing in this country in infrastructure and all you have to do is international comparisons to see the extent to which that's true and why people aren't concerned about that puzzles me but I think that at some point people will have to wake up and smell the roses on this.

QUESTION: (Michael Sainsbury, *The Australian*.) A couple of questions. The first one is what sort of alternatives are you now looking at as part of the fixed line broadband deployment to get high speeds to customers? The second one is with your description I guess of a confused regulatory settings between the government and the ACCC, obviously these are things that Sol Trujillo and John Stanhope have to talk about to investors if they are trying to sell the shares in T3. I mean, why would people invest if this is the message coming from management?

PHIL BURGESS: Say your second point? I didn't get the second one. I got distracted here, so say the second one?

QUESTION: The second one is about your description of the regulatory settings being confused and unworkable and there is no reason for Telstra to invest. I mean if Sol Trujillo and John Stanhope are going out to investors trying to sell T3 means there is going to be a confused message there, you know, "Come and invest in our company but we don't think it is worth investing money in ourselves."

PHIL BURGESS: On the first question on the fixed line, I can't answer that. Once again that's not what I do and that's going to be for Greg Winn and others to answer. On the second one, though, I think Sol and John Stanhope and others have made clear from the outset that they

are going to support T3 in every way that they can, but they have also said they are going to tell the truth about what the regulatory and other risks are here. I mean that's their obligation and that's what they are going to do and if the regulatory settings here are a problem, they are going to have to say that.

I mean there are a lot of good things going on in Telstra and you wouldn't know that by reading the paper but there are some incredible things happening with transformation and those are things that they are going to be talking about, but they are also going to be talking about the value-destroying regulations that weigh heavily on the financial performance of this company. The bottom line is that we have to recover our costs in everything that we do and we have to have the opportunity to make a competitive return on our investment.

Nobody gets upset with Macquarie Bank or with Woolies or with anything else when they are very successful, but if we get to be very successful we have people say, "That's an unreasonable return." Well, our view is that our shareholders want us to make large returns, they want us to be very successful and that's what we intend to do and so, when they do the T3, if our leadership has to go on the campaign trail, and I'm sure they will, and number one and number two I'm sure they will have a great story to tell and, number three, I'm sure there will be some down sides in that story, one of which will be the regulatory setting but how they destroy share value.

QUESTION: (John Durie from the AFR.) A couple of questions. Firstly, there's been several - you said you agreed on the weighted average cost of capital. There have been several figures out there, one of 11, one of

15, one of 18, so which one of those did you agree on?

TONY WARREN: We will put out a statement this afternoon with more of the cost details. It is probably best if you have a look at that, John.

QUESTION: You can't tell me that now?

PHIL BURGESS: We are going to have a paper out this afternoon that has a lot of the details.

TONY WARREN: I don't have it in front of me, John, is the bottom line and the fact was it wasn't the biggest issue on the planet so the other issues came back, the other issues that bit back are the ones we were more prepared to talk about now.

QUESTION: Okay. Is the ACCC going to come up with a decision in the next few weeks on one of your arbitrations on ULL pricing in which they are going to use a de-average price so what are you going do about that?

PHIL BURGESS: We will have to wait till me see it. The one thing for sure is that we have an average price around the country of \$30. We have a price in band 2 where most of the customers are of \$22 and there are indications that they may be thinking about under \$22. If they do, that simply takes the money out of the pot that would be used to fund high cost areas, number one. Number two, we have the question about what is the rationale for this. The cost of petrol is going up, the cost of trucks is going on, the cost of copper is going up, the cost of labour is going up, so it makes one wonder where do you get these kinds of 10 per cent and 20 per cent reductions in cost and it also makes you want to ask where are the cost studies on the ACCC side?

I mean they have made clear to us they don't like our cost studies and we have gone back and tried to update our cost studies,

update our data, get a better hand on what we are saying, but we haven't seen their cost studies on any of this. I don't know what accounts for a decision they might make or they're reputed to be in the process of making that would lower that \$22 band 2 price to something south of \$20 and, if that happens, what they are really doing is declaring war on our shareholders because we have statutory obligations to fund high cost areas and the only way that can be done with this kind of action is to take it out of our shareholders' back pockets and that is not something that management is willing to do.

QUESTION: So is that what today's exercise is all about, just to get the war settings right, because you know that's what they're going to do. They have already said they have rejected your \$30 price.

PHIL BURGESS: We think one step at a time. Right now we are dealing with FTTN issue and, whatever happens in other areas, we will deal with those when they come along.

QUESTION: Can I ask another question? There's been the 850 megahertz. Could you tell us how that's going along? There have been some reports that there has been a lot of trouble with the build of it.

PHIL BURGESS: The 3G 850 network is proceeding ahead of schedule. It is under budget and so far things are going very well. I read that report you are referring to, but I didn't read that anybody was quoted in it. It just said somebody said. I don't know if it was over the clothes line or the TV set or where that somebody said something and who that somebody was and whether it was one somebody or many somebodies, but the fact is that I think that people in Australia are going to be very proud of the first nation-wide 3G network built more rapidly and to a larger area than any other 3G installation in the

world. It is going to be a world-class achievement that will I think get world-class attention and it is a great gift to regional, rural and remote Australia because we are going to have lots of people out there, within a year after we light it up, they are first of all going to have over one and a half megabits and within a year upwards of 14 megabits and that's the kind of service delivery that we are trying to achieve with these kinds of innovations.

QUESTION: One final question. From your HFC cable what sort of band width can you get there?

PHIL BURGESS: Say again?

QUESTION: Using your HFC cable, the existing one.

TONY WARREN: Currently, John, we have a 17 megabit service out there, as you know, and that's what we are offering at the moment. Just to go back to your earlier question on the WACC, Telstra's starting point was 11.02 WACC. We agreed to reduce that as part of the discussions down to 10.32, so I think that shows some of the fancy that has been in the press.

QUESTION: So you started at 11.02 and reduced to 10.3?

TONY WARREN: 10.32, and the bottom line is this wasn't a major stumbling block in the discussions. As Phil said, the major stumbling block in discussions was around how much the FTTN high speed access service contributes to the upkeep for the rural network and the bottom line is that gap proved to be just impossible to bridge.

QUESTION: Is that something to be redressed by a large government subsidy?

PHIL BURGESS: By a large what?

QUESTION: Government subsidy?

PHIL BURGESS: I think the point is that there are all kinds of ways to do it. You can close that gap. If you want to have nationally averaged

prices, which is the policy of this country, which we agree with, then there are all kinds of ways to pay for it. One way to pay for it is through an industry-funded model like the USO here in Australia; another one is through a government funded USO model which is found in some other countries around the world; another way to do it is through cross-subsidies; another way to do it is through vouchers. There are all kinds of ways to pay for nationally averaged prices.

In this country the decision has been made to pay for it using two mechanisms: Number one, an industry-funded universal service fund, which by the way goes down 8 per cent every year and, number two, supplement it by cross-subsidies where the nine million people in urban areas subsidise one million people in rural areas. That's a perfectly rational way to do it. We are agnostic on how it's done; it could be done any way the government wants to do it.

The only thing that we care about is that it is done in a competitively neutral way, number one; in a technologically neutral way, number two; and number three, that it pays the full cost of providing the services that we are required by law to provide to high cost areas and those three standards need to be met in any good public policy. You don't want to favour one company over another, you don't want to favour one technology over another and you don't want to do this in a way that forces a company to pick the pockets of shareholders in order to pay bills it is legally required to pay. That is, it's the right thing to do.

QUESTION: (Fergus Maguire from Bloomberg.) Gidday, Phil. Can I just clarify: Now that you are not going ahead with fibre at this stage, will you be increasing your investment in your pay TV table?

PHIL BURGESS: Once again, Fergus, I don't know the answer to that. That is

something that is for other people to deal with. I can tell you one thing. Let me go back to something I said earlier. In this company what I think people don't know because they are interested in other things is that everybody is totally focused on this transformation. Everybody is working hard to change this company. You know, while people write these stories about bright star and \$70 million really isn't very much money after all and (indistinct), those kind of things, the fact is we have got people out digging holes in Australia, digging trenches across the landscape, putting fibre in to connect the 3G towers to give this country more capacity, telecommunications capacity. That is what we are doing.

We are not issuing press releases like the G9 group, we are not talking about doing things. We are actually out doing things and on July 1st we put out a report of 27 pages we tried to outline for the media and for our shareholders and others the concrete achievements that have been realised since last July and especially since November of 2005 and we have got a very positive response from our shareholders on that. So, our focus is on doing things and people like me, I am focused on trying to change the environment in which we do things, but the rest of the crowd around here are people who simply have their nose to the grindstone trying to make the transformation work on schedule and under budget and so far things are looking pretty well.

QUESTION: Given that, as a part of that transformation, the fibre network and the new services that were going to be offered over that were such an important part of that transformation, how is Telstra going to be offering all these new content and media services that they want if they don't have a fibre network?

PHIL BURGESS: Once again, that's something I think you will hear Sol talking when he is ready to talk about it. Sol is a guy - and I don't think I have been to one senior team meeting since I have been here where Sol hasn't surprised everybody with a new idea for something that we can do with one or another of our platforms. I think that when we are ready to announce what we are going to do, we will be ready when we are prepared to do it, that's when we will announce it and that's when people will know.

I mean, we live in a competitive environment. Even though there are some in certain quarters here who don't believe that, we live in a very competitive environment and we have a leader now who is a competitor to the bone and so I think what you are going to see from us is hard, aggressive, competition in every single market with every single market segment and as new opportunities come along to do things on one or another of the platforms we have, you will hear about them and we will see results from them. But we are not going to be saying in advance what those are.

QUESTION: (Malcolm Maiden from The Age.) Hi there. I am wondering whether from your perspective the impasse that you have reached in the regulatory settings as they now stand preclude a more limited fibre roll-out in the denser urban areas.

PHIL BURGESS: Once again, Malcolm, when that happens it will happen. I mean we are going to do everything we can to be effective competitors and what form that takes will be announced when it is announced.

QUESTION: Is that a no?

PHIL BURGESS: We are not going to announce it in advance.

QUESTION: Thanks. And you said that you hadn't seen from the ACCC any costings by the ACCC. Was that a ULL comment or was that also one

that applied to the FTTN discussions?

PHIL BURGESS: I think one of the frustrations we had with the discussions with the ACCC is that they ask us what our costs are and we tell them and then their response is "I don't like that cost." Well, why?

QUESTION: That's during the FTTN discussions?

PHIL BURGESS: During any of the discussions that we have had and, if they don't like them, then why don't they like them? I mean, on the one hand we use things like invoices and other hard costs we have paid to establish what we our cost basis is and if the other side doesn't like it, then we need to know why. To me a cheque book stub is worth a lot more than an economic model in terms of establishing what a cost is and we deal in cheque book stubs.

QUESTION: Okay. Thanks.

QUESTION: (Rhys Haynes, Australian Associated Press.) In the last couple of minutes Graeme Samuel has just told a colleague of mine that he is bewildered and disappointed by Telstra's decision to abandon the negotiations and he is not sure why it has killed off the negotiations, so I just wanted to get your thoughts there.

PHIL BURGESS: I talked to Graeme, as I said, Friday. I talked to him again this morning and I think that one of the - - -

QUESTION: Why did he come out and say these things, then? I don't understand why he would come out and contradict you, that's all.

PHIL BURGESS: How is he contradicting me?

QUESTION: He just kind of made it seem like you both agreed to disagree but he seems a lot more disappointed than - - -

PHIL BURGESS: We had a very explicit agreement when we talked this morning, that it is best to call these off and then come back with fresh eyes to the range of issues that we are considering and when we

come back, I think the exact phrase I used was whether it is this week, next month or three months from now, whenever it is, what we want to do is to keep the doors open.

Look, there is nobody more disappointed than I am about the collapse of these talks, but we reached the point where we are at \$13 and they are at \$1.77 and we weren't getting any closer and I think that, when that happens, the best thing to do is to go back to the drawing board and figure out what can be done next. I told Graeme this this morning. I said my hope is that we can find some way to work together to develop an approach to costings that they can be comfortable with, a fully transparent approach that they can be comfortable with, that we can be comfortable with, that will show our real costs so that we can move on to the real decision which is price. Price is what we have to be able to agree on and if you can't agree on costs, you can't agree on prices. That's just as fundamental as any rule in business, so I am disappointed, as he is.

When we talked this morning I think both of us expressed that disappointment. I think both of us - I don't think - I mean both of us agreed, because I wanted to make sure that one of the things we agreed to early on is that, if we decided these talks were not going any place, that we would talk to each other first. He kept his side of that bargain, I kept my side of that bargain and today we agreed that we would terminate the discussions for now and I don't care whether you use the term "terminate" or "suspend" or whatever you want to call them.

We are going to be working with the ACCC every week on one issue or another and we are going to be working with the ACCC on big issues like ULL and hopefully at some point again fibre to the

node, so we have built a great asset, I think, in the trust that exists on both sides as a result of these talks and I hope that isn't undermined by anything that happens because we weren't able to reach agreement at this time. But I think my disappointment is as great as his.

QUESTION: So this morning was he quite happy for you to come out and say that the negotiations were over, or did he sort of say to you should we keep going with this or was it just your decision to say it's over?

PHIL BURGESS: No. I told him that we had reached a conclusion over this weekend that we didn't see a lot of reason to continue and kind of asked him by implication does he see any reason not to continue and he didn't. I mean he didn't have any response that indicated he saw reason why we should continue.

From the beginning we have had the understanding, and I am going to spell this out more later today, but we had what kind of what Graeme called a green light, amber light, red light approach and we both wanted to get to a position. The ACCC can't approve anything, they can't endorse anything, but they can say we think that where we are is worthy of industry discussion and there are some green lights, a lot of green lights, some amber lights but no red lights. The problem we had was we had a lot of red lights and we had a couple of big red lights and those red lights really led us to the conclusion that we really need to get back to business and it isn't going to be FTTN, it is going to be other things.

QUESTION: Thank you.

QUESTION: (Patrick Russell from Merrill Lynch.) I think my question has already been asked. It is in relation to plan B, the HFC network and what the plans might be to (indistinct).

PHIL BURGESS: Yes. I can't answer that. That is something you may want to bring up with Sol or John Stanhope or others but that's not something we do.

QUESTION: (Andrew Hines from Morgan Stanley.) Hi, Phil. I guess you have been running this campaign for 12 months or so on trying to get the regulatory environment in Australia changed with not much success. It is not just the ACCC, I guess the highest levels of government have said they are not going to change the rules and try and appeal the line sharing agreement from the ACCC to the Australian (indistinct) tribunal who also upheld the costings of the ACCC. Do you think it's time now to (several indistinct words). One way to get around the regulation here is to separate those parts of your business that are heavily regulated from those that aren't and leave the regulation to the regulation and get on with the retail part of what you can control?

PHIL BURGESS: I don't know why anybody would want what happened to BP to happen to them, but, look, let me put it this way: You know, in this country like in my country there are lots of laws and regulations that people adhere to but don't make a lot of sense and the people who oppose them or suggest they ought to be reformed are always looked on as somehow "why don't you just live with the rules the way they are", but fortunately for this country the people who wanted to float the dollar, who were viewed as kind of silly for a long time, you know, turned out that their views prevailed and everybody looks back and says, "You know, when we changed the rules and started to float the dollar, things got better."

The same way on tariffs, I mean you had high tariffs for a long time and you had a bunch of crazy people out there who decided

we ought to have tariff reform and a more free trade approach and people who kind of said, "Why don't you just play by the rules and not worry about these things?" In fact, this country is prosperous today because you had tariff reform and you started to float the dollar. So my view is that the rules that exist in this country prima facie are not good rules for investment in telecommunications. I think the evidence is overwhelming to support that. That is number one.

Number two, I think the evidence is overwhelming that the future for the next 25 years for most of the developed countries is going to be shaped by biotechnology and telecommunications. I don't know what the biotechnology industry is like in this country, but I do know what the telecommunications industry is like and we have to have a healthier, more competitive, more aggressive industry that has more freedom to invest and to explore and to take risks than we have now.

There is a third point and that is that telecommunications has the biggest impact where distances are long, where the terrain is difficult and where the densities are low because those are the places where - because telecommunications is the death of distance, but it costs a lot to do it, it costs a lot to get a stranglehold on the distance issues and so that is only going to be handled by investment.

We do not have a pro-investment policy in this country, so I appreciate what you are saying and I think everybody ought to have some humility, but the fact is I think that, despite the resistance, despite the inability to get people to see things our way, I do think we have made progress and I do think that the positions we are taking, which is a pro-investment, pro-consumer, pro-innovation, pro-growth

approach for this country is the way to go and we are going to continue to talk about that to our shareholders and to the public and hopefully people will come along just like they did on floating the dollar and getting rid of onerous tariffs.

QUESTION: You don't see any merit in separating Telstra into structure and retail components?

PHIL BURGESS: What's the merit?

QUESTION: Just in terms of having a regulated part of the business that can operate separately and then a retail business that competes for equal access to that infrastructure along with all the other competitors.

PHIL BURGESS: The point is I don't know where that's worked very well.

TONY WARREN: Andrew, it is Tony Warren here. Let me just add to that.

When you see the details of what we proposed this afternoon in these discussions, I think you will see very clearly that what was proposed was very much equivalent access to this large investment. The problem here, Andrew, is that we needed to get the settings right to make sure that that investment was commercial and the regulatory regime in this country which you have derided us for trying to change for the last year doesn't allow for those settings to be correctly put in place and as a result we have decisions like today where unfortunately a substantial investment that would be very beneficial to a large number of Australians has been killed off.

I mean this is not something that we look at and say "This is fantastic", this is something we look at and we are all quite disappointed on, but that's the nature of the beast, that's what the regulatory regime has imposed on this company and this country and, until it gets changed, this country is going to be stuck in the slow lane.

QUESTION: (Tim Smeallie from Citigroup.) Phil, if we look back at November, I guess there were three factors underpinning the new strategy. One was business transformation, the other was a ULL at \$30 and the other was FTTN to deliver the growth from 2009 onwards. Given two out of three of these are no longer occurring, should we expect to see a new strategy outline on Thursday, is probably my first question. And, secondly, are we now really reliant on the G9 to prevent Australia becoming a broadband backwater given the technology problems with DSL?

PHIL BURGESS: On the first one, Tim, I can't say. I'm going to be fighting for a front row seat there just like you are to hear the answer. On the G9 thing, I don't know. I hope we are not relying on the G9 because I haven't seen much from them except press releases. I mean what we had in our case for the FTTN, we had a deployment plan which we shared the deployment plan for Melbourne, I think it was - Melbourne or Sydney, I think it was Melbourne - with the ACCC one day showing exactly the exchanges, where things were going to do, what the footprint was and so on. We also had a capital spending plan, we also had arrangements with vendors to build it, so I am not sure what the G9 has. If they build it, I think it will be a good thing and, as I said, we will be access seekers.

QUESTION: Phil, would you say given the problems with DSL that we are looking at trending back to dial-up speeds within five years if we are relying on DSL?

PHIL BURGESS: I wouldn't say go back to dial-up speeds but I do think you are not going to have the kinds of speeds that are increasingly demanded by the band width-hungry applications that are anticipated and coming forward in some areas. I think that Korea

and Japan are moving to 100 megabits for a reason and that's because, number one, people want that, not because they want to have faster speeds, but because they want applications that require those faster speeds, and the same thing is true in Europe and also in the United States where people are moving up the speed limits because the applications require those kinds of speeds and that is why it is so perplexing to us why a company that wants to build this out, has the money to do it, has a plan to do it, has the talent to do it, is being prevented from doing it because of the unwillingness of the regulator to give us the financial assurances that we need to make sure our shareholders are not pillaged once it gets built.

I mean, just last week the ACCC declared a new service and under the current regime, under the current legislative regime and other mandates that are available, they could do the same thing with the FTTN. So we are not going to build, we are not going to spend \$4 billion just to have it taken away a year later or six months later by a regulator who decides they can set the prices better than the market.

SPEAKER: Ladies and gentlemen, we are going to finish at 1 o'clock which allows us three more questions.

QUESTION: ( Laurent Horrut from JP Morgan.) I just had a quick question on the discussion with ACCC. You mentioned the fact that one of the differences were in fact the costs of providing services to the bush. I was just wondering what is the logic for you to (indistinct) because these costs on a network that was going to be available to metropolitan customers only.

PHIL BURGESS: The network wasn't going to be available to metropolitan customers only. That was only the first phase. The first phase was the five cities. We said to the ACCC and they understood and also it

will be apparent when you see the summary of our plan that we will make available later today, that the initial footprint would go to the five cities, but then it would expand within the five cities over time and also leap-frog to other cities like Hobart or Newcastle or Canberra or places where commercial opportunities develop, so the whole point is that this was not for the cities only.

The second point is that the cities have always subsidised the bush. I mean that has always been the case, so I mean that's one reason why this came up in the FTTN discussion because, if we have a new bit stream service we call high speed access service, if we have a new bit stream service, then the question is how are you going to continue to fund the cross-subsidy pool that's used from the nine million people who live in urban and metropolitan areas to pay for the high cost areas that have one million people and that is why it would be irresponsible just to look at the cities. You have to look at the entire nation.

Just as the government says let's look at the entire nation, not just the cities, we are not going to have an urban-centric policy, we are going to have a telecommunications policy for the whole country; for the rural areas, for the bush, for the regional areas, not just for the cities, and that's why we had to pay attention to some kind of a surcharge or other approach that would allow for the FTTN regime to fill the coffers of the cross-subsidy pool that's used to subsidise services to the bush.

TONY WARREN: To be very clear, that's been an issue that's been on the table with the commission from the very beginning of these discussions. We made it very clear at the outset of these discussions that we would need to have some kind of contribution from the FTTN

footprint as there is at the moment and would have to continue to be into the future.

QUESTION: But then isn't the issue more the one of the universal service obligation funding, which is a different framework for that one, so it would have definitely confused the discussion in that sense.

TONY WARREN: The USO is - Phil I think made clear in his opening statement that there are two instruments in Australia to fund the bush. One is the USO, the second is cross-subsidisation. If anyone in their right mind believes the USO covers the costs in and of itself, I think they really need to go and have a look at that a bit more closely.

PHIL BURGESS: Let's take an example. The last study done by government of the cost of the bush was done by ACA which is now ACFA(?). They said that it was \$550 million, that was in the late 1990s, a year to provide services to the bush over and above the universal service, but the government decided last year, for example, that it really wasn't 550, it was really only 170, so the universal service fund was cut to \$170 million and of that \$170 million Telstra pays \$110 million, the other competitors pay \$60 million, so even if we take figures that are going on eight to 10 years now, we are way behind in the amount of money provided by the universal service fund to cover those costs.

QUESTION: Just a last one, if I can. Can you just clarify: When you said that you are still talking with the ACCC and you will be talking to the ACCC in the future, are you still trying to work through the issues or from your end the discussion is very much terminated at this stage?

PHIL BURGESS: These discussions are terminated and Graeme and I agreed on that this morning. But, yes, we are still talking to them. We have to talk to them and they need to talk to us, too. I mean we are the largest telco in the country and they are the regulator and we need to

be talking with them every week about one thing or another and we will and, as Graeme and I discussed this morning, at some point we are going to want to revisit these issues. I don't know if it is going to be sooner or later, but at some point we want to revisit these issues as well as other issues.

I don't view this as a break with the ACCC, not at all. I think one of the consequences of this process has been that we have developed some good and trustful relationships and throughout this those agreements and trusts have never been broken. We came close a couple of times, we said we wouldn't negotiate in the press and I think Graeme Samuel slipped a couple of times and I may have slipped a couple of times, I can't remember, but the fact is that I think that we are going continue to work with them in every way we can and try to have as positive and constructive a relationship as possible.

QUESTION: (Ian Martin ... ABN Amro.) Just a couple of questions. First, the obligations that concern you here, the cross-subsidy on the national pricing, can you just confirm that just applies to voice and in particular to the basic line rental product for voice? Secondly, in relation to an earlier question about why you wouldn't do this project that presumably is profitable now on the provisional access terms you have agreed, I think you said something like why do something that's going to hasten the decline of revenue for this cross-subsidy. Just going back to the strategy day, though, I think the understanding was that it would hasten the decline of voice revenue, that the total pool of revenue would go up if you went ahead with this projects, that is the average revenue per customer or the share of wallet would go up because of other services you could sell.

TONY WARREN: The first question about does the (several indistinct words) price control applies only to voice. However, you will probably know, as most do, that our ADSL broadband pricing is actually nationally uniform, so in practice we do in the broadband level apply uniform pricing construct.

In terms of the comment about hastening the end of the cross-subsidy, let's just be clear about what happens, right? At the moment the bush is paid for by the USO contributions, minimal as they are as Phil just expressed and, secondly, they are paid for by cross-subsidies. Now, those cross-subsidies are borne by Telstra retail customers when they pay their \$30 a month basic access charge. If customers take a wholesale line under the current ACCC pricing arrangements, ULL and, if this went ahead, under FTTN, they would not be, on the ACCC's preferred model, continuing to contribute to the bush. So, what Phil said by hastening this is at the moment they don't pay it on ULL and under the ACCC's proposal they wouldn't pay a cross-subsidy on FTTN. Hence, the pool of money, if you like, for the cross-subsidy would be getting narrower and narrower as more and more wholesale lines are purchased.

PHIL BURGESS: The bottom line is if you can't recover today's costs, why invest another \$4 billion? I mean, if you are not recovering your costs, you are not going to make it up on volume.

QUESTION: (Phil Campbell from Citigroup.) Thanks, guys. I just had a question on the kind of second and third derivative of this decision because obviously this is a first derivative decision you are making, but if we just look across the Tasman, several months ago Telecom New Zealand kind of made several decisions based on the first derivative and the second and third derivatives were extremely

negative for that company.

So my question to you guys is what discussions have you had with (indistinct) or the minister's office and have you built in any risk for any similar types of decisions that may come out in terms of policy changes as a result of this decision?

TONY WARREN: First of all, let me take some umbrage about you comparing us to Telecom New Zealand. I think Telecom New Zealand is about where we were in about '96/'97 now, so we have got a little way to go on that side of the channel. Look, clearly we understand that there are risks with all these decisions. Clearly we understand that and we have thought through very carefully what all of the second and third derivative items should be. But, putting it very simply, this company cannot invest \$4 billion of its shareholders' money if it doesn't feel it can protect that investment and so that is in fact our first, second and third derivative obligation under the Corporations Act and we really do need to, I think, keep that squarely in our mind.

QUESTION: So if you are kind of, I suppose, doing some financial analysis on this, you can work out that the value that you would lose from building, say, \$4 billion of fibre to the node, given if you agreed to some of the stuff (indistinct) is actually a better outcome than your analysis of the second or third derivatives.

TONY WARREN: We don't ascribe to that (indistinct).

PHIL BURGESS: I guess time's up. I just want to say thanks to everybody for coming. This was a big decision on our part and I wish we had a different result from these five months but I think a lot was gained in the five months. If you think back to the things I read out where we made substantial progress, I think they were important and I think that they will lay ground work for future work.

If we can help you in any way, let us know later this afternoon. We will have on our web site, now we are talking, some materials related to what we have been talking about this morning and if you want to get more information you can go there or feel free to call Andrew or Liz Jurman, our media staff, if you want to contact any of us to talk more about any of this.

But I want to say in closing that Graeme Samuel and his colleagues at the ACCC worked hard with us to try to make this happen. He said when we started he would make this his high priority and he never disappointed me on that. I told him that we would make this our highest priority and we did. I think we have invested close to \$2 million trying to make this project work because we had to undertake a lot of cost studies, we had to get lawyers involved to help us think through some of the legislative and other issues that were involved, so I think everybody on both sides made a big investment in the right spirit to make this thing work and I have high regard for Graeme Samuel and his colleagues over there and we are going to do everything we can to work with them in the future on the whole range of issues that touch us that they have jurisdiction over.

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